Invesco Mortgage Capital Inc.
Form 10-Q
November 03, 2015

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2015

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 001-34385

(Exact Name of Registrant as Specified in Its Charter)

Maryland (State or Other Jurisdiction of Incorporation or Organization)	26-2749336 (I.R.S. Employer Identification No.)
1555 Peachtree Street, N.E., Suite 1800 Atlanta, Georgia	30309
(Address of Principal Executive Offices)	(Zip Code)

(404) 892-0896
(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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 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. (Check one):

Large Accelerated filer	ý		Accelerated filer	o
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

As of October 28, 2015, there were 119,455,302 outstanding shares of common stock of Invesco Mortgage Capital Inc.

Table of Contents

INVESCO MORTGAGE CAPITAL INC.
TABLE OF CONTENTS

Table of Contents

PART I
ITEM 1. FINANCIAL STATEMENTS
INVESCO MORTGAGE CAPITAL INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

In thousands except share amounts	As of September 30, 2015 (Unaudited)	December 31, 2014 (As Restated)
ASSETS		
Mortgage-backed and credit risk transfer securities, at fair value	16,814,961	17,248,895
Residential loans, held-for-investment [1]	3,307,249	3,365,003
Commercial loans, held-for-investment	187,038	145,756
Cash and cash equivalents	76,658	164,144
Due from counterparties	174,741	57,604
Investment related receivable	24,897	38,717
Accrued interest receivable	69,064	66,044
Derivative assets, at fair value	1,308	24,178
Deferred securitization and financing costs	10,689	13,080
Other investments	113,297	106,498
Other assets	1,444	1,098
Total assets [1]	20,781,346	21,231,017
LIABILITIES AND EQUITY		
Liabilities:		
Repurchase agreements	12,912,131	13,622,677
Secured loans	1,675,000	1,250,000
Asset-backed securities issued by securitization trusts [1]	2,859,423	2,929,820
Exchangeable senior notes	400,000	400,000
Derivative liabilities, at fair value	343,897	254,026
Dividends and distributions payable	54,067	61,757
Investment related payable	54,996	17,008
Accrued interest payable	37,296	29,670
Collateral held payable	—	14,890
Accounts payable and accrued expenses	3,910	2,439
Due to affiliate	11,259	9,880
Total liabilities [1]	18,351,979	18,592,167
Equity:		
Preferred Stock, par value $0.01 per share; 50,000,000 shares authorized:		
7.75% Series A Cumulative Redeemable Preferred Stock: 5,600,000 shares issued and outstanding ($140,000 aggregate liquidation preference)	135,356	135,356
7.75% Fixed-to-Floating Series B Cumulative Redeemable Preferred Stock: 6,200,000 shares issued and outstanding ($155,000 aggregate liquidation preference)	149,860	149,860
Common Stock, par value $0.01 per share; 450,000,000 shares authorized; 119,453,846 and 123,110,454 shares issued and outstanding, respectively	1,195	1,231
Additional paid in capital	2,482,742	2,532,130
Accumulated other comprehensive income	446,857	424,592
Retained earnings (distributions in excess of earnings)	(813,520)	(632,854)

Total stockholders’ equity	2,402,490	2,610,315
Non-controlling interest	26,877	28,535
Total equity	2,429,367	2,638,850
Total liabilities and equity	20,781,346	21,231,017

(1) The condensed consolidated balance sheets include assets of consolidated variable interest entities (“VIEs”) that can only be used to settle obligations and liabilities of the VIEs for which creditors do not have recourse to the Company. As of September 30, 2015 and December 31, 2014, total assets of the consolidated VIEs were $3,331,942 and $3,380,597, respectively, and total liabilities of the consolidated VIEs were $2,876,059 and $2,938,512, respectively. Refer to Note 3 - "Variable Interest Entities" for further discussion.

The accompanying notes are an integral part of these condensed consolidated financial statements.

INVESCO MORTGAGE CAPITAL INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

In thousands, except share amounts	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014 (As Restated)	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2014 (As Restated)
Interest Income				
Mortgage-backed and credit risk transfer securities	129,260	139,419	390,623	436,019
Residential loans [1]	28,380	22,713	88,001	60,888
Commercial loans	3,743	2,649	11,349	6,329
Total interest income	161,383	164,781	489,973	503,236
Interest Expense				
Repurchase agreements	41,303	45,756	125,544	142,649
Secured loans	1,622	1,223	4,639	1,399
Exchangeable senior notes	5,620	5,620	16,840	16,840
Asset-backed securities [1]	20,686	17,660	64,913	47,421
Total interest expense	69,231	70,259	211,936	208,309
Net interest income	92,152	94,522	278,037	294,927
(Reduction in) provision for loan losses	(81)	(209)	(213)	(52)
Net interest income after (reduction in) provision for loan losses	92,233	94,731	278,250	294,979
Other Income (loss)				
Gain (loss) on investments, net	(2,958)	(48,364)	10,090	(86,333)
Equity in earnings of unconsolidated ventures	1,894	1,145	9,131	5,480
Gain (loss) on derivative instruments, net	(220,602)	(3,704)	(287,344)	(322,832)
Realized and unrealized credit derivative income (loss), net	2,928	(28,613)	24,904	20,929
Other investment income (loss), net	739	(1,358)	1,518	(1,358)
Total other income (loss)	(217,999)	(80,894)	(241,701)	(384,114)
Expenses				
Management fee – related party	10,058	9,214	28,816	27,876
General and administrative	2,507	2,519	6,186	6,906
Consolidated securitization trusts [1]	2,132	1,560	6,544	4,108
Total expenses	14,697	13,293	41,546	38,890
Net income (loss)	(140,463)	544	(4,997)	(128,025)
Net income (loss) attributable to non-controlling interest	(1,629)	6	(80)	(1,456)
Net income (loss) attributable to Invesco Mortgage Capital Inc.	(138,834)	538	(4,917)	(126,569)
Dividends to preferred stockholders	5,716	2,713	17,148	8,138
Undeclared cumulative dividends to preferred stockholders	—	661	—	661
Net income (loss) attributable to common stockholders	(144,550)	(2,836)	(22,065)	(135,368)
Earnings (loss) per share:				
Net income (loss) attributable to common stockholders				
Basic	(1.18)	(0.02)	(0.18)	(1.10)
Diluted	(1.18)	(0.02)	(0.18)	(1.10)
Dividends declared per common share	0.40	0.50	1.30	1.50

(1) The condensed consolidated statements of operations include income and expenses of consolidated VIEs. Refer to Note 3 - “Variable Interest Entities” for further discussion.

The accompanying notes are an integral part of these condensed consolidated financial statements.

INVESCO MORTGAGE CAPITAL INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

In thousands	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014 (As Restated)	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2014 (As Restated)
Net income (loss)	(140,463)	544	(4,997)	(128,025)
Other comprehensive income (loss):				
Unrealized gain (loss) on mortgage-backed and credit risk transfer securities, net	41,978	(81,267)	(25,390)	325,045
Reclassification of unrealized (gain) loss on sale of mortgage-backed and credit risk transfer securities to gain (loss) on investments, net	1,380	49,169	(3,223)	81,653
Reclassification of amortization of net deferred losses on de-designated interest rate swaps to repurchase agreements interest expense	15,724	21,227	51,182	64,055
Currency translation adjustments on investment in unconsolidated venture	(33)	—	(33)	—
Total other comprehensive income (loss)	59,049	(10,871)	22,536	470,753
Comprehensive income (loss)	(81,414)	(10,327)	17,539	342,728
Less: Comprehensive income (loss) attributable to non-controlling interest	942	117	(191)	(3,919)
Less: Dividends to preferred stockholders	(5,716)	(2,713)	(17,148)	(8,138)
Less: Undeclared cumulative dividends to preferred shareholders	—	(661)	—	(661)
Comprehensive income (loss) attributable to common stockholders	(86,188)	(13,584)	200	330,010

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

INVESCO MORTGAGE CAPITAL INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF EQUITY
For the nine months ended September 30, 2015
(Unaudited)

	Attributable to Common Stockholders									
	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid in Capital	Accumulated Other Comprehensive Income (loss)	Retained Earnings (Distributions in excess of earnings)	Total Stockholders' Equity
In thousands except share amounts	Shares	Amount	Shares	Amount	Shares	Amount				
Balance at January 1, 2015 (As Restated)	5,600,000	135,356	6,200,000	149,860	123,110,454	1,231	2,532,130	424,592	(632,854)	2,610,315
Net income (loss)	—	—	—	—			—	—	(4,917)	(4,917)
Other comprehensive income	—	—	—	—	—	—	—	22,265	—	22,265
Proceeds from issuance of common stock, net of offering costs	—	—	—	—	10,317	—	158	—	—	158
Repurchase of shares of common stock	—	—	—	—	(3,695,368)	(36)	(49,963)	—	—	(49,999)
Stock awards	—	—	—	—	28,443	—	—	—	—	—
Common stock dividends	—	—	—	—	—	—	—	—	(158,601)	(158,601)
Common unit dividends	—	—	—	—	—	—	—	—	—	—
Preferred stock dividends	—	—	—	—	—	—	—	—	(17,148)	(17,148)
Amortization of equity-based compensation	—	—	—	—	—	—	417	—		417
Balance at September 30, 2015	5,600,000	135,356	6,200,000	149,860	119,453,846	1,195	2,482,742	446,857	(813,520)	2,402,490

The accompanying notes are an integral part of this condensed consolidated financial statement.

Table of Contents

INVESCO MORTGAGE CAPITAL INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
In thousands	2015	2014 (As Restated)
Cash Flows from Operating Activities		
Net income (loss)	(4,997)	(128,025)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Amortization of mortgage-backed and credit risk transfer securities premiums and (discounts), net	96,121	99,698
Amortization of residential loans and asset-backed securities premiums (discount), net	(639)	2,195
Amortization of commercial loan origination fees	(51)	(1)
(Reduction in) provision for loan losses	(213)	(52)
Unrealized (gain) loss on derivative instruments, net	104,546	133,863
Unrealized (gain) loss on credit derivatives, net	(7,923)	(8,121)
(Gain) loss on investments, net	(10,090)	86,333
Realized (gain) loss on derivative instruments, net	44,394	34,877
Realized (gain) loss on credit derivatives, net	2,184	—
Equity in earnings of unconsolidated ventures	(9,131)	(5,480)
Amortization of equity-based compensation	422	378
Amortization of deferred securitization and financing costs	2,391	2,220
Reclassification of amortization of net deferred losses on de-designated interest rate swaps to repurchase agreements interest expense	51,182	64,055
Non-cash interest income capitalized in commercial loans	—	(768)
(Gain) loss on foreign currency transactions, net	619	1,479
Changes in operating assets and liabilities:		
(Increase) decrease in operating assets	(3,289)	1,790
Increase (decrease) in operating liabilities	10,512	(6,174)
Net cash provided by operating activities	276,038	278,267
Cash Flows from Investing Activities		
Purchase of mortgage-backed and credit risk transfer securities	(1,821,811)	(3,752,261)
Distributions from investment in unconsolidated ventures, net	15,174	7,602
Change in other investments	(12,875)	(52,500)
Principal payments from mortgage-backed and credit risk transfer securities	1,910,904	1,422,082
Proceeds from sale of mortgage-backed and credit risk transfer securities	290,561	3,069,978
Payments on sale of credit derivatives	(2,184)	—
Payment of premiums for interest rate swaptions	(1,485)	(10,328)
Payments for termination of futures/currency forward contracts, swaps, swaptions and TBAs	(34,066)	(11,604)
Purchase of residential loans held-for-investment	(372,305)	(1,417,864)
Principal payments from residential loans held-for-investment	424,644	120,930
Principal payments from commercial loans held-for-investment	63,132	400
Origination and advances of commercial loans, net of origination fees	(104,965)	(81,201)
Net cash provided by (used in) investing activities	354,724	(704,766)
Cash Flows from Financing Activities		

Proceeds from issuance of common stock	158	191
Repurchase of common stock	(49,999)	(21,130)
Cost of issuance of preferred stock	(36)	150,096
Due from counterparties	(118,562)	(26,999)
Collateral held payable	(14,890)	(13,771)
Proceeds from repurchase agreements	105,832,915	108,739,181
Principal repayments of repurchase agreements	(106,543,411)	(110,638,714)
Proceeds from asset-backed securities issued by securitization trusts	336,077	1,213,405
Principal repayments of asset-backed securities issued by securitization trusts	(400,207)	(109,587)
Proceeds from secured loans	2,100,000	2,835,247
Principal repayments on secured loans	(1,675,000)	(1,585,247)
Payments of deferred costs	—	(1,811)
Payments of dividends and distributions	(185,293)	(196,030)
Net cash (used in) provided by financing activities	(718,248)	344,831
Net change in cash and cash equivalents	(87,486)	(81,668)
Cash and cash equivalents, beginning of period	164,144	210,612
Cash and cash equivalents, end of period	76,658	128,944
Supplement Disclosure of Cash Flow Information		
Interest paid	162,906	146,209
Non-cash Investing and Financing Activities Information		
Net change in unrealized gain on mortgage-backed and credit risk transfer securities	(28,613)	406,698
Dividends and distributions declared not paid	54,067	64,976
(Receivable) / payable for mortgage-backed and credit risk transfer securities, net	53,089	457,049
Repurchase agreements, not settled	(50)	19,747
Collateral held payable, not settled	—	(3,481)
Net change in due from counterparties	1,425	—

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

INVESCO MORTGAGE CAPITAL INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 – Organization and Business Operations

Invesco Mortgage Capital Inc. (the “Company”) is a Maryland corporation primarily focused on investing in, financing and managing residential and commercial mortgage-backed securities and mortgage loans. The Company is externally managed and advised by Invesco Advisers, Inc. (the "Manager"), a registered investment adviser and an indirect, wholly-owned subsidiary of Invesco Ltd. (“Invesco”), a leading independent global investment management firm.

The Company conducts its business through IAS Operating Partnership LP (the “Operating Partnership”) as its sole general partner. As of September 30, 2015, the Company owned 98.8% of the Operating Partnership, and a wholly-owned subsidiary of Invesco owned the remaining 1.2%. The Company has one operating segment.

The Company primarily invests in:

- Residential mortgage-backed securities ("RMBS") that are guaranteed by a U.S. government agency such as the Government National Mortgage Association, or a federally chartered corporation such as the Federal National Mortgage Association ("Fannie Mae") or the Federal Home Loan Mortgage Corporation ("Freddie Mac") (collectively "Agency RMBS");
- RMBS that are not guaranteed by a U.S. government agency (“non-Agency RMBS”);
- Credit risk transfer securities that are unsecured obligations issued by government-sponsored enterprises ("GSE CRT");
- Commercial mortgage-backed securities ("CMBS");
- Residential and commercial mortgage loans; and
- Other real estate-related financing agreements.

The Company generally finances its investments through short- and long-term borrowings structured as repurchase agreements and secured loans. The Company finances its residential loans held-for-investment through asset-backed securities ("ABS") issued by consolidated securitization trusts. The Company has also financed investments through the issuances of debt and equity and may utilize other forms of financing in the future.

The Company elected to be taxed as a real estate investment trust (“REIT”) for U.S. federal income tax purposes under the provisions of the Internal Revenue Code of 1986, as amended, commencing with the Company's taxable year ended December 31, 2009. To maintain the Company’s REIT qualification, the Company is generally required to distribute at least 90% of its REIT taxable income to its stockholders annually. The Company operates its business in a manner that permits exclusion from the "Investment Company" definition under the Investment Company Act of 1940, as amended.

Note 2 – Summary of Significant Accounting Policies

Restatement Background

On August 9, 2015, the Audit Committee of the Board of Directors of the Company concluded, based on the recommendation of management, that each of the Company’s previously issued (i) consolidated financial statements as of and for the years ended December 31, 2013 and 2014, which were included in its Annual Report on Form 10-K for the year ended December 31, 2014, and (ii) interim consolidated financial statements as of and for the quarter ended March 31, 2013 and for all subsequent quarters through the quarter ended March 31, 2015 needed to be restated and should no longer be relied upon. The Company filed Amendment No. 1 to its Annual Report on Form 10-K for the year ended December 31, 2014 ("Form 10-K/A") and Amendment No. 1 to its Quarterly Report on Form 10-Q for the quarter ended March 31, 2015 ("Form 10-Q/A") on August 17, 2015. Additional information regarding the restatement is contained in those filings. Prior period financial information in this Form 10-Q has been amended where necessary to reflect the restatement. Therefore, this Form 10-Q should be read in conjunction with the Company’s Annual Report on Form 10-K/A for the year ended December 31, 2014.

Basis of Presentation and Consolidation

Certain disclosures included in the Company’s Form 10-K/A are not required to be included on an interim basis in the Company’s quarterly reports on Form 10-Q. The Company has condensed or omitted these disclosures. Therefore, this

Form 10-Q should be read in conjunction with the Company’s Annual Report on Form 10-K/A for the year ended December 31, 2014.

In the opinion of management, the condensed consolidated financial statements reflect all adjustments, consisting of normal recurring accruals, which are necessary for a fair presentation of the financial condition and results of operations for the periods presented. All significant intercompany transactions, balances, revenues and expenses are eliminated upon consolidation.

The condensed consolidated financial statements have been prepared in accordance with U.S. GAAP and consolidate the financial statements of the Company and its controlled subsidiaries. The condensed consolidated financial statements also include the consolidation of certain securitization trusts that meet the definition of a variable interest entity ("VIE") because the Company has been deemed to be the primary beneficiary of the securitization trusts. These securitization trusts hold pools of residential mortgage loans and issue series of asset-backed securities payable from the cash flows generated by the underlying pools of residential mortgage loans. The securitizations are non-recourse financing for the residential mortgage loans held-for-investment. Generally, a portion of the asset-backed securities issued by the securitization trusts is sold to unaffiliated third parties and the balance is purchased by the Company. The Company classifies the underlying residential mortgage loans owned by the securitization trusts as residential loans held-for-investment in its condensed consolidated balance sheets. The asset-backed securities issued to third parties are recorded as liabilities on the Company's condensed consolidated balance sheets. The Company records interest income on the residential loans held-for-investment, interest expense on the asset-backed securities issued to third parties and direct operating expenses incurred by the securitization trusts in the Company's condensed consolidated statements of operations. The Company eliminates all intercompany balances and transactions between itself and the consolidated securitization trusts. The Company records the initial underlying assets and liabilities of the consolidated securitization trusts at their fair value upon consolidation into the Company and, as such, no gain or loss is recorded upon consolidation. Refer to Note 3 - "Variable Interest Entities" for additional information regarding the impact of consolidation of securitization trusts.

The consolidated securitization trusts are VIEs because the securitization trusts do not have equity that meets the definition of U.S. GAAP equity at risk. In determining if a securitization trust should be consolidated, the Company evaluates whether it has both (i) the power to direct the activities of the securitization trust that most significantly impact its economic performance and (ii) the right to receive benefits from the securitization trust or the obligation to absorb losses of the securitization trust that could be significant. The Company's determination of whether it is the primary beneficiary of a securitization trust includes both a qualitative and quantitative analysis. The Company determined that it was the primary beneficiary of certain securitization trusts because it was involved in certain aspects of the design of the securitization trusts and has certain default oversight rights on defaulted residential loans. In addition, the Company owns the most subordinated class of asset-backed securities issued by the securitization trusts and has the obligation to absorb losses and right to receive benefits from the securitization trust that could potentially be significant to the securitization trust. The Company assesses modifications to VIEs on an ongoing basis to determine if a significant reconsideration event has occurred that would change the Company's initial consolidation assessment.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. Examples of estimates include, but are not limited to, estimates of the fair values of financial instruments, interest income on mortgage-backed and credit risk transfer securities, allowance for loan losses and other-than-temporary impairment charges. Actual results may differ from those estimates.

Significant Accounting Policies

A summary of the Company's significant accounting policies is included in Note 2 to the consolidated financial statements of the Company’s 2014 Annual Report on Form 10-K/A. A summary of additional accounting policies that are significant to the Company's consolidated financial condition and results of operations for the three and nine months ended September 30, 2015 is provided below.

Translation of Foreign Currencies

The functional currency of the Company and its subsidiaries is U.S. dollars. Transactions in foreign currencies are recorded at the rates of exchange prevailing on the date of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are remeasured at the rates prevailing at the balance sheet date. Gains and losses arising on revaluation are included in the condensed consolidated statements of operations.

The Company's reporting currency is U.S. dollars. Upon consolidation, the assets and liabilities of the Company’s investment in an unconsolidated venture whose functional currency is the Euro is translated to U.S. dollars using the period-end exchange rates. Equity accounts are translated at historical rates, except for the change in retained earnings during the year,

Table of Contents

which is the result of the income statement translation process. Revenue and expense accounts are translated using the weighted average exchange rate during the period. The cumulative translation adjustments associated with the investment in the unconsolidated venture are recorded in accumulated other comprehensive income (loss), a component of condensed consolidated stockholders' equity.
The Company generally hedges interest rate and foreign currency exposure with derivative financial instruments. Refer to Note 8 - "Derivatives and Hedging Activities" for further information.
Fair Value Measurements
The Company discloses the fair value of its financial instruments according to a fair value hierarchy (Levels 1, 2, and 3, as defined). In accordance with U.S. GAAP, the Company is required to provide enhanced disclosures regarding instruments in the Level 3 category (which require significant management judgment), including a separate reconciliation of the beginning and ending balances for each major category of assets and liabilities.
To determine fair value of its financial instruments, the Company generally obtains one price per instrument from its primary valuation service. If this service cannot provide a price, the Company will seek a value from other vendors. The valuation services use various observable inputs which may include a combination of benchmark yields, trades, broker/dealer quotes, issuer spreads, bids, offers and benchmark securities to determine prices. Both the Company and the pricing vendor continuously monitor market indicators and economic events to determine if any may have an impact on the valuations.
Overrides of prices from pricing vendors are rare in the current market environment for the assets the Company holds. Examples of instances that would cause an override include if the Company recently traded the same security or there is an indication of market activity that would cause the vendor price to be unreliable. In the rare instance where a price is adjusted, the Company has a control process to monitor the reason for such adjustment.
To gain comfort that vendor prices are representative of current market information, the Company compares the transaction prices of security purchases and sales to the valuation levels provided by the vendors. Price differences exceeding pre-defined tolerance levels are identified and investigated and may be challenged. Trends are monitored over time and if there are indications that the valuations are not comparable to market activity, the vendors are asked to provide detailed information regarding their methodology and inputs. Transparency tools are also available from the vendors which help the Company understand data points and/or market inputs used for pricing securities.
In addition, the Company performs due diligence procedures on all vendors on at least an annual basis. A questionnaire is sent to vendors which requests information such as changes in methodologies, business recovery preparedness, internal controls and confirmation that evaluations are generated based on market data. Physical visits are also made to each vendor's office.
As described in Note 10 - "Fair Value of Financial Instruments," the Company evaluates the source used to provide the market price for each security and makes a determination on its categorization within the fair value hierarchy. If the price of a security is obtained from quoted prices for identical instruments in active markets, the security is classified as a level 1 security. If the price of a security is obtained from quoted prices for similar instruments or model-derived valuations whose inputs are observable, the security is classified as a level 2 security. If the inputs appear to be unobservable, the security would be classified as a level 3 security. Transfers between levels, if any, are determined by the Company at the end of the reporting period.
Mortgage-Backed and Credit Risk Transfer Securities
All of the Company's mortgage-backed securities ("MBS") except for Agency interest-only securities ("Agency MBS IOs"), are classified as available-for-sale and reported at fair value. Fair value is determined by obtaining valuations from an independent source. If the fair value of a security is not available from a third-party pricing service, or such data appears unreliable, the Company may estimate the fair value of the security using a variety of methods including other pricing services, discounted cash flow analysis, matrix pricing, option adjusted spread models and other fundamental analysis of observable market factors.
The Company records its purchases of mortgage-backed and credit risk transfer securities on the trade date. Although the Company generally intends to hold most of its mortgage-backed and credit risk transfer securities until maturity, the Company may, from time to time, sell any of its mortgage-backed and credit risk transfer securities as part of its

overall management of its investment portfolio.
Unrealized gains or losses on all MBS, except for Agency MBS IOs, are recorded in accumulated other comprehensive income, a separate component of stockholders' equity, until sale or disposition of the investment. Upon sale or disposition, the cumulative gain or loss previously reported in stockholders' equity is recognized in income. Realized gains and losses from sales of MBS are determined based upon the specific identification method.

Agency MBS IOs are hybrid financial instruments that contain embedded derivatives. Agency MBS IOs are carried at fair value on the Company's consolidated balance sheet with changes in fair value recognized in the Company's condensed consolidated statements of operations because the embedded interest derivative in Agency MBS IOs cannot be reliably measured.

GSE CRTs are unsecured obligations of Fannie Mae and Freddie Mac. Coupon payments on the securities are based on LIBOR and principal payments are based on prepayments and defined credit events in a reference pool of mortgage loans that collateralize Agency RMBS. GSE CRTs are accounted for as hybrid financial instruments consisting of a debt host contract and an embedded derivative. GSE CRTs are measured at fair value. Unrealized gains or losses arising from changes in fair value of the debt host contract, excluding other-than-temporary impairment, are recognized in accumulated other comprehensive income, a separate component of stockholders’ equity, until sale or disposition of the investment. Upon sale or disposition of the debt host contract, the cumulative gain or loss previously reported as a separate component of stockholders’ equity is recognized in income. Realized gains and losses from sales of GSE CRTs are determined based upon the specific identification method. Realized and unrealized gains or losses arising from changes in fair value of the embedded derivative are recognized in realized and unrealized credit derivative income (loss), net in the Company’s condensed consolidated statements of operations.

The Company considers its portfolio of Agency RMBS to be of high credit quality under applicable accounting guidance. For non-Agency RMBS, GSE CRTs and CMBS, the Company does not rely on ratings from third party agencies to determine the credit quality of the investment. The Company uses internal models that analyze the loans underlying each security and evaluates factors including, but not limited to, delinquency status, loan-to-value ratios, borrower credit scores, occupancy status and geographic concentration to estimate the expected future cash flows. The Company places reliance on these internal models in determining credit quality.

While non-Agency RMBS, GSE CRTs and CMBS with expected future losses would generally be purchased at a discount to par, the potential for a significant adverse change in expected cash flows remains. The Company therefore evaluates each security for other-than-temporary impairment at least quarterly.

The determination of whether a security is other-than-temporarily impaired involves judgments and assumptions based on subjective and objective factors. Consideration is given to (i) the length of time and the extent to which the fair value has been less than amortized cost, (ii) the financial condition and near-term prospects of recovery in fair value of the security, and (iii) the Company’s intent and ability to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value.

The Company recognizes in earnings and reflects as a reduction in the cost basis of the security the amount of any other-than-temporary impairment related to credit losses or impairments on securities that the Company intends to sell or for which it is more likely than not that the Company will need to sell before recoveries. The amount of the other-than-temporary impairment on debt securities related to other factors is recorded consistent with changes in the fair value of all other available-for-sale securities as a component of condensed consolidated stockholders’ equity in other comprehensive income or loss with no change to the cost basis of the security.

Residential Loans Held-For-Investment

Residential loans held-for-investment are residential mortgage loans held by consolidated securitization trusts. Residential loans held-for-investment are carried at unpaid principal balance net of any premiums and an allowance for loan losses. The Company expects that it will be required to continue to consolidate the securitization trusts that hold the residential loans.

The Company establishes an allowance for residential loan losses based on the Company's estimate of credit losses. The Company calculates expected losses by estimating the default rate and expected loss severities on the loans. The Company considers the following factors in its evaluation of the allowance for loan losses:

- Loan-to-value ratios, credit scores, geographic concentration and other observable data;
- Historical default rates of loans with similar characteristics; and
- Expected future macroeconomic trends including changes in home prices and the unemployment rate.

Commercial Loans Held-For-Investment

Commercial loans held-for-investment by the Company are carried at cost, net of any allowance for loan losses. An individual loan is considered impaired when it is deemed probable that the Company will not be able to recover its investment and any other anticipated futures payments. The Company generally considers the following factors in evaluating whether a commercial loan is impaired:

Table of Contents

- Loan-to-value ratios;
- The most recent financial information available for each loan and associated properties, including net operating income, debt service coverage ratios, occupancy rates, rent rolls, as well as any other factors the Company considers relevant, including, but not limited to, specific loan trigger events that would indicate an adverse change in expected cash flows or payment delinquency;
- Economic trends, both macroeconomic as well as those directly affecting the properties associated with the loans, and the supply and demand trends in the market in which the subject property is located; and
- The loan sponsor or borrowing entity's ability to ensure that properties associated with the loan are managed and operated sufficiently.

Where an individual commercial loan is deemed to be impaired, the Company records an allowance to reduce the carrying value of the loan to the current present value of expected future cash flows discounted at the loan's effective interest rate, with a corresponding charge to provision for loan losses on the Company's condensed consolidated statements of operations.

Interest Income Recognition

Mortgage-Backed Securities

Interest income on MBS is accrued based on the outstanding principal balance of the securities and their contractual terms. Premiums or discounts are amortized or accreted into interest income over the life of the investment using the effective interest method. Interest income on the Company's non-Agency RMBS (and other prepayable mortgage-backed securities where the Company may not recover substantially all of its initial investment) is based on estimated cash flows. Management estimates, at the time of purchase, the future expected cash flows and determines the effective interest rate based on these estimated cash flows and the Company's purchase price. Over the life of the investments, these estimated cash flows are updated and a revised yield is computed based on the current amortized cost of the investment. In estimating these cash flows, there are a number of assumptions that are subject to uncertainties and contingencies, including the rate and timing of principal payments (prepayments, repurchases, defaults and liquidations), the pass through or coupon rate and interest rate fluctuations. These uncertainties and contingencies are difficult to predict and are subject to future events that may impact management's estimates and the Company's interest income.

For Agency RMBS that cannot be prepaid in such a way that the Company would not recover substantially all of its initial investment, interest income recognition is based on contractual cash flows. The Company does not estimate prepayments in applying the effective interest method.

Credit Risk Transfer Securities

Interest income on credit risk transfer securities is accrued based on the coupon rate of the debt host contract which reflects the credit risk of GSE unsecured senior debt with a similar maturity. Premiums or discounts associated with the purchase of credit risk transfer securities are amortized or accreted into interest income over the life of the debt host contract using the effective interest method. The difference between the coupon rate on the hybrid instrument and the coupon rate on the GSE CRT debt host contract is considered premium income associated with the embedded derivative and is recorded in realized and unrealized credit derivative income (loss), net in the Company's condensed consolidated statements of operations.

Residential Loans

The Company recognizes interest income from residential loans on an accrual basis and amortizes the related premiums into interest income using the effective interest method over the weighted average life of these loans. In estimating the weighted average life of these loans, there are a number of assumptions that are subject to estimation, including the rate and timing of principal payments, defaults, loss severity given default and other factors. Coupon interest is recognized as revenue when earned and deemed collectible or until a loan becomes more than 90 days past due, at which point the loan is placed on nonaccrual status. Interest previously accrued for loans that have been placed on non-accrual status is reversed against interest income in the period the loan is placed in nonaccrual status. Residential loans delinquent more than 90 days or in foreclosure are characterized as delinquent. Cash principal and interest that is advanced from servicers after a loan becomes greater than 90 days past due is recorded as a liability due to the servicer. When a delinquent loan previously placed on nonaccrual status has cured, meaning all delinquent principal and interest have been remitted by the borrower, the loan is placed back on accrual status. Alternatively, nonaccrual loans may be placed back on accrual status if restructured and after the loan is considered re-performing. A restructured loan is considered re-performing when the loan has been current for at least 12 months.

Table of Contents

Commercial Loans

The Company recognizes interest income from commercial loans when earned and deemed collectible, or until a loan becomes past due based on the terms of the loan agreement. Any related origination fees, net of origination cost are amortized into interest income using the effective interest method over the life of the loan. Interest received after a loan becomes past due or impaired is used to reduce the outstanding loan principal balance. When a delinquent loan previously placed on nonaccrual status has cured, meaning all delinquent principal and interest have been remitted by the borrower, the loan is placed back on accrual status. Alternately, loans that have been individually impaired may be placed back on accrual status if restructured and after the loan is considered re-performing. A restructured loan is considered re-performing when the loan has been current for at least 12 months.

Repurchase Agreements

Effective January 1, 2015, the Company adopted newly issued accounting guidance for repurchase financings. Under the new standard, the Company no longer applies the "linked" accounting model to instances where the Company purchases mortgage-backed and credit risk transfer securities and enters into repurchase agreements to finance the purchase with the same counterparty. Purchases of mortgage-backed and credit risk transfer securities and repurchase financings are considered separately, and the repurchase agreement component of the transaction is accounted for as a secured borrowing. The Company records the mortgage-backed and credit risk transfer securities and the related repurchase agreement financing on a gross basis in its condensed consolidated balance sheets, and the corresponding interest income and interest expense on a gross basis in its condensed consolidated statements of operations.

None of the Company's repurchase financing transactions prior to January 1, 2015 qualified as linked transactions and therefore were not accounted for as derivatives. Accordingly, the Company did not record a cumulative effect adjustment to retained earnings as of January 1, 2015 as a result of adopting the new guidance.

Asset-Backed Securities Issued by Securitization Trusts

Asset-backed securities issued by securitization trusts are recorded at principal balances net of unamortized premiums or discounts. The Company recognizes interest expense on an accrual basis and amortizes the related premiums or discounts into interest expense using the effective interest method over the weighted average contractual maturity of these asset-backed securities.

Comprehensive Income

The Company's comprehensive income consists of net income, as presented in the condensed consolidated statements of operations, adjusted for changes in fair value of MBS classified as available for sale securities; changes in the fair value of the debt host contract associated with GSE CRTs; amortization of repurchase agreement interest expense resulting from the de-designation of derivatives previously accounted for as cash flow hedges and foreign currency translation adjustments. Unrealized gains and losses on the Company's MBS and the debt host contract associated with GSE CRTs are reclassified into net income upon their sale or termination.

Accounting for Derivative Financial Instruments

U.S. GAAP provides disclosure requirements for derivatives and hedging activities with the intent to provide users of financial statements with an enhanced understanding of: (i) how and why an entity uses derivative instruments; (ii) how derivative instruments and related hedged items are accounted for; and (iii) how derivative instruments and related hedged items affect an entity’s financial position, financial performance, and cash flows. U.S. GAAP requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about the fair value of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments.

The Company records all derivatives on its condensed consolidated balance sheets at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Derivatives may also be designated as hedges of the foreign currency exposure of a net investment in a foreign operation. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts, such as credit default swaps, that are intended to economically hedge certain of its risks, even though hedge accounting does not apply or the Company elects not to apply hedge accounting under U.S. GAAP.

The Company is a party to hybrid financial instruments that contain embedded derivative instruments. At inception, the Company assesses whether the economic characteristics of the embedded derivative instruments are clearly and closely related to the economic characteristics of the remaining component of the financial instrument (i.e., the debt host contract), whether the financial instrument is remeasured to fair value through earnings and whether a separate instrument with the same terms as the embedded instrument would meet the definition of a derivative instrument. When it is determined that (1) the embedded instrument possesses economic characteristics that are not clearly and closely related to the economic characteristics of the debt host contract, (2) the financial instrument is not remeasured to fair value through earnings and (3) a separate instrument with the same terms would qualify as a derivative instrument, the embedded instrument qualifies as an embedded derivative that is separated from the debt host contract. The embedded derivative is recorded at fair value, and changes in fair value are recorded in realized and unrealized credit derivative income (loss), net in the Company's condensed consolidated statements of operations.

Effective December 31, 2013, the Company voluntarily discontinued hedge accounting for its interest rate swap agreements by de-designating the interest rate swaps as cash flow hedges. No interest rate swaps were terminated in conjunction with this action, and the Company’s risk management and hedging practices were not impacted. However, the Company’s accounting for these transactions changed beginning January 1, 2014. All of the Company’s interest rate swaps had previously been accounted for as cash flow hedges under the applicable guidance. As a result of discontinuing hedge accounting, changes in the fair value of the interest rate swap agreements are recorded in gain (loss) on derivative instruments, net in the Company’s condensed consolidated statements of operations, rather than in accumulated other comprehensive income (loss) (“AOCI”). Also, net interest paid or received under the interest rate swaps, which up through December 31, 2013 was recognized in interest expense, is now recognized in gain (loss) on derivative instruments, net on the Company's condensed consolidated statements of operations. The interest rate swaps continue to be reported as derivative assets or derivative liabilities on the Company’s condensed consolidated balance sheets at their fair value.

As long as the forecasted transactions that were being hedged (i.e., rollovers of the Company’s repurchase agreement borrowings) are still expected to occur, the balance in AOCI from the interest rate swap activity up through December 31, 2013 will remain in AOCI and be recognized in the Company’s condensed consolidated statements of operations as interest expense over the remaining term of the interest rate swaps. Refer to Note 8 - "Derivatives and Hedging Activities" for further information.

The Company evaluates the terms and conditions of its holdings of swaptions, futures contracts, currency forward contracts and to-be-announced ("TBA") securities to determine if an instrument has the characteristics of an investment or should be considered a derivative under U.S. GAAP. Accordingly swaptions, futures contracts, currency forward 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 the condensed consolidated statements of operations. The fair value of these swaptions, futures contracts, currency forward contracts and TBAs is included in derivative assets or derivative liabilities on the condensed consolidated balance sheets.

Reclassifications

Certain prior period reported amounts have been reclassified to be consistent with the current presentation. Such reclassifications had no impact on net income or equity attributable to common stockholders.

Recent Accounting Pronouncements Not Yet Adopted

In February 2015, the FASB issued modifications to existing consolidation guidance for reporting organizations that are required to evaluate whether they should consolidate certain legal entities. The guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2015, and requires either a retrospective or a modified retrospective approach to adoption. Early adoption is permitted. The new guidance is not expected to have a material impact on the Company's condensed consolidated financial statements.

In April 2015, the FASB issued guidance to amend the presentation of debt issuance cost related to a recognized debt liability. Under the new guidance, the debt issuance costs will be presented in the balance sheet as a direct deduction from the carrying amount of the recognized debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected under the new guidance. The standard is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Early adoption is permitted. The guidance should be applied on a retrospective basis. The balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. Upon adoption, an entity is required to comply with the applicable disclosures for a change in an accounting principle. These disclosures include the nature of and reason for the change in accounting principle,

Table of Contents

the transition method, a description of the prior-period information that has been retrospectively adjusted, and the effect of the change on the financial statement line items (i.e., debt issuance cost asset and the debt liability). The new guidance is not expected to have a material impact on the Company's condensed consolidated financial statements.

Note 3 – Variable Interest Entities

The Company's maximum risk of loss in VIEs in which the Company is not the primary beneficiary at September 30, 2015 is presented in the table below.

$ in thousands	Carrying Amount	Company's Maximum Risk of Loss
Non-Agency RMBS	2,624,608	2,624,608
CMBS	3,304,214	3,304,214
Total	5,928,822	5,928,822

Refer to Note 4 - "Mortgage-Backed and Credit Risk Transfer Securities" for additional details regarding these investments.

As discussed in Note 2 - "Summary of Significant Accounting Policies," the Company has determined that it is the primary beneficiary of certain securitization trusts. The following table presents a summary of the assets and liabilities of the Company's consolidated securitization trusts as of September 30, 2015 and December 31, 2014. Intercompany balances have been eliminated for purposes of this presentation.

$ in thousands	September 30, 2015	December 31, 2014
Residential loans, held-for-investment	3,307,249	3,365,003
Accrued interest receivable	20,211	10,562
Deferred costs	4,482	5,032
Total assets	3,331,942	3,380,597
Accrued interest and accrued expenses payable	16,636	8,692
Asset-backed securities issued by securitization trusts	2,859,423	2,929,820
Total liabilities	2,876,059	2,938,512

The Company’s risk with respect to each investment in a securitization trust is limited to its direct ownership in the securitization trust. The residential loans held by the consolidated securitization trusts are held solely to satisfy the liabilities of the securitization trusts, and the investors in the securitization trusts have no recourse to the general credit of the Company for the asset-backed securities issued by the securitization trusts. The assets of a consolidated securitization trust can only be used to satisfy the obligations of that trust. The Company is not contractually required to provide, and has not provided, any additional financial support to the securitization trusts for the period ended September 30, 2015.

During the nine months ended September 30, 2015, the Company invested in and consolidated one new securitization trust. The following table presents the balances of the assets and liabilities of the newly consolidated securitization trust before consolidation into the Company. The current period activity for the securitization trust is reflected in the Company’s condensed consolidated financial statements.

$ in thousands	2015
Residential loans, held-for-investment	372,305
Accrued interest receivable	1,236
Total assets	373,541
Accrued interest and accrued expenses payable	1,236
Asset-backed securities issued by securitization trusts	372,305
Total liabilities	373,541

The Company did not deconsolidate any securitization trusts during the nine months ended September 30, 2015.

Table of Contents

Residential Loans Held by Consolidated Securitization Trusts

Residential loans held by consolidated securitization trusts are carried at unpaid principal balance net of any premiums and discount and allowance for loan losses. The residential loans are secured by a lien on the underlying residential property.

The following table details the carrying value for residential loans held-for-investment at September 30, 2015 and December 31, 2014.

$ in thousands	September 30, 2015	December 31, 2014
Principal balance	3,279,984	3,332,192
Unamortized premium (discount), net	27,794	33,553
Recorded investment	3,307,778	3,365,745
Allowance for loan losses	(529)	(742)
Carrying value	3,307,249	3,365,003

The following table summarizes residential loans held-for-investment at September 30, 2015 by year of origination.

$ in thousands	2014	2013	2012	2011	2010	2009	2008	2007	Total
Portfolio Characteristics:									
Number of Loans	692	2,596	720	86	25	6	14	14	4,153
Current Principal Balance	513,819	1,998,969	625,255	91,620	23,841	2,737	12,327	11,416	3,279,984
Net Weighted Average Coupon Rate	3.46 %	3.45 %	3.24 %	3.38 %	3.74 %	3.69 %	5.47 %	4.67 %	3.42 %
Weighted Average Maturity (years)	28.72	27.81	27.28	25.74	25.22	23.76	22.92	21.84	27.73
Current Performance:									
Current	513,819	1,997,171	625,255	91,620	23,841	2,737	11,697	11,416	3,277,556
30 Days Delinquent	—	560	—	—	—	—	630	—	1,190
60 Days Delinquent	—	—	—	—	—	—	—	—	—
90+ Days Delinquent (1)	—	1,238	—	—	—	—	—	—	1,238
Bankruptcy/Foreclosure	—	—	—	—	—	—	—	—	—
Total	513,819	1,998,969	625,255	91,620	23,841	2,737	12,327	11,416	3,279,984

(1) The Company has stopped recording interest income on these loans as of September 30, 2015.

The following table summarizes the geographic concentrations of residential loans held-for-investment at September 30, 2015 based on principal balance outstanding.

State	Percent
California	53.1 %
New York	7.6 %
Massachusetts	5.9 %
Illinois	3.6 %
Other states (none greater than 3%)	29.8 %
Total	100.0 %

Table of Contents

The following table presents future contractual minimum annual principal payments of residential loans held-for-investment at September 30, 2015.

$ in thousands

Scheduled Principal	September 30, 2015
Within one year	58,964
One to three years	125,167
Three to five years	135,008
Greater than or equal to five years	2,960,845
Total	3,279,984

Allowance for Loan Losses on Residential Loans Held by Consolidated Securitization Trusts

As discussed in Note 2 - "Summary of Significant Accounting Policies," the Company establishes and maintains an allowance for loan losses on residential loans held by consolidated securitization trusts based on the Company's estimate of credit losses.

The following table summarizes the activity in the allowance for loan losses for the nine months ended September 30, 2015 and 2014.

$ in thousands	September 30, 2015	September 30, 2014
Balance at beginning of period	(742)	(884)
Charge-offs, net	—	—
Reduction in (provision for) loan losses	213	52
Balance at end of period	(529)	(832)

Asset-Backed Securities Issued by Securitization Trusts

Asset-backed securities issued by securitization trusts are recorded at principal balance net of unamortized premiums or discounts. Asset-backed securities issued by securitization trusts are issued in various tranches and have a weighted average contractual maturity of 28.37 years and 28.94 years at September 30, 2015 and December 31, 2014, respectively. The investors in the asset-backed securities are not affiliated with the Company and have no recourse to the general credit of the Company.

Table of Contents

The asset-backed securities are collateralized by residential loans held in the securitization trusts as summarized in the following table at September 30, 2015 and December 31, 2014.

	September 30, 2015		December 31, 2014	
$ in thousands	ABS Outstanding	Residential loans Held as Collateral	ABS Outstanding	Residential loans Held as Collateral
Principal balance	2,836,398	3,279,984	2,902,378	3,332,192
Interest-only securities	12,930	—	15,040	—
Unamortized premium	19,763	34,810	23,735	41,928
Unamortized discount	(9,668)	(7,016)	(11,333)	(8,375)
Allowance for loan losses	—	(529)	—	(742)
Carrying value	2,859,423	3,307,249	2,929,820	3,365,003
Range of weighted average interest rates	2.8% - 3.9%		2.8% - 4.0%	
Number of securitization trusts consolidated	11		10	

The following table presents the estimated principal repayment schedule of asset-backed securities issued by securitization trusts at September 30, 2015 based on estimated cash flows of the underlying residential mortgage loans, as adjusted for projected prepayments and losses on such loans. The estimated principal repayments may differ from actual amounts to the extent prepayments and/or loan losses vary.

$ in thousands

Estimated principal repayment	September 30, 2015
Within one year	378,803
One to three years	621,255
Three to five years	464,837
Greater than or equal to five years	1,371,503
Total	2,836,398

Table of Contents

Note 4 – Mortgage-Backed and Credit Risk Transfer Securities

The following tables summarize the Company’s MBS and GSE CRT portfolio by asset type as of September 30, 2015 and December 31, 2014.

September 30, 2015

$ in thousands	Principal Balance	Unamortized Premium (Discount)	Amortized Cost	Unrealized Gain/ (Loss), net	Fair Value	Net Weighted Average Coupon (1)	Period-end Weighted Average Yield (2)	Quarterly Weighted Average Yield (3)
Agency RMBS:								
15 year fixed-rate	1,602,338	77,013	1,679,351	23,031	1,702,382	3.73 %	2.44 %	2.26 %
30 year fixed-rate	3,905,465	259,092	4,164,557	50,389	4,214,946	4.26 %	2.70 %	2.68 %
ARM*	438,335	5,088	443,423	9,408	452,831	2.73 %	2.63 %	2.22 %
Hybrid ARM	3,335,619	65,957	3,401,576	46,037	3,447,613	2.73 %	2.55 %	2.18 %
Total Agency pass-through	9,281,757	407,150	9,688,907	128,865	9,817,772	3.55 %	2.60 %	2.41 %
Agency-CMO(4)	1,928,406	(1,521,514)	406,892	9,770	416,662	2.26 %	3.60 %	2.31 %
Non-Agency RMBS(5)(6)	3,066,848	(526,501)	2,540,347	84,261	2,624,608	3.41 %	3.64 %	4.94 %
GSE CRT(7)	645,000	23,376	668,376	(16,671)	651,705	1.01 %	0.51 %	0.53 %
CMBS(8)	3,745,038	(551,404)	3,193,634	110,580	3,304,214	4.12 %	4.44 %	4.38 %
Total	18,667,049	(2,168,893)	16,498,156	316,805	16,814,961	3.42 %	3.05 %	3.11 %

* Adjustable-rate mortgage ("ARM")

(1) Net weighted average coupon as of September 30, 2015 is presented net of servicing and other fees.

(2) Period-end weighted average yield is based on amortized cost as of September 30, 2015 and incorporates future prepayment and loss assumptions but excludes changes in anticipated interest rates.

(3) Quarterly weighted average portfolio yield for the period was calculated by dividing interest income, including amortization of premiums and discounts, by the Company's average of the amortized cost of the investments. All yields are annualized.

(4) Agency collateralized mortgage obligation ("Agency-CMO") includes Agency MBS IOs which represent 31.6% of the balance based on fair value.

(5) Non-Agency RMBS held by the Company is 51.3% variable rate, 41.5% fixed rate, and 7.2% floating rate based on fair value.

(6) Of the total discount in non-Agency RMBS, $328.4 million is non-accretable.

(7) GSE CRT weighted average coupon and weighted average yield excludes embedded derivative coupon interest recorded as realized and unrealized credit derivative income (loss), net.

(8) CMBS includes interest-only securities and commercial real estate mezzanine loan pass-through certificates, which represent 0.8% and 1.3% of the balance based on fair value, respectively.

Table of Contents

December 31, 2014 (As Restated)

$ in thousands	Principal Balance	Unamortized Premium (Discount)	Amortized Cost	Unrealized Gain/ (Loss), net	Fair Value	Net Weighted Average Coupon (1)	Period-end Weighted Average Yield (2)	Quarterly Weighted Average Yield (3)
Agency RMBS:								
15 year fixed-rate	1,236,297	60,764	1,297,061	30,040	1,327,101	4.05 %	2.60 %	2.66 %
30 year fixed-rate	4,432,301	297,311	4,729,612	60,681	4,790,293	4.29 %	2.97 %	3.05 %
ARM	531,281	9,068	540,349	6,433	546,782	2.83 %	2.27 %	2.29 %
Hybrid ARM	2,901,078	50,757	2,951,835	25,083	2,976,918	2.78 %	2.34 %	2.24 %
Total Agency pass-through	9,100,957	417,900	9,518,857	122,237	9,641,094	3.69 %	2.68 %	2.71 %
Agency-CMO(4)	1,957,296	(1,502,785)	454,511	(3,616)	450,895	2.34 %	4.57 %	3.62 %
Non-Agency RMBS(5)(6)	3,555,249	(583,890)	2,971,359	90,288	3,061,647	3.51 %	4.12 %	4.86 %
GSE CRT(7)	615,000	25,814	640,814	(15,390)	625,424	1.03 %	0.49 %	0.48 %
CMBS(8)	3,277,208	54,893	3,332,101	137,734	3,469,835	4.74 %	4.39 %	4.38 %
Total	18,505,710	(1,588,068)	16,917,642	331,253	17,248,895	3.61 %	3.24 %	3.36 %

(1) Net weighted average coupon as of December 31, 2014 is presented net of servicing and other fees.
(2) Period-end weighted average yield based on amortized cost as of December 31, 2014 incorporates future prepayment and loss assumptions but excludes changes in anticipated interest rates.
(3) Quarterly weighted average portfolio yield for the period was calculated by dividing interest income, including amortization of premiums and discounts, by the Company's average of the amortized cost of the investments. All yields are annualized.
(4) Agency-CMO includes Agency MBS IOs, which represent 29.1% of the balance based on fair value.
(5) Non-Agency RMBS held by the Company is 52.8% variable rate, 40.1% fixed rate, and 7.1% floating rate based on fair value.
(6) Of the total discount in non-Agency RMBS, $405.5 million is non-accretable.
(7) GSE CRT weighted average coupon and weighted average yield excludes embedded derivative coupon interest recorded as realized and unrealized credit derivative income (loss), net.
(8) CMBS includes commercial real estate mezzanine loan pass-through certificates which represent 1.3% of the balance based on fair value.

The following table summarizes the Company's non-Agency RMBS portfolio by asset type as of September 30, 2015 and December 31, 2014.

$ in thousands	September 30, 2015	% of Non-Agency	December 31, 2014	% of Non-Agency
Prime	821,249	31.3 %	969,849	31.7 %
Re-REMIC	790,577	30.1 %	1,000,635	32.7 %
Alt-A	598,198	22.8 %	694,467	22.7 %
Subprime/reperforming	414,584	15.8 %	396,696	12.9 %
Total Non-Agency	2,624,608	100.0 %	3,061,647	100.0 %

Table of Contents

The following table summarizes the credit enhancement provided to the Company's re-securitization of real estate mortgage investment conduit ("Re-REMIC") holdings as of September 30, 2015 and December 31, 2014.

	Percentage of Re-REMIC Holdings at Fair Value			
Re-REMIC Subordination[1]	September 30, 2015		December 31, 2014	
0% - 10%	9.4	%	7.0	%
10% - 20%	5.0	%	4.4	%
20% - 30%	12.4	%	11.9	%
30% - 40%	25.4	%	26.1	%
40% - 50%	32.5	%	31.8	%
50% - 60%	11.7	%	15.2	%
60% - 70%	3.6	%	3.6	%
Total	100.0	%	100.0	%

(1) Subordination refers to the credit enhancement provided to the Re-REMIC tranche held by the Company by any junior Re-REMIC tranche or tranches in a resecuritization. This figure reflects the percentage of the balance of the underlying securities represented by any junior tranche or tranches at the time of resecuritization. Generally, principal losses on the underlying securities in excess of the subordination amount would result in principal losses on the Re-REMIC tranche held by the Company. 19.5% of the Company's Re-REMIC holdings are not senior tranches.

The components of the carrying value of the Company’s MBS and GSE CRT portfolio at September 30, 2015 and December 31, 2014 are presented below.

$ in thousands	September 30, 2015		December 31, 2014 (As Restated)	
Principal balance	18,667,049		18,505,710	
Unamortized premium	522,515		550,071	
Unamortized discount	(2,691,408	)	(2,138,139	)
Gross unrealized gains	404,948		439,513	
Gross unrealized losses	(88,143	)	(108,260	)
Fair value	16,814,961		17,248,895	

The following table summarizes the Company’s MBS and GSE CRT portfolio according to estimated weighted average life classifications as of September 30, 2015 and December 31, 2014.

$ in thousands	September 30, 2015	December 31, 2014
Less than one year	478,122	440,471
Greater than one year and less than five years	7,806,669	7,997,709
Greater than or equal to five years	8,530,170	8,810,715
Total	16,814,961	17,248,895

Table of Contents

The following tables present the estimated fair value and gross unrealized losses of the Company's MBS and GSE CRTs by length of time that such securities have been in a continuous unrealized loss position at September 30, 2015 and December 31, 2014.

September 30, 2015

	Less than 12 Months			12 Months or More			Total		
$ in thousands	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses	Number of Securities
Agency RMBS:									
15 year fixed-rate	565,796	(2,633)	30	81,804	(804)	6	647,600	(3,437)	36
30 year fixed-rate	571,870	(7,717)	20	1,154,766	(26,693)	45	1,726,636	(34,410)	65
ARM	2,277	(1)	1	—	—	—	2,277	(1)	1
Hybrid ARM	484,179	(1,761)	21	—	—	—	484,179	(1,761)	21
Total Agency pass-through	1,624,122	(12,112)	72	1,236,570	(27,497)	51	2,860,692	(39,609)	123
Agency-CMO	124,401	(2,399)	10	13,831	(6,714)	9	138,232	(9,113)	19
Non-Agency RMBS	299,461	(2,074)	20	423,348	(12,583)	31	722,809	(14,657)	51
GSE CRT (1)	230,241	(7,236)	13	121,475	(13,124)	4	351,716	(20,360)	17
CMBS	428,580	(4,133)	38	32,191	(271)	1	460,771	(4,404)	39
Total	2,706,805	(27,954)	153	1,827,415	(60,189)	96	4,534,220	(88,143)	249

(1) Balance includes unrealized losses on both the debt host contract and the embedded derivative.

December 31, 2014 (As Restated)

	Less than 12 Months			12 Months or More			Total		
$ in thousands	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses	Number of Securities
Agency RMBS:									
15 year fixed-rate	10,897	(42)	1	105,644	(1,395)	6	116,541	(1,437)	7
30 year fixed-rate	137,680	(2,662)	5	1,756,894	(40,181)	62	1,894,574	(42,843)	67
ARM	24,074	(9)	1	3,719	(23)	1	27,793	(32)	2
Hybrid ARM	630,775	(1,544)	28	20,361	(197)	2	651,136	(1,741)	30
Total Agency pass-through	803,426	(4,257)	35	1,886,618	(41,796)	71	2,690,044	(46,053)	106
Agency-CMO	36,723	(6,192)	18	265,863	(9,481)	10	302,586	(15,673)	28
Non-Agency RMBS	573,122	(5,799)	34	354,532	(11,990)	21	927,654	(17,789)	55
GSE CRT (1)	306,603	(25,394)	13	—	—	—	306,603	(25,394)	13
CMBS	134,364	(277)	11	227,452	(3,074)	19	361,816	(3,351)	30
Total	1,854,238	(41,919)	111	2,734,465	(66,341)	121	4,588,703	(108,260)	232

(1) Balance includes unrealized losses on both the debt host contract and the embedded derivative.

Gross unrealized losses on the Company’s Agency RMBS were $39.6 million at September 30, 2015. Due to the inherent credit quality of Agency RMBS, the Company determined that at September 30, 2015, any unrealized losses on its Agency RMBS portfolio are temporary.

Gross unrealized losses on the Company's Agency-CMO, non-Agency RMBS, GSE CRT and CMBS were $48.5 million at September 30, 2015. The Company does not consider these unrealized losses to be credit related, but rather due to non-credit

Table of Contents

related factors such as interest rate spreads, prepayment speeds, and market fluctuations. These investment securities are included in the Company's assessment for other-than-temporary impairment on a quarterly basis.

The following table presents the impact of the Company's MBS and GSE CRT debt host contract on its accumulated other comprehensive income (loss) for the three and nine months ended September 30, 2015 and 2014. The table excludes Agency MBS IOs because unrealized gains and losses on Agency MBS IOs are included in earnings on the condensed consolidated statements of operations.

$ in thousands	Three Months ended September 30, 2015	Three Months ended September 30, 2014 (As Restated)	Nine Months ended September 30, 2015	Nine Months ended September 30, 2014 (As Restated)
Accumulated other comprehensive income (loss) from investment securities:				
Unrealized gain (loss) on MBS and GSE CRT at beginning of period	279,803	278,713	351,774	(160,083)
Unrealized gain (loss) on MBS and GSE CRT	41,978	(81,267)	(25,390)	325,045
Reclassification of unrealized (gain) loss on sale of MBS and GSE CRT to gain (loss) on investments, net	1,380	49,169	(3,223)	81,653
Balance at the end of period	323,161	246,615	323,161	246,615

During the three months ended September 30, 2015 and 2014, the Company reclassified $1.4 million of net unrealized losses and $49.2 million of net unrealized losses, respectively, from other comprehensive income into gain (loss) on investments, net as a result of the Company selling certain investments.

During the nine months ended September 30, 2015 and 2014, the Company reclassified $3.2 million of net unrealized gains and $81.7 million of net unrealized losses, respectively, from other comprehensive income into gain (loss) on investments as a result of the Company selling certain investments.

The following table summarizes the Company's gross realized gains and losses during the three and nine months ended September 30, 2015 and 2014.

$ in thousands	Three Months ended September 30, 2015	Three Months ended September 30, 2014 (As Restated)	Nine Months ended September 30, 2015	Nine Months ended September 30, 2014 (As Restated)
Gross realized gain on sale of investments	—	3,038	4,487	13,888
Gross realized loss on sale of investments	(1,404)	(50,990)	(1,288)	(94,324)
Net unrealized gain (loss) on Agency MBS IOs	(1,554)	(412)	6,891	(5,897)
Total gains (loss) on investments, net	(2,958)	(48,364)	10,090	(86,333)

The Company assesses its investment securities for other-than-temporary impairment on a quarterly basis. When the fair value of an investment is less than its amortized cost at the balance sheet date of the reporting period for which impairment is assessed, the impairment is designated as either "temporary" or "other-than-temporary." The Company evaluates each security that has had a fair value less than amortized cost for nine or more consecutive months for other-than-temporary impairment. This analysis includes a determination of estimated future cash flows through an evaluation of the characteristics of the underlying loans and the structural features of the investment. Loan characteristics reviewed include, but are not limited to, delinquency status, loan-to-value ratios, borrower credit scores, occupancy status and geographic concentration. To the extent a security is deemed impaired, the amount by which the amortized cost exceeds the security's market value would be considered other-than-temporary impairment.

The Company did not have other-than-temporary impairments for the three and nine months ended September 30, 2015 and 2014.

Table of Contents

The following table presents components of interest income on the Company's MBS and GSE CRT portfolio for the three and nine months ended September 30, 2015 and 2014. GSE CRT interest income excludes coupon interest associated with embedded derivatives recorded in realized and unrealized credit derivative income (loss), net.

For the three months ended September 30, 2015

$ in thousands	Coupon Interest	Net (Premium Amortization)/Discount Accretion	Interest Income
Agency	93,366	(32,153)	61,213
Non-Agency	26,761	5,407	32,168
GSE CRT	1,663	(782)	881
CMBS	38,350	(3,342)	35,008
Other	(10)	—	(10)
Total	160,130	(30,870)	129,260

For the three months ended September 30, 2014 (As Restated)

$ in thousands	Coupon Interest	Net (Premium Amortization)/Discount Accretion	Interest Income
Agency	98,106	(29,371)	68,735
Non-Agency	32,313	2,971	35,284
GSE CRT	1,489	(792)	697
CMBS	40,164	(5,434)	34,730
Other	(27)	—	(27)
Total	172,045	(32,626)	139,419

For the nine months ended September 30, 2015

$ in thousands	Coupon Interest	Net (Premium Amortization)/Discount Accretion	Interest Income
Agency	282,132	(93,840)	188,292
Non-Agency	85,854	8,224	94,078
GSE CRT	4,849	(2,312)	2,537
CMBS	113,862	(8,193)	105,669
Other	47	—	47
Total	486,744	(96,121)	390,623

For the nine months ended September 30, 2014 (As Restated)

$ in thousands	Coupon Interest	Net (Premium Amortization)/Discount Accretion	Interest Income
Agency	308,683	(80,099)	228,584
Non-Agency	102,785	7,639	110,424
GSE CRT	3,888	(2,242)	1,646
CMBS	120,290	(24,996)	95,294
Other	71	—	71
Total	535,717	(99,698)	436,019

Table of Contents

Note 5 – Commercial Loans Held-for-Investment

The following table summarizes commercial loans held-for-investment as of September 30, 2015 and December 31, 2014 that were purchased or originated by the Company.

September 30, 2015

$ in thousands	Number of loans	Principal Balance	Unamortized (fees)/ costs, net	Carrying value	Unfunded commitment
First mortgage loan	1	19,789	4	19,793	892
Mezzanine loans	7	167,515	(270)	167,245	2,128
Total	8	187,304	(266)	187,038	3,020

December 31, 2014

$ in thousands	Number of loans	Principal Balance	Unamortized (fees)/ costs, net	Carrying value	Unfunded commitment
First mortgage loan	1	19,978	41	20,019	1,623
Subordinate interests:					
Mezzanine loans	4	71,643	(94)	71,549	3,357
Other[(1)]	2	54,188	—	54,188	—
Total	7	145,809	(53)	145,756	4,980

(1) Other subordinate interests include a B-note and a preferred equity investment.

These loans were not impaired, and no allowance for loan loss has been recorded as of September 30, 2015 and December 31, 2014.

Note 6 – Other Investments

The following table summarizes the Company's other investments as of September 30, 2015 and December 31, 2014.

$ in thousands	September 30, 2015	December 31, 2014
FHLBI stock	75,375	62,500
Investments in unconsolidated ventures	37,922	43,998
Total	113,297	106,498

IAS Services LLC, the Company's wholly-owned subsidiary, is required to purchase and hold FHLBI stock as a condition of membership in the Federal Home Loan Bank of Indianapolis ("FHLBI"). The stock is recorded at cost. The Company has invested in unconsolidated ventures that are managed by an affiliate of the Company's Manager. The unconsolidated ventures invest in the Company's target assets. Refer to Note 15 - "Commitments and Contingencies" for additional details regarding the Company's commitments to these unconsolidated ventures.

Table of Contents

Note 7 – Borrowings

The Company has entered into repurchase agreements and secured loans and issued exchangeable senior notes to finance the majority of its portfolio of investments. The following table summarizes certain characteristics of the Company’s borrowings at September 30, 2015 and December 31, 2014.

$ in thousands	September 30, 2015			December 31, 2014		
	Amount Outstanding	Weighted Average Interest Rate	Weighted Average Remaining Maturity (days)	Amount Outstanding	Weighted Average Interest Rate	Weighted Average Remaining Maturity (days)
Repurchase Agreements:						
Agency RMBS	8,637,589	0.43 %	25	9,018,818	0.35 %	18
Non-Agency RMBS	2,362,985	1.56 %	34	2,676,626	1.51 %	36
GSE CRT	497,213	1.74 %	25	468,782	1.55 %	27
CMBS	1,414,344	1.37 %	27	1,458,451	1.32 %	26
Secured Loans	1,675,000	0.42 %	2,979	1,250,000	0.37 %	3,472
Exchangeable Senior Notes	400,000	5.00 %	897	400,000	5.00 %	1,170
Total	14,987,131	0.86 %	380	15,272,677	0.81 %	335

The Company finances its residential loans held-for-investment through asset-backed securities issued by securitization trusts. Refer to Note 3 - "Variable Interest Entities" for a discussion of asset-backed securities issued by securitization trusts.

Repurchase Agreements

Repurchase agreements bear interest at a contractually agreed upon rate and have maturities ranging from one month to twelve months. Repurchase agreements are accounted for as secured borrowings since the Company maintains effective control of the financed assets. Under the repurchase agreements, the respective lender retains the right to mark the underlying collateral to fair value. A reduction in the value of pledged assets would require the Company to provide additional collateral or fund margin calls. The Company intends to maintain a level of liquidity that will enable the Company to meet margin calls. In addition, the repurchase agreements are subject to certain financial covenants. The Company was in compliance with these covenants at September 30, 2015.

Table of Contents

The following tables summarize certain characteristics of the Company’s repurchase agreements at September 30, 2015 and December 31, 2014.
September 30, 2015

$ in thousands Repurchase Agreement Counterparties	Amount Outstanding	Percent of Total Amount Outstanding	Company MBS and GSE CRTs Held as Collateral	
HSBC Securities (USA) Inc	1,309,753	10.1 %	1,348,367	
Royal Bank of Canada	1,180,780	9.1 %	1,415,584	
ING Financial Market LLC	950,618	7.4 %	1,005,589	
Citigroup Global Markets Inc.	865,237	6.7 %	1,066,005	(1)
South Street Securities LLC	842,839	6.5 %	884,109	
Goldman, Sachs & Co.	702,265	5.4 %	847,918	
J.P. Morgan Securities LLC	635,905	4.9 %	737,560	
Industrial and Commercial Bank of China Financial Services LLC	629,954	4.9 %	664,662	
Mitsubishi UFJ Securities (USA), Inc.	628,936	4.9 %	662,515	
Pierpont Securities LLC	610,956	4.7 %	636,871	
Wells Fargo Securities, LLC	566,916	4.4 %	684,380	
Scotia Capital	522,070	4.0 %	543,435	
Morgan Stanley & Co. Incorporated	495,090	3.8 %	551,500	(2)
CRT Capital Group LLC	491,160	3.8 %	517,341	
BNP Paribas Securities Corp.	487,219	3.8 %	550,913	
Banc of America Securities LLC	467,057	3.6 %	545,628	(3)
KGS-Alpha Capital Markets, L.P.	394,015	3.1 %	415,438	
All other counterparties (5)	1,131,361	8.9 %	1,348,841	(4)
Total	12,912,131	100.0 %	14,426,656	

(1) Includes $204.6 million of MBS held as collateral which are eliminated in consolidation.
(2) Includes $41.0 million of MBS held as collateral which are eliminated in consolidation.
(3) Includes $81.6 million of MBS held as collateral which are eliminated in consolidation.
(4) Includes $85.1 million of MBS held as collateral which are eliminated in consolidation.
(5) Represents amounts outstanding with eleven counterparties.

Table of Contents

December 31, 2014

$ in thousands Repurchase Agreement Counterparties	Amount Outstanding	Percent of Total Amount Outstanding		Company MBS and GSE CRTs Held as Collateral	
Credit Suisse Securities (USA) LLC	1,517,530	11.1	%	1,925,973	(1)
HSBC Securities (USA) Inc	1,190,769	8.7	%	1,225,194	
Royal Bank of Canada	1,057,798	7.8	%	1,278,612	
Citigroup Global Markets Inc.	979,247	7.2	%	1,157,265	(2)
South Street Securities LLC	961,938	7.1	%	1,020,054	
Banc of America Securities LLC	791,196	5.9	%	875,984	(3)
ING Financial Market LLC	767,733	5.6	%	820,166	
Mitsubishi UFJ Securities (USA), Inc.	710,058	5.2	%	744,836	
J.P. Morgan Securities LLC	698,856	5.1	%	814,896	
Industrial and Commercial Bank of China Financial Services LLC	682,193	5.0	%	716,989	
Wells Fargo Securities, LLC	627,071	4.6	%	754,706	
Pierpont Securities LLC	601,222	4.4	%	627,534	
Morgan Stanley & Co. Incorporated	589,950	4.3	%	632,002	
BNP Paribas Securities Corp.	559,658	4.1	%	622,749	
Scotia Capital	521,778	3.8	%	542,044	
KGS-Alpha Capital Markets, L.P.	407,920	3.0	%	430,241	
All other counterparties (4)	957,760	7.1	%	1,071,019	
Total	13,622,677	100.0	%	15,260,264	

(1) Includes $276.1 million of MBS held as collateral which are eliminated in consolidation.
(2) Includes $20.3 million of MBS held as collateral which are eliminated in consolidation.
(3) Includes $106.8 million of MBS held as collateral which are eliminated in consolidation.
(4) Represents amounts outstanding with ten counterparties.

Company MBS and GSE CRTs held by counterparties as security for repurchase agreements was $14.4 billion and $15.3 billion at September 30, 2015 and December 31, 2014, respectively. This represents a collateral ratio (Company MBS and GSE CRTs Held as Collateral/Amount Outstanding) of 112% and 112% for September 30, 2015 and December 31, 2014, respectively.

No cash collateral was held by the counterparties at September 30, 2015 and December 31, 2014.

Secured Loans

The Company's wholly-owned subsidiary, IAS Services LLC is a member of the FHLBI. As a member of the FHLBI, IAS Services LLC may borrow funds from the FHLBI in the form of secured advances.

As of September 30, 2015, IAS Services LLC, had $1.675 billion in outstanding secured advances from the FHLBI and is approved for total available uncommitted credit for borrowing of an amount up to $2.5 billion. These secured advances have fixed or floating rates. Floating rates are based on the three-month FHLB swap rate plus a spread. For the nine months ended September 30, 2015, IAS Services LLC had average borrowings of $1.6 billion with a weighted average borrowing rate of 0.39% and a weighted average maturity of 8.16 years.

The ability to borrow from the FHLBI is subject to the Company's continued creditworthiness, pledging of sufficient eligible collateral to secure advances, and compliance with certain agreements with FHLBI. Each advance requires approval by the FHLBI and is secured by collateral in accordance with FHLBI’s credit and collateral guidelines. The FHLBI retains the right to mark the underlying collateral for FHLBI advances to fair value. A reduction in the value of pledged assets would require IAS Services LLC to provide additional collateral.

Table of Contents

As of September 30, 2015, the FHLBI advances were collateralized by CMBS and Agency RMBS with a fair value of $1.5 billion and $519.6 million, respectively. Cash collateral posted by the Company to FHLBI was $5.0 million at September 30, 2015.
As discussed in Note 6 - "Other Investments," IAS Services LLC is required to purchase and hold a certain amount of FHLBI stock, which is based, in part, upon the outstanding principal balance of secured advances from the FHLBI.
Note 8 – Derivatives and Hedging Activities
Credit Derivatives
As discussed in Note 2 - "Summary of Significant Accounting Policies", the Company's GSE CRTs are accounted for as hybrid financial instruments consisting of a debt host contract and an embedded derivative. At September 30, 2015 and December 31, 2014, terms of the GSE CRT embedded derivatives are:

$ in thousand	September 30, 2015	December 31, 2014
Fair value amount	(14,220)	(21,495)
Notional amount	645,000	615,000
Maximum potential amount of future undiscounted payments	645,000	615,000

In 2010, the Company entered into a credit default swap contract ("CDS"). The Company sold protection against losses on a specific pool of non-Agency RMBS in excess of a specified threshold. In exchange, the Company is paid a stated fixed rate fee of 3% of the notional amount of the CDS. As of September 30, 2015, the Company has not made any payments related to the CDS contract.
At September 30, 2015 and December 31, 2014, terms of the CDS are:

$ in thousand	September 30, 2015	December 31, 2014
Fair value amount	1,044	396
Notional amount	25,987	36,684
Maximum potential amount of future undiscounted payments	25,987	36,684
Recourse provisions with third parties	—	—
Collateral held by counterparty	4,073	5,642

Interest Rate Swaps
The Company's repurchase agreements are usually settled on a short-term basis ranging from one to twelve months. At each settlement date, the Company typically refinances each repurchase agreement at the market interest rate at that time. In addition, the Company's secured loans have floating interest rates. As such, the Company is exposed to changing interest rates. The Company’s objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposures to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount.
Effective December 31, 2013, the Company voluntarily discontinued cash flow hedge accounting for its interest rate swaps to gain greater flexibility in managing interest rate exposures. Amounts recorded in AOCI through December 31, 2013 related to cash flow hedges are reclassified to interest expense on repurchase agreements on the condensed consolidated statements of operations as interest is accrued and paid on the related repurchase agreements over the remaining life of the interest rate swap agreements. The Company reclassified $15.7 million (September 30, 2014: $21.2 million) and $51.2 million (September 30, 2014: $64.1 million) as an increase to interest expense for the three and nine months ended September 30, 2015, respectively. During the next 12 months, the Company estimates that $26.9 million will be reclassified as an increase to interest expense, repurchase agreements.
As a result of discontinuing hedge accounting, beginning January 1, 2014, changes in the fair value of the Company’s interest rate swaps are recorded in gain (loss) on derivative instruments, net on the condensed consolidated statements of operations. Monthly net cash settlements under swaps are recorded in gain (loss) on derivative instruments, net on the condensed consolidated statements of operations.

27

Table of Contents

As of September 30, 2015, the Company had the following interest rate swaps outstanding:

$ in thousands Counterparty		Notional	Maturity Date	Fixed Interest Rate in Contract	
Credit Suisse International		500,000	4/15/2016	2.27	%
The Bank of New York Mellon		500,000	4/15/2016	2.24	%
JPMorgan Chase Bank, N.A.		500,000	5/16/2016	2.31	%
Goldman Sachs Bank USA		500,000	5/24/2016	2.34	%
Goldman Sachs Bank USA		250,000	6/15/2016	2.67	%
Wells Fargo Bank, N.A.		250,000	6/15/2016	2.67	%
JPMorgan Chase Bank, N.A.		500,000	6/24/2016	2.51	%
Citibank, N.A.		500,000	10/15/2016	1.93	%
Deutsche Bank AG		150,000	2/5/2018	2.90	%
ING Capital Markets LLC		350,000	2/24/2018	0.95	%
ING Capital Markets LLC		300,000	5/5/2018	0.79	%
UBS AG		500,000	5/24/2018	1.10	%
ING Capital Markets LLC		400,000	6/5/2018	0.87	%
The Royal Bank of Scotland Plc		500,000	9/5/2018	1.04	%
Citibank, N.A. CME Clearing House	(1)	300,000	2/5/2021	2.50	%
The Royal Bank of Scotland Plc CME Clearing House	(1)	300,000	2/5/2021	2.69	%
Wells Fargo Bank, N.A.		200,000	3/15/2021	3.14	%
JPMorgan Chase Bank, N.A. CME Clearing House	(2)	500,000	5/24/2021	2.25	%
Citibank, N.A.		200,000	5/25/2021	2.83	%
HSBC Bank USA, National Association CME Clearing House	(3)	500,000	6/24/2021	2.44	%
HSBC Bank USA, National Association		550,000	2/24/2022	2.45	%
Deutsche Bank AG CME Clearing House		1,000,000	6/9/2022	2.21	%
HSBC Bank USA, National Association		250,000	6/5/2023	1.91	%
The Royal Bank of Scotland Plc		500,000	8/15/2023	1.98	%
Goldman Sachs Bank USA CME Clearing House		600,000	8/24/2023	2.88	%
UBS AG		250,000	11/15/2023	2.23	%
HSBC Bank USA, National Association		500,000	12/15/2023	2.20	%
Morgan Stanley Capital Services, LLC CME Clearing House		100,000	4/2/2025	2.04	%
Total		11,450,000		2.12	%

(1) Forward start date of February 2016
(2) Forward start date of May 2016
(3) Forward start date of June 2016

At September 30, 2015, the Company's counterparties held $174.7 million in cash margin deposits and approximately $215.8 million in Agency RMBS as collateral against its interest rate swaps, CDS and currency forward contracts. Cash margin posted by the Company is classified as due from counterparties, and cash margin posted by counterparties that are restricted in use, if any, is classified as restricted cash. As of September 30, 2015 and December 31, 2014, the Company did not have any restricted cash. The Agency RMBS collateral posted by the Company is included in total mortgage-backed and credit risk transfer securities on the Company's condensed consolidated balance sheets. Cash collateral that is not restricted for use by the Company is included in cash and cash equivalents and the liability to return the collateral is included in collateral held payable on the condensed consolidated balance sheets. Non-cash collateral posted by counterparties to the Company would be recognized if any counterparty defaults or if the Company sold the pledged collateral. As of September 30, 2015 and December 31, 2014, the Company did not recognize any non-cash collateral held as collateral.

Table of Contents

Interest Rate Swaptions

The Company has purchased interest rate swaptions to help mitigate the potential impact of increases or decreases in interest rates on the performance of a portion of the Company’s investment portfolio (referred to as “convexity risk”). The interest rate swaptions provide the Company the option to enter into interest rate swap agreements for a predetermined notional amount, stated term and pay and receive interest rates in the future. The premium paid for interest rate swaptions is reported as an asset in the Company’s condensed consolidated balance sheets. The premium is valued at an amount equal to the fair value of the swaption that would have the effect of closing the position adjusted for nonperformance risk, if any. The difference between the premium and the fair value of the swaption is reported in gain (loss) on derivative instruments, net in the Company’s condensed consolidated statements of operations. If an interest rate swaption expires unexercised, the loss on the interest rate swaption would be equal to the premium paid. If the Company sells or exercises an interest rate swaption, the realized gain or loss on the interest rate swaption would be equal to the difference between the cash or the fair value of the underlying interest rate swap received and the premium paid. The Company had $2.6 million (September 30, 2014: $0) and $10.3 million (September 30, 2014: $23.3 million) of realized loss for the interest rate swaptions that expired unexercised during the three and nine months ended September 30, 2015 and 2014, respectively. For the three and nine months ended September 30, 2015 and 2014, the Company had $2.6 million (September 30, 2014: $2.2 million unrealized loss) and $8.6 million (September 30, 2014: $13.6 million) of unrealized gain, respectively, which represents the change in fair value of the Company's interest rate swaptions that are recognized directly in earnings.

As of September 30, 2015, the Company had the following outstanding interest rate swaptions:

$ in thousands	Option					Underlying Swap			
Interest Rate Swaptions	Expiration	Cost	Fair Value	Average Months to Expiration	Notional Amount	Average Fixed Pay Rate	Average Receive rate		Average Term (Years)
Receiver	< 6 Months	1,485	73	4	300,000	3M LIBOR	1.11	%	10.0
Total Receiver		1,485	73	4	300,000	3M LIBOR	1.11	%	10.0

TBAs, Futures and Currency Forward Contracts

The Company purchases or sells certain TBAs and U.S. Treasury futures contracts to help mitigate the potential impact of changes in interest rates on the performance of the Company's portfolio. Realized and unrealized gains and losses associated with the purchase or sales of the TBAs and U.S. Treasury futures contracts are recognized in gain (loss) on derivative instruments, net in the Company's condensed consolidated statements of operations.

The Company uses currency forward contracts to help mitigate the potential impact of changes in foreign currency exchange rates on the Company's investments denominated in foreign currencies. Realized and unrealized gains and losses associated with the purchases or sales of currency forward contracts are recognized in gain (loss) on derivative instruments, net in the Company's condensed consolidated statements of operations.

Table of Contents

The following table presents information with respect to the Company's derivative instruments:

$ in thousands	Notional Amount as of January 1, 2015	Additions	Settlement, Termination, Expiration or Exercise	Notional Amount as of September 30, 2015	Amount of Realized Gain (Loss), net on Derivative Instruments (excluding net interest paid or received) for the nine months ended September 30, 2015
Interest Rate Swaptions	1,050,000	300,000	(1,050,000)	300,000	(10,328)
Interest Rate Swaps	10,550,000	2,100,000	(1,200,000)	11,450,000	(31,881)
Sale of TBAs	198,000	248,000	(446,000)	—	(2,292)
Futures Contracts	127,400	120,900	(248,300)	—	(943)
Currency Forward Contracts	35,688	98,840	(127,613)	6,915	1,050
Total	11,961,088	2,867,740	(3,071,913)	11,756,915	(44,394)

Tabular Disclosure of the Effect of Derivative Instruments on the Balance Sheet

The table below presents the fair value of the Company’s derivative financial instruments, as well as their classification on the condensed consolidated balance sheets as of September 30, 2015 and December 31, 2014.

$ in thousands

Derivative Assets			Derivative Liabilities		
	As of September 30, 2015	As of December 31, 2014		As of September 30, 2015	As of December 31, 2014
Balance Sheet	Fair Value	Fair Value	Balance Sheet	Fair Value	Fair Value
Interest Rate Swap Asset	—	22,772	Interest Rate Swap Liability	343,847	253,468
CDS Contract	1,044	396	TBAs	—	558
Interest Rate Swaptions	73	322	Currency Forward Contracts	50	—
Futures Contracts	—	89			
Currency Forward Contracts	191	599			

Embedded derivatives associated with GSE CRTs are recorded within mortgage-backed and credit risk transfer securities, at fair value, on the consolidated balance sheets. The fair value of the embedded derivatives associated with the GSE CRTs is a net liability of $14.2 million as of September 30, 2015 (December 31, 2014: $21.5 million net liability).

Tabular Disclosure of the Effect of Derivative Instruments on the Income Statement

The tables below present the effect of the Company’s derivative financial instruments on the condensed consolidated statements of operations for the three and nine months ended September 30, 2015 and 2014.

$ in thousands

Derivative not designated as hedging instrument	Location of unrealized gain (loss) recognized in income on derivative	Three months ended September 30, 2015	Three Months ended September 30, 2014

			(As Restated)
CDS Contract	Realized and unrealized credit derivative income (loss), net	(96)	(78)
GSE CRT Embedded Derivatives	Realized and unrealized credit derivative income (loss), net	(3,848)	(33,644)
Total		(3,944)	(33,722)

30

Table of Contents

$ in thousands

Derivative not designated as hedging instrument	Location of unrealized gain (loss) recognized in income on derivative	Nine months ended September 30, 2015	Nine Months ended September 30, 2014 (As Restated)
CDS Contract	Realized and unrealized credit derivative income (loss), net	648	(185)
GSE CRT Embedded Derivatives	Realized and unrealized credit derivative income (loss), net	7,275	8,307
Total		7,923	8,122

The following table summarizes the effect of interest rate swaps, swaption contracts, TBAs, futures contracts and currency forwards reported in gain (loss) on derivative instruments, net on the condensed consolidated statements of operations for the three and nine months ended September 30, 2015 and 2014:

$ in thousands	Three months ended September 30, 2015			
Derivative not designated as hedging instrument	Realized gain (loss) on settlement, termination, expiration or exercise, net	Contractual interest expense	Unrealized gain (loss), net	Gain (loss) on derivative instruments, net
Interest Rate Swaps	—	(46,785)	(173,817)	(220,602)
Interest Rate Swaptions	(2,590)	—	2,589	(1)
TBAs	—	—	—	—
Futures Contracts	—	—	—	—
Currency Forward Contracts	(489)	—	490	1
Total	(3,079)	(46,785)	(170,738)	(220,602)

$ in thousands	Nine months ended September 30, 2015			
Derivative not designated as hedging instrument	Realized gain (loss) on settlement, termination, expiration or exercise, net	Contractual interest expense	Unrealized gain (loss), net	Gain (loss) on derivative instruments, net
Interest Rate Swaps	(31,881)	(138,404)	(113,151)	(283,436)
Interest Rate Swaptions	(10,328)	—	8,594	(1,734)
TBAs	(2,292)	—	558	(1,734)
Futures Contracts	(943)	—	(90)	(1,033)
Currency Forward Contracts	1,050	—	(457)	593
Total	(44,394)	(138,404)	(104,546)	(287,344)

$ in thousands	Three months ended September 30, 2014			
Derivative not designated as hedging instrument	Realized gain (loss) on settlement, termination, expiration or exercise, net	Contractual interest expense	Unrealized gain (loss), net	Gain (loss) on derivative instruments, net

Interest Rate Swaps	1,348	(50,446)	47,709	(1,389)
Interest Rate Swaptions	—	—	(2,185)	(2,185)
TBAs	(2,943)	—	368	(2,575)
Futures Contracts	249	—	786	1,035
Currency Forward Contracts	330	—	1,080	1,410
Total	(1,016)	(50,446)	47,758	(3,704)

31

Table of Contents

$ in thousands	Nine months ended September 30, 2014			
Derivative not designated as hedging instrument	Realized gain (loss) on settlement, termination, expiration or exercise, net	Contractual interest expense	Unrealized gain (loss), net	Gain (loss) on derivative instruments, net
Interest Rate Swaps	1,348	(154,092)	(146,116)	(298,860)
Interest Rate Swaptions	(23,275)	—	13,596	(9,679)
TBAs	(4,343)	—	(867)	(5,210)
Futures Contracts	(8,937)	—	(1,556)	(10,493)
Currency Forward Contracts	330	—	1,080	1,410
Total	(34,877)	(154,092)	(133,863)	(322,832)

Credit-risk-related Contingent Features

The Company has agreements with each of its bilateral derivative counterparties. Some of those agreements contain a provision whereby if the Company defaults on any of its indebtedness, including default whereby repayment of the indebtedness has not been accelerated by the lender, the Company could be declared in default on its derivative obligations.

At September 30, 2015, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for non-performance risk related to these agreements, was $183.4 million. The Company has minimum collateral posting thresholds with certain of its derivative counterparties and has posted collateral of $215.8 million of Agency RMBS and $174.7 million of cash as of September 30, 2015. If the Company had breached any of these provisions at September 30, 2015, it could have been required to settle its obligations under the agreements at their termination value.

In addition, as of September 30, 2015, the Company has an agreement with a central clearing counterparty. The fair value of such derivatives in a net liability position, which includes accrued interest but excludes any adjustment for non-performance risk related to this agreement, was $160.5 million.

The Company was in compliance with all of the financial provisions of these counterparty agreements as of September 30, 2015.

Note 9 – Offsetting Assets and Liabilities

Certain of the Company's repurchase agreements and derivative transactions are governed by underlying agreements that generally provide for a right of setoff under master netting arrangements (or similar agreements) in the event of default or in the event of bankruptcy of either party to the transactions. Assets and liabilities subject to such arrangements are presented on a gross basis in the condensed consolidated balance sheets.

The following tables present information about the assets and liabilities that are subject to master netting agreements (or similar agreements) and can potentially be offset on the Company’s condensed consolidated balance sheets at September 30, 2015 and December 31, 2014.

Offsetting of Derivative Assets
As of September 30, 2015

				Gross Amounts Not Offset in the Condensed Consolidated Balance Sheets		
$ in thousands Description	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Condensed Consolidated	Net Amounts of Assets presented in	Financial Instruments (1)	Collateral Received (4)	Net Amount

		Balance Sheets	the Condensed Consolidated Balance Sheets			
Derivatives	1,308	—	1,308	(1,308)	—	—
Total	1,308	—	1,308	(1,308)	—	—

Table of Contents

Offsetting of Derivative Liabilities, Repurchase Agreements and Secured Loans
As of September 30, 2015

$ in thousands Description	Gross Amounts of Recognized Liabilities	Gross Amounts Offset in the Condensed Consolidated Balance Sheets	Net Amounts of Liabilities presented in the Condensed Consolidated Balance Sheets	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheets: Financial Instruments (2)(3)(5)	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheets: Collateral Posted (2)(4)(5)	Net Amount
Derivatives	343,897	—	343,897	(180,965)	(160,482)	2,450
Repurchase Agreements	12,912,131	—	12,912,131	(12,912,131)	—	—
Secured Loans	1,675,000	—	1,675,000	(1,675,000)	—	—
Total	14,931,028	—	14,931,028	(14,768,096)	(160,482)	2,450

Offsetting of Derivative Assets
As of December 31, 2014

$ in thousands Description	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Condensed Consolidated Balance Sheets	Net Amounts of Assets presented in the Condensed Consolidated Balance Sheets	Gross Amounts Not Offset in the Consolidated Balance Sheets: Financial Instruments (1)	Gross Amounts Not Offset in the Consolidated Balance Sheets: Collateral Received (4)	Net Amount
Derivatives	24,178	—	24,178	(5,277)	(18,901)	—
Total	24,178	—	24,178	(5,277)	(18,901)	—

Offsetting of Derivative Liabilities and Repurchase Agreements
As of December 31, 2014

$ in thousands Description	Gross Amounts of Recognized Liabilities	Gross Amounts Offset in the Condensed Consolidated Balance Sheets	Net Amounts of Liabilities presented in the Condensed Consolidated Balance Sheets	Gross Amounts Not Offset in the Consolidated Balance Sheets: Financial Instruments (2)(3)	Gross Amounts Not Offset in the Consolidated Balance Sheets: Collateral Posted (2)(4)	Net Amount
Derivatives	254,026	—	254,026	(235,908)	(18,118)	—
Repurchase Agreements	13,622,677	—	13,622,677	(13,622,677)	—	—

Secured Loans	1,250,000	—	1,250,000	(1,250,000)	—	—
Total	15,126,703	—	15,126,703	(15,108,585)	(18,118)	—

(1) Amounts represent derivatives in an asset position which could potentially be offset against derivatives in a liability position at September 30, 2015 and December 31, 2014, subject to a netting arrangement.

(2) Amounts represent collateral pledged that is available to be offset against liability balances associated with repurchase agreements, secured loans and derivatives.

(3) The fair value of securities pledged against the Company's borrowing under repurchase agreements was $14.4 billion and $15.3 billion at September 30, 2015 and December 31, 2014, respectively, including securities held as collateral that are eliminated in consolidation of $412.3 million and $403.2 million, respectively at September 30, 2015 and December 31, 2014.

(4) Cash collateral received on the Company's derivatives was $0 and $14.9 million at September 30, 2015 and December 31, 2014, respectively. Non-cash collateral received on the Company's derivatives was $0 and $10.8 million

Table of Contents

at September 30, 2015 and December 31, 2014. Cash collateral posted by the Company on its derivatives was $174.7 million and $57.6 million at September 30, 2015 and December 31, 2014, respectively.

(5) The fair value of securities pledged against IAS Services LLC's borrowing under secured loans was $2.0 billion and $1.5 billion at September 30, 2015 and December 31, 2014, respectively. Cash collateral posted by the Company to FHLBI was $5.0 million at September 30, 2015. No cash collateral was posted by the Company at December 31, 2014.

Note 10 – Fair Value of Financial Instruments

A three-level valuation hierarchy exists for disclosure of fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect the Company’s market assumptions. The three levels are defined as follows:

- Level 1 Inputs – Quoted prices for identical instruments in active markets.
- Level 2 Inputs – Quoted prices for similar instruments 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 3 Inputs – Instruments with primarily unobservable value drivers.

Table of Contents

The following tables present the Company's assets and liabilities measured at fair value on a recurring basis.

	September 30, 2015			
	Fair Value Measurements Using:			
$ in thousands	Level 1	Level 2	Level 3	Total at Fair Value
Assets:				
Mortgage-backed and credit risk transfer securities[1] [2]	—	16,829,181	(14,220)	16,814,961
Derivative assets	—	1,308	—	1,308
Total assets	—	16,830,489	(14,220)	16,816,269
Liabilities:				
Derivative liabilities	—	343,897	—	343,897
Total liabilities	—	343,897	—	343,897

	December 31, 2014 (As Restated)			
	Fair Value Measurements Using:			
$ in thousands	Level 1	Level 2	Level 3	Total at Fair Value
Assets:				
Mortgage-backed and credit risk transfer securities[1] [2]	—	17,270,390	(21,495)	17,248,895
Derivative assets	89	23,693	396	24,178
Total assets	89	17,294,083	(21,099)	17,273,073
Liabilities:				
Derivative liabilities	—	254,026	—	254,026
Total liabilities	—	254,026	—	254,026

(1) For more detail about the fair value of the Company's MBS and GSE CRTs, refer to Note 4 - "Mortgage-Backed and Credit Risk Transfer Securities."

(2) As discussed in Note 2 "Summary of Significant Accounting Policies", the Company's GSE CRTs are accounted for as hybrid financial instruments with an embedded derivative. The hybrid instruments consist of debt host contracts classified as Level 2 and embedded derivatives classified as Level 3. As of September 30, 2015, the net embedded derivative liability position of $14.2 million includes $3.7 million of embedded derivatives in an asset position and $17.9 million of embedded derivatives in a liability position. As of December 31, 2014, the net embedded derivative liability position of $21.5 million includes $3.1 million of embedded derivatives in an asset position and $24.6 million of embedded derivatives in a liability position.

The following table shows a reconciliation of the beginning and ending fair value measurements of the Company's GSE CRT embedded derivatives, which the Company has valued utilizing Level 3 inputs:

$ in thousands	September 30, 2015	December 31, 2014
Beginning balance	(21,495)	—
Sales and settlements	2,184	—
Total net gains / (losses) included in net income:		
Realized gains/(losses), net	(2,184)	—
Unrealized gains/(losses), net	7,275	(21,495)
Ending balance	(14,220)	(21,495)

Table of Contents

The following table summarizes significant unobservable inputs used in the fair value measurement of the Company's GSE CRT embedded derivative:

$ in thousands	Fair Value at September 30, 2015	Valuation Technique	Unobservable Input	Range	Weighted Average
GSE CRT Embedded Derivatives	(14,220)	Market Comparables	Prepayment Rate	4.95% - 9.85%	6.17%
		Vendor Pricing	Default Rate	0.11% - 0.36%	0.17%

$ in thousands	Fair Value at December 31, 2014	Valuation Technique	Unobservable Input	Range	Weighted Average
GSE CRT Embedded Derivatives	(21,495)	Market Comparables	Prepayment Rate	4.46% - 8.98%	5.29%
		Vendor Pricing	Default Rate	0.12% - 0.37%	0.18%

These significant unobservable inputs change according to market conditions and security performance. Prepayment rate and default rate are used to estimate the maturity of GSE CRTs in order to identify GSE corporate debt with a similar maturity. Therefore, changes in prepayment rate and default rate do not have an explicit directional impact on the fair value measurement.

The following table shows a reconciliation of the beginning and ending Level 3 fair value measurements of the Company's credit default swap ("CDS") contract:

$ in thousands	September 30, 2015	December 31, 2014
Beginning balance	396	654
Unrealized gains/(losses), net	648	(258)
Transfer out of level 3 [1]	(1,044)	—
Ending balance	—	396

(1) During the three months ended September 30, 2015, the CDS contract was transferred from Level 3 to Level 2. As of September 30, 2015, the Company accepted an offer to terminate the CDS in October 2015 in exchange for a payment to the Company of $1.0 million. As of September 30, 2015, the fair value of the CDS was the offer amount.

The following table summarizes significant unobservable inputs used in the fair value measurement of the Company's CDS contract as of December 31, 2014:

$ in thousands	Fair Value at December 31, 2014	Valuation Technique	Unobservable Input	Range	Weighted Average
CDS Contract	396	Discounted cash flow	Swap Rate		2.39%
			Discount Rate		0.76%
			Credit Spread		0.24%
			Constant Prepayment Rate	1.0% - 20.0%	5.46%
			Constant Default Rate	0.6% - 100.0%	4.15%
			Loss Severity	1.1% - 62.3%	39.35%

These significant unobservable inputs change according to market conditions and security performance expectations. Significant increases (decreases) in swap rate, discount rate, credit spread, constant prepayment rate, constant default rate or loss severity in isolation would result in a lower (higher) fair value measurement. Generally, a change in the assumption used for the constant default rate would likely be accompanied by a directionally similar change in the assumptions used for swap rate, credit spread and loss severity and a directionally opposite change in the assumption used for discount rate and constant prepayment rate.

Table of Contents

The following table presents the carrying value and estimated fair value of the Company's financial instruments that are not carried at fair value on the condensed consolidated balance sheets, at September 30, 2015 and December 31, 2014:

	September 30, 2015		December 31, 2014	
$ in thousands	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial Assets				
Residential loans, held-for-investment	3,307,249	3,303,889	3,365,003	3,399,964
Commercial loans, held-for-investment	187,038	188,723	145,756	147,497
Other investments	113,297	113,297	106,498	106,498
Total	3,607,584	3,605,909	3,617,257	3,653,959
Financial Liabilities				
Repurchase agreements	12,912,131	12,919,190	13,622,677	13,630,571
Secured loans	1,675,000	1,675,000	1,250,000	1,250,000
Asset-backed securities issued by securitization trusts	2,859,423	2,843,143	2,929,820	2,930,422
Exchangeable senior notes	400,000	378,000	400,000	379,500
Total	17,846,554	17,815,333	18,202,497	18,190,493

The following describes the Company’s methods for estimating the fair value for financial instruments.

- The fair value of residential loans held-for-investment is a Level 3 fair value measurement which is based on an expected present value technique. This method discounts future estimated cash flows using rates the Company determined best reflect current market interest rates that would be offered for loans with similar characteristics and credit quality.
- The fair value of commercial loans held-for-investment is a Level 3 fair value measurement. New commercial loans are carried at their unpaid principal balance until the end of the calendar year in which they were originated or purchased unless market factors indicate cost may not be a reliable indicator of fair value. Subsequent to the year of origination, commercial loan investments are valued on at least an annual basis by an independent third party valuation agent using a discounted cash flow technique.
- The fair value of FHLBI stock, included in "Other investments," is a Level 3 fair value measurement. FHLBI stock may only be sold back to the FHLBI at its discretion at cost. As a result, the cost of the FHLBI stock approximates its fair value.
- The fair value of investments in unconsolidated ventures, included in "Other investments," is a Level 3 fair value measurement. The fair value measurement is based on the net asset value per share of the Company's investments.
- The fair value of repurchase agreements is a Level 3 fair value measurement based on an expected present value technique. This method discounts future estimated cash flows using rates the Company determined best reflect current market interest rates that would be offered for repurchase agreements with similar characteristics and credit quality.
- The fair value of asset-backed securities issued by securitization trusts is a Level 3 fair value measurement based on valuations obtained from a third party pricing service. There is not an active trading market for many of the underlying asset-backed securities. Accordingly, these securities are valued by the third party pricing service by discounting future estimated cash flows using rates that best reflect current market interest rates that would be offered for securities with similar characteristics and credit quality.
- The fair value of secured loans is a Level 3 fair value measurement. The secured loans have floating rates based on an index plus a spread. Accordingly, the interest rates on these secured loans are at market, and thus the carrying amount approximates fair value.
- The fair value of the exchangeable senior notes issued is a Level 2 fair value measurement based on valuation obtained from a third-party pricing service.

Note 11 – Related Party Transactions
The Company is externally managed and advised by Invesco Advisers, Inc., a wholly-owned subsidiary of Invesco Ltd. Under the terms of the management agreement, the Manager and its affiliates provide the Company with its management team, including its officers, along with appropriate support personnel. Each of the Company's officers is an employee of the Manager or one of its affiliates. The Company does not have any employees. The Manager is not obligated to dedicate any of its employees exclusively to the Company, nor are the Manager or its employees obligated to dedicate any specific portion of its or their time to the Company's business. The Manager is at all times subject to the supervision and oversight of the Company's Board of Directors and has only such functions and authority as the Company delegates to it.
The Company has invested $76.3 million and $149.3 million as of September 30, 2015 and December 31, 2014, respectively, in money market or mutual funds managed by affiliates of the Company's Manager. The investments are reported as cash and cash equivalents on the Company's condensed consolidated balance sheets.
Management Fee
The Company pays its Manager a management fee equal to 1.50% of the Company's stockholders' equity per annum. The fee is calculated and payable quarterly in arrears. For purposes of calculating the management fee, stockholders' equity is equal to the sum of the net proceeds from all issuances of equity securities since inception (allocated on a pro rata daily basis for such issuances during the fiscal quarter of any such issuance), plus retained earnings at the end of the most recently completed calendar quarter (without taking into account any non-cash equity compensation expense incurred in current or prior periods), less any amount paid to repurchase common stock since inception. Stockholder's equity shall exclude (i) any unrealized gains, losses or other items that do not affect realized net income (regardless of whether such items are included in other comprehensive income or loss, or in net income); (ii) cumulative net realized losses that are not attributable to permanently impaired investments and that relate to the investments for which market movement is accounted for in other comprehensive income; provided, however, that such adjustment shall not exceed cumulative unrealized net gains in other comprehensive income; (iii) one-time events pursuant to changes in U.S. GAAP; and (iv) certain non-cash items after discussions between the Manager and the Company's independent directors and approval by a majority of the Company's independent directors.
The Manager has agreed to reduce (but not below zero) the management fee payable by the Company under the management agreement with respect to any equity investment managed by the Manager. The fee reduction occurs at the equity investment level.
For the three and nine months ended September 30, 2015, the Company incurred management fees of $10.1 million (September 30, 2014: $9.2 million) and $28.8 million (September 30, 2014: $27.9 million), of which $9.9 million (September 30, 2014: $9.2 million) was accrued but has not been paid.
Expense Reimbursement
The Company is required to reimburse its Manager for Company operating expenses incurred on its behalf by the Manager, including directors and officers insurance, accounting services, auditing and tax services, filing fees, and miscellaneous general and administrative costs. The Company's reimbursement obligation is not subject to any dollar limitation.
The following table summarizes the costs originally paid by the Manager, incurred on behalf of the Company for the three and nine months ended September 30, 2015 and 2014.

	Three Months Ended September 30,		Nine Months Ended September 30,	
$ in thousands	2015	2014	2015	2014
Incurred costs, prepaid or expensed	2,668	1,274	5,017	4,373
Incurred costs, charged against equity as a cost of raising capital	22	—	22	—
Total incurred costs, originally paid by the Manager	2,690	1,274	5,039	4,373

Termination Fee
A termination fee is due to the Manager upon termination of the management agreement by the Company. The termination fee is equal to three times the sum of the average annual management fee earned by the Manager during

the 24-month period before termination, calculated as of the end of the most recently completed fiscal quarter.

Note 12 – Stockholders' Equity
Securities Convertible into Shares of Common Stock
The non-controlling interest holder of the Operating Partnership units, a wholly-owned Invesco subsidiary, has the right to cause the Operating Partnership to redeem their operating partnership ("OP Units") for cash equal to the market value of an equivalent number of shares of common stock, or at the Company's option, the Company may purchase their OP Units by issuing one share of common stock for each OP Unit redeemed. The Company has also adopted an equity incentive plan which allows the Company to grant securities convertible into the Company's common stock to its non-executive directors and employees of the Company's Manager and its affiliates.
Common Stock
The Company has a dividend reinvestment and stock purchase plan (the "DRSPP") that allows participating stockholders to purchase shares of common stock directly from the Company. DRSPP participants may also automatically reinvest all or a portion of their dividends in exchange for additional shares of common stock.
During the nine months ended September 30, 2015, the Company issued 10,317 shares of common stock at an average price of $15.29 under the DRSPP. The Company received total proceeds of approximately $158,000.
Preferred Stock
Holders of the Company's Series A Preferred Stock are entitled to receive dividends at an annual rate of 7.75% of the liquidation preference of $25.00 per share or $1.9375 per share per annum. The dividends are cumulative and payable quarterly in arrears.
Holders of the Company's Series B Preferred Stock are entitled to receive dividends at an annual rate of 7.75% of the liquidation preference of $25.00 per share or $1.9375 per share per annum until December 27, 2024. After December 27, 2024, holders are entitled to receive dividends at a floating rate equal to three-month LIBOR plus a spread of 5.18% of the $25.00 liquidation preference per annum. Dividends are cumulative and payable quarterly in arrears.
The Company may elect to redeem shares of preferred stock at its option after July 26, 2017 (with respect to the Series A Preferred Stock) and after December 27, 2024 (with respect to the Series B Preferred Stock) for $25.00 per share, plus any accumulated and unpaid dividends through the date of the redemption. These shares are not redeemable, convertible into or exchangeable for any other property or any other securities of the Company prior to those times, except under circumstances intended to preserve the Company's qualification as a REIT or upon the occurrence of a change in control.
Share Repurchase Program
During the three and nine months ended September 30, 2015, the Company repurchased 3,695,368 shares of its common stock at an average repurchase price of $13.53 per share for a net cost of $50.0 million, including acquisition expenses. As of September 30, 2015, the Company had authority to purchase 11,146,416 additional shares of its common stock under its share repurchase program. The share repurchase program has no stated expiration date.
Share-Based Compensation
The Company has currently reserved 1,000,000 shares of common stock for issuance to its non-executive directors and officers and employees of the Manger and its affiliates under the terms of its 2009 Equity Incentive Plan (the "Incentive Plan"). Unless terminated earlier, the Incentive Plan will terminate in 2019, but will continue to govern the unexpired awards.
The Company recognized compensation expense of approximately $85,000 (September 30, 2014: $60,000) and approximately $255,000 (September 30, 2014: $172,000) related to the Company's non-executive directors for the three and nine months ended September 30, 2015 and 2014, respectively. During the three months ended September 30, 2015 and 2014, the Company issued 6,152 shares and 3,532 shares of stock, respectively, pursuant to the Incentive Plan to the Company's non-executive directors. During the nine months ended September 30, 2015 and 2014, the Company issued 16,896 shares and 9,356 shares of stock, respectively, pursuant to the Incentive Plan to the Company's non-executive directors. The fair market value of the shares granted was determined by the closing stock market price on the date of the grant.
The Company recognized compensation expense of approximately $31,000 (September 30, 2014: $62,000) and $168,000 (September 30, 2014: $223,000) for the three and nine months ended September 30, 2015, respectively,

related to awards to employees of the Manager and its affiliates which is reimbursed by the Manager under the management agreement. During March 2015, the Company issued 11,547 shares of common stock (net of tax withholding) to employees of the Manager and its affiliates in exchange for 17,783 restricted stock units that vested under the Incentive Plan. In addition, during the nine months

Table of Contents

ended September 30, 2015, the Company awarded 17,652 restricted stock units to employees of the Manager and its affiliates and employees forfeited 4,600 restricted stock units.

Dividends

On September 15, 2015, the Company declared the following dividends:

- a dividend of $0.40 per share of common stock to be paid on October 27, 2015 to stockholders of record as of the close of business on September 28, 2015;
- a dividend of $0.4844 per share of Series A Preferred Stock to be paid on October 26, 2015 to stockholders of record as of the close of business on October 1, 2015; and
- a dividend of $0.4844 per share of Series B Preferred Stock to be paid on December 28, 2015 to stockholders of record as of the close of business on December 5, 2015.

Note 13 – Earnings per Common Share

Earnings per share for the three and nine months ended September 30, 2015 and 2014 is computed as follows:

$ and share amounts in thousands	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014 (As Restated)	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2014 (As Restated)
Numerator (Income)				
Basic Earnings				
Net income (loss) available to common stockholders	(144,550)	(2,836)	(22,065)	(135,368)
Effect of dilutive securities:				
Income allocated to exchangeable senior notes	—	—	—	—
Income (loss) allocated to non-controlling interest	(1,629)	6	(80)	(1,456)
Dilutive net income (loss) available to stockholders	(146,179)	(2,830)	(22,145)	(136,824)
Denominator (Weighted Average Shares)				
Basic Earnings:				
Shares available to common stockholders	122,047	123,098	122,763	123,105
Effect of dilutive securities:				
Restricted stock awards	—	—	—	—
OP units	1,425	1,425	1,425	1,425
Exchangeable senior notes	—	—	—	—
Dilutive Shares	123,472	124,523	124,188	124,530

The following potential common shares were excluded from diluted earnings per common share for the three and nine months ended September 30, 2015 as the effect would be anti-dilutive: 16,835,720 for the exchangeable senior notes, respectively, and 40,810 and 41,404 for restricted stock awards, respectively. The following potential common shares were excluded from diluted earnings per common share for the three and nine months ended September 30, 2014 as the effect would be anti-dilutive: 16,835,720 for the exchangeable senior notes, respectively, and 45,540 and 44,046 for restricted stock awards, respectively.

Note 14 – Non-controlling Interest - Operating Partnership

Non-controlling interest represents the aggregate Operating Partnership Units in the Company's Operating Partnership held by a wholly-owned Invesco subsidiary. Income allocated to the non-controlling interest is based on the Unit Holders' ownership percentage of the Operating Partnership. The ownership percentage is determined by dividing the number of OP Units held by the Unit Holders by the total number of dilutive shares of common stock. The issuance of common stock ("Share" or "Shares") or OP Units changes the percentage ownership of both the Unit Holders and the holders of common stock. Since an OP unit is generally redeemable for cash or Shares at the option of the Company, it is deemed to be a Share equivalent. Therefore, such transactions are treated as capital transactions and result in an allocation between stockholders' equity and non-controlling interest in the accompanying condensed consolidated balance sheets. As of September 30, 2015 and December 31, 2014, non-controlling interest related to the outstanding 1,425,000 OP Units represented a 1.2% interest and 1.1% interest in the Operating Partnership, respectively.

The following table presents the net income (loss) allocated and distributions paid to the Operating Partnership non-controlling interest for the three and nine months ended September 30, 2015 and 2014.

	Three Months Ended September 30,		Nine Months Ended September 30,	
$ in thousands	2015	2014 (As Restated)	2015	2014 (As Restated)
Net income (loss) allocated	(1,629)	6	(80)	(1,456)
Distributions paid	570	713	1,853	2,138

As of September 30, 2015 and December 31, 2014, distributions payable to the non-controlling interest were approximately $570,000 and $641,000, respectively.

Note 15 – Commitments and Contingencies

Commitments and Contingencies

Commitments and contingencies may arise in the ordinary course of business.

Off Balance Sheet Commitments

As discussed in Note 6 - "Other Investments", the Company has invested in unconsolidated ventures that are sponsored by an affiliate of the Company's Manager. The unconsolidated ventures are structured as partnerships, and the Company invests in the partnerships as a limited partner. The entities are structured such that capital commitments are to be drawn down over the life of the partnership as investment opportunities are identified. As of September 30, 2015 and December 31, 2014, the Company's undrawn capital and purchase commitments were $25.4 million and $31.0 million, respectively.

As discussed in Note 5 - "Commercial Loans Held-for-Investment", the Company purchases and originates commercial loans. As of September 30, 2015 and December 31, 2014, the Company has unfunded commitments on commercial loans held-for-investment of $3.0 million and $5.0 million, respectively.

The Company has entered into agreements with financial institutions to guarantee certain obligations of its subsidiaries. The Company would be required to perform under these guarantees in the event of certain defaults. The Company has not had prior claims or losses pursuant to these contracts and expects the risk of loss to be remote.

Note 16 – Subsequent Events

The Company has reviewed subsequent events occurring through the date that these condensed consolidated financial statements were issued, and determined that no subsequent events occurred that would require accrual or additional disclosure.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

In this quarterly report on Form 10-Q, or this “Report,” we refer to Invesco Mortgage Capital Inc. and its consolidated subsidiaries as “we,” “us,” “our Company,” or “our,” unless we specifically state otherwise or the context indicates otherwise. We refer to our external manager, Invesco Advisers, Inc., as our “Manager,” and we refer to the indirect parent company of our Manager, Invesco Ltd. together with its consolidated subsidiaries (which does not include us), as “Invesco.”
The following discussion should be read in conjunction with our condensed consolidated financial statements and the accompanying notes to our condensed consolidated financial statements, which are included in Item 1 of this Report, as well as the information contained in our most recent Form 10-K/A filed with the Securities and Exchange Commission (the “SEC”).

Forward-Looking Statements

We make forward-looking statements in this Report and other filings we make with the SEC within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and such statements are intended to be covered by the safe harbor provided by the same. Forward-looking statements are subject to substantial risks and uncertainties, many of which are difficult to predict and are generally beyond our control. These forward-looking statements include information about possible or assumed future results of our business, investment strategies, financial condition, liquidity, results of operations, plans and objectives. When we use the words “believe,” “expect,” “anticipate,” “estimate,” “plan,” “continue,” “intend,” “should,” “ similar expressions and future or conditional verbs such as “will,” “may,” “could,” “should,” and “would,” and any other statement that necessarily depends on future events, we intend to identify forward-looking statements. Factors that could cause actual results to differ from those expressed in our forward-looking statements include, but are not limited to:

- our business and investment strategy;
- our investment portfolio;
- our projected operating results;
- general volatility of financial markets and effects of governmental responses, including actions and initiatives of the U.S. governmental agencies and changes to U.S. government policies, including the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), mortgage loan modification programs, actions and initiatives of foreign governmental agencies and central banks, and the completion of the Federal Reserve long-term asset purchases (quantitative easing or "QE"), and our ability to respond to and comply with such actions, initiatives and changes;
- the availability of financing sources, including our ability to obtain additional financing arrangements and the terms of such arrangements;
- financing and advance rates for our target assets;
- changes to our expected leverage;
- our expected investments;
- our expected book value per share of common stock;
- interest rate mismatches between our target assets and our borrowings used to fund such investments;
- the adequacy of our cash flow from operations and borrowings to meet our short-term liquidity needs;
- our ability to maintain sufficient liquidity to meet any margin calls;
- changes in the credit rating of the U.S. government;
- changes in interest rates and interest rate spreads and the market value of our target assets;
- changes in prepayment rates on our target assets;
- the impact of any deficiencies in foreclosure practices of third parties and related uncertainty in the timing of collateral disposition;
- our reliance on third parties in connection with services related to our target assets;
- effects of hedging instruments on our target assets;

- rates of default or decreased recovery rates on our target assets;

Table of Contents

- modifications to whole loans or loans underlying securities;
- the degree to which our hedging strategies may or may not protect us from interest rate volatility;
- the degree to which derivative contracts expose us to contingent liabilities;
- counterparty defaults;
- compliance with financial covenants in our financing arrangements;
- changes in governmental regulations, tax law and rates, and similar matters and our ability to respond to such changes;
- our ability to maintain our qualification as a real estate investment trust for U.S. federal income tax purposes;
- our ability to maintain our exception from the definition of "investment company" under the Investment Company Act of 1940, as amended (the "1940 Act");
- availability of investment opportunities in mortgage-related, real estate-related and other securities;
- availability of U.S. Government Agency guarantees with regard to payments of principal and interest on securities;
- the market price and trading volume of our capital stock;
- availability of qualified personnel of our Manager;
- the relationship with our Manager;
- estimates relating to taxable income and our ability to continue to make distributions to our stockholders in the future;
- estimates relating to fair value of our target assets and loan loss reserves;
- our understanding of our competition;
- changes to generally accepted accounting principles in the United States of America ("U.S. GAAP");
- the impact of the Restatement and the adequacy of our disclosure controls and procedures over financial reporting; and
- market trends in our industry, interest rates, real estate values, the debt securities markets or the general economy.

The forward-looking statements are based on our beliefs, assumptions and expectations of our future performance, taking into account all information currently available to us. You should not place undue reliance on these forward-looking statements. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to us. Some of these factors are described under the headings "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Business." If a change occurs, our business, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made. New risks and uncertainties arise over time, and it is not possible for us to predict those events or how they may affect us. Except as required by law, we are not obligated to, and do not intend to, update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

The following discussion should be read in conjunction with our condensed consolidated financial statements and the accompanying notes to our condensed consolidated financial statements, which are included in this Report.

Overview

We are a Maryland corporation primarily focused on investing in, financing and managing residential and commercial mortgage-backed securities ("MBS") and mortgage loans. We are externally managed and advised by Invesco Advisers, Inc., our Manager, a registered investment adviser and an indirect, wholly-owned subsidiary of Invesco Ltd., a leading independent global investment management firm. We elected to be taxed as a real estate investment trust ("REIT") for U.S. federal income tax purposes under the provisions of the Internal Revenue Code of 1986, as amended ("Code"), commencing with our taxable year ended December 31, 2009. To maintain our REIT qualification, we are generally required to distribute at least 90% of our REIT taxable income to our stockholders annually. We operate our business in a manner that permits our exclusion from the definition of "Investment Company" under the 1940 Act.

Our objective is to provide attractive risk-adjusted returns to our investors, primarily through dividends and secondarily through capital appreciation. To achieve this objective, we primarily invest in the following:

-

Residential mortgage-backed securities (“RMBS”) that are guaranteed by a U.S. government agency such as the Government National Mortgage Association ("Ginnie Mae") or a federally chartered corporation such as the Federal National Mortgage Association (“Fannie Mae”) or the Federal Home Loan Mortgage Corporation (“Freddie Mac”) (collectively "Agency RMBS");

- RMBS that are not guaranteed by a U.S. government agency ("non-Agency RMBS");
- Credit risk transfer securities that are unsecured obligations issued by government-sponsored enterprises ("GSE CRT");
- Commercial mortgage-backed securities ("CMBS");
- Residential and commercial mortgage loans; and
- Other real estate-related financing arrangements.

We generally finance our investments through short- and long-term borrowings structured as repurchase agreements and secured loans. We finance our residential loans held-for-investment through asset-backed securities ("ABS") issued by consolidated securitization trusts. We have also financed investments through the issuances of debt and equity and may utilize other forms of financing in the future.

Capital Activities

On September 15, 2015, we declared the following dividends:

- a dividend of $0.40 per share of common stock to be paid on October 27, 2015 to stockholders of record as of the close of business on September 28, 2015;
- a dividend of $0.4844 per share of Series A Preferred Stock to be paid on October 26, 2015 to stockholders of record as of the close of business on October 1, 2015; and
- a dividend of $0.4844 per share of Series B Preferred Stock to be paid on December 28, 2015 to stockholders of record as of the close of business on December 5, 2015.

During the three and nine months ended September 30, 2015, we repurchased 3,695,368 shares of our common stock at an average repurchase price of $13.53 per share for a net cost of $50.0 million, including acquisition expenses.

Factors Impacting Our Operating Results

Our operating results can be affected by a number of factors and primarily depend on the level of our net interest income and the market value of our assets. Our net interest income, which includes the amortization of purchase premiums, reclassification of amortization of net deferred losses on de-designated interest rate swaps to repurchase agreements interest expense and accretion of purchase discounts, varies primarily as a result of changes in market interest rates and prepayment speeds, as measured by the constant prepayment rate ("CPR") on our target assets. Interest rates and prepayment speeds vary according to the type of investment, conditions in the financial markets, competition and other factors, none of which can be predicted with any certainty. The market value of our assets can be impacted by asset spreads and the supply of, and demand for, target assets in which we invest.

Market Conditions

Macroeconomic factors that affect our business include credit spread premiums, market interest rates, Federal Reserve policy initiatives, residential and commercial real estate prices, credit availability, personal income, corporate earnings, employment conditions, financial conditions and inflation. In the third quarter of 2015 market attention was focused on global events, particularly economic weakness in China and the potential actions of the Federal Reserve. Many investors decreased risk exposure due to the potential for tighter U.S. monetary policy, a stronger dollar, declining commodity prices, and generally weaker global economic growth. As a result, equity and interest rate volatility increased, interest rates declined, credit spread premiums widened, and financial conditions generally tightened.

Consensus forecasts for domestic economic activity in the second half of 2015 are being reduced. Monthly increases in payroll employment averaged just 167,000 for the third quarter after increasing by 213,000 per month in the first half of 2015. Still, the unemployment rate has continued to decline to 5.1% as of September 2015 from 5.3% as of June 2015. Third quarter financial conditions weakened with increased interest rate volatility, wider credit spreads, and lower U.S. equity prices. Still, the low interest rate environment, coupled with the decline in energy prices, should be supportive of U.S. economic growth, as policy rates are below levels that would be historically indicated by recent unemployment and inflation indicators alone. Countering the positive influence on the economy is weak capital investment, tepid wage and consumer debt growth, and the stronger dollar. Households are once again increasing their debt levels, albeit at a modest rate, which increases their ability to consume goods and services. Inflation data has continued to indicate smaller increases than the Federal Reserve's 2% target, with core personal consumption expenditures prices having increased 1.3% year-over-year as of August 2015. Markets continue to try to discern the timing of the first interest rate increase by the Federal Reserve and still expect that it may come later this year.

The interest rate environment has been broadly supportive for Agency RMBS, and we believe it will continue to be. Range-bound interest rates create a good environment for MBS investors, as the prepayment option embedded in Agency RMBS is less onerous if interest rates are likely to neither fall nor rise dramatically. Further, continued tight residential mortgage loan underwriting standards restrict the ability of homeowners to refinance, which is normally to the detriment of MBS investors. We believe quantitative easing in Europe and Japan will create international demand for Agency RMBS due to the relatively attractive yield and the implicit U.S. government guarantee. Further, Agency RMBS investors saw the muted market impact from Federal Reserve tapering of Agency RMBS purchases in the fourth quarter of 2014 as that program ended with little noticeable impact on Agency RMBS valuations. There has been adequate demand from investors and limited supply of new Agency RMBS to offset the decline in demand from the Federal Reserve. Still, Agency MBS modestly underperformed equal duration U.S. Treasury notes during the third quarter reflecting worsening financial conditions including wider investment grade credit spreads. Exacerbating the under performance of Agency MBS was the strong performance of interest rate swaps which are commonly used to hedge the interest rate duration risk in MBS portfolios. Interest rate swap spreads, generally thought likely to widen in times of weakening financial conditions, actually tightened markedly in the third quarter. Ten year swap yields declined by approximately 46 basis points while similar maturity Treasury yields only declined by 31 basis points, thus the spread or difference narrowed by 15 basis points. By comparison, the 30 year current coupon mortgage yield declined 30 basis points. Repurchase agreement financing one-month rates for Agency RMBS increased in the third quarter from the high 30’s basis points range in July to nearly 50 basis points in early September due in large part to expectations of a September rate increase by the Federal Reserve and possibly also due to weakening financial conditions. After the September Federal Reserve meeting passed with no rate increase, rates declined to the low 40’s basis points range, which was still somewhat elevated due to quarter end pressures.

With respect to mortgage credit assets, CMBS yield spreads over comparable term interest rate swaps widened over the quarter as financial conditions deteriorated and supply of CMBS increased. Spreads in unrated GSE CRTs also widened over the third quarter of 2015, while legacy non-Agency RMBS prices were generally stable. We continue to believe a gradually improving economy, coupled with low interest rates, should foster a favorable environment for residential and commercial real estate. Specifically, this environment should support modest growth in property prices and rents, encourage favorable financing terms and aid in tempering new supply.

The impact of regulatory initiatives on the economy may also affect our business and our financial results. The Dodd-Frank Act, enacted in July 2010, contains numerous provisions affecting the financial and mortgage industries, many of which may affect our cost of doing business, may limit our investment opportunities and may affect the competitive balance within our industry and the markets in which we invest. For example, the Ability-to-Repay (“ATR”) rule requires lenders to make a reasonable, good-faith determination that residential borrowers have a reasonable ability to repay a mortgage loan. In addition to the ATR rule, the Consumer Financial Protection Bureau adopted a Qualified Mortgage (“QM”) framework that provides certain legal protections to residential mortgage loan lenders, which includes restrictions on loan features, points and fees and borrower debt-to-income ratios. While we are not directly subject to compliance with the implementation of rules regarding the origination of residential mortgage loans, the impact of these regulations and others could affect our ability to securitize or invest in newly originated loans in the future.

In addition, the regulatory landscape for our repurchase agreement counterparties continues to evolve following the adoption of new capital rules which generally affects the manner in which banks lend. Regulators are also focused on liquidity requirements which will likely impact how banks fund themselves. While we are not directly subject to compliance with the implementation of rules regarding financial institutions, the effect of these regulations and others could affect our ability to finance our assets in the future.

On September 2, 2014, the Federal Housing Finance Agency ("FHFA"), proposed to revise its regulations governing Federal Home Loan Bank membership to, among other things, exclude captive insurance companies. However, the proposed rules would permit existing captive insurers, such as our captive insurance company subsidiary IAS Services

LLC, to remain members for a period of five years following the effective date of the final rules. In addition, the Federal Home Loan Bank of Indianapolis ("FHLBI") would be permitted to allow outstanding advances to IAS Services LLC that were made prior to the effective date of the final rules to honor contractual terms to maturity. Therefore, under the proposed rules, we do not expect there would be any impact to our existing FHLBI borrowings. The rules are subject to change prior to their final adoption. However, if the FHFA’s rules are adopted substantially as proposed, we do not expect that the rules would have a material effect on our sources or costs of funding or our results of operations. The date set for the end of the comment period was January 23, 2015. The vast majority of the comments were against adoption of the proposed rule. The FHFA has not yet made a formal statement as to their intentions with respect to the proposed rule.

Table of Contents

Investment Activities

In the third quarter of 2015, our investment portfolio remained positioned to take advantage of opportunities in both mortgage-backed and credit risk transfer securities and newly originated loans against a backdrop of improving housing and commercial real estate markets. We have over the last year and over the last quarter maintained a relatively balanced allocation of our equity among residential credit, commercial credit and Agency RMBS.

The table below shows the allocation of our equity as of September 30, 2015, December 31, 2014 and September 30, 2014:

$ in thousands	As of September 30, 2015		December 31, 2014		September 30, 2014	
Agency RMBS	35	%	32	%	33	%
Residential Credit (1)	31	%	34	%	33	%
Commercial Credit (2)	34	%	34	%	34	%
Total	100	%	100	%	100	%

(1) Non-Agency RMBS, GSE CRT and Residential Loans are considered residential credit.

(2) CMBS, Commercial Loans and Investments in unconsolidated ventures of $37.9 million (which are included in Other Investments), are considered commercial credit.

The table below shows the breakdown of our investment portfolio as of September 30, 2015, December 31, 2014 and September 30, 2014:

$ in thousands	As of September 30, 2015	December 31, 2014	September 30, 2014
Agency RMBS:			
30 year fixed-rate, at fair value	4,214,946	4,790,293	4,901,116
15 year fixed-rate, at fair value	1,702,382	1,327,101	1,389,953
Hybrid ARM, at fair value	3,447,613	2,976,918	2,650,321
ARM, at fair value	452,831	546,782	532,880
Agency CMO, at fair value	416,662	450,895	453,748
Non-Agency RMBS, at fair value	2,624,608	3,061,647	3,302,080
GSE CRT, at fair value	651,705	625,424	610,326
CMBS, at fair value	3,304,214	3,469,835	3,456,610
Residential loans, at amortized cost	3,307,249	3,365,003	3,103,434
Commercial loans, at amortized cost	187,038	145,756	144,707
Total Investment portfolio	20,309,248	20,759,654	20,545,175

During 2015, we have reinvested cash flows from our Agency RMBS portfolio into 15 year fixed-rate Agency RMBS and Hybrid ARM Agency RMBS. We have continued to hold certain 30 year fixed-rate Agency RMBS that have relatively short durations because they are collateralized by higher coupons. We expect these securities to prepay more favorably than their applicable cohorts based on their seasoning and collateral attributes. The average coupon of our 30 year fixed-rate Agency RMBS declined to 4.26% at September 30, 2015, compared to 4.30% at September 30, 2014. Additionally, we hold 15 year fixed-rate Agency RMBS, Hybrid ARM Agency RMBS and ARM Agency RMBS that we believe have lower durations and better cash flow certainty relative to current coupon 30 year fixed-rate Agency RMBS. Further, we own Agency collateralized mortgage obligations ("CMOs"), some of which are interest-only securities, to hedge the risk of higher interest rates.

Our portfolio of investments that have credit exposure include non-Agency RMBS, GSE CRTs, CMBS and residential and commercial real estate loans. We use our proprietary models to perform a detailed review of each investment which often includes loan level analysis of expected performance. We do not place any reliance on ratings by various agencies as we believe our models more accurately evaluate the performance based on our assumptions about market conditions. As shown in the table above, exposure to credit assets has remained relatively stable as we believe the

improving economy will provide better risk-adjusted returns for this asset class while having lower interest rate exposure relative to Agency RMBS.
With respect to our non-Agency RMBS portfolio, we primarily invest in RMBS collateralized by prime and Alt-A loans. In addition, we have invested in re-securitizations of real estate mortgage investment conduit ("Re-REMIC") RMBS and

Table of Contents

reperforming mortgage loans that we believe provide attractive risk adjusted returns. We also invest in GSE CRTs, which have the added benefit of paying a floating rate coupon and reduces our need to hedge interest rate risk. Based on our view of the improving housing market and relative value opportunities, we increased holdings in GSE CRTs over the past twelve months as paydowns from principal repayments and limited dispositions have reduced our non-Agency RMBS holdings.

Our CMBS portfolio generally consists of assets originated before 2007, assets originated after 2010 (“CMBS 2.0”) and multi-family CMBS issued by Freddie Mac under their “K” program. Over the past twelve months we have primarily invested in CMBS 2.0. The allocation of our CMBS holdings in our MBS and GSE CRT portfolio is approximately 19.7% as of September 30, 2015.

During 2015, we invested in and consolidated one additional residential loan securitization trust collateralized by prime jumbo loans that were generally originated in 2011 or later. We believe these loans have high credit quality based on their risk characteristics, including but not limited to high FICO scores, low historical delinquencies and low loan-to-value ratios based on current estimated home values. We have invested in and consolidated eleven residential loan securitization trusts that hold $3.3 billion of residential loans as of September 30, 2015. For further details on the residential loan portfolio, refer to Note 3 - "Variable Interest Entities" of our condensed consolidated financial statements.

During 2015, we originated three new commercial real estate loans, and two of our existing commercial real estate loans prepaid ahead of their contractual maturities. As of September 30, 2015, our commercial real estate loan portfolio includes a first mortgage loan and seven mezzanine loans that we purchased or originated. For further details on our commercial loan portfolio, see Note 5 - "Commercial Loans Held-for-Investment" of our condensed consolidated financial statements.

Portfolio Characteristics

The table below represents the vintage of our MBS and GSE CRT credit assets as of September 30, 2015 as a percentage of the fair value:

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total
Prime	0.5%	1.6%	4.0 %	3.8 %	9.9 %	2.1%	— %	— %	0.1 %	— %	7.4 %	1.9 %	— %	31.3 %
Re-REMIC [(1)]	— %	— %	— %	— %	0.3 %	— %	0.9%	4.2%	16.7%	7.5 %	0.5 %	— %	— %	30.1 %
Alt-A	— %	0.6%	8.1 %	6.2 %	7.9 %	— %	— %	— %	— %	— %	— %	— %	— %	22.8 %
Subprime/reperforming	— %	— %	— %	0.1 %	0.3 %	— %	— %	— %	— %	— %	2.0 %	11.9%	1.5%	15.8 %
Total Non-Agency	0.5%	2.2%	12.1%	10.1%	18.4%	2.1%	0.9%	4.2%	16.8%	7.5 %	9.9 %	13.8%	1.5%	100.0%
GSE CRT	— %	— %	— %	— %	— %	— %	— %	— %	— %	— %	38.6%	52.5%	8.9%	100.0%
CMBS	— %	— %	4.1 %	10.0%	0.4 %	— %	— %	7.4%	22.6%	12.2%	13.7%	27.7%	1.9%	100.0%

(1) For Re-REMICs, the table reflects the year in which the resecuritizations were issued. The vintage distribution of the securities that collateralize the Company’s Re-REMIC investments is 11.0% for 2005, 32.3% for 2006, and 56.7% for 2007.

The tables below represent the geographic concentration of the underlying collateral for our MBS and GSE CRT credit assets as of September 30, 2015:

Non-Agency RMBS State	Percentage		GSE CRT State	Percentage		CMBS State	Percentage	
California	41.8	%	California	22.0	%	California	16.1	%
New York	6.8	%	Texas	5.6	%	New York	12.6	%
Florida	6.8	%	Virginia	4.5	%	Texas	9.3	%
Virginia	3.8	%	New York	4.1	%	Florida	5.7	%
New Jersey	3.7	%	Illinois	4.0	%	Pennsylvania	4.2	%
Maryland	3.7	%	Massachusetts	3.6	%	Illinois	4.2	%
Washington	2.8	%	Florida	3.6	%	New Jersey	3.5	%
Illinois	2.8	%	Washington	3.3	%	Ohio	3.0	%
Massachusetts	2.1	%	Colorado	3.3	%	Virginia	2.9	%
Georgia	2.1	%	New Jersey	3.2	%	Maryland	2.8	%
Other	23.6	%	Other	42.8	%	Other	35.7	%
Total	100.0	%	Total	100.0	%	Total	100.0	%

The following table displays certain characteristics of our residential loans held-for-investment at September 30, 2015 by year of origination.

$ in thousands	2014		2013		2012		2011		2010		2009		2008		2007		Total	
Portfolio Characteristics:																		
Number of Loans	692		2,596		720		86		25		6		14		14		4,153	
Current Principal Balance	513,819		1,998,969		625,255		91,620		23,841		2,737		12,327		11,416		3,279,984	
% of Current Principal Balance to Total	15.7	%	60.9	%	19.1	%	2.8	%	0.7	%	0.1	%	0.4	%	0.3	%	100.0	%
Net Weighted Average Coupon Rate	3.46	%	3.45	%	3.24	%	3.38	%	3.74	%	3.69	%	5.47	%	4.67	%	3.42	%
Weighted Average Maturity (years)	28.72		27.81		27.28		25.74		25.22		23.76		22.92		21.84		27.73	
Current Performance:																		
Current	513,819		1,997,171		625,255		91,620		23,841		2,737		11,697		11,416		3,277,556	
30 Days Delinquent	—		560		—		—		—		—		630		—		1,190	
60 Days Delinquent	—		—		—		—		—		—		—		—		—	
90+ Days Delinquent	—		1,238		—		—		—		—		—		—		1,238	
Bankruptcy/Foreclosure	—		—		—		—		—		—		—		—		—	
Total	513,819		1,998,969		625,255		91,620		23,841		2,737		12,327		11,416		3,279,984	

The following table presents the geographic concentrations of our residential loans held-for-investment at September 30, 2015 based on principal balance outstanding:

State	Percent	
California	53.1	%
New York	7.6	%
Massachusetts	5.9	%
Illinois	3.6	%
Other states (none greater than 3%)	29.8	%
Total	100.0	%

Financing and Other Liabilities
We enter into repurchase agreements to finance the majority of our target assets. These agreements are secured by our Agency RMBS, non-Agency RMBS, GSE CRTs and CMBS. In addition, these agreements are generally settled on a short-term basis, usually from one to twelve months, and bear interest at rates that have historically moved in close relationship to LIBOR. At each settlement date, we typically refinance each repurchase agreement at the market interest rate at that time. As of September 30, 2015, we had entered into repurchase agreements totaling $12.9 billion (December 31, 2014: $13.6 billion). The decrease in our repurchase agreement balance over the past nine months was primarily due to replacing some of our repurchase borrowings with secured loans, as discussed below.
Our wholly-owned subsidiary, IAS Services LLC, is a member of the FHLBI. As a member of the FHLBI, IAS Services LLC has borrowed funds from the FHLBI in the form of secured advances. As of September 30, 2015, IAS Services LLC had $1.675 billion in outstanding secured advances and is approved for total available uncommitted credit for borrowing of an amount up to $2.5 billion. Available uncommitted credit may be adjusted at the sole discretion of the FHLBI. For the three and nine months ended September 30, 2015, IAS Services LLC had average borrowings of $1.6 billion with a weighted average borrowing rate of 0.40% and 0.39%, respectively.
During the nine months ended September 30, 2015, we repurchased 3,695,368 shares of our common stock at an average repurchase price of $13.53 per share for a net cost of $50.0 million, including acquisition expenses.
We have also committed to invest up to $122.4 million in unconsolidated ventures that are sponsored by an affiliate of our Manager. As of September 30, 2015, $97.0 million of our commitment to these unconsolidated ventures has been called. We are committed to fund $25.4 million in additional capital to fund future investments and cover future expenses should they occur.
We record a liability for mortgage-backed and credit risk transfer securities purchased, for which settlement has not taken place, as an investment related payable. As of September 30, 2015 and December 31, 2014, we had investment related payables of $55.0 million, and $17.0 million, respectively. None of these investment related payables were outstanding more than thirty days. The change in balance was primarily due to an increase in unsettled MBS purchases as of September 30, 2015. We record a receivable for mortgage-backed and credit risk transfer securities sold for which settlement has not taken place as an investment related receivable. As of September 30, 2015 and December 31, 2014, the Company had investment related receivables of $24.9 million and $38.7 million, respectively. None of these investment related receivables were outstanding more than thirty days.
Hedging Instruments. We generally hedge as much of our interest rate and foreign exchange risk as we deem prudent in light of market conditions. No assurance can be given that our hedging activities will have the desired beneficial impact on our results of operations or financial condition. Our investment policies do not contain specific requirements as to the percentages or amount of risk that we are required to hedge.
Hedging may fail to protect or could adversely affect us because, among other things:

- available interest rate hedging may not correspond directly with the interest rate risk for which protection is sought;
- the duration of the hedge may not match the duration of the related liability;
- the party owing money in the hedging transaction may default on its obligation to pay;
- the credit quality of the party 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 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.

As of September 30, 2015, we have entered into interest rate swap agreements designed to mitigate the effects of increases in interest rates under a portion of our borrowings. These swap agreements provide for fixed interest rates indexed off of one-month LIBOR and effectively fix the floating interest rates on $11.5 billion (September 30, 2014: $12.2 billion) of borrowings. The notional amount of interest rate swaps was reduced in line with the reduced interest rate risk in our portfolio after the reallocation away from longer duration 30 year fixed-rate Agency RMBS into shorter duration 15 year fixed-rate Agency RMBS and Hybrid ARM Agency RMBS. As of September 30, 2015, included in this amount are forward starting swaps with a total notional amount of $1.6 billion, with starting dates ranging from February 5, 2016 to June 24, 2016. The change in the amount of interest rate swaps was due to our view of interest rate risk and the expected duration of our investment portfolio and liabilities.