CAPSTEAD MORTGAGE CORP
Form 10-Q
August 07, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended: June 30, 2007

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: 1-8896

CAPSTEAD MORTGAGE CORPORATION

(Exact name of Registrant as specified in its Charter)

Maryland	**75-2027937**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
8401 North Central Expressway, Suite 800, Dallas, TX	**75225**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(214) 874-2323**

Indicate by check mark whether the Registrant (1) has filed all documents and 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 þ NO o

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer 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 þ

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the last practicable date.

Common Stock ($0.01 par value)	19,392,461 as of August 6, 2007

CAPSTEAD MORTGAGE CORPORATION
FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2007
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ITEM 1. FINANCIAL STATEMENTS
PART I. ¾ FINANCIAL INFORMATION
CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share amounts)

	June 30, 2007 (unaudited)	*December 31, 2006 (NOTE 2)*
Assets:		
Mortgage securities and similar investments ($5.3 billion pledged under repurchase arrangements)	$ 5,490,449	$ 5,252,399
Investments in unconsolidated affiliates	10,523	20,073
Receivables and other assets	78,556	69,869
Cash and cash equivalents	6,560	5,661
	$ 5,586,088	$ 5,348,002
Liabilities:		
Repurchase arrangements and similar borrowings	$ 5,115,170	$ 4,876,134
Unsecured borrowings	103,095	103,095
Common stock dividend payable	775	385
Accounts payable and accrued expenses	22,400	28,426
	5,241,440	5,008,040
Stockholders equity:		
Preferred stock $0.10 par value; 100,000 shares authorized:		
$1.60 Cumulative Preferred Stock, Series A, 202 shares issued and outstanding at June 30, 2007 and December 31, 2006 ($3,317 aggregate liquidation preference)	2,828	2,828
$1.26 Cumulative Convertible Preferred Stock, Series B, 15,819 shares issued and outstanding at June 30, 2007 and December 31, 2006 ($180,025 aggregate liquidation preference)	176,705	176,705
Common stock $0.01 par value; 100,000 shares authorized: 19,392 and 19,253 shares issued and outstanding at June 30, 2007 and December 31, 2006, respectively	194	192
Paid-in capital	498,208	497,418
Accumulated deficit	(352,809)	(354,617)
Accumulated other comprehensive income	19,522	17,436
	344,648	339,962
	$ 5,586,088	$ 5,348,002

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)
(unaudited)

	Quarter Ended June 30		*Six Months Ended June 30*	
	2007	***2006***	***2007***	***2006***
Mortgage securities and similar investments:				
Interest income	$ 75,795	$ 57,349	$ 147,937	$ 110,275
Interest expense	(67,107)	(54,685)	(130,696)	(102,228)
	8,688	2,664	17,241	8,047
Other revenue (expense):				
Other revenue	237	200	1,108	366
Interest expense on unsecured borrowings	(2,187)	(1,621)	(4,374)	(3,208)
Other operating expense	(1,539)	(1,576)	(3,213)	(3,249)
	(3,489)	(2,997)	(6,479)	(6,091)
Income (loss) before equity in earnings of unconsolidated affiliates	5,199	(333)	10,762	1,956
Equity in earnings of unconsolidated affiliates	575	608	1,239	1,030
Net income	$ 5,774	$ 275	$ 12,001	$ 2,986
Net income available (loss attributable) to common stockholders:				
Net income	$ 5,774	$ 275	$ 12,001	$ 2,986
Less cash dividends paid on preferred stock	(5,064)	(5,064)	(10,128)	(10,128)
	$ 710	$ (4,789)	$ 1,873	$ (7,142)
Basic and diluted earnings (loss) per common share	$ 0.04	$ (0.25)	$ 0.10	$ (0.38)
Cash dividends declared per share:				
Common	$ 0.040	$ 0.020	$ 0.060	$ 0.040
Series A Preferred	0.400	0.400	0.800	0.800
Series B Preferred	0.315	0.315	0.630	0.630

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Six Months Ended June 30 2007	2006
Operating activities:		
Net income	$ 12,001	$ 2,986
Noncash items:		
Amortization of investment premiums	11,808	11,737
Depreciation and other amortization	117	50
Stock-based compensation	437	244
Undistributed earnings of unconsolidated affiliates		(181)
Net change in receivables, other assets, accounts payable and accrued expenses	(10,378)	(13,418)
Net cash provided by operating activities	13,985	1,418
Investing activities:		
Purchases of mortgage securities and similar investments	(1,153,451)	(1,306,819)
Principal collections on mortgage securities and similar investments	901,280	855,293
Distributions from (investments in) unconsolidated affiliates - commercial real estate loan limited partnership	9,550	(9,218)
Net cash used in investing activities of continuing operations	(242,621)	(460,744)
Net cash used in investing activities of discontinued operation		(2,884)
Net cash used in investing activities	(242,621)	(463,628)
Financing activities:		
Net increase (decrease) in repurchase arrangements and similar borrowings:		
Borrowings based on 30-day rates	4,175	509,331
Borrowings based on greater than 30-day rates	234,862	(70,161)
Capital stock transactions	1,396	(8)
Dividends paid	(10,898)	(10,889)
Net cash provided by financing activities	229,535	428,273
Net change in cash and cash equivalents	899	(33,937)
Cash and cash equivalents at beginning of period	5,661	33,937
Cash and cash equivalents at end of period	$ 6,560	$

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2007
(unaudited)

NOTE 1 ¾ BUSINESS

Capstead Mortgage Corporation operates as a real estate investment trust for federal income tax purposes (a REIT) and is based in Dallas, Texas. Unless the context otherwise indicates, Capstead Mortgage Corporation, together with its subsidiaries, is referred to as Capstead or the Company. Capstead earns income from investing in real estate-related assets on a leveraged basis. These investments currently consist primarily of a core portfolio of residential adjustable-rate mortgage (ARM) securities issued and guaranteed by government-sponsored entities, either Fannie Mae or Freddie Mac, or by an agency of the federal government, Ginnie Mae (collectively, Agency Securities). Capstead also seeks to opportunistically invest a portion of its investment capital in credit-sensitive commercial real estate-related assets, including subordinate commercial real estate loans.

NOTE 2 ¾ BASIS OF PRESENTATION

Interim Financial Reporting

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the quarter and six months ended June 30, 2007 are not necessarily indicative of the results that may be expected for the calendar year ending December 31, 2007. For further information refer to the consolidated financial statements and footnotes thereto incorporated by reference in the Company s annual report on Form 10-K for the year ended December 31, 2006.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Accounting for Uncertainty in Income Taxes

The Company adopted the provisions for Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes, (FIN 48) on January 1, 2007. The Company did not recognize any liability for unrecognized tax benefits in implementing FIN 48 and does not expect to recognize a change in unrecognized tax benefits within the next twelve months. If applicable, the Company will recognize interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. No such accruals were necessary as of June 30, 2007. The Company and certain of its subsidiaries file federal and various state income tax returns. The Company is generally no longer subject to income tax examinations by tax authorities for years before 2003.

Accounting for Acquisitions of Mortgage Securities Seller-Financed using Repurchase Arrangements

Capstead occasionally finances acquisitions of mortgage investments with the seller using repurchase arrangements. Consistent with prevailing industry practice, the Company records such assets and the related borrowings gross on its balance sheet, and the corresponding interest income and interest expense

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gross on its income statement. In addition, the asset is typically a security held available-for-sale, and any change in fair value of the asset is recorded as a component of *Other comprehensive income*. The Company had less than $25 million in seller-financed acquisitions as of June 30, 2007.

Under a recent technical interpretation of the pertinent accounting rules, seller-financed acquisitions may not qualify as a sale from the seller s perspective and the seller may be required to continue to consolidate the assets sold. As a result, buyers may be precluded from presenting seller-financed acquisitions gross on their balance sheets and required to treat net investments in such assets as derivative financial instruments (Derivatives) until such time as the assets are no longer financed with the sellers. The resulting Derivatives would be marked to market through earnings. Prior to year-end, the FASB is expected to finalize guidance that would require consideration as to whether the Derivative accounting described above should be followed in situations where the acquisition and subsequent financing by a seller is sufficiently linked. Management does not believe changing the accounting treatment for any past transactions, if required, would have a material effect on Capstead s reported earnings, taxable income or financial condition. Also, it would not affect the Company s status as a REIT or cause it to fail to qualify for its Investment Company Act exemption which requires that the Company must, among other things, maintain at least 55% of its assets directly in qualifying real estate interests.

Fair Value Accounting Rule Changes

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The Company is required to adopt SFAS No. 157 on January 1, 2008. The adoption of SFAS No. 157 is not expected to have a material impact on the Company s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115* (SFAS No. 159). This statement permits, but does not require, entities to measure many financial instruments, including liabilities and certain other items, at fair value with resulting changes in fair value reported in earnings. The Company is required to adopt SFAS No. 159 on January 1, 2008 and is currently evaluating which, if any, of its financial assets or liabilities to report at fair value with related adjustments reported in earnings. Therefore, the impact, if any, that SFAS No. 159 will have on its consolidated financial statements has not been determined.

In June 2007, the American Institute of Certified Public Accountants issued Statement of Position 07-1, *Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies* (SOP 07-1). SOP 07-1 addresses whether the accounting principles set forth in this audit and accounting guide are applicable to an entity by clarifying the definition of an investment company for accounting purposes and eliminating a previous exclusion from the definition for REITs. The SOP has no bearing on whether an entity is considered an investment company under the Investment Company Act of 1940. Investment company accounting principles, among other things, require entities to report investments at fair value with the resulting changes in fair value reported in earnings. SOP 07-1 is effective January 1, 2008, concurrent with the effective date of SFAS 159. The Company is currently evaluating whether or not it meets the definition of an investment company for accounting purposes as set forth in the SOP. Given that most of the Company s investments are currently reported at fair value with changes in fair value included as a component of *Stockholders equity*, the provisions of SOP 07-1, if applicable, are not expected to have a material impact on the financial condition of the Company and have no impact on future taxable income; however, future operating results may be more volatile because of the inclusion of fair value changes in reported earnings.

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NOTE 3 ¾ EARNINGS (LOSS) PER COMMON SHARE

Basic earnings (loss) per common share is computed by dividing net income, after deducting preferred share dividends, by the weighted average number of common shares outstanding. Diluted earnings (loss) per common share is computed by dividing net income, after deducting dividends on convertible preferred shares when such shares are antidilutive, by the weighted average number of common shares and common share equivalents outstanding, giving effect to equity awards and convertible preferred shares, when such awards and shares are dilutive. For calculation purposes the Series A and B preferred shares are considered dilutive whenever basic income per common share exceeds each Series dividend divided by the conversion rate applicable for that period. Components of the computation of basic and diluted earnings (loss) per common share were as follows (in thousands, except per share amounts):

	Quarter Ended June 30		*Six Months Ended June 30*	
	2007	***2006***	***2007***	***2006***
Numerators for basic earnings (loss) per common share:				
Net income	$ 5,774	$ 275	$ 12,001	$ 2,986
Less Series A and B preferred share dividends	(5,064)	(5,064)	(10,128)	(10,128)
Income available (loss attributable) to common stockholders	$ 710	$ (4,789)	$ 1,873	$ (7,142)
Weighted average common shares outstanding	19,013	18,894	18,973	18,883
Basic earnings (loss) per common share	$ 0.04	$ (0.25)	$ 0.10	$ (0.38)
Numerators for diluted earnings (loss) per common share:				
Net income	$ 5,774	$ 275	$ 12,001	$ 2,986
Less dividends on antidilutive convertible preferred shares	(5,064)	(5,064)	(10,128)	(10,128)
Income available (loss attributable) to common stockholders	$ 710	$ (4,789)	$ 1,873	$ (7,142)
Denominator for diluted earnings (loss) per common share:				
Weighted average common shares outstanding	19,013	18,894	18,973	18,883
Net effect of dilutive equity awards	244		182	
	19,257	18,894	19,155	18,883
Diluted earnings (loss) per common share	$ 0.04	$ (0.25)	$ 0.10	$ (0.38)

Potentially dilutive securities excluded from the calculation of diluted earnings (loss) per common share were as follows (in thousands):

	Quarter Ended June 30		*Six Months Ended June 30*	
	2007	***2006***	***2007***	***2006***
Equity awards:				
Shares issuable under option awards	406	836	406	836
Nonvested stock awards		112		112
Convertible preferred shares:				
Series A shares	202	202	202	202
Series B shares	15,819	15,819	15,819	15,819

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NOTE 4 ¾ MORTGAGE SECURITIES AND SIMILAR INVESTMENTS

Agency Securities carry an implied AAA rating and therefore limited, if any, credit risk. Private residential mortgage pass-through securities formed prior to 1995 when Capstead operated a mortgage conduit are referred to as Non-agency Securities. The related credit risk is borne by the Company or by AAA-rated private mortgage insurers. Commercial loans are subordinate loans that carry credit risk associated with specific commercial real estate collateral. Collateral for structured financings consists of Non-agency Securities pledged to secure these securitizations. The related credit risk is borne by bondholders of the securitization to which the collateral is pledged. The maturity of mortgage securities is directly affected by the rate of principal prepayments on the underlying mortgage loans. *Mortgage securities and similar investments* and related weighted average rates classified by collateral type and interest rate characteristics were as follows (dollars in thousands):

	Principal Balance	***Investment Premiums***	***Basis***	***Carrying Amount** (a)*	***Net WAC** (b)*	***Average Yield** (b)*
June 30, 2007						
Agency Securities:						
Fannie Mae/Freddie Mac:						
Fixed-rate	$ 14,654	$ 43	$ 14,697	$ 14,719	6.63%	6.36%
ARMs	4,715,121	65,873	4,780,994	4,795,189	6.30	5.56
Ginnie Mae ARMs	623,079	2,698	625,777	630,656	5.66	5.45
	5,352,854	68,614	5,421,468	5,440,564	6.23	5.55
Non-agency Securities:						
Fixed-rate	14,873	28	14,901	14,932	7.22	6.91
ARMs	25,842	242	26,084	26,345	7.22	6.58
	40,715	270	40,985	41,277	7.22	6.70
Commercial loans	2,881		2,881	2,881	18.00	18.00
Collateral for structured financings	5,638	89	5,727	5,727	8.06	7.96
	$ 5,402,088	$ 68,973	$ 5,471,061	$ 5,490,449	6.25	5.57
December 31, 2006						
Agency Securities:						
Fannie Mae/Freddie Mac:						
Fixed-rate	$ 16,819	$ 52	$ 16,871	$ 16,895	6.63%	6.29%
ARMs	4,343,740	61,381	4,405,121	4,418,446	6.14	5.36
Ginnie Mae ARMs	752,301	2,757	755,058	758,660	5.23	5.20
	5,112,860	64,190	5,177,050	5,194,001	6.01	5.34
Non-agency Securities:						
Fixed-rate	17,734	41	17,775	17,804	7.19	6.83
ARMs	31,562	303	31,865	32,164	6.99	6.81

	49,296	344	49,640	49,968	7.06	6.81
Commercial loans	2,635		2,635	2,635	18.00	18.00
Collateral for structured financings	5,705	90	5,795	5,795	8.06	7.58
	$ 5,170,496	$ 64,624	$ 5,235,120	$ 5,252,399	6.03	5.36

(a) *Includes mark-to-market for securities classified as available-for-sale, if applicable (see NOTE 8).*

(b) *Net WAC, or weighted average coupon, is presented net of servicing and other fees as of the indicated balance sheet date. Average Yield is presented for the quarter then ended, calculated including the amortization of investment premiums, mortgage insurance costs on Non-agency Securities and excluding unrealized gains and losses. Yields averaged 5.53% for the six months ended June 30, 2007.*

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Fixed-rate investments generally are mortgage securities backed by mortgage loans that have fixed rates of interest over the contractual term of the loans. Adjustable-rate investments generally are ARM securities backed by residential mortgage loans that have coupon interest rates that adjust at least annually to more current interest rates or begin doing so after an initial fixed-rate period. After the initial fixed-rate period, if applicable, ARM securities either (i) adjust annually based on a specified margin over the one-year Constant Maturity U.S. Treasury Note Rate (CMT) or the one-year London Interbank Offered Rate (LIBOR), (ii) adjust semiannually based on a specified margin over six-month LIBOR, or (iii) adjust monthly based on a specified margin over an index such as LIBOR, CMT or the Eleventh District Federal Reserve Bank Cost of Funds Index, usually subject to periodic and lifetime limits on the amount of such adjustments during any single interest rate adjustment period and over the contractual term of the loans.

NOTE 5 ¾ INVESTMENTS IN UNCONSOLIDATED AFFILIATES

In July 2005 Capstead and Crescent Real Estate Equities Company (NYSE: CEI) formed a limited partnership owned and capitalized 75% by Capstead and 25% by CEI, to invest in a leveraged portfolio of subordinate commercial real estate loans meeting certain criteria over a two-year investment period that ended in July 2007. CEI sourced investment opportunities (subject to Capstead s approval) and manages the venture s loan portfolio earning management fees and incentives based on portfolio performance. Investments made by the partnership are financed using a committed master repurchase agreement with a major investment banking firm. Amounts available to be borrowed under this facility and related borrowing rates are dependent upon the characteristics of the pledged collateral and can change based on changes in the fair value of the pledged collateral. Amounts borrowed are repayable in four equal installments due quarterly beginning November 1, 2007. As of June 30, 2007, the partnership had borrowed $28.8 million under this facility to fund investments totaling $38.3 million consisting of junior liens on a luxury hospitality property. Capstead s investment in the partnership totaled $7.4 million as of June 30, 2007 and the Company s equity in its earnings totaled $510,000 and $1.1 million during the three and six months ended June 30, 2007, respectively.

On August 3, 2007 CEI announced the completion of the proposed acquisition of CEI by affiliates of Morgan Stanley (NYSE: MS) which was approved by a majority vote of CEI s stockholders on August 1, 2007. Capstead is currently evaluating several options relative to the partnership with an expected resolution by year-end.

To facilitate the issuance of unsecured borrowings, in September and December 2005 and in September 2006 Capstead formed and capitalized a series of three Delaware statutory trusts through the issuance to the Company of the trusts common securities totaling $3.1 million (see NOTE 7). The Company s equity in the earnings of the trusts (consisting solely of the common trust securities pro rata share in interest accruing on Capstead s junior subordinated notes issued to the trusts) totaled $65,000 and $130,000 during the three and six months ended June 30, 2007, respectively.

NOTE 6 ¾ REPURCHASE ARRANGEMENTS AND SIMILAR BORROWINGS

Capstead generally pledges its *Mortgage securities and similar investments* as collateral under uncommitted repurchase arrangements with well-established investment banking firms, the terms and conditions of which are negotiated on a transaction-by-transaction basis. These repurchase arrangements generally have maturities of less than 31 days, although the Company routinely extends maturities on a portion of its borrowings. Interest rates on these borrowings are generally based on the corresponding LIBOR rate for the maturity of each borrowing. Amounts available to be borrowed under these arrangements are dependent upon the fair value of the securities pledged as collateral, which fluctuates with changes in interest rates, credit quality and liquidity conditions within the investment banking, mortgage finance and real estate industries. Until 1995 the Company operated a mortgage conduit, pooling mortgage loans into Non-agency Securities and issuing structured financings backed by both Agency and Non-agency Securities. The maturity of outstanding structured financings is directly affected by the rate of principal prepayments on the related collateral and are subject to redemption provided certain requirements specified in the related indentures have been met (referred to as Clean-up Calls). *Repurchase arrangements and similar borrowings*, classified by type of collateral and maturities, and related weighted average interest rates were as follows (dollars in thousands):

	June 30, 2007		*December 31, 2006*	
	Borrowings Outstanding	***Average Rate (a)***	***Borrowings Outstanding***	***Average Rate (a)***
Borrowings with maturities of 30 days or less:				
Agency Securities	$ 2,769,761	5.28%	$ 2,048,151	5.30%
Non-agency Securities	36,858	5.82	45,764	5.85
	2,806,619	5.29	2,093,915	5.32
Borrowings with maturities greater than 30 days:				
Agency Securities (31 to 90 days)	823,151	5.29	1,741,751	5.16
Agency Securities (91 to 360 days)	25,025	4.76		
Agency Securities (greater than 360 days)	1,454,648	4.98	1,034,673	4.98
	2,302,824	5.09	2,776,424	5.09
Structured financings	5,727	7.96	5,795	7.58
	$ 5,115,170	5.20	$ 4,876,134	5.19

(a) Average rate is presented as of the indicated balance sheet date.

The weighted average effective interest rate on *Repurchase arrangements and similar borrowings* was 5.21% and 5.20% during the quarter and six months ended June 30, 2007, respectively.

NOTE 7 ¾ UNSECURED BORROWINGS

Unsecured borrowings consist of 30-year junior subordinated notes issued in September 2005, December 2005 and September 2006 by Capstead to Capstead Mortgage Trust I, Trust II and Trust III, respectively. These unconsolidated affiliates of the Company were formed to issue $3.1 million of the trusts common securities to Capstead and to privately place $100 million of preferred securities with unrelated third party investors. Note balances and related weighted average interest rates (calculated including issue cost amortization) listed by trust were as follows (dollars in thousands):

	June 30, 2007		*December 31, 2006*	
	Borrowings Outstanding	***Average Rate (a)***	***Borrowings Outstanding***	***Average Rate (a)***

Junior subordinated notes:				
Capstead Mortgage Trust I	$ 36,083	8.31%	$ 36,083	8.31%
Capstead Mortgage Trust II	41,238	8.46	41,238	8.46
Capstead Mortgage Trust III	25,774	8.78	25,774	8.78
	$ 103,095	8.49	$ 103,095	8.49

(a) *Average rate is presented as of the indicated balance sheet date.*

The junior subordinated notes pay interest to the trusts quarterly calculated at fixed rates of 8.19% to 8.685% for ten years from issuance and subsequently at prevailing three-month LIBOR rates plus 3.30% to 3.50% for 20 years, reset quarterly. The trusts remit dividends pro rata to the common and preferred trust securities based on the same terms as the subordinated notes provided that payments on the trusts common securities are subordinate to payments on the related preferred securities. The Capstead

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Mortgage Trust I notes and trust securities mature in October 2035 and are redeemable, in whole or in part, without penalty, at the Company s option anytime on or after October 30, 2010. The Capstead Mortgage Trust II notes and trust securities mature in December 2035 and are redeemable, in whole or in part, without penalty, at the Company s option anytime on or after December 15, 2015. The Capstead Mortgage Trust III notes and trust securities mature in September 2036 and are redeemable, in whole or in part, without penalty, at the Company s option anytime on or after September 15, 2016. Included in *Receivables and other assets* are $2.9 million in issue costs associated with these transactions. The weighted average effective interest rate for *Unsecured borrowings* (calculated including issue cost amortization) was 8.49% for both the quarter and six months ended June 30, 2007.

NOTE 8 ¾ DISCLOSURES REGARDING FAIR VALUES OF FINANCIAL INSTRUMENTS

Fair values of Capstead s financial assets and related liabilities are influenced by changes in, and market expectations for changes in, interest rates and levels of mortgage prepayments as well as other factors beyond the control of management. Currently, only investments in mortgage securities classified as available-for-sale are reported at fair value on the Company s balance sheet with unrealized gains and losses recorded as a component of *Accumulated other comprehensive income* in stockholders equity. Fair value disclosures for available-for-sale securities were as follows (in thousands):

	Basis	*Gross Unrealized Gains*	*Gross Unrealized Losses*	*Fair Value*
As of June 30, 2007				
Agency Securities	$ 5,407,057	$ 25,080	$ 5,984	$ 5,426,153
Non-agency Securities	21,084	298	6	21,376
	$ 5,428,141	$ 25,378	$ 5,990	$ 5,447,529
As of December 31, 2006				
Agency Securities	$ 5,160,508	$ 25,160	$ 8,209	$ 5,177,459
Non-agency Securities	25,292	334	6	25,620
	$ 5,185,800	$ 25,494	$ 8,215	$ 5,203,079

Fair value disclosures for mortgage securities classified as held-to-maturity were as follows (in thousands):

	Basis	*Gross Unrealized Gains*	*Gross Unrealized Losses*	*Fair Value*
As of June 30, 2007				
Collateral released from structured financings:				
Agency Securities	$ 14,411	$ 202	$ 3	$ 14,610
Non-agency Securities	19,901	296	32	20,165
Collateral for structured financings	5,727			5,727
	$ 40,039	$ 498	$ 35	$ 40,502
As of December 31, 2006				

Collateral released from structured financings:				
Agency Securities	$ 16,542	$ 306	$ 1	$ 16,847
Non-agency Securities	24,348	328	15	24,661
Collateral for structured financings	5,795			5,795
	$ 46,685	$ 634	$ 16	$ 47,303

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Because most of the Company s investments adjust to more current rates at least annually, or will begin adjusting annually after an initial fixed-rate period, declines in fair value caused by increases in interest rates can be largely recovered in a relatively short period of time. Additionally, these declines tend to be offset by improvements in fair value of longer-dated repurchase arrangements. Given that managing a large portfolio of primarily ARM mortgage securities remains the core focus of Capstead s investment strategy, management expects these securities will be held to maturity. Consequently, temporary declines in value because of increases in interest rates would not constitute other-than-temporary impairments in value necessitating writedowns, absent a major shift in the Company s investment focus. Disclosures for mortgage securities in an unrealized loss position were as follows (in thousands):

	June 30, 2007		*December 31, 2006*	
	Fair Value	*Unrealized Loss*	*Fair Value*	*Unrealized Loss*
Securities in an unrealized loss position:				
One year or greater	$ 948,684	$ 4,997	$ 837,123	$ 6,392
Less than one year	794,876	1,028	487,144	1,839
	$ 1,743,560	$ 6,025	$ 1,324,267	$ 8,231

NOTE 9 ¾ COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) is net income plus other comprehensive income (loss), which, for the periods presented, consists primarily of the noncash change in valuation of mortgage securities classified as available-for-sale. As of June 30, 2007, the *Accumulated other comprehensive income* component of *Stockholders equity* consisted of $19.4 million in net unrealized gains on mortgage securities held available for sale and $134,000 in amounts related to terminated cash flow hedges. Disclosures related to comprehensive income (loss) were as follows (in thousands):

	Quarter Ended June 30		*Six Months Ended June 30*	
	2007	*2006*	*2007*	*2006*
Net income	$ 5,774	$ 275	$ 12,001	$ 2,986
Other comprehensive income (loss):				
Amounts related to cash flow hedges:				
Reclassification adjustment for amounts included in net income	(11)	(14)	(23)	(30)
Amounts related to securities held available-for-sale:				
Change in valuation of mortgage securities held available-for-sale	(7,357)	(8,456)	2,109	(15,974)
Other comprehensive income (loss)	(7,368)	(8,470)	2,086	(16,004)
Comprehensive income (loss)	$ (1,594)	$ (8,195)	$ 14,087	$ (13,018)

NOTE 10 ¾ LONG-TERM INCENTIVE AND OTHER PLANS

The Company sponsors long-term incentive plans to provide for the issuance of stock awards, option awards and other incentive-based equity awards to directors and employees (collectively, the Plans). As of June 30, 2007, the Plans had 1,907,957 common shares remaining available for future issuance. In May and June 2005 stock awards for a total of 172,600 common shares were issued to directors and employees (average grant date fair value: $7.86 per share) that vest proportionally over four years, subject to certain restrictions, including continuous service. In December 2006 stock awards for a total of 197,500 common shares were issued to employees (average grant date fair value: $8.19 per share) that

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vest over four years, subject to similar restrictions. Also during 2006, stock awards for 21,457 common shares were issued to a new employee and certain directors (average grant date fair value: $6.86 per share), 6,457 shares of which were vested at grant with the remaining shares vesting proportionally over three years, subject to similar restrictions. Stock award activity during the six months ended June 30, 2007 is summarized below:

	Number of Shares	*Weighted Average Grant Date Fair Value*
Stock awards outstanding as of December 31, 2006	321,550	$ 8.02
Grants issued directors	6,000	9.81
Forfeitures	(6,250)	7.97
Vested	(35,100)	7.87
Stock awards outstanding as of June 30, 2007	286,200	8.07

Option awards currently outstanding have contractual terms and vesting requirements at the grant date of up to ten years and generally have been issued with strike prices equal to the quoted market prices of the Company s common shares on the date of grant. The fair value of each option award is estimated on the date of grant using a Black-Scholes option pricing model. The Company estimates option exercises, expected holding periods and forfeitures based on past experience and current expectations for option performance and employee/director attrition. The risk-free rate is based on market rates for the expected life of the option. Expected dividends are based on historical experience and expectations for future performance. In measuring volatility factors in recent years, the Company considered volatilities experienced by certain other companies in the mortgage REIT industry in addition to historical volatilities of Capstead shares given past circumstances affecting the trading of Capstead shares not expected to reoccur. During 2005 option awards granted to directors and employees totaled 430,000 shares with an average price of $7.85 and an average fair value of $0.61 per share, which was determined using average expected terms of four years, volatility factors of 27%, dividend yields of 10% and risk-free rates of 3.76%. During 2006 option awards granted to directors and employees totaled 258,000 shares with an average price of $7.43 and an average fair value of $0.78 per share, which was determined using average expected terms of four years, volatility factors of 31%, dividend yields of 10% and risk-free rates of 4.91%. Option award activity during the six months ended June 30, 2007 is summarized below:

	Number of Shares	*Weighted Average Exercise Price*
Option awards outstanding as of December 31, 2006	855,552	$ 13.02
Grants (average fair value $0.89) [(a)]	220,500	10.46
Expirations	(53,520)	33.77
Exercises	(2,500)	7.82
Option awards outstanding as of June 30, 2007	1,020,032	$ 11.39

(a) Option awards granted during 2007 were

valued with average expected terms of four years, volatility factors of 27%, dividend yields of 10% and risk-free rates of 4.60%.

The weighted average remaining contractual term, average exercise price and aggregate intrinsic value for the 497,782 exercisable option awards outstanding as June 30, 2007 was five years, $14.12 and $692,000, respectively. The total intrinsic value of option awards exercised during 2007 and 2006 was $2,000 and $5,000, respectively. There were no exercises of option awards in 2005. Unrecognized compensation costs for all unvested equity awards totaled $2.4 million as of June 30, 2007, to be expensed over a weighted average period of two years.

The Company also sponsors a qualified defined contribution retirement plan for all employees and a nonqualified deferred compensation plan for certain of its officers. In general the Company matches up to 50% of a participant s voluntary contribution up to a maximum of 6% of a participant s compensation and discretionary contributions of up to another 3% of compensation regardless of participation in the plans. All Company contributions are subject to certain vesting requirements. Contribution expenses were $28,000 and $57,000 for the three and six months ended June 30, 2007, respectively.

NOTE 11 ¾ CAPITAL RAISING ACTIVITIES

Between May 10, 2007 and June 28, 2007 Capstead sold 137,300 of its common shares into the open market on a limited basis at an average price of $10.06 per share, after expenses, raising $1.4 million of new common equity capital. These sales were accretive to book value by $0.0136 per common share and the proceeds were invested in additional ARM Agency Securities. Such sales may resume in the third quarter.

Also during the second quarter, the Company filed a $500 million shelf registration statement with the Securities and Exchange Commission in order to facilitate raising additional common equity capital through the use of more traditional follow-on offerings if market conditions, including the availability of attractive investment opportunities, allow.

NOTE 12 ¾ NET INTEREST INCOME ANALYSIS

The following tables summarize interest income, interest expense and weighted average interest rates for *Mortgage securities and similar investments* and related changes in interest income and interest expense due to changes in interest rates versus changes in volume (dollars in thousands):

	Quarter Ended June 30					
	2007		*2006*		*Related Changes in*	
	Amount	*Average Rate*	*Amount*	*Average Rate*	*Average Rate**	*Volume**
Interest income	$ 75,795	5.57%	$ 57,349	4.77%	$ 10,323	$ 8,123
Interest expense	(67,107)	5.21	(54,685)	4.83	4,462	7,960
	$ 8,688	0.36	$ 2,664	(0.06)	$ 5,861	$ 163

	Six Months Ended June 30					
	2007		*2006*		*Related Changes in*	
	Amount	*Average Rate*	*Amount*	*Average Rate*	*Average Rate**	*Volume**
Interest income	$ 147,937	5.53%	$ 110,275	4.65%	$ 22,459	$ 15,203
Interest expense	(130,696)	5.20	(102,228)	4.61	13,851	14,617
	$ 17,241	0.33	$ 8,047	0.04	$ 8,608	$ 586

* *The change in interest income and interest expense due to both volume and rate has been allocated to*

volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

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

Overview

Capstead Mortgage Corporation (together with its subsidiaries, Capstead or the Company) operates as a real estate investment trust for federal income tax purposes (a REIT) and is based in Dallas, Texas. Capstead earns income from investing in real estate-related assets on a leveraged basis. These investments currently consist primarily of a core portfolio of residential adjustable-rate mortgage (ARM) securities issued and guaranteed by government-sponsored entities, either Fannie Mae or Freddie Mac, or by an agency of the federal government, Ginnie Mae (collectively, Agency Securities). Agency Securities carry an implied AAA rating with limited credit risk.

Capstead also seeks to opportunistically invest a portion of its long-term investment capital in commercial real estate-related assets, including subordinate commercial real estate loans that have been prudently underwritten and have attractive risk-adjusted returns. Management believes such investments can provide earnings support during periods of rising short-term interest rates. As of June 30, 2007, the Company had committed approximately 2% of its long-term investment capital to these assets down from 5% at year-end with a June 2007 payoff of a commercial loan position. The Company did not make any new commercial investments during the first half of 2007. This reflects management s cautious approach to investing in this sector and attractive opportunities that have been available to grow the Company s residential mortgage securities portfolio. Over the next several years the Company may allocate up to 20% of its long-term investment capital to this sector, as attractive opportunities become available. To this end, the Company has focused its efforts on developing and expanding capabilities and opportunities to internally source, close and monitor this type of investment.

The size and composition of Capstead s investment portfolios depend on investment strategies being implemented by management, the availability of investment capital and overall market conditions, including the availability of attractively priced investments. Market conditions are influenced by, among other things, current levels of, and expectations for future levels of, short-term interest rates and mortgage prepayments.

Capstead s long-term investment capital totaled $445 million as of June 30, 2007, consisting of $345 million in common and perpetual preferred stockholders equity and $100 million of long-term unsecured borrowings (net of related investments in statutory trusts). Common stockholders equity increased approximately $5 million from year-end, attributable primarily to a higher valuation of the Company s $5.49 billion residential mortgage securities portfolio as a result of increased portfolio yields.

Financing spreads earned on the Company s mortgage securities and similar investments (the difference between yields earned on these investments and interest rates charged on related borrowings) have continued to show improvement during the first half of 2007. Financing spreads began recovering late in 2006 after having declined steadily, despite increasing portfolio yields, due to higher borrowing rates because of actions taken by the Federal Open Market Committee (the Federal Reserve) to increase the federal funds rate a total of 425 basis points to 5.25% between June 2004 and June 2006. While interest rates on over 70% of the Company s borrowings rise (and fall) almost immediately in response to changes in short-term interest rates, yields on ARM securities change slowly by comparison because coupon interest rates on the underlying mortgage loans may reset only once a year or begin resetting after an initial fixed-rate period and the amount of each reset can be limited or capped. Yields on the Company s holdings of ARM securities are expected to continue increasing in the coming quarters. As a result, financing spreads and financial results are expected to continue to improve, provided the Federal Reserve has finished raising rates for this interest rate cycle. Should the Federal Reserve eventually lower the federal funds rate, improvements in financing spreads and financial results should be more pronounced then as described in the forward-looking statements included in this filing.

Risk Factors and Critical Accounting Policies

Under the captions Risk Factors and Critical Accounting Policies are discussions of risk factors and critical accounting policies affecting Capstead s financial condition and results of operations that are an integral part of this discussion and analysis. Readers are strongly urged to consider the potential impact of these factors and accounting policies on the Company while reading this document.

Accounting for Acquisitions of Mortgage Securities Seller-Financed using Repurchase Arrangements

Under a recent interpretation of the related accounting rules, when assets are acquired from and financed under a repurchase agreement with the same counterparty, the acquisitions may not qualify as purchases precluding buyers from presenting these assets and related borrowings gross on their balance sheets and requiring them to treat the net investment in such assets as derivative financial instruments (Derivatives) until such time as the assets are no longer financed with the sellers. The resulting Derivatives would be marked to market through earnings. Prior to year-end, the FASB is expected to finalize guidance that would require consideration as to whether Derivative accounting should be followed in situations where the acquisition and subsequent financing by a seller is sufficiently linked. Management does not believe changing the accounting treatment for any past transactions, if required, would have a material effect on Capstead s reported earnings, taxable income or financial condition and would not affect its status as a REIT or cause it to fail to qualify for its Investment Company Act exemption.

Fair Value Accounting Rule Changes

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The Company is required to adopt SFAS No. 157 on January 1, 2008. The adoption of SFAS No. 157 is not expected to have a material impact on the Company s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115* (SFAS No. 159). This statement permits, but does not require, entities to measure many financial instruments, including liabilities and certain other items, at fair value with resulting changes in fair value reported in earnings. The Company is required to adopt SFAS No. 159 on January 1, 2008 and is currently evaluating which, if any, of its financial assets or liabilities to report at fair value with related adjustments reported in earnings. Therefore, the impact, if any, that SFAS No. 159 will have on its consolidated financial statements has not been determined.

In June 2007, the AICPA issued a statement of position (SOP 07-1) addressing whether accounting principles set forth in the AICPA s audit and accounting guide for investment companies apply to an entity by clarifying the definition of an investment company for accounting purposes and eliminating a previous exclusion from the definition for REITs. SOP 07-1 has no bearing on whether an entity is considered an investment company under the Investment Company Act. Investment company accounting principles require reporting investments at fair value with the resulting changes in fair value reported in earnings. SOP 07-1 is effective January 1, 2008, concurrent with the effective date of SFAS 159. The Company is currently evaluating whether or not it meets the definition of an investment company for accounting purposes as set forth in SOP 07-1. Given that most of the Company s investments are currently reported at fair value with changes in fair value included as a component of *Stockholders equity*, the provisions of SOP 07-1, if applicable, are not expected to have a material impact on the financial condition of the Company and have no impact on future taxable income; however, future operating results may be more volatile because of the inclusion of fair value changes in reported earnings.

Residential Mortgage Investments

As of June 30, 2007, Capstead s residential mortgage securities portfolio consisted primarily of ARM Agency Securities. ARM securities held by the Company are backed by residential mortgage loans that have coupon interest rates that adjust at least annually to more current interest rates or begin doing so after an initial fixed-rate period. The Company classifies its ARM securities based on each security s average number of months until coupon reset (months-to-roll). Current-reset ARM securities have a months-to-roll of 18 months or less while longer-to-reset ARM securities have a months-to-roll of greater than 18 months. The average months-to-roll for the Company s $3.50 billion in current-reset ARM securities was less than five months as of June 30, 2007 while the average months-to-roll for the Company s $1.95 billion in longer-to-reset ARM securities was 45 months. Agency Securities carry an implied AAA-rating with limited credit risk. Non-agency securities are private mortgage pass-through securities whereby the related credit risk of the underlying loans is borne by the Company or by AAA-rated private mortgage insurers (Non-agency Securities). Mortgage securities held by Capstead are generally financed under repurchase arrangements with investment banking firms pursuant to which specific securities are pledged as collateral.

During the first six months of 2007, Capstead increased its residential mortgage securities portfolio nearly $238 million to approximately $5.49 billion with acquisitions of ARM securities totaling $1.13 billion, more than offsetting $901 million of portfolio runoff. The increase in the portfolio reflects the deployment of a modest increase in long-term investment capital primarily attributable to higher portfolio valuations due to increased portfolio yields and the reinvestment into additional ARM securities of over $9 million of capital available from the payoff of a commercial loan investment.

Mortgage prepayments increased slightly during the second quarter of 2007 to an annualized runoff rate of 30% from 28% during the first quarter. Since Capstead typically purchases investments at a premium to the asset s unpaid principal balance, high levels of mortgage prepayments can put downward pressure on ARM security yields because the level of mortgage prepayments impacts how quickly these investment premiums are written off against earnings as portfolio yield adjustments. Prepayments are generally lower during the winter months reflecting seasonal housing patterns in the United States. As the underlying coupon interest rates on the Company s current-reset ARM securities reset higher, more of these loans become susceptible to prepayment if prevailing mortgage interest rates provide an incentive for homeowners with ARM loans to refinance and lock in attractive longer-term interest rates. Conversely, higher mortgage interest rates can ease prepayment pressures by removing much of this incentive to refinance. Additionally, ARM loans with initial fixed-rate periods tend to prepay relatively quickly as the initial fixed-rate period approaches. Since the Company began significantly increasing the residential mortgage securities portfolio in late 2005, the overall focus has been on acquiring securities with relatively low investment premiums and limited prepay protection, when available at attractive pricing, which has helped lessen the Company s exposure to higher levels of prepayments.

Commercial Real Estate-related Assets

Over the next several years, Capstead may allocate up to 20% of its long-term investment capital to investments in credit-sensitive commercial real estate-related assets, which will typically consist of subordinate mortgage loans, or mezzanine debt supported by interests in commercial real estate, that have been prudently underwritten and have attractive risk-adjusted returns. This strategy is designed to augment the Company s core portfolio of residential ARM securities by providing an additional earnings stream that can help support overall earnings during periods of rising short-term interest rates. As of June 30, 2007, the Company had committed approximately 2% of its long-term investment capital to these assets down from 5% at year-end with a June 2007 payoff of a commercial loan position. No new commercial investments were made during 2007. This reflects management s cautious approach to this sector and attractive opportunities that have been available to grow the Company s core portfolio of residential mortgage securities. Over the past year the Company focused its efforts on developing and expanding its capabilities and opportunities to make these investments and the Company is now in a position to internally source, close and monitor these more complicated and labor-intensive investments.

Commercial mortgage investments as of June 30, 2007 consisted of $7 million invested in a 75%-owned limited partnership with Crescent Real Estate Equities Company (NYSE: CEI), and several loans totaling less than $3 million to a Dallas, Texas-based developer. The Company s investment in the commercial loan partnership is reflected as an unconsolidated affiliate and the commercial loans are included with mortgage securities and similar investments on the Company s balance sheet.

The partnership with CEI was formed to invest in a leveraged portfolio of subordinated commercial real estate loans meeting certain criteria over a two-year investment period that ended in July 2007. CEI sourced investment opportunities (subject to Capstead s approval) and manages the loan portfolio earning management fees and incentives based on portfolio performance. Investments made by the partnership are currently financed using a committed master repurchase agreement with a major investment banking firm. Amounts available to be borrowed under this facility and related borrowing rates are dependent upon the characteristics of the pledged collateral and can change based on changes in the fair value of the pledged collateral with quarterly repayments of amounts drawn beginning November 1, 2007. As of June 30, 2007, the partnership had borrowed $29 million under this facility to fund investments totaling $38 million consisting of junior liens on a luxury hospitality property in the Caribbean. On August 3, 2007 CEI announced the completion of the proposed acquisition of CEI by affiliates of Morgan Stanley (NYSE: MS) which was approved by a majority vote of CEI s stockholders on August 1, 2007. Capstead is currently evaluating several options relative to the partnership with an expected resolution by year-end.

Book Value per Common Share

The combination of Capstead s reported book value per common share and the mark-to-market of its longer-term borrowings supporting investments in longer-to-reset ARM securities increased during the second quarter and year-to-date by $0.07 and $0.45, respectively, primarily as a result of steadily increasing portfolio yields. Reported book value per common share declined $0.37 during the second quarter to $8.32 as of June 30, 2007 after having increased $0.56 during the first quarter, for a net increase of $0.19 year-to-date. The second quarter book value decline was more than offset by an increase in the fair value of the above-mentioned longer-term borrowings, which are excluded from the calculation of book value for financial reporting purposes. These borrowings improved in value by $0.44 during the second quarter to an unrealized gain of $0.41 as of June 30, 2007 after having declined in value $0.18 during the first quarter, for a net improvement of $0.26 year-to-date.

Reported book value per common share is calculated considering the liquidation preferences of the Company s Series A and B preferred shares and includes unrealized gains and losses on the Company s residential mortgage securities, most of which are carried at fair value with changes in fair value reflected in stockholders equity. The fair value of the Company s residential mortgage securities can be expected to fluctuate with changes in portfolio size and composition as well as changes in interest rates and market liquidity, and such changes will largely be reflected in book value per common share. Because most of the Company s investments adjust to more current rates at least annually, declines in fair value caused by increases in interest rates can be largely recovered in a relatively short period of time. Book value will also be affected by other factors, including capital stock transactions and the level of dividend distributions relative to quarterly operating results; however, temporary changes in fair value of investments not held in the form of securities, such as commercial real estate loans, generally will not affect book value. As noted above, the fair value of the Company s liabilities, such as its longer-term borrowings supporting investments in longer-to-reset ARM securities, are not reflected in book value.

The fair value of these liabilities tends to move in the opposite direction as the fair value of the related longer-to-reset securities.

Mortgage Securities and Similar Investments Yield and Cost Analysis

The following yield and cost analysis illustrates results achieved during the second quarter of 2007 for the Company s mortgage securities and similar investments and projected third quarter 2007 annualized portfolio yields, borrowing rates and financing spreads given the assumptions more fully described in the accompanying notes (dollars in thousands):

	2nd Quarter Average			As of June 30, 2007		Projected 3rd Quarter Yield/Cost	Lifetime Runoff
	Basis *(a)*	***Yield/Cost***	***Runoff***	***Premiums***	***Basis*** *(a)*	*(b)*	***Assumptions***
Agency Securities:							
Fannie Mae/Freddie Mac:							
Fixed-rate	$ 15,294	6.36%	24%	$ 43	$ 14,697	6.42%	38%
ARMs	4,722,469	5.56	29	65,873	4,780,994	5.70	31
Ginnie Mae ARMs	657,306	5.45	36	2,698	625,777	5.60	29
	5,395,069	5.55					