

PENNYMAC FINANCIAL SERVICES, INC.

Form 10-Q

August 08, 2017

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

---

Form 10-Q

---

(Mark One)

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

For the quarterly period ended June 30, 2017

Or

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

For the transition period from            to

Commission file number: 001-35916

---

PennyMac Financial Services, Inc.

(Exact name of registrant as specified in its charter)

---

Delaware	80-0882793
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

3043 Townsgate Road, Westlake Village, California	91361
(Address of principal executive offices)	(Zip Code)

(818) 224-7442

(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 No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated

filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Indicate the number of shares outstanding of each of the registrant’s classes of common stock, as of the latest practicable date.

Class	Outstanding at August 4, 2017
Class A Common Stock, \$0.0001 par value	23,510,542
Class B Common Stock, \$0.0001 par value	50

Table of Contents

PENNYMAC FINANCIAL SERVICES, INC.

FORM 10-Q

June 30, 2017

TABLE OF CONTENTS

	Page
<u>Special Note Regarding Forward-Looking Statements</u>	3
<u>PART I. FINANCIAL INFORMATION</u>	5
<u>Item 1.</u>	5
<u>Consolidated Balance Sheets</u>	5
<u>Consolidated Statements of Income</u>	6
<u>Consolidated Statements of Changes in Stockholders' Equity</u>	7
<u>Consolidated Statements of Cash Flows</u>	8
<u>Notes to Consolidated Financial Statements</u>	9
<u>Item 2.</u> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	64
<u>Item 3.</u> <u>Quantitative and Qualitative Disclosures About Market Risk</u>	80
<u>Item 4.</u> <u>Controls and Procedures</u>	80
<u>PART II. OTHER INFORMATION</u>	82
<u>Item 1.</u> <u>Legal Proceedings</u>	82
<u>Item 1A.</u> <u>Risk Factors</u>	82
<u>Item 2.</u> <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	82
<u>Item 3.</u> <u>Defaults Upon Senior Securities</u>	82
<u>Item 4.</u> <u>Mine Safety Disclosures</u>	82
<u>Item 5.</u> <u>Other Information</u>	82
<u>Item 6.</u> <u>Exhibits</u>	83



Table of Contents

SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (“Report”) contains certain forward looking statements that are subject to various risks and uncertainties. Forward looking statements are generally identifiable by use of forward looking terminology such as “may,” “will,” “should,” “potential,” “intend,” “expect,” “seek,” “anticipate,” “estimate,” “approximately,” “believe,” “predict,” “continue,” “plan” or other similar words or expressions.

Forward looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain financial and operating projections or state other forward looking information. Examples of forward looking statements include the following:

- projections of our revenues, income, earnings per share, capital structure or other financial items;
- descriptions of our plans or objectives for future operations, products or services;
- forecasts of our future economic performance, interest rates, profit margins and our share of future markets; and
- descriptions of assumptions underlying or relating to any of the foregoing expectations regarding the timing of generating any revenues.

Our ability to predict results or the actual effect of future events, actions, plans or strategies is inherently uncertain. Although we believe that the expectations reflected in such forward looking statements are based on reasonable assumptions, our actual results and performance could differ materially from those set forth in the forward looking statements. There are a number of factors, many of which are beyond our control that could cause actual results to differ significantly from management’s expectations. Some of these factors are discussed below.

You should not place undue reliance on any forward looking statement and should consider the following uncertainties and risks, as well as the risks and uncertainties discussed elsewhere in this Report and the section entitled “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2016, filed with the Securities and Exchange Commission (“SEC”) on March 9, 2017.

Factors that could cause actual results to differ materially from historical results or those anticipated include, but are not limited to:

- the continually changing federal, state and local laws and regulations applicable to the highly regulated industry in which we operate;
- lawsuits or governmental actions if we do not comply with the laws and regulations applicable to our businesses;
- the mortgage lending and servicing-related regulations promulgated by the Consumer Financial Protection Bureau (“CFPB”) and its enforcement of these regulations;
- our dependence on U.S. government sponsored entities and changes in their current roles or their guarantees or guidelines;

- changes to government mortgage modification programs;
- certain banking regulations that may limit our business activities;
- foreclosure delays and changes in foreclosure practices;
- the licensing and operational requirements of states and other jurisdictions applicable to our businesses, to which our bank competitors are not subject;
- our dependence on the multi-family and commercial real estate sectors for future originations and investments in commercial mortgage loans and other commercial real estate related loans;
- changes in macroeconomic and U.S. real estate market conditions;
- difficulties inherent in growing loan production volume;
- difficulties inherent in adjusting the size of our operations to reflect changes in business levels;

Table of Contents

- any required additional capital and liquidity to support business growth that may not be available on acceptable terms, if at all;
- changes in prevailing interest rates;
- increases in loan delinquencies and defaults;
- our dependence on the success of the small balance multifamily market for future originations of commercial mortgage loans and other commercial real estate-related loans;
- our reliance on PennyMac Mortgage Investment Trust (“PMT”) as a significant source of financing for, and revenue related to, our mortgage banking business;
- our obligation to indemnify third party purchasers or repurchase loans if loans that we originate, acquire, service or assist in the fulfillment of, fail to meet certain criteria or characteristics or under other circumstances;
  
- our ability to realize the anticipated benefit of potential future acquisitions of mortgage servicing rights (“MSRs”);
- our obligation to indemnify PMT and certain investment funds if our services fail to meet certain criteria or characteristics or under other circumstances;
- decreases in the returns on the assets that we select and manage for our clients, and our resulting management and incentive fees;
- the extensive amount of regulation applicable to our investment management segment;
- conflicts of interest in allocating our services and investment opportunities among ourselves and certain advised entities;
- the effect of public opinion on our reputation;
- our recent growth;
- our ability to effectively identify, manage, monitor and mitigate financial risks;
- our initiation of new business activities or expansion of existing business activities;
  - our ability to detect misconduct and fraud; and
- our ability to mitigate cybersecurity risks and cyber incidents.

Other factors that could also cause results to differ from our expectations may not be described in this Report or any other document. Each of these factors could by itself, or together with one or more other factors, adversely affect our business, results of operations and/or financial condition.

Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update any forward-looking statement to reflect the impact of circumstances or events that arise after the date the forward-looking statement was made.



Table of Contents

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	June 30, 2017	December 31, 2016
	(in thousands, except share amounts)	
<b>ASSETS</b>		
Cash (includes \$50,458 and \$91,788 pledged to creditors)	\$ 75,978	\$ 99,367
Short-term investments at fair value	145,440	85,964
Mortgage loans held for sale at fair value (includes \$3,019,088 and \$2,125,174 pledged to creditors)	3,037,602	2,172,815
Derivative assets	70,075	82,905
Servicing advances, net (includes valuation allowance of \$48,161 and \$45,425; \$72,010 and \$81,306 pledged to creditors)	291,907	348,306
Carried Interest due from Investment Funds pledged to creditors	71,019	70,906
Investment in PennyMac Mortgage Investment Trust at fair value	1,372	1,228
Mortgage servicing rights (includes \$678,441 and \$515,925 at fair value; \$1,736,119 and \$1,617,671 pledged to creditors)	1,951,599	1,627,672
Real estate acquired in settlement of loans	822	1,418
Furniture, fixtures, equipment and building improvements, net (includes \$27,476 and \$25,134 pledged to creditors)	31,418	31,321
Capitalized software, net (includes \$1,797 and \$515 pledged to creditors)	18,197	11,205
Assets purchased from PennyMac Mortgage Investment Trust under agreements to resell pledged to creditors	150,000	150,000
Receivable from PennyMac Mortgage Investment Trust	17,725	16,416
Receivable from Investment Funds	1,330	1,219
Mortgage loans eligible for repurchase	462,487	382,268
Other	77,767	50,892
Total assets	\$ 6,404,738	\$ 5,133,902
<b>LIABILITIES</b>		
Assets sold under agreements to repurchase	\$ 3,021,328	\$ 1,735,114
Mortgage loan participation and sale agreements	243,361	671,426
Notes payable	429,692	150,942
Obligations under capital lease	26,641	23,424
Excess servicing spread financing payable to PennyMac Mortgage Investment Trust at fair value	261,796	288,669
Derivative liabilities	16,564	22,362
Accounts payable and accrued expenses	132,053	134,611
Mortgage servicing liabilities at fair value	18,295	15,192
Payable to Investment Funds	15,236	20,393
Payable to PennyMac Mortgage Investment Trust	132,709	170,036

Payable to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement	73,084	75,954
Income taxes payable	40,672	25,088
Liability for mortgage loans eligible for repurchase	462,487	382,268
Liability for losses under representations and warranties	19,568	19,067
Total liabilities	4,893,486	3,734,546

Commitments and contingencies – See Note 20

#### STOCKHOLDERS' EQUITY

Class A common stock—authorized 200,000,000 shares of \$0.0001 par value; issued and outstanding, 23,472,795 and 22,426,779 shares, respectively	2	2
Class B common stock—authorized 1,000 shares of \$0.0001 par value; issued and outstanding, 50 and 49 shares, respectively	—	—
Additional paid-in capital	199,146	182,772
Retained earnings	185,907	164,549
Total stockholders' equity attributable to PennyMac Financial Services, Inc. common stockholders	385,055	347,323
Noncontrolling interest in Private National Mortgage Acceptance Company, LLC	1,126,197	1,052,033
Total stockholders' equity	1,511,252	1,399,356
Total liabilities and stockholders' equity	\$ 6,404,738	\$ 5,133,902

Table of Contents

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

## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands, except earnings per share)			
Revenues				
Net gains on mortgage loans held for sale at fair value:				
From non-affiliates	\$ 99,597	\$ 132,118	\$ 188,248	\$ 225,594
Recapture payable to PennyMac Mortgage Investment Trust	(1,506)	(1,915)	(3,201)	(3,867)
	98,091	130,203	185,047	221,727
Mortgage loan origination fees:				
From non-affiliates	28,303	27,443	52,498	48,870
From PennyMac Mortgage Investment Trust	1,890	1,464	3,269	2,471
	30,193	28,907	55,767	51,341
Fulfillment fees from PennyMac Mortgage Investment Trust	21,107	19,111	37,677	32,046
Net mortgage loan servicing fees:				
Mortgage loan servicing fees:				
From non-affiliates	112,348	92,770	218,815	184,097
From PennyMac Mortgage Investment Trust	10,099	16,427	20,585	27,880
From Investment Funds	543	723	1,039	1,424
Ancillary and other fees	11,202	10,818	23,068	22,270
	134,192	120,738	263,507	235,671
Amortization, impairment and change in fair value of mortgage servicing rights and mortgage servicing liabilities	(94,435)	(111,611)	(152,360)	(228,474)
Change in fair value of excess servicing spread payable to PennyMac Mortgage Investment Trust	7,156	17,428	9,929	36,877
	(87,279)	(94,183)	(142,431)	(191,597)
Net mortgage loan servicing fees	46,913	26,555	121,076	44,074
Management fees:				
From PennyMac Mortgage Investment Trust	5,638	5,199	10,646	10,551
From Investment Funds	369	531	735	1,091
	6,007	5,730	11,381	11,642
Carried Interest from Investment Funds	241	244	113	837
Net interest expense:				
Interest income:				
From non-affiliates	32,948	18,332	55,002	30,259
From PennyMac Mortgage Investment Trust	2,025	2,222	3,830	3,824
	34,973	20,554	58,832	34,083
Interest expense:				
To non-affiliates	32,511	19,753	57,338	33,725
To PennyMac Mortgage Investment Trust	4,366	5,713	9,013	12,728

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

	36,877	25,466	66,351	46,453
Net interest expense	(1,904)	(4,912)	(7,519)	(12,370)
Change in fair value of investment in and dividends received from PennyMac Mortgage Investment Trust	76	229	215	143
Results of real estate acquired in settlement of loans	(119)	393	(144)	(42)
Other	1,116	1,346	2,581	1,809
Total net revenues	201,721	207,806	406,194	351,207
Expenses				
Compensation	82,967	83,147	168,207	151,445
Servicing	24,702	13,430	51,545	34,317
Technology	11,581	7,733	22,937	14,580
Loan origination	5,116	4,910	9,249	9,096
Professional services	4,523	4,559	8,341	8,292
Other	14,872	9,769	25,923	19,080
Total expenses	143,761	123,548	286,202	236,810
Income before provision for income taxes	57,960	84,258	119,992	114,397
Provision for income taxes	7,214	9,963	14,860	13,559
Net income	50,746	74,295	105,132	100,838
Less: Net income attributable to noncontrolling interest	40,267	59,820	83,774	81,188
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 10,479	\$ 14,475	\$ 21,358	\$ 19,650
Earnings per common share				
Basic	\$ 0.45	\$ 0.66	\$ 0.93	\$ 0.89
Diluted	\$ 0.44	\$ 0.65	\$ 0.91	\$ 0.89
Weighted average common shares outstanding				
Basic	23,388	22,078	23,006	22,042
Diluted	77,650	76,280	77,641	76,236

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

Table of Contents

## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)

	Class A Common Stock				Noncontrolling interest in Private National Mortgage Acceptance Company, LLC	Total stockholders' equity
	Number of shares (in thousands)	Par value	Additional paid-in capital	Retained earnings		
Balance at December 31, 2015	21,991	\$ 2	\$ 172,354	\$ 98,470	\$ 791,524	\$ 1,062,350
Net income	—	—	—	19,650	81,188	100,838
Stock and unit-based compensation	93	—	2,119	—	5,917	8,036
Issuance of Class A common stock in settlement of directors' fees	12	—	149	—	—	149
Exchange of Class A units of Private National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	93	—	2,640	—	(2,640)	—
Tax effect of exchange of Class A units of Private National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	—	—	(520)	—	—	(520)
Balance at June 30, 2016	22,189	\$ 2	\$ 176,742	\$ 118,120	\$ 875,989	\$ 1,170,853
Balance at December 31, 2016	22,427	\$ 2	\$ 182,772	\$ 164,549	\$ 1,052,033	\$ 1,399,356
Net income	—	—	—	21,358	83,774	105,132
Stock and unit-based compensation	—	—	3,450	—	7,256	10,706
Issuance of Class A common stock in settlement of directors' fees	—	—	108	—	61	169
Exchange of Class A units of Private National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	1,046	—	16,927	—	(16,927)	—
	—	—	(4,111)	—	—	(4,111)

Tax effect of exchange of Class  
A units of Private National  
Mortgage Acceptance  
Company, LLC to Class A  
common stock of PennyMac  
Financial Services, Inc.

Balance at June 30, 2017	23,473	\$ 2	\$ 199,146	\$ 185,907	\$ 1,126,197	\$ 1,511,252
--------------------------	--------	------	------------	------------	--------------	--------------

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

Table of Contents

## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six months ended June 30,	
	2017	2016
	(in thousands)	
Cash flow from operating activities		
Net income	\$ 105,132	\$ 100,838
Adjustments to reconcile net income to net cash used in operating activities:		
Net gains on mortgage loans held for sale at fair value	(185,047)	(221,727)
Accrual of servicing rebate payable to Investment Funds	100	148
Amortization, impairment and change in fair value of mortgage servicing rights, mortgage servicing liabilities and excess servicing spread	142,431	191,597
Carried Interest from Investment Funds	(113)	(837)
Capitalization of interest on mortgage loans held for sale at fair value	(21,615)	(13,513)
Accrual of interest on excess servicing spread financing	9,013	12,728
Amortization of debt issuance costs	7,122	5,215
Change in fair value of investment in common shares of PennyMac Mortgage Investment Trust	(144)	(72)
Results of real estate acquired in settlement in loans	144	42
Stock and unit-based compensation expense	10,390	8,036
Provision for servicing advance losses	18,030	12,519
Loss from disposition of fixed assets	377	—
Depreciation and amortization	4,117	2,274
Purchase of mortgage loans held for sale from PennyMac Mortgage Investment Trust	(21,244,194)	(16,783,840)
Originations of mortgage loans held for sale	(2,353,899)	(2,736,621)
Purchase of mortgage loans from Ginnie Mae securities and early buyout investors for modification and subsequent sale	(1,814,080)	(703,464)
Sale and principal payments of mortgage loans held for sale	24,497,179	19,176,697
Sale of mortgage loans held for sale to PennyMac Mortgage Investment Trust	40,222	8,139
Repurchase of mortgage loans subject to representations and warranties	(11,520)	(11,399)
Decrease (increase) in servicing advances	38,821	(11,182)
Increase in receivable from Investment Funds	(211)	(120)
Increase in receivable from PennyMac Mortgage Investment Trust	(1,092)	(2,056)
Decrease in deferred tax asset	—	13,515
Payments to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement	(6,221)	—
Increase in other assets	(29,608)	(10,941)
(Decrease) increase in accounts payable and accrued expenses	(30,395)	9,781
Decrease in payable to Investment Funds	(5,157)	(2,220)
Decrease in payable to PennyMac Mortgage Investment Trust	(37,650)	(2,332)
Increase in income taxes payable	14,824	—
Net cash used in operating activities	(853,044)	(958,795)

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Cash flow from investing activities		
(Increase) decrease in short-term investments	(59,476)	5,256
Net settlement of derivative financial instruments used for hedging	(30,949)	138,801
Purchase of mortgage servicing rights	(159,465)	(11)
Purchase of furniture, fixtures, equipment and leasehold improvements	(4,668)	(14,459)
Acquisition of capitalized software	(7,719)	(3,342)
Increase in margin deposits and restricted cash	(12,071)	(16,443)
Net cash (used in) provided by investing activities	(274,348)	109,802
Cash flow from financing activities		
Sale of assets under agreements to repurchase	13,332,610	18,461,897
Repurchase of assets sold under agreements to repurchase	(12,046,244)	(18,037,356)
Issuance of mortgage loan participation certificates	10,491,796	10,843,858
Repayment of mortgage loan participation certificates	(10,919,650)	(10,341,436)
Advances on notes payable	435,000	68,000
Repayment of notes payable	(153,073)	(15,671)
Advances of obligations under capital lease	10,298	12,652
Repayment of obligations under capital lease	(7,081)	(3,345)
Repayment of excess servicing spread financing	(28,910)	(38,281)
Settlement of excess servicing spread financing	—	(59,045)
Payment of debt issuance costs	(11,059)	(4,037)
Proceeds from common stock options exercised	316	—
Net cash provided by financing activities	1,104,003	887,236
Net (decrease) increase in cash	(23,389)	38,243
Cash at beginning of period	99,367	105,472
Cash at end of period	\$ 75,978	\$ 143,715

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



Table of Contents

PENNYMAC FINANCIAL SERVICES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1—Organization and Basis of Presentation

PennyMac Financial Services, Inc. (“PFSI” or the “Company”) was formed as a Delaware corporation on December 31, 2012. Pursuant to a reorganization, the Company became a holding corporation and its primary asset is an equity interest in Private National Mortgage Acceptance Company, LLC (“PennyMac”). The Company is the managing member of PennyMac and operates and controls all of the businesses and affairs of PennyMac subject to the consent rights of other members under certain circumstances, and consolidates the financial results of PennyMac and its subsidiaries.

PennyMac is a Delaware limited liability company which, through its subsidiaries, engages in mortgage banking and investment management activities. PennyMac’s mortgage banking activities consist of residential mortgage loan production (including correspondent production and consumer direct lending) and mortgage loan servicing. PennyMac’s investment management activities and a portion of its mortgage loan servicing activities are conducted on behalf of entities that invest in residential mortgage loans and related assets. PennyMac’s primary wholly owned subsidiaries are:

- PNMAC Capital Management, LLC (“PCM”)—a Delaware limited liability company registered with the Securities and Exchange Commission (“SEC”) as an investment adviser under the Investment Advisers Act of 1940, as amended. PCM enters into investment management agreements with entities that invest in residential mortgage loans and related assets.

Presently, PCM has management agreements with, PNMAC Mortgage Opportunity Fund, LLC and PNMAC Mortgage Opportunity Fund, L.P. (the “Master Fund”), both registered under the Investment Company Act of 1940, as amended, an affiliate of these registered funds, PNMAC Mortgage Opportunity Fund Investors, LLC (collectively, the “Investment Funds”) and PennyMac Mortgage Investment Trust (“PMT”), a publicly held real estate investment trust (“REIT”). Together, the Investment Funds and PMT are referred to as the “Advised Entities.”

- PennyMac Loan Services, LLC (“PLS”)—a Delaware limited liability company that services residential mortgage loans on behalf of non-affiliates and the Advised Entities, purchases and originates new prime credit quality residential mortgage loans, and engages in other mortgage banking activities for its own account and the account of PMT.

PLS is approved as a seller/servicer of mortgage loans by the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Corporation (“Freddie Mac”) and as an issuer of securities guaranteed by the

Government National Mortgage Association (“Ginnie Mae”). PLS is a licensed Federal Housing Administration Nonsupervised Title II Lender with the U.S. Department of Housing and Urban Development (“HUD”) and a lender/servicer with the Veterans Administration (“VA”) and U.S. Department of Agriculture (“USDA”) (each an “Agency” and collectively the “Agencies”).

- PNMAC Opportunity Fund Associates, LLC (“PMOFA”)—a Delaware limited liability company and the general partner of the Master Fund. PMOFA is entitled to incentive fees representing allocations of profits (“Carried Interest”) from the Master Fund.

The accompanying consolidated financial statements have been prepared in compliance with accounting principles generally accepted in the United States (“GAAP”) as codified in the Financial Accounting Standards Board’s (“FASB”) Accounting Standards Codification (“ASC”) for interim financial information and with the SEC’s instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these financial statements and notes do not include all of the information required by GAAP for complete financial statements. The interim consolidated information should be read together with the Company’s Annual Report on Form 10-K for the year ended December 31, 2016.

The accompanying unaudited consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, income, and cash flows for the interim periods, but are not necessarily

Table of Contents

indicative of income to be anticipated for the full year ending December 31, 2017. Intercompany accounts and transactions have been eliminated.

Preparation of financial statements in compliance with GAAP requires management to make judgments and estimates that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the reporting period. Actual results will likely differ from those estimates.

Note 2—Concentration of Risk

A substantial portion of the Company's activities relate to the Advised Entities. Revenues generated from these entities (generally comprised of servicing recapture fees, mortgage loan origination fees, fulfillment fees, mortgage loan servicing fees, management fees, Carried Interest, and net interest charged to these entities) totaled 21% and 26% of total net revenue for the quarters ended June 30, 2017 and 2016, respectively, and 19% and 28% for the six months ended June 30, 2017 and 2016, respectively.

Note 3—Transactions with Affiliates

Transactions with PMT

Operating Activities

Mortgage Loan Production Activities and Mortgage Servicing Rights ("MSR") Recapture

The Company provides fulfillment and other services to PMT under a mortgage banking services agreement. Before September 12, 2016, the Company was entitled to a fulfillment fee based on the type of mortgage loan that PMT acquired and equal to a percentage of the unpaid principal balance ("UPB") of such mortgage loan. The applicable fulfillment fee percentages were (i) 0.50% for conventional mortgage loans, (ii) 0.88% for loans sold in accordance with the Ginnie Mae Mortgage Backed Securities Guide, and (iii) 0.50% for all other mortgage loans not contemplated above; provided, however, that the Company was permitted, in its sole discretion, to reduce the amount of the applicable fulfillment fee and credit the amount of such reduction to the reimbursement otherwise due as described below. This reduction was only credited to the reimbursement applicable to the month in which the related mortgage loan was funded.

Effective September 12, 2016, pursuant to the terms of an amended and restated mortgage banking services agreement, the applicable fulfillment fee percentages are (i) 0.35% for mortgage loans sold or delivered to Fannie Mae or Freddie Mac, and (ii) 0.85% for all other mortgage loans; provided, however, that no fulfillment fee shall be due or payable to the Company with respect to any mortgage loans underwritten to Ginnie Mae guidelines. PMT does not hold the Ginnie Mae approval required to issue Ginnie Mae mortgage-backed securities (“MBS”) and act as a servicer. Accordingly, under the agreement, the Company currently purchases mortgage loans underwritten in accordance with the Ginnie Mae Mortgage-Backed Securities Guide “as is” and without recourse of any kind from PMT at PMT’s cost less an administrative fee plus accrued interest and a sourcing fee ranging from two to three and one-half basis points, generally based on the average number of calendar days mortgage loans are held by PMT before being purchased by the Company.

In consideration for the mortgage banking services provided by the Company with respect to PMT’s acquisition of mortgage loans under the Company’s early purchase program, the Company is entitled to fees accruing (i) at a rate equal to \$1,500 per year per early purchase facility administered by the Company, and (ii) in the amount of \$35 for each mortgage loan that PMT acquires thereunder.

Pursuant to the terms of an amended and restated MSR recapture agreement, effective September 12, 2016, if the Company refinances mortgage loans for which PMT previously held the MSRs, the Company is generally required to transfer and convey to one of PMT’s wholly owned subsidiaries, without cost to PMT, the MSRs with respect to new mortgage loans originated in those refinancings (or, under certain circumstances, other mortgage loans) that have an aggregate UPB that is not less than 30% of the aggregate UPB of all the mortgage loans so originated.

Table of Contents

Where the fair value of the aggregate MSR to be transferred for the applicable month is less than \$200,000, the Company may, at its option, pay cash to PMT in an amount equal to such fair value instead of transferring such MSRs. The MSR recapture agreement expires, unless terminated earlier in accordance with the agreement, on September 12, 2020, subject to automatic renewal for additional 18-month periods, unless terminated earlier in accordance with the terms of the agreement.

Following is a summary of mortgage loan production activities and MSR recapture between the Company and PMT:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Mortgage servicing rights and excess servicing spread recapture incurred included in Net gains on mortgage loans held for sale at fair value	\$ 1,506	\$ 1,915	\$ 3,201	\$ 3,867
Fulfillment fee revenue	\$ 21,107	\$ 19,111	\$ 37,677	\$ 32,046
Unpaid principal balance of mortgage loans fulfilled for PMT	\$ 5,918,027	\$ 5,174,020	\$ 10,549,933	\$ 8,433,383
Sourcing fees paid to PMT	\$ 3,204	\$ 2,824	\$ 6,065	\$ 4,773
Unpaid principal balance of mortgage loans purchased from PMT	\$ 10,641,243	\$ 9,409,399	\$ 20,215,960	\$ 15,905,121
Proceeds from sale of mortgage loans held for sale to PMT	\$ 18,692	\$ 3,424	\$ 40,222	\$ 8,139
Tax service fees received from PMT included in Mortgage loan origination fees	\$ 1,890	\$ 1,464	\$ 3,269	\$ 2,471
Property management fees received from PMT included in Other income	\$ 95	\$ 54	\$ 166	\$ 85
Early purchase program fees earned from PMT included in Mortgage loan servicing fees	\$ 1	\$ 1	\$ 6	\$ 2

## Mortgage Loan Servicing

The Company has a loan servicing agreement with PMT (“Servicing Agreement”). The Servicing Agreement provides for servicing fees of per loan monthly amounts based on the delinquency, bankruptcy and/or foreclosure status of the serviced mortgage loan or the real estate acquired in settlement of loans (“REO”). The Company also remains entitled to customary ancillary income and market-based fees and charges, including boarding and deboarding fees, liquidation and disposition fees, assumption, modification and origination fees and late charges relating to mortgage loans it services for PMT. The Servicing Agreement was amended and restated as of September 12, 2016; however, the fee

structure was not amended in any material respect.

- The base servicing fee rates for distressed whole mortgage loans range from \$30 per month for current loans up to \$100 per month for loans where the borrower has declared bankruptcy. The base servicing fee rate for REO is \$75 per month. To the extent the Company facilitates rentals of PMT's REO under its REO rental program, the Company collects an REO rental fee of \$30 per month per REO, an REO property lease renewal fee of \$100 per lease renewal, and a property management fee in an amount equal to the Company's cost if property management services and/or any related software costs are outsourced to a third-party property management firm or 9% of gross rental income if the Company provides property management services directly. The Company is also entitled to retain any tenant paid application fees and late rent fees and seek reimbursement for certain third-party vendor fees.
- The base servicing fees for non-distressed mortgage loans are calculated through a monthly per-loan dollar amount, with the actual dollar amount for each loan based on whether the mortgage loan is a fixed-rate or adjustable-rate loan. The base servicing fee rates are \$7.50 per month and \$8.50 per month for fixed-rate loans and adjustable-rate loans, respectively.

Table of Contents

- The Company is also entitled to certain activity-based fees for distressed whole mortgage loans that are charged based on the achievement of certain events. These fees range from 0.50% for a streamline modification to 1.50% for a liquidation and \$500 for a deed-in-lieu of foreclosure. The Company is not entitled to earn more than one liquidation fee, reperformance fee or modification fee per mortgage loan in any 18-month period.
- Because PMT has limited employees and infrastructure, the Company is required to provide a range of services and activities significantly greater in scope than the services provided in connection with a customary servicing arrangement. For these services, the Company receives a supplemental servicing fee of \$25 per month for each distressed mortgage loan. The Company is entitled to reimbursement for all customary, good faith reasonable and necessary out-of-pocket expenses incurred by the Company in performance of its servicing obligations.
- Except as otherwise provided in the MSR recapture agreement, when the Company effects a refinancing of a mortgage loan on behalf of PMT and not through a third-party lender and the resulting mortgage loan is readily saleable, or the Company originates a loan to facilitate the disposition of a REO, the Company is entitled to receive from PMT market-based fees and compensation consistent with pricing and terms the Company offers unaffiliated parties on a retail basis.
- The Company is entitled to retain any incentive payments made to it and to which it is entitled under the U.S. Department of Treasury's Home Affordable Modification Plan ("HAMP"); provided, however, that with respect to any such incentive payments paid to the Company in connection with a mortgage loan modification for which PMT previously paid the Company a modification fee, the Company is required to reimburse PMT an amount equal to the incentive payments.

The Servicing Agreement expires on September 12, 2020, subject to automatic renewal for additional 18-month periods, unless terminated earlier in accordance with the terms of the agreement.

Following is a summary of mortgage loan servicing fees earned from PMT:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands)			
Mortgage loans acquired for sale at fair value:				
Base and supplemental	\$ 82	\$ 79	\$ 147	\$ 135
Activity-based	176	172	319	287
	258	251	466	422
Mortgage loans at fair value:				
Base and supplemental	1,754	2,959	3,713	6,359
Activity-based	1,767	8,518	4,157	11,967
	3,521	11,477	7,870	18,326

Mortgage servicing rights:				
Base and supplemental	6,188	4,583	12,025	8,927
Activity-based	132	116	224	205
	6,320	4,699	12,249	9,132
	\$ 10,099	\$ 16,427	\$ 20,585	\$ 27,880

#### Investment Management Activities

The Company has a management agreement with PMT (“Management Agreement”). The Management Agreement provides that:

- The base management fee is calculated quarterly and is equal to the sum of (i) 1.5% per year of PMT’s average shareholders’ equity up to \$2 billion, (ii) 1.375% per year of PMT’s average shareholders’ equity in excess of \$2 billion and up to \$5 billion, and (iii) 1.25% per year of PMT’s average shareholders’ equity in excess of \$5 billion.



Table of Contents

- The performance incentive fee is calculated quarterly at a defined annualized percentage of the amount by which PMT's "net income," on a rolling four quarter basis and before deducting the incentive fee, exceeds certain levels of return on "equity."

The performance incentive fee is equal to the sum of: (a) 10% of the amount by which PMT's net income for the quarter exceeds (i) an 8% return on equity plus the "high watermark," up to (ii) a 12% return on PMT's equity; plus (b) 15% of the amount by which PMT's net income for the quarter exceeds (i) a 12% return on PMT's equity plus the "high watermark," up to (ii) a 16% return on PMT's equity; plus (c) 20% of the amount by which PMT's net income for the quarter exceeds a 16% return on equity plus the "high watermark."

For the purpose of determining the amount of the performance incentive fee:

"Net income" is defined as net income or loss computed in accordance with GAAP adjusted for certain other non cash charges determined after discussions between the Company and PMT's independent trustees and approval by a majority of PMT's independent trustees.

"Equity" is the weighted average of the issue price per common share of all of PMT's public offerings, multiplied by the weighted average number of common shares outstanding (including restricted share units) in the rolling four quarter period.

The "high watermark" is the quarterly adjustment that reflects the amount by which the net income (stated as a percentage of return on equity) in that quarter exceeds or falls short of the lesser of 8% and the average Fannie Mae 30 year MBS yield (the "Target Yield") for the four quarters then ended. If the net income is lower than the Target Yield, the high watermark is increased by the difference. If the net income is higher than the Target Yield, the high watermark is reduced by the difference. Each time a performance incentive fee is earned, the high watermark returns to zero. As a result, the threshold amounts required for the Company to earn a performance incentive fee are adjusted cumulatively based on the performance of PMT's net income over (or under) the Target Yield, until the net income in excess of the Target Yield exceeds the then current cumulative high watermark amount, and a performance incentive fee is earned.

The base management fee and the performance incentive fee are both receivable quarterly in arrears. The performance incentive fee may be paid in cash or a combination of cash and PMT's common shares (subject to a limit of no more than 50% paid in common shares), at PMT's option.

The Management Agreement expires on September 12, 2020, subject to automatic renewal for additional 18-month periods, unless terminated earlier in accordance with the terms of the agreement. In the event of termination of the

Management Agreement between PMT and the Company, the Company may be entitled to a termination fee in certain circumstances. The termination fee is equal to three times the sum of (a) the average annual base management fee, and (b) the average annual performance incentive fee earned by the Company, in each case during the 24-month period immediately preceding the date of termination.

Following is a summary of the base management and performance incentive fees earned from PMT:

	Quarter ended		Six months ended	
	June 30, 2017	2016	June 30, 2017	2016
	(in thousands)			
Base management	\$ 5,334	\$ 5,199	\$ 10,342	\$ 10,551
Performance incentive	304	—	304	—
	\$ 5,638	\$ 5,199	\$ 10,646	\$ 10,551

#### Expense Reimbursement

Under the Management Agreement, PMT reimburses the Company for its organizational and operating expenses, including third-party expenses, incurred on PMT's behalf, it being understood that the Company and its affiliates shall allocate a portion of their personnel's time to provide certain legal, tax and investor relations services for the direct benefit of PMT. With respect to the allocation of the Company's and its affiliates' personnel, from and after

Table of Contents

September 12, 2016, the Company shall be reimbursed \$120,000 per fiscal quarter, such amount to be reviewed annually and not preclude reimbursement for any other services performed by the Company or its affiliates.

PMT is also required to pay its pro rata portion of rent, telephone, utilities, office furniture, equipment, machinery and other office, internal and overhead expenses of the Company and its affiliates required for PMT's and its subsidiaries' operations. These expenses will be allocated based on the ratio of PMT's proportion of gross assets compared to all remaining gross assets managed by the Company as calculated at each fiscal quarter end.

The Company received reimbursements from PMT for expenses as follows:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands)		2017	2016
Reimbursement of:				
Common overhead incurred by the Company	\$ 1,593	\$ 2,435	\$ 3,027	\$ 4,996
Expenses incurred on PMT's behalf, net	398	(169)	653	(114)
	\$ 1,991	\$ 2,266	\$ 3,680	\$ 4,882
Payments and settlements during the period (1)	\$ 16,070	\$ 28,952	\$ 40,463	\$ 56,613

(1) Payments and settlements include payments for management fees and correspondent production activities itemized in the preceding tables and netting settlements made pursuant to master netting agreements between the Company and PMT.

#### Conditional Reimbursement of Underwriting Fees

In connection with its initial public offering of common shares of beneficial interest on August 4, 2009 ("IPO"), PMT conditionally agreed to reimburse the Company up to \$2.9 million for underwriting fees paid to the IPO underwriters by the Company on PMT's behalf. The Company received no reimbursement from PMT during the six months ended June 30, 2017 and 2016. In the event a termination fee is payable to the Company under the Management Agreement, and the Company has not received the full amount of the reimbursements and payments under the reimbursement agreement, such amount will be paid in full. The term of the reimbursement agreement expires on February 1, 2019.

#### Investing Activities

Master Repurchase Agreement with the Issuer Trust

On December 19, 2016, the Company, through PLS, entered into a master repurchase agreement with one of PMT's wholly-owned subsidiaries, PennyMac Holdings, LLC ("PMH") (the "PMH Repurchase Agreement"), pursuant to which PMH may borrow from the Company for the purpose of financing PMH's participation certificates representing beneficial ownership in excess servicing spread ("ESS"). PLS then re-pledges such participation certificates to PNMAC GMSR ISSUER TRUST (the "Issuer Trust") under a master repurchase agreement by and among PLS, the Issuer Trust and PennyMac, as guarantor (the "PC Repurchase Agreement"). The Issuer Trust was formed for the purpose of allowing PLS to finance MSR's and ESS relating to such MSR's (the "GNMA MSR Facility").

In connection with the GNMA MSR Facility, PLS pledges and/or sells to the Issuer Trust participation certificates representing beneficial interests in MSR's and ESS pursuant to the terms of the PC Repurchase Agreement. In return, the Issuer Trust (a) has issued to PLS, pursuant to the terms of an indenture, the Series 2016-MSRVF1 Variable Funding Note, dated December 19, 2016, known as the "PNMAC GMSR ISSUER TRUST MSR Collateralized Notes, Series 2016-MSRVF1" (the "VFN"), and (b) has issued and may, from time to time pursuant to the terms of any supplemental indenture, issue to institutional investors additional term notes ("Term Notes"), in each case secured on a pari passu basis by the participation certificates relating to the MSR's and ESS. The maximum principal balance of the VFN is \$1,000,000,000.

The principal amount paid by PLS for the participation certificates under the PMH Repurchase Agreement is based upon a percentage of the market value of the underlying ESS. Upon PMH's repurchase of the participation certificates, PMH is required to repay PLS the principal amount relating thereto plus accrued interest (at a rate reflective

Table of Contents

of the current market and consistent with the weighted average note rate of the VFN and any outstanding Term Notes) to the date of such repurchase. PLS is then required to repay the Issuer Trust the corresponding amount under the PC Repurchase Agreement.

Prior to the Company’s entry into the PMH Repurchase Agreement and PC Repurchase Agreement in connection with the GNMA MSR Facility, the Company was a party to a repurchase agreement with Credit Suisse First Boston Mortgage Capital LLC (“CSFB”) (the “MSR Repo”), pursuant to which it financed Ginnie Mae MSRs and servicing advance receivables and pledged to CSFB all of its rights and interests in any Ginnie Mae MSRs it owned or acquired, and a separate acknowledgement agreement with respect thereto, by and among Ginnie Mae, CSFB and the Company.

In connection with the MSR Repo described above, the Company and PMT entered into an underlying loan and security agreement, dated as of April 30, 2015, pursuant to which PMT was able to borrow up to \$150 million from the Company for the purpose of financing ESS (the “Underlying LSA”). In order to secure its borrowings, PMT pledged its ESS to the Company under the Underlying LSA and the Company, in turn, re-pledged such ESS to CSFB under the MSR Repo. The principal amount of the borrowings under the Underlying LSA was based upon a percentage of the market value of the ESS pledged by PMT, subject to the \$150 million sublimit described above. Pursuant to the Underlying LSA, PMT granted to the Company a security interest in all of its right, title and interest in, to and under the ESS pledged to secure the borrowings.

The Company and PMT agreed in connection with the Underlying LSA that PMT was required to repay the Company the principal amount of borrowings plus accrued interest to the date of such repayment, and the Company was required to repay CSFB the corresponding amount under the MSR Repo. Interest accrued on PMT’s note relating to the Underlying LSA at a rate based on CSFB’s cost of funds under the MSR Repo. PMT was also required to pay the Company a fee for the structuring of the Underlying LSA in an amount equal to the portion of the corresponding fee paid by the Company to CSFB and allocable to the \$150 million relating to the ESS financing. The note receivable was replaced by the PMH Repurchase Agreement upon the closing of the GNMA MSR facility.

The Company also holds an investment in PMT in the form of 75,000 common shares of beneficial interest.

Following is a summary of investing activities between the Company and PMT:

Quarter ended		Six months ended	
June 30,		June 30,	
2017	2016	2017	2016
(in thousands)			

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Assets purchased from PennyMac Mortgage Investment Trust under agreements to resell:				
Interest income	\$ 2,025	\$ —	\$ 3,830	\$ —
Note receivable from PennyMac Mortgage Investment Trust:				
Interest income	\$ —	\$ 2,222	\$ —	\$ 3,824
Common shares of beneficial interest of PennyMac Mortgage Investment Trust:				
Dividends received from PennyMac Mortgage Investment Trust	\$ 35	\$ 36	\$ 71	\$ 71
Change in fair value of investment in common shares of PennyMac Mortgage Investment Trust	41	193	144	72
	\$ 76	\$ 229	\$ 215	\$ 143

	June 30, 2017 (in thousands)	December 31, 2016
Assets purchased from PennyMac Mortgage Investment Trust under agreements to resell	\$ 150,000	\$ 150,000
Common shares of beneficial interest of PennyMac Mortgage Investment Trust:		
Fair value	\$ 1,372	\$ 1,228
Number of shares	75	75

Table of Contents

Financing Activities

Spread Acquisition and MSR Servicing Agreements

Effective February 1, 2013, the Company entered into a master spread acquisition and MSR servicing agreement (the “2/1/13 Spread Acquisition Agreement”), pursuant to which it sold to PMT or one of its wholly-owned subsidiaries the rights to receive certain ESS from MSRs acquired by the Company from banks and other third party financial institutions. The Company was generally required to service or subservice the related mortgage loans for the applicable Agency or investor. The terms of each transaction under the 2/1/13 Spread Acquisition Agreement were subject to the terms thereof, as modified and supplemented by the terms of a confirmation executed in connection with such transaction.

To the extent the Company refinanced any of the mortgage loans relating to the ESS sold to PMT, the 2/1/13 Spread Acquisition Agreement contained recapture provisions requiring that the Company transfer to PMT, at no cost, the ESS relating to a certain percentage of the UPB of the newly originated mortgage loans. To the extent the fair value of the aggregate ESS to be transferred for the applicable month was less than \$200,000, the Company was, at its option, permitted to pay cash to PMT in an amount equal to such fair value instead of transferring such ESS.

On February 29, 2016, the parties terminated the 2/1/13 Spread Acquisition Agreement and all amendments thereto. In connection with the termination of the 2/1/13 Spread Acquisition Agreement, PLS reacquired from PMH all of its right, title and interest in and to all of the Fannie Mae ESS previously sold by PLS to PMH and then subject to such 2/1/13 Spread Acquisition Agreement.

On December 19, 2014, the Company entered into a second master spread acquisition and MSR servicing agreement with PMT (the “12/19/14 Spread Acquisition Agreement”). The terms of the 12/19/14 Spread Acquisition Agreement are substantially similar to the terms of the 2/1/13 Spread Acquisition Agreement, except that the Company only intends to sell ESS relating to Freddie Mac MSRs under the 12/19/14 Spread Acquisition Agreement.

To the extent the Company refinances any of the mortgage loans relating to the ESS it sells to PMT, the 12/19/14 Spread Acquisition Agreement also contains recapture provisions requiring that the Company transfer to PMT, at no cost, the ESS relating to a certain percentage of the UPB of the newly originated mortgage loans. To the extent the fair market value of the aggregate ESS to be transferred for the applicable month is less than \$200,000, the Company may, at its option, pay cash to PMT in an amount equal to such fair market value in lieu of transferring such ESS.

On February 29, 2016, PLS also reacquired from PMT all of its right, title and interest in and to all of the Freddie Mac ESS previously sold by PLS to PMT and then subject to such 12/19/14 Spread Acquisition Agreement. The 12/19/14

Spread Acquisition Agreement remains in full force and effect.

On December 19, 2016, the Company amended and restated a third master spread acquisition and MSR servicing agreement with PMT (the "12/19/16 Spread Acquisition Agreement"). The terms of the 12/19/16 Spread Acquisition Agreement are substantially similar to the terms of the 2/1/13 Spread Acquisition Agreement and the 12/19/14 Spread Acquisition Agreement, except that the Company only intends to sell ESS relating to Ginnie Mae MSR's under the 12/19/16 Spread Acquisition Agreement. Pursuant to the 12/19/16 Spread Acquisition Agreement, the Company may sell to PMT, from time to time, the right to receive participation certificates representing beneficial ownership in ESS arising from Ginnie Mae MSR's acquired by the Company, in which case the Company generally would be required to service or subservice the related mortgage loans for Ginnie Mae. The primary purpose of the amendment and restatement was to facilitate the continued financing of the ESS owned by PMT in connection with the parties' participation in the GNMA MSR Facility.

To the extent the Company refinances any of the mortgage loans relating to the ESS it has acquired, the 12/19/16 Spread Acquisition Agreement also contains recapture provisions requiring that the Company transfer to PMT, at no cost, the ESS relating to a certain percentage of the unpaid principal balance of the newly originated mortgage loans. However, under the 12/19/16 Spread Acquisition Agreement, in any month where the transferred ESS relating to newly originated Ginnie Mae mortgage loans is not equivalent to at least 90% of the product of the excess servicing fee rate and the unpaid principal balance of the refinanced mortgage loans, the Company is also required to transfer additional ESS or cash in the amount of such shortfall. Similarly, in any month where the transferred ESS relating to modified Ginnie Mae mortgage loans is not equivalent to at least 90% of the product of the excess servicing fee rate and



Table of Contents

the unpaid principal balance of the modified mortgage loans, the 12/19/16 Spread Acquisition Agreement contains provisions that require the Company to transfer additional ESS or cash in the amount of such shortfall. To the extent the fair market value of the aggregate ESS to be transferred for the applicable month is less than \$200,000, the Company may, at its option, wire cash to PMT in an amount equal to such fair market value in lieu of transferring such ESS.

Following is a summary of financing activities between the Company and PMT:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30, 2017	2016
	(in thousands)			
Excess servicing spread financing:				
Issuance pursuant to recapture agreement	\$ 1,380	\$ 1,690	\$ 2,953	\$ 3,601
Repayment	\$ 14,278	\$ 17,400	\$ 28,910	\$ 38,281
Settlement	\$ —	\$ —	\$ —	\$ 59,045
Change in fair value	\$ (7,156)	\$ (17,428)	\$ (9,929)	\$ (36,877)
Interest expense	\$ 4,366	\$ 5,713	\$ 9,013	\$ 12,728
Recapture incurred pursuant to refinancings by the Company of mortgage loans subject to excess servicing spread financing included in Net gains on mortgage loans held for sale at fair value	\$ 1,271	\$ 1,604	\$ 2,674	\$ 3,426

## Receivable from and Payable to PMT

Amounts receivable from and payable to PMT are summarized below:

	June 30, 2017	December 31, 2016
	(in thousands)	
Receivable from PMT:		
Management fees	\$ 5,638	\$ 5,081
Servicing fees	4,231	5,465
Correspondent production fees	2,495	2,371
Allocated expenses and expenses incurred on PMT's behalf	2,324	1,046
Fulfillment fees	2,022	1,300
Conditional Reimbursement	900	900
Interest on assets purchased under agreements to resell	115	253

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

	\$ 17,725	\$ 16,416
Payable to PMT:		
Deposits made by PMT to fund servicing advances	\$ 127,696	\$ 162,945
Mortgage servicing rights recapture payable	428	707
Other	4,585	6,384
	\$ 132,709	\$ 170,036

Table of Contents

Investment Funds

The Company has investment management agreements with the Investment Funds pursuant to which it receives management fees consisting of base management fees and carried interest. The management fees are based on the lesser of the funds' net asset values or aggregate capital contributions. The base management fees accrue at annual rates ranging from 1.5% to 2.0% of the applicable amounts on which they are based.

The Carried Interest that the Company recognizes from the Investment Funds is determined by the Investment Funds' performance and its contractual rights to share in the Investments Funds' returns in excess of the preferred returns, if any, accruing to the funds' investors. The Company recognizes Carried Interest as a participation in the profits in the Investment Funds after the investors in the Investment Funds have achieved a preferred return as defined in the fund agreements. After the investors have achieved the preferred returns specified in the respective fund agreements, a "catch up" return accrues to the Company until it receives a specified percentage of the preferred return. Thereafter, the Company participates in future returns in excess of the preferred return at the rates specified in the fund agreements.

The amount of the Carried Interest that the Company receives depends on the Investment Funds' future performance. As a result, the amount of Carried Interest recorded by the Company at period end is subject to adjustment based on future results of the Investment Funds and may be reduced as a result of subsequent performance. However, the Company is not required to pay guaranteed returns to the Investment Funds and the amount of Carried Interest will only be reversed to the extent of amounts previously recognized.

The Investment Funds will continue in existence through December 31, 2017, subject to two one-year extensions at the Company's discretion, in accordance with the terms of the limited liability company and limited partnership agreements that govern the Investment Funds.

The Company also has loan servicing agreements with the Investment Funds. The loan servicing to be provided by the Company under the loan servicing agreements with the Investment Funds includes collecting principal, interest and escrow account payments, if any, with respect to mortgage loans, as well as managing loss mitigation, which may include, among other things, collection activities, loan workouts, modifications, foreclosures and short sales. The Company may also engage in certain loan origination activities that include refinancing mortgage loans and arranging financings that facilitate sales of REOs.

The loan servicing agreements with the Investment Funds generally provide for fee revenue, which varies depending on the type and quality of the loans being serviced. The Company is also entitled to certain customary market-based fees and charges. This arrangement was modified, effective January 1, 2012, with respect to one of the Investment Funds. At that time, the Company settled its accrued servicing fee rebate and amended its loan servicing agreement with such fund to charge scheduled servicing fees in place of the previous "at cost" servicing arrangement.



Table of Contents

Amounts due from and payable to the Investment Funds are summarized below:

	June 30, 2017	December 31, 2016
	(in thousands)	
Carried Interest due from Investment Funds:		
PNMAC Mortgage Opportunity Fund, LLC	\$ 42,174	\$ 42,427
PNMAC Mortgage Opportunity Fund Investors, LLC	28,845	28,479
	\$ 71,019	\$ 70,906
Receivable from Investment Funds:		
Expense reimbursements	\$ 453	\$ 238
Management fees	359	500
Mortgage loan servicing fees	263	231
Mortgage loan servicing fee rebate deposit	255	250
	\$ 1,330	\$ 1,219
Payable to Investment Funds:		
Deposits received to fund servicing advances	\$ 15,103	\$ 20,221
Other	133	172
	\$ 15,236	\$ 20,393

#### Exchanged Private National Mortgage Acceptance Company, LLC Unitholders

The Company entered into a tax receivable agreement with owners of PennyMac other than the Company on the date of the IPO that provides for the payment from time to time by the Company to PennyMac's exchanged unitholders an amount equal to 85% of the amount of the net tax benefits, if any, that the Company is deemed to realize as a result of (i) increases in tax basis of PennyMac's assets resulting from such unitholders' exchanges and (ii) certain other tax benefits related to entering into the tax receivable agreement, including tax benefits attributable to payments under the tax receivable agreement. Based on the PennyMac unitholder exchanges to date, the Company has recorded a \$73.1 million and \$76.0 million Payable to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement as of June 30, 2017 and December 31, 2016, respectively. The Company made payments of \$6.2 million during the six months ended June 30, 2017. No payments were made during the six months ended June 30, 2016.

#### Note 4—Earnings Per Share of Common Stock

Basic earnings per share of common stock is determined using net income attributable to the Company's common stockholders divided by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share of common stock is determined by dividing net income attributable to the Company's common stockholders by the weighted average number of shares of common stock outstanding, assuming all dilutive

shares of common stock were issued.

Potentially dilutive shares of common stock include non-vested unit and stock-based compensation awards and PennyMac Class A units. The Company applies the treasury stock method to determine the diluted weighted average shares of common stock outstanding represented by the non-vested unit and stock-based compensation awards. The diluted earnings per share calculation assumes the exchange of PennyMac Class A units for shares of common stock. Accordingly, earnings attributable to the Company's common stockholders is also adjusted to include the earnings allocated to the PennyMac Class A units after taking into account the income taxes that would be applicable to such earnings.

Table of Contents

The following table summarizes the basic and diluted earnings per share calculations:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands, except per share amounts)			
Basic earnings per share of common stock:				
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 10,479	\$ 14,475	\$ 21,358	\$ 19,650
Weighted average shares of common stock outstanding	23,388	22,078	23,006	22,042
Basic earnings per share of common stock	\$ 0.45	\$ 0.66	\$ 0.93	\$ 0.89
Diluted earnings per share of common stock:				
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 10,479	\$ 14,475	\$ 21,358	\$ 19,650
Effect of net income attributable to PennyMac Class A units exchangeable to common stock, net of income taxes	23,849	35,433	49,403	48,040
Diluted net income attributable to common stockholders	\$ 34,328	\$ 49,908	\$ 70,761	\$ 67,690
Weighted average shares of common stock outstanding	23,388	22,078	23,006	22,042
Dilutive shares:				
PennyMac Class A units exchangeable to common stock	53,375	54,021	53,481	54,032
Common shares issuable under stock-based compensation plan	887	181	1,154	162
Diluted weighted average shares of common stock outstanding	77,650	76,280	77,641	76,236
Diluted earnings per share of common stock	\$ 0.44	\$ 0.65	\$ 0.91	\$ 0.89

Calculations of diluted earnings per share require certain potentially dilutive shares to be excluded based on whether their inclusion in the diluted earnings per share calculation would be anti-dilutive. The following table summarizes the anti-dilutive weighted-average number of outstanding stock options and performance-based restricted stock units ("RSUs") excluded from the calculation of diluted earnings per share:

	Quarter ended		Six months ended	
	June 30,	2016	June 30,	2016
	2017		2017	
	(in thousands except for weighted-average exercise price)			
Stock options (1)	2,636	2,795	2,335	2,450
Performance-based RSUs (2)	1,433	2,684	1,192	2,512
Time-based RSUs	134	-	87	-
Total anti-dilutive stock-based compensation units	4,203	5,479	3,614	4,962
	\$ 16.38	\$ 15.81	\$ 16.38	\$ 15.81

Weighted average exercise price of anti-dilutive stock options

(1)

---

- (1) Certain stock options were outstanding but not included in the computation of diluted earnings per share because the weighted-average exercise prices were anti-dilutive.
- (2) Certain performance-based RSUs were outstanding but not included in the computation of diluted earnings per share because the performance thresholds included in such RSUs have not been achieved.

Note 5—Loan Sales and Servicing Activities

The Company originates or purchases and sells mortgage loans in the secondary mortgage market without recourse for credit losses. However, the Company maintains continuing involvement with the mortgage loans sold in the form of servicing arrangements and the liability under representations and warranties it makes to purchasers and insurers of the mortgage loans sold.

20

---



Table of Contents

The following table summarizes cash flows between the Company and transferees as a result of the sale of mortgage loans in transactions where the Company maintains continuing involvement as servicer with the mortgage loans:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Cash flows:				
Sales proceeds	\$ 12,637,046	\$ 11,234,497	\$ 24,497,179	\$ 19,176,697
Servicing fees received (1)	\$ 89,970	\$ 60,623	\$ 174,991	\$ 119,103
Net servicing advances (recoveries)	\$ 15,700	\$ (1,264)	\$ 13,791	\$ (9,545)

(1) Net of guarantee fees paid to the Agencies.

	June 30, 2017	December 31, 2016
	(in thousands)	
Unpaid principal balance of mortgage loans outstanding	\$ 106,297,560	\$ 89,516,155
Delinquencies:		
30-89 days	\$ 3,042,877	\$ 2,545,970
90 days or more:		
Not in foreclosure	\$ 1,204,131	\$ 735,263
In foreclosure	\$ 397,412	\$ 137,856
Foreclosed	\$ 27,740	\$ 2,552
Bankruptcy	\$ 518,416	\$ 256,471

The UPB of the Company's mortgage loan servicing portfolio is summarized as follows:

	June 30, 2017		
	Servicing rights owned (in thousands)	Contract servicing and subservicing	Total mortgage loans serviced
Investor:			
Non-affiliated entities	\$ 158,922,497	\$ —	\$ 158,922,497
Affiliated entities	—	67,125,932	67,125,932
Mortgage loans held for sale	2,915,346	—	2,915,346
	\$ 161,837,843	\$ 67,125,932	\$ 228,963,775
Amounts subserviced for the Company (1)	\$ 11,909,829	\$ 61,108	\$ 11,970,937

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Delinquent mortgage loans:			
30 days	\$ 3,803,957	\$ 410,437	\$ 4,214,394
60 days	1,067,664	134,083	1,201,747
90 days or more:			
Not in foreclosure	2,138,947	512,227	2,651,174
In foreclosure	795,309	491,142	1,286,451
Foreclosed	35,352	361,521	396,873
	\$ 7,841,229	\$ 1,909,410	\$ 9,750,639
Bankruptcy	\$ 900,628	\$ 254,396	\$ 1,155,024
Custodial funds managed by the Company (2)	\$ 3,455,435	\$ 982,652	\$ 4,438,087

- 
- (1) Certain of the mortgage loans serviced by the Company are subserviced on the Company's behalf by other mortgage loan servicers including commercial real estate loans and certain mortgage loans on a transitional basis where the Company has obtained the rights to service the loans but servicing of the loans has not yet been transferred to the Company's servicing system.
- (2) Custodial funds include borrower and investor custodial cash accounts relating to mortgage loans serviced under the servicing agreements and are not recorded on the Company's consolidated balance sheets. The Company earns

Table of Contents

placement fees on certain of the custodial funds it manages on behalf of the mortgage loans' investors, which are included in Interest income in the Company's consolidated statements of income.

	December 31, 2016		
	Servicing rights owned (in thousands)	Contract servicing and subservicing	Total mortgage loans serviced
Investor:			
Non-affiliated entities	\$ 131,252,002	\$ —	\$ 131,252,002
Affiliated entities	—	60,886,717	60,886,717
Mortgage loans held for sale	2,101,283	—	2,101,283
	\$ 133,353,285	\$ 60,886,717	\$ 194,240,002
Commercial real estate loans subserviced for the Company	\$ —	\$ 22,338	\$ 22,338
Delinquent mortgage loans:			
30 days	\$ 3,240,640	\$ 407,177	\$ 3,647,817
60 days	1,035,871	145,720	1,181,591
90 days or more:			
Not in foreclosure	2,203,895	566,496	2,770,391
In foreclosure	937,204	685,001	1,622,205
Foreclosed	28,943	448,017	476,960
	\$ 7,446,553	\$ 2,252,411	\$ 9,698,964
Bankruptcy	\$ 793,517	\$ 280,459	\$ 1,073,976
Custodial funds managed by the Company (1)	\$ 3,097,365	\$ 736,398	\$ 3,833,763

(1) Custodial funds include borrower and investor custodial cash accounts relating to mortgage loans serviced under the servicing agreements and are not recorded on the Company's consolidated balance sheets. The Company earns placement fees on custodial funds it manages on behalf of the mortgage loans' investors, which are included in Interest income in the Company's consolidated statements of income.

Following is a summary of the geographical distribution of mortgage loans included in the Company's servicing portfolio for the top five and all other states as measured by UPB:

State	June 30, 2017 (in thousands)	December 31, 2016
California	\$ 45,679,111	\$ 42,303,952
Texas	18,468,384	16,037,426
Florida	15,829,653	12,817,627
Virginia	15,002,859	13,143,510
Maryland	10,215,463	8,564,923
All other states	123,768,305	101,372,564
	\$ 228,963,775	\$ 194,240,002



Table of Contents

## Note 6—Mortgage Loans Held for Sale at Fair Value

Mortgage loans held for sale at fair value include the following:

	June 30, 2017	December 31, 2016
	(in thousands)	
Government-insured or guaranteed	\$ 2,523,757	\$ 1,984,020
Conventional conforming	133,761	141,524
Purchased from Ginnie Mae pools serviced by the Company	373,938	40,437
Repurchased pursuant to representations and warranties	6,146	6,834
	\$ 3,037,602	\$ 2,172,815
Fair value of mortgage loans pledged to secure:		
Assets sold under agreements to repurchase	\$ 2,766,171	\$ 1,422,255
Mortgage loan participation and sale agreements	252,917	702,919
	\$ 3,019,088	\$ 2,125,174

## Note 7—Derivative Activities

The Company is exposed to fair value risk relative to its mortgage loans held for sale as well as to its interest rate lock commitments (“IRLCs”) and MSR. The Company bears fair value risk from the time an IRLC is made to PMT or a loan applicant to the time the mortgage loan is sold. The Company is exposed to loss in fair value of its IRLCs and mortgage loans held for sale when market mortgage interest rates increase. The Company is exposed to loss in fair value of its MSR when market mortgage interest rates decrease.

The Company engages in interest rate risk management activities in an effort to reduce the variability of earnings caused by changes in market interest rates. To manage this fair value risk resulting from interest rate risk, the Company uses derivative financial instruments acquired with the intention of reducing the risk that changes in market interest rates will result in unfavorable changes in the fair value of the Company’s IRLCs, inventory of mortgage loans held for sale and the portion of its MSR not financed with ESS.

The Company does not use derivative financial instruments other than IRLCs or for purposes other than in support of its risk management activities. IRLCs are generated in the process of purchasing or originating mortgage loans held for sale. The Company records all derivative financial instruments at fair value and records changes in fair value in current period income.



Table of Contents

## Derivative Notional Amounts and Fair Value of Derivatives

The Company had the following derivative financial instruments recorded on its consolidated balance sheets:

Instrument	June 30, 2017			December 31, 2016		
	Notional amount (in thousands)	Fair value Derivative assets	Derivative liabilities	Notional amount	Fair value Derivative assets	Derivative liabilities
Derivatives not designated as hedging instruments: Not subject to master netting arrangements:						
Interest rate lock commitments	3,999,761	\$ 51,287	\$ 5,129	4,279,611	\$ 65,848	\$ 6,457
Used for hedging purposes:						
Forward purchase contracts	7,819,706	25	33,731	12,746,191	77,905	16,914
Forward sales contracts	7,641,979	28,759	528	16,577,942	28,324	85,035
MBS put options	6,075,000	11,232	—	1,175,000	3,934	—
MBS call options	—	—	—	1,600,000	217	—
Put options on interest rate futures purchase contracts	1,250,000	2,520	63	1,125,000	3,109	—
Call options on interest rate futures purchase contracts	200,000	438	—	900,000	203	—
Put options on interest rate futures sale contracts	200,000	—	—	—	—	—
Interest rate swap futures purchase contracts	325,000	—	—	200,000	—	—
Total derivatives before netting		94,261	39,451		179,540	108,406
Netting		(24,186)	(22,887)		(96,635)	(86,044)
		\$ 70,075	\$ 16,564		\$ 82,905	\$ 22,362
Deposits placed with derivative counterparties		\$ 1,299			\$ 10,591	

The following table summarizes the notional value activity for derivative contracts used in the Company's hedging activities:

Instrument	Quarter ended June 30, 2017			Balance end of period
	Balance beginning of period (in thousands)	Additions	Dispositions/ expirations	
Forward purchase contracts	9,292,052	46,756,266	(48,228,612)	7,819,706
Forward sale contracts	11,383,749	56,284,621	(60,026,391)	7,641,979
MBS put options	2,950,000	7,325,000	(4,200,000)	6,075,000
MBS call options	—	4,200,000	(4,200,000)	—
Put options on interest rate futures purchase contracts	1,160,000	1,400,000	(1,310,000)	1,250,000
Call options on interest rate futures purchase contracts	482,300	534,300	(816,600)	200,000
Put options on interest rate futures sale contracts	—	1,510,000	(1,310,000)	200,000
Call options on interest rate futures sale contracts	57,300	759,300	(816,600)	—
Treasury futures purchase contracts	—	61,300	(61,300)	—
Treasury futures sale contracts	—	61,300	(61,300)	—
Interest rate swap futures purchase contracts	200,000	325,000	(200,000)	325,000
Interest rate swap futures sale contracts	—	200,000	(200,000)	—



Table of Contents

Instrument	Quarter ended June 30, 2016			Balance end of period
	Balance beginning of period (in thousands)	Additions	Dispositions/ expirations	
Forward purchase contracts	9,464,470	46,870,345	(42,823,952)	13,510,863
Forward sale contracts	10,418,906	56,521,979	(53,326,689)	13,614,196
MBS put options	1,375,000	6,750,000	(4,575,000)	3,550,000
Put options on interest rate futures purchase contracts	1,750,000	1,650,000	(2,400,000)	1,000,000
Call options on interest rate futures purchase contracts	3,937,500	—	(3,485,400)	452,100

Instrument	Six months ended June 30, 2017			Balance end of period
	Balance beginning of period (in thousands)	Additions	Dispositions/ expirations	
Forward purchase contracts	12,746,191	88,940,575	(93,867,061)	7,819,706
Forward sale contracts	16,577,942	107,934,447	(116,870,410)	7,641,979
MBS put options	1,175,000	12,850,000	(7,950,000)	6,075,000
MBS call options	1,600,000	4,200,000	(5,800,000)	—
Put options on interest rate futures purchase contracts	1,125,000	4,460,000	(4,335,000)	1,250,000
Call options on interest rate futures purchase contracts	900,000	1,489,300	(2,189,300)	200,000
Put options on interest rate futures sale contracts	—	4,535,000	(4,335,000)	200,000
Call options on interest rate futures sale contracts	—	2,189,300	(2,189,300)	—
Treasury futures purchase contracts	—	166,100	(166,100)	—
Treasury futures sale contracts	—	166,100	(166,100)	—
Interest rate swap futures purchase contracts	200,000	525,000	(400,000)	325,000
Interest rate swap futures sales contracts	—	400,000	(400,000)	—

Instrument	Six months ended June 30, 2016			Balance end of period
	Balance beginning of period (in thousands)	Additions	Dispositions/ expirations	
Forward purchase contracts	5,254,293	77,682,720	(69,426,150)	13,510,863
Forward sale contracts	6,230,811	95,918,405	(88,535,020)	13,614,196

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

MBS put options	1,275,000	9,450,000	(7,175,000)	3,550,000
Put options on interest rate futures purchase contracts	1,650,000	4,675,000	(5,325,000)	1,000,000
Call options on interest rate futures purchase contracts	600,000	3,637,500	(3,785,400)	452,100

25

---

Table of Contents

## Derivative Balances and Netting of Financial Instruments

The Company has elected to present net derivative asset and liability positions, and cash collateral obtained from (or posted to) its counterparties when subject to a master netting arrangement that is legally enforceable on all counterparties in the event of default. The derivatives that are not subject to a master netting arrangement are IRLCs.

## Offsetting of Derivative Assets

Following are summaries of derivative assets and related netting amounts.

	June 30, 2017			December 31, 2016		
	Gross amount of recognized assets (in thousands)	Gross amount offset in the consolidated balance sheet	Net amount of assets in the consolidated balance sheet	Gross amount of recognized assets	Gross amount offset in the consolidated balance sheet	Net amount of assets in the consolidated balance sheet
Derivatives not subject to master netting arrangements - IRLCs	\$ 51,287	\$ —	\$ 51,287	\$ 65,848	\$ —	\$ 65,848
Derivatives subject to a master netting arrangements:						
Forward purchase contracts	25	—	25	77,905	—	77,905
Forward sale contracts	28,759	—	28,759	28,324	—	28,324
MBS put options	11,232	—	11,232	3,934	—	3,934
MBS call options	—	—	—	217	—	217
Put options on interest rate futures purchase contracts	2,520	—	2,520	3,109	—	3,109
Call options on interest rate futures purchase contracts	438	—	438	203	—	203
Netting	—	(24,186)	(24,186)	—	(96,635)	(96,635)
	42,974	(24,186)	18,788	113,692	(96,635)	17,057

\$ 94,261      \$ (24,186)      \$ 70,075      \$ 179,540      \$ (96,635)      \$ 82,905

### Derivative Assets, Financial Instruments, and Cash Collateral Held by Counterparty

The following table summarizes by significant counterparty the amount of derivative asset positions after considering master netting arrangements and financial instruments or cash pledged that do not meet the accounting guidance qualifying for netting.

	June 30, 2017				December 31, 2016			
	Net amount of assets in the consolidated balance sheet (in thousands)	Gross amount not offset in the consolidated balance sheet			Net amount	Net amount of assets in the consolidated balance sheet	Gross amount not offset in the consolidated balance sheet	
Financial instruments		Cash collateral received		Financial instruments			Cash collateral received	
IRLCs	\$ 51,287	\$ —	\$ —	\$ 51,287	\$ 65,848	\$ —	\$ —	\$ 65,848
Barclays Capital	7,105	—	—	7,105	12,002	—	—	12,002
Goldman Sachs	3,446	—	—	3,446	—	—	—	—
RJ O'Brien	2,895	—	—	2,895	2,750	—	—	2,750
Bank of America, N.A.	2,803	—	—	2,803	—	—	—	—
Others	2,539	—	—	2,539	2,305	—	—	2,305
	\$ 70,075	\$ —	\$ —	\$ 70,075	\$ 82,905	\$ —	\$ —	\$ 82,905

Table of Contents

## Offsetting of Derivative Liabilities and Financial Liabilities

Following is a summary of net derivative liabilities and assets sold under agreements to repurchase and related netting amounts. Assets sold under agreements to repurchase do not qualify for netting.

	June 30, 2017			December 31, 2016		
	Gross amount of recognized liabilities (in thousands)	Gross amount offset in the consolidated balance sheet	Net amount of liabilities in the consolidated balance sheet	Gross amount of recognized liabilities	Gross amount offset in the consolidated balance sheet	Net amount of liabilities in the consolidated balance sheet
Derivatives not subject to master netting arrangements - IRLCs	\$ 5,129	\$ —	\$ 5,129	\$ 6,457	\$ —	\$ 6,457
Derivatives subject to a master netting arrangement:						
Forward purchase contracts	33,731	—	33,731	16,914	—	16,914
Forward sale contracts	528	—	528	85,035	—	85,035
Put options on interest rate futures purchase contracts	63	—	63	—	—	—
Netting	—	(22,887)	(22,887)	—	(86,044)	(86,044)
Total derivatives	34,322	(22,887)	11,435	101,949	(86,044)	15,905
Total derivatives	39,451	(22,887)	16,564	108,406	(86,044)	22,362
Mortgage loans sold under agreements to repurchase:						
Amount outstanding	3,023,288	—	3,023,288	1,736,922	—	1,736,922
Unamortized debt issuance costs	(1,960)	—	(1,960)	(1,808)	—	(1,808)

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

3,021,328	—	3,021,328	1,735,114	—	1,735,114
\$ 3,060,779	\$ (22,887)	\$ 3,037,892	\$ 1,843,520	\$ (86,044)	\$ 1,757,476

Table of Contents

## Derivative Liabilities, Financial Instruments, and Collateral Held by Counterparty

The following table summarizes by significant counterparty the amount of derivative liabilities and assets sold under agreements to repurchase after considering master netting arrangements and financial instruments or cash pledged that do not qualify under the accounting guidance for netting. All assets sold under agreements to repurchase are secured by sufficient collateral or have fair value that exceeds the liability amount recorded on the consolidated balance sheets.

	June 30, 2017				December 31, 2016			
	Net amount of liabilities in the consolidated balance sheet (in thousands)	Gross amounts not offset in the consolidated balance sheet Financial instruments	Cash collateral pledged	Net amount	Net amount of liabilities in the consolidated balance sheet	Gross amounts not offset in the consolidated balance sheet Financial instruments	Cash collateral pledged	Net amount
IRLCs	\$ 5,129	\$ —	\$ —	\$ 5,129	\$ 6,457	\$ —	\$ —	\$ 6,457
Credit Suisse								
First Boston								
Mortgage Capital LLC	1,231,323	(1,231,323)	—	—	961,533	(960,988)	—	545
Bank of America, N.A.	766,544	(766,544)	—	—	349,638	(342,769)	—	6,869
JP Morgan Chase Bank, N.A.	490,058	(489,474)	—	584	135,322	(135,322)	—	—
Citibank, N.A.	175,878	(175,878)	—	—	81,555	(80,525)	—	1,030
Barclays Capital	135,757	(135,757)	—	—	28,467	(28,467)	—	—
Morgan Stanley Bank, N.A.	135,439	(131,399)	—	4,040	189,756	(188,851)	—	905
Royal Bank of Canada	93,780	(92,913)	—	867	2,937	—	—	2,937
Wells Fargo Bank, N.A.	5,403	—	—	5,403	—	—	—	—
BNP Paribas	—	—	—	—	1,151	—	—	1,151
Federal National Mortgage Association	—	—	—	—	1,033	—	—	1,033
Goldman Sachs	—	—	—	—	823	—	—	823
Others	541	—	—	541	612	—	—	612

\$ 3,039,852   \$ (3,023,288)   \$ —   \$ 16,564   \$ 1,759,284   \$ (1,736,922)   \$ —   \$ 22,362

Following are the gains and (losses) recognized by the Company on derivative financial instruments and the income statement line items where such gains and losses are included:

Hedged item	Income statement line	Quarter ended June 30,		Six months ended June 30,	
		2017	2016	2017	2016
		(in thousands)			
Interest rate lock commitments and mortgage loans held for sale	Net gains on mortgage loans held for sale	\$ (1,918)	\$ (48,943)	\$ (210)	\$ (118,119)
Mortgage servicing rights	Net mortgage loan servicing fees - Amortization, impairment and change in fair value of mortgage servicing rights and mortgage servicing liabilities	\$ (2,026)	\$ 64,948	\$ (24,192)	\$ 123,668



## Table of Contents

### Note 8—Fair Value

The Company's consolidated financial statements include assets and liabilities that are measured based on their fair values. The application of fair value may be on a recurring or nonrecurring basis depending on the accounting principles applicable to the specific asset or liability and whether management has elected to carry the item at its fair value as discussed in the following paragraphs.

The Company groups its assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the observability of the inputs used to determine fair value. These levels are:

- Level 1—Quoted prices in active markets for identical assets or liabilities.
  
- Level 2—Prices determined or determinable using other significant observable inputs. Observable inputs are inputs that other market participants would use in pricing an asset or liability and are developed based on market data obtained from sources independent of the Company. These may include quoted prices for similar assets and liabilities, interest rates, prepayment speeds, credit risk and other inputs.
  
- Level 3—Prices determined using significant unobservable inputs. In situations where observable inputs are unavailable, unobservable inputs may be used. Unobservable inputs reflect the Company's own judgments about the factors that market participants use in pricing an asset or liability, and are based on the best information available in the circumstances.

As a result of the difficulty in observing certain significant valuation inputs affecting "Level 3" fair value assets and liabilities, the Company is required to make judgments regarding these items' fair values. Different persons in possession of the same facts may reasonably arrive at different conclusions as to the inputs to be applied in valuing these assets and liabilities and their fair values. Likewise, due to the general illiquidity of some of these assets and liabilities, subsequent transactions may be at values significantly different from those reported.

### Fair Value Accounting Elections

Management identified all of its non-cash financial assets other than Assets purchased from PennyMac Mortgage Investment Trust under agreements to resell, as well as its originated MSR's relating to loans with initial interest rates of more than 4.5%, its purchased MSR's and its mortgage servicing liabilities ("MSLs") to be accounted for at fair value so changes in fair value will be reflected in income as they occur and more timely reflect the results of the Company's performance. Management has also identified its ESS financing to be accounted for at fair value as a means of hedging the related MSR's fair value risk. Originated MSR's backed by mortgage loans with initial interest rates of less

than or equal to 4.5% are accounted for using the amortization method.

Table of Contents

## Assets and Liabilities Measured at Fair Value on a Recurring Basis

Following is a summary of assets and liabilities that are measured at fair value on a recurring basis:

	June 30, 2017			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
<b>Assets:</b>				
Short-term investments	\$ 145,440	\$ —	\$ —	\$ 145,440
Mortgage loans held for sale at fair value	—	2,657,518	380,084	3,037,602
<b>Derivative assets:</b>				
Interest rate lock commitments	—	—	51,287	51,287
Forward purchase contracts	—	25	—	25
Forward sales contracts	—	28,759	—	28,759
MBS put options	—	11,232	—	11,232
Put options on interest rate futures purchase contracts	2,520	—	—	2,520
Call options on interest rate futures purchase contracts	438	—	—	438
Total derivative assets before netting	2,958	40,016	51,287	94,261
Netting	—	—	—	(24,186)
Total derivative assets	2,958	40,016	51,287	70,075
Investment in PennyMac Mortgage Investment Trust	1,372	—	—	1,372
Mortgage servicing rights at fair value	—	—	678,441	678,441
	\$ 149,770	\$ 2,697,534	\$ 1,109,812	\$ 3,932,930
<b>Liabilities:</b>				
Excess servicing spread financing at fair value payable to PennyMac Mortgage Investment Trust	\$ —	\$ —	\$ 261,796	\$ 261,796
<b>Derivative liabilities:</b>				
Interest rate lock commitments	—	—	5,129	5,129
Forward purchase contracts	—	33,731	—	33,731
Forward sales contracts	—	528	—	528
Put options on interest rate futures purchase contracts	63	—	—	63
Total derivative liabilities before netting	63	34,259	5,129	39,451
Netting	—	—	—	(22,887)
Total derivative liabilities	63	34,259	5,129	16,564
Mortgage servicing liabilities at fair value	—	—	18,295	18,295
	\$ 63	\$ 34,259	\$ 285,220	\$ 296,655



Table of Contents

	December 31, 2016			Total
	Level 1 (in thousands)	Level 2	Level 3	
<b>Assets:</b>				
Short-term investments	\$ 85,964	\$ —	\$ —	\$ 85,964
Mortgage loans held for sale at fair value	—	2,125,544	47,271	2,172,815
<b>Derivative assets:</b>				
Interest rate lock commitments	—	—	65,848	65,848
Forward purchase contracts	—	77,905	—	77,905
Forward sales contracts	—	28,324	—	28,324
MBS put options	—	3,934	—	3,934
MBS call options	—	217	—	217
Put options on interest rate futures purchase contracts	3,109	—	—	3,109
Call options on interest rate futures purchase contracts	203	—	—	203
Total derivative assets before netting	3,312	110,380	65,848	179,540
Netting	—	—	—	(96,635)
Total derivative assets	3,312	110,380	65,848	82,905
Investment in PennyMac Mortgage Investment Trust	1,228	—	—	1,228
Mortgage servicing rights at fair value	—	—	515,925	515,925
	\$ 90,504	\$ 2,235,924	\$ 629,044	\$ 2,858,837
<b>Liabilities:</b>				
Excess servicing spread financing at fair value payable to PennyMac Mortgage Investment Trust	\$ —	\$ —	\$ 288,669	\$ 288,669
<b>Derivative liabilities:</b>				
Interest rate lock commitments	—	—	6,457	6,457
Forward purchase contracts	—	16,914	—	16,914
Forward sales contracts	—	85,035	—	85,035
Total derivative liabilities before netting	—	101,949	6,457	108,406
Netting	—	—	—	(86,044)
Total derivative liabilities	—	101,949	6,457	22,362
Mortgage servicing liabilities at fair value	—	—	15,192	15,192
	\$ —	\$ 101,949	\$ 310,318	\$ 326,223

Table of Contents

As shown above, all or a portion of the Company's mortgage loans held for sale, IRLCs, MSR at fair value, ESS and MSLs are measured using Level 3 fair value inputs. Following are roll forwards of these items for the quarters and six months ended June 30, 2017 and 2016:

	Quarter ended June 30, 2017			Total
	Mortgage loans held for sale (in thousands)	Net interest rate lock commitments (1)	Mortgage servicing rights	
Assets:				
Balance, March 31, 2017	\$ 327,682	\$ 66,007	\$ 506,916	\$ 900,605
Purchases	625,492	—	183,586	809,078
Sales and repayments	(264,558)	—	—	(264,558)
Interest rate lock commitments issued, net	—	71,062	—	71,062
Mortgage servicing rights resulting from mortgage loan sales	—	—	7,945	7,945
Changes in fair value included in income arising from:				
Changes in instrument-specific credit risk	(3,046)	—	—	(3,046)
Other factors	—	32,613	(20,006)	12,607
	(3,046)	32,613	(20,006)	9,561
Transfers from Level 3 to Level 2	(305,486)	—	—	(305,486)
Transfers of interest rate lock commitments to mortgage loans held for sale	—	(123,524)	—	(123,524)
Balance, June 30, 2017	\$ 380,084	\$ 46,158	\$ 678,441	\$ 1,104,683
Changes in fair value recognized during the period relating to assets still held at June 30, 2017				
	\$ (3,042)	\$ 46,158	\$ (20,006)	\$ 23,110

(1) For the purpose of this table, the IRLC asset and liability positions are shown net.

	Quarter ended June 30, 2017		
	Excess servicing spread financing (in thousands)	Mortgage servicing liabilities	Total
Liabilities:			
Balance, March 31, 2017	\$ 277,484	\$ 15,994	\$ 293,478
Issuance of excess servicing spread financing pursuant to a recapture agreement with PennyMac Mortgage Investment Trust	1,380	—	1,380
Accrual of interest	4,366	—	4,366

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Repayments	(14,278)	—	(14,278)
Mortgage servicing liabilities resulting from mortgage loan sales	—	3,810	3,810
Changes in fair value included in income	(7,156)	(1,509)	(8,665)
Balance, June 30, 2017	\$ 261,796	\$ 18,295	\$ 280,091
Changes in fair value recognized during the period relating to liabilities still outstanding at June 30, 2017	\$ (7,156)	\$ (1,509)	\$ (8,665)

Table of Contents

	Quarter ended June 30, 2016			
	Mortgage loans held for sale (in thousands)	Net interest rate lock commitments (1)	Mortgage servicing rights	Total
Assets:				
Balance, March 31, 2016	\$ 33,030	\$ 71,885	\$ 594,403	\$ 699,318
Purchases	142,912	—	—	142,912
Sales and repayments	(14,443)	—	—	(14,443)
Interest rate lock commitments issued, net	—	102,755	—	102,755
Mortgage servicing rights resulting from mortgage loan sales	—	—	4,820	4,820
Changes in fair value included in income arising from:				
Changes in instrument-specific credit risk	(1,078)	—	—	(1,078)
Other factors	—	77,518	(72,929)	4,589
	(1,078)	77,518	(72,929)	3,511
Transfers from Level 3 to Level 2	(122,342)	—	—	(122,342)
Transfers of interest rate lock commitments to mortgage loans held for sale	—	(161,896)	—	(161,896)
Balance, June 30, 2016	\$ 38,079	\$ 90,262	\$ 526,294	\$ 654,635
Changes in fair value recognized during the period relating to assets still held at June 30, 2016				
	\$ 442	\$ 90,262	\$ (72,929)	\$ 17,775

(1) For the purpose of this table, the IRLC asset and liability positions are shown net.

	Quarter ended June 30, 2016		
	Excess servicing spread financing (in thousands)	Mortgage servicing liabilities	Total
Liabilities:			
Balance, March 31, 2016	\$ 321,976	\$ 6,747	\$ 328,723
Issuance of excess servicing spread financing pursuant to a recapture agreement with PennyMac Mortgage Investment Trust	1,690	—	1,690
Accrual of interest	5,713	—	5,713
Repayments	(17,400)	—	(17,400)
Changes in fair value included in income	(17,428)	(2,066)	(19,494)
Balance, June 30, 2016	\$ 294,551	\$ 4,681	\$ 299,232
Changes in fair value recognized during the period relating to liabilities still outstanding at June 30, 2016			
	\$ (17,428)	\$ (2,066)	\$ (19,494)





Table of Contents

	Six months ended June 30, 2017			Total
	Mortgage loans held for sale (in thousands)	Net interest rate lock commitments (1)	Mortgage servicing rights	
Assets:				
Balance, December 31, 2016	\$ 47,271	\$ 59,391	\$ 515,925	\$ 622,587
Purchases	1,315,963	—	183,789	1,499,752
Sales and repayments	(538,860)	—	—	(538,860)
Interest rate lock commitments issued, net	—	142,819	—	142,819
Mortgage servicing rights resulting from mortgage loan sales	—	—	13,929	13,929
Changes in fair value included in income arising from:				
Changes in instrument-specific credit risk	(4,974)	—	—	(4,974)
Other factors	—	57,732	(35,202)	22,530
	(4,974)	57,732	(35,202)	17,556
Transfers from Level 3 to Level 2	(439,316)	—	—	(439,316)
Transfers of interest rate lock commitments to mortgage loans held for sale	—	(213,784)	—	(213,784)
Balance, June 30, 2017	\$ 380,084	\$ 46,158	\$ 678,441	\$ 1,104,683
Changes in fair value recognized during the period relating to assets still held at June 30, 2017	\$ (4,620)	\$ 46,158	\$ (35,202)	\$ 6,336

(1) For the purpose of this table, the IRLC asset and liability positions are shown net.

	Six months ended June 30, 2017		
	Excess servicing spread financing (in thousands)	Mortgage servicing liabilities	Total
Liabilities:			
Balance, December 31, 2016	\$ 288,669	\$ 15,192	\$ 303,861
Issuance of excess servicing spread financing pursuant to a recapture agreement with PennyMac Mortgage Investment Trust	2,953	—	2,953
Accrual of interest	9,013	—	9,013
Repayments	(28,910)	—	(28,910)
Mortgage servicing liabilities resulting from mortgage loan sales	—	7,869	7,869
Changes in fair value included in income	(9,929)	(4,766)	(14,695)
Balance, June 30, 2017	\$ 261,796	\$ 18,295	\$ 280,091
	\$ (9,929)	\$ (4,766)	\$ (14,695)

Changes in fair value recognized during the period relating to liabilities still outstanding at June 30, 2017

34

---

Table of Contents

	Six months ended June 30, 2016			
	Mortgage loans held for sale (in thousands)	Net interest rate lock commitments (1)	Mortgage servicing rights	Total
Assets:				
Balance December 31, 2015	\$ 48,531	\$ 43,773	\$ 660,247	\$ 752,551
Purchases	488,798	—	11	488,809
Sales and repayments	(298,176)	—	—	(298,176)
Interest rate lock commitments issued, net	—	181,218	—	181,218
Mortgage servicing rights resulting from mortgage loan sales	—	—	9,288	9,288
Changes in fair value included in income arising from:				
Changes in instrument-specific credit risk	691	—	—	691
Other factors	—	149,188	(143,252)	5,936
	691	149,188	(143,252)	6,627
Transfers from Level 3 to Level 2	(201,765)	—	—	(201,765)
Transfers of interest rate lock commitments to mortgage loans held for sale	—	(283,917)	—	(283,917)
Balance, June 30, 2016	\$ 38,079	\$ 90,262	\$ 526,294	\$ 654,635
Changes in fair value recognized during the year relating to assets still held at June 30, 2016				
	\$ 860	\$ 90,262	\$ (143,252)	\$ (52,130)

(1) For the purpose of this table, the IRLC asset and liability positions are shown net.

	Six months ended June 30, 2016		
	Excess servicing spread financing (in thousands)	Mortgage servicing liabilities	Total
Liabilities:			
Balance December 31, 2015	\$ 412,425	\$ 1,399	\$ 413,824
Issuance of excess servicing spread financing pursuant to a recapture agreement with PennyMac Mortgage Investment Trust	3,601	—	3,601
Accrual of interest	12,728	—	12,728
Repurchase	(59,045)	—	(59,045)
Repayments	(38,281)	—	(38,281)
Mortgage servicing liabilities resulting from mortgage loan sales	—	5,409	5,409
Changes in fair value included in income	(36,877)	(2,127)	(39,004)
Balance, June 30, 2016	\$ 294,551	\$ 4,681	\$ 299,232
Changes in fair value recognized during the year relating to liabilities still outstanding at June 30, 2016			
	\$ (29,667)	\$ (2,127)	\$ (31,794)

The information used in the preceding roll forwards represents activity for assets and liabilities measured at fair value on a recurring basis and identified as using “Level 3” inputs that are significant to the fair value measurement at either the beginning or the end of the periods presented. The Company had transfers among the fair value levels arising from transfers of IRLCs to mortgage loans held for sale at fair value upon purchase or funding of the respective mortgage loans and from the return to salability in the active secondary market of certain mortgage loans held for sale.

Table of Contents

## Assets and Liabilities Measured at Fair Value under the Fair Value Option

Net changes in fair values included in income for assets and liabilities carried at fair value as a result of management's election of the fair value option by income statement line item are summarized below:

	Quarter ended June 30, 2017			2016		
	Net gains on	Net	Total	Net gains on	Net	Total
	mortgage	mortgage		mortgage	mortgage	
	loans held	loan		loans held	loan	
	for sale at	servicing		for sale at	servicing	
	fair value	fees		fair value	fees	
	(in thousands)					
Assets:						
Mortgage loans held for sale at fair value	\$ 123,657	\$ —	\$ 123,657	\$ 164,527	\$ —	\$ 164,527
Mortgage servicing rights at fair value	—	(20,006)	(20,006)	—	(72,929)	(72,929)
	\$ 123,657	\$ (20,006)	\$ 103,651	\$ 164,527	\$ (72,929)	\$ 91,598
Liabilities:						
Excess servicing spread financing at fair value payable to PennyMac Mortgage Investment Trust	\$ —	\$ 7,156	\$ 7,156	\$ —	\$ 17,428	\$ 17,428
Mortgage servicing liabilities at fair value	—	1,509	1,509	—	2,066	2,066
	\$ —	\$ 8,665	\$ 8,665	\$ —	\$ 19,494	\$ 19,494

	Six months ended June 30, 2017			2016		
	Net gains on	Net	Total	Net gains on	Net	Total
	mortgage	mortgage		mortgage	mortgage	
	loans held	loan		loans held	loan	
	for sale at	servicing		for sale at	servicing	
	fair value	fees		fair value	fees	
	(in thousands)					
Assets:						
Mortgage loans held for sale at fair value	\$ 205,967	\$ —	\$ 205,967	\$ 300,608	\$ —	\$ 300,608

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Mortgage servicing rights at fair value	—	(35,202)	(35,202)	—	(143,252)	(143,252)
	\$ 205,967	\$ (35,202)	\$ 170,765	\$ 300,608	\$ (143,252)	\$ 157,356
Liabilities:						
Excess servicing spread financing at fair value payable to PennyMac Mortgage Investment Trust	\$ —	\$ 9,929	\$ 9,929	\$ —	\$ 36,877	\$ 36,877
Mortgage servicing liabilities at fair value	—	4,766	4,766	—	2,127	2,127
	\$ —	\$ 14,695	\$ 14,695	\$ —	\$ 39,004	\$ 39,004

Table of Contents

Following are the fair value and related principal amounts due upon maturity of assets accounted for under the fair value option:

	June 30, 2017		
	Fair value (in thousands)	Principal amount due upon maturity	Difference
Mortgage loans held for sale:			
Current through 89 days delinquent	\$ 2,719,560	\$ 2,592,354	\$ 127,206
90 days or more delinquent:			
Not in foreclosure	239,660	244,419	(4,759)
In foreclosure	78,382	78,573	(191)
	\$ 3,037,602	\$ 2,915,346	\$ 122,256

	December 31, 2016		
	Fair value (in thousands)	Principal amount due upon maturity	Difference
Mortgage loans held for sale:			
Current through 89 days delinquent	\$ 2,148,947	\$ 2,077,034	\$ 71,913
90 days or more delinquent:			
Not in foreclosure	19,227	19,399	(172)
In foreclosure	4,641	4,850	(209)
	\$ 2,172,815	\$ 2,101,283	\$ 71,532

## Assets Measured at Fair Value on a Nonrecurring Basis

Following is a summary of assets and liabilities that were measured at fair value on a nonrecurring basis during the periods presented:

June 30, 2017		Level 3	Total
Level 1	Level 2		
(in thousands)			
\$ —	\$ —	\$ 1,254,152	\$ 1,254,152



Mortgage servicing rights at lower of amortized cost or fair value

Real estate acquired in settlement of loans	—	—	523	523
	\$ —	\$ —	\$ 1,254,675	\$ 1,254,675

	December 31, 2016			Total
	Level 1	Level 2	Level 3	
	(in thousands)			
Mortgage servicing rights at lower of amortized cost or fair value	\$ —	\$ —	\$ 1,093,242	\$ 1,093,242
Real estate acquired in settlement of loans	—	—	1,152	1,152
	\$ —	\$ —	\$ 1,094,394	\$ 1,094,394

Table of Contents

The following table summarizes the total gains (losses) on assets measured at fair value on a nonrecurring basis:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Mortgage servicing rights at lower of amortized cost or fair value	\$ (30,635)	\$ (72,647)	\$ (16,636)	\$ (149,720)
Real estate acquired in settlement of loans	(73)	393	(105)	(42)
	\$ (30,708)	\$ (72,254)	\$ (16,741)	\$ (149,762)

## Fair Value of Financial Instruments Carried at Amortized Cost

The Company's Assets purchased from PennyMac Mortgage Investment Trust under agreements to resell, Assets sold under agreements to repurchase, Mortgage loan participation and sale agreements, Notes payable, Obligations under capital lease and amounts receivable from and payable to the Advised Entities are carried at amortized cost.

The Company's borrowings carried at amortized cost and the receivables from and payables to the Advised Entities do not have observable inputs and the fair value is measured using management's estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation. The Company has classified these financial instruments as "Level 3" fair value liabilities due to the lack of observable inputs to estimate their fair values and has concluded that those liabilities' fair values approximate the carrying value due to their short terms and/or variable interest rates.

## Valuation Techniques and Inputs

Most of the Company's financial assets, a portion of its MSRs and its ESS financing and MSLs are carried at fair value with changes in fair value recognized in current period income. Certain of the Company's financial assets and all of its MSRs, ESS and MSLs are "Level 3" fair value assets and liabilities which require the use of unobservable inputs that are significant to the estimation of the items' fair values. Unobservable inputs reflect the Company's own judgments about the factors that market participants use in pricing an asset or liability, and are based on the best information available under the circumstances.

Due to the difficulty in estimating the fair values of "Level 3" fair value assets and liabilities, management has assigned the responsibility for estimating the fair value of these items to specialized staff and subjects the valuation process to

significant senior management oversight. The Company's Financial Analysis and Valuation group (the "FAV group") is the Company's specialized staff responsible for estimating the fair values of "Level 3" fair value assets and liabilities other than IRLCs.

With respect to the non-IRLC "Level 3" valuations, the FAV group reports to the Company's senior management valuation committee, which oversees and approves the valuations. The FAV group monitors the models used for valuation of the Company's "Level 3" fair value assets and liabilities, including the models' performance versus actual results, and reports those results to the Company's senior management valuation committee. The Company's senior management valuation committee includes the Company's executive chairman and chief executive, chief financial, chief risk, chief enterprise operations and deputy chief financial officers.

The FAV group is responsible for reporting to the Company's senior management valuation committee on a monthly basis on the changes in the valuation of the "Level 3" fair value assets and liabilities, including major factors affecting the valuation and any changes in model methods and inputs. To assess the reasonableness of its valuations, the FAV group presents an analysis of the effect on the valuation of changes to the significant inputs to the models.

With respect to IRLCs, the Company has assigned responsibility for developing fair values to its Capital Markets Risk Management staff. The fair values developed by the Capital Markets Risk Management staff are reviewed by the Company's Capital Markets Operations group.

Table of Contents

Following is a description of the techniques and inputs used in estimating the fair values of “Level 2” and “Level 3” fair value assets and liabilities:

Mortgage Loans Held for Sale

Most of the Company’s mortgage loans held for sale at fair value are saleable into active markets and are therefore categorized as “Level 2” fair value assets and their fair values are determined using their quoted market or contracted selling price or market price equivalent.

Certain of the Company’s mortgage loans held for sale are non-saleable into active markets and are therefore categorized as “Level 3” fair value assets:

- The Company may purchase certain delinquent government guaranteed or insured mortgage loans from Ginnie Mae guaranteed pools in its mortgage loan servicing portfolio. The Company’s right to purchase delinquent government guaranteed or insured mortgage loans arises as the result of the borrower’s failure to make payments for at least three consecutive months preceding the month of repurchase by the Company and provides an alternative to the Company’s obligation to continue advancing principal and interest at the coupon rate of the related Ginnie Mae security. Such repurchased mortgage loans may be resold to third-party investors and thereafter may be repurchased to the extent eligible for resale into a new Ginnie Mae guaranteed pool. Such eligibility for resale generally occurs when the repurchased mortgage loans held by the Company that are not saleable into active markets become current either through the borrower’s reperformance or through completion of a modification of the mortgage loan’s terms.
- Certain of the Company’s mortgage loans held for sale may become non-saleable into active markets due to identification of a defect by the Company or to the repurchase by the Company of a mortgage loan with an identified defect.

The significant unobservable inputs used in the fair value measurement of the Company’s “Level 3” fair value mortgage loans held for sale at fair value are discount rates, home price projections, voluntary prepayment/resale speeds and total prepayment speeds. Significant changes in any of those inputs in isolation could result in a significant change to the mortgage loans’ fair value measurement. Increases in home price projections are generally accompanied by an increase in voluntary prepayment speeds.

Following is a quantitative summary of key “Level 3” fair value inputs used in the valuation of mortgage loans held for sale at fair value:

Key inputs	June 30, 2017	December 31, 2016
Discount rate:		
Range	2.9% – 9.4%	2.6% – 8.8%
Weighted average	2.9%	3.0%
Twelve-month projected housing price index change:		
Range	2.6% – 4.7%	2.0% – 4.5%
Weighted average	3.8%	3.7%
Voluntary prepayment / resale speed (1):		
Range	0.1% – 19.3%	0.1% – 24.4%
Weighted average	17.3%	20.9%
Total prepayment speed (2):		
Range	0.1% – 40.0%	0.1% – 39.8%
Weighted average	37.7%	34.3%

---

(1) Voluntary prepayment/resale speed is measured using Life Voluntary Conditional Prepayment Rate (“CPR”).

(2) Total prepayment speed is measured using Life Total CPR.

Changes in fair value attributable to changes in instrument specific credit risk are measured by reference to the change in the respective mortgage loan’s delinquency status and performance history at period end from the later of the

Table of Contents

beginning of the period or acquisition date. Changes in fair value of mortgage loans held for sale are included in Net gains on mortgage loans held for sale at fair value in the Company's consolidated statements of income.

## Derivative Financial Instruments

## Interest Rate Lock Commitments

The Company categorizes IRLCs as a "Level 3" fair value asset or liability. The Company estimates the fair value of an IRLC based on quoted Agency MBS prices, its estimate of the fair value of the MSR it expects to receive in the sale of the mortgage loans and the probability that the mortgage loan will fund or be purchased (the "pull-through rate").

The significant unobservable inputs used in the fair value measurement of the Company's IRLCs are the pull-through rate and the MSR component of the Company's estimate of the fair value of the mortgage loans it has committed to purchase. Significant changes in the pull-through rate or the MSR component of the IRLCs, in isolation, could result in significant changes in fair value measurement. The financial effects of changes in these inputs are generally inversely correlated as increasing interest rates have a positive effect on the fair value of the MSR component of IRLC fair value, but increase the pull-through rate for the mortgage loan principal and interest payment cash flow component, which has decreased in fair value. Changes in fair value of IRLCs are included in Net gains on mortgage loans acquired for sale at fair value and may be allocated to Net mortgage loan servicing fees as a hedge of the fair value of MSRs in the consolidated statements of income when it is included as a component of the MSR hedging strategy.

Following is a quantitative summary of key "Level 3" fair value inputs used in the valuation of IRLCs:

Key inputs	June 30, 2017	December 31, 2016
Pull-through rate:		
Range	38.7% – 100.0%	35.0% – 100.0%
Weighted average	86.2%	84.9%
Mortgage servicing rights value expressed as:		
Servicing fee multiple:		
Range	1.1 – 5.7	1.2 – 5.9
Weighted average	4.0	4.3
Percentage of unpaid principal balance:		
Range	0.3% – 2.5%	0.3% – 2.8%
Weighted average	1.3%	1.3%

## Hedging Derivatives

Fair value of hedging derivative financial instruments based on exchange traded market prices are categorized by the Company as “Level 1” fair value assets and liabilities. Fair value of hedging derivative financial instruments based on observable MBS prices or interest rate volatilities in the MBS market are categorized as “Level 2” fair value assets and liabilities. Changes in the fair value of hedging derivatives are included in Net gains on mortgage loans acquired for sale at fair value, or Net mortgage loan servicing fees – Amortization, impairment and change in fair value of mortgage servicing rights and mortgage servicing liabilities, as applicable, in the consolidated statements of income.

## Mortgage Servicing Rights

MSRs are categorized as “Level 3” fair value assets. The Company uses a discounted cash flow approach to estimate the fair value of MSRs. This approach consists of projecting net servicing cash flows discounted at a rate that management believes market participants would use in their determinations of fair value. The key inputs used in the estimation of the fair value of MSRs include the applicable pricing spread (discount rate), the prepayment rates of the underlying mortgage loans, and the per-loan annual cost to service the respective mortgage loans. Changes in the fair value of MSRs are included in Net servicing fees—Amortization, impairment and change in fair value of mortgage servicing rights and mortgage servicing liabilities in the consolidated statements of income.

Table of Contents

Following are the key inputs used in determining the fair value of MSR's at the time of initial recognition, excluding MSR purchases:

	Quarter ended June 30,		2016	
	2017	2016	2016	2015
	Fair value	Amortized cost	Fair value	Amortized cost
(Amount recognized and unpaid principal balance of underlying mortgage loans in thousands)				
MSR and pool characteristics:				
Amount recognized	\$ 7,945	\$ 128,927	\$ 4,820	\$ 127,652
Unpaid principal balance of underlying mortgage loans	\$ 795,875	\$ 11,005,607	\$ 400,433	\$ 10,370,549
Weighted average servicing fee rate (in basis points)	29	30	33	29
Key inputs:				
Pricing spread (1)				
Range	7.6% – 11.0%	7.6% – 15.2%	7.2% – 9.5%	7.2% – 14.4%
Weighted average	10.4%	10.7%	8.7%	8.9%
Annual total prepayment speed (2)				
Range	4.2% – 71.8%	4.0% – 45.7%	3.3% – 45.1%	3.9% – 50.9%
Weighted average	12.9%	9.7%	12.2%	9.8%
Life (in years)				
Range	0.8 – 11.5	1.6 – 11.7	1.6 – 11.8	1.3 – 11.8
Weighted average	6.5	7.7	6.7	7.7
Per-loan annual cost of servicing				
Range	\$78 – \$98	\$79 – \$98	\$68 – \$105	\$68 – \$106
Weighted average	\$88	\$89	\$89	\$90

(1) Pricing spread represents a margin that is applied to a reference interest rate's forward rate curve to develop periodic discount rates. The Company applies a pricing spread to the United States Dollar London Interbank Offered Rate ("LIBOR") curve for purposes of discounting cash flows relating to MSR's.

(2) Prepayment speed is measured using Life Total CPR.

	Six months ended June 30,		2016	
	2017	2016	2016	2015
	Fair value	Amortized cost	Fair value	Amortized cost
(Amount recognized and unpaid principal balance of underlying mortgage loans in thousands)				
MSR and pool characteristics:				
Amount recognized	\$13,929	\$259,145	\$9,288	\$223,966
Unpaid principal balance of underlying mortgage loans	\$1,299,940	\$21,706,206	\$768,240	\$17,354,721



Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Weighted average servicing fee rate (in basis points)	30	29	33	31
Key inputs:				
Pricing spread (1)				
Range	7.6% – 11.0%	7.6% – 15.2%	7.2% – 9.8%	7.2% – 14.4%
Weighted average	10.5%	10.7%	8.7%	8.9%
Annual total prepayment speed (2)				
Range	4.2% – 71.8%	3.4% – 45.7%	3.3% – 52.3%	3.8% – 50.9%
Weighted average	12.1%	9.0%	12.7%	10.3%
Life (in years)				
Range	0.8 – 11.5	1.6 – 12.2	1.3 – 11.8	1.3 – 11.9
Weighted average	6.7	8.0	6.5	7.5
Per-loan annual cost of servicing				
Range	\$78 – \$101	\$79 – \$101	\$68 – \$105	\$68 – \$106
Weighted average	\$89	\$90	\$85	\$87

41

---

Table of Contents

(1) Pricing spread represents a margin that is applied to a reference interest rate's forward rate curve to develop periodic discount rates. The Company applies a pricing spread to the United States Dollar LIBOR curve for purposes of discounting cash flows relating to MSR.

(2) Prepayment speed is measured using Life Total CPR.

Following is a quantitative summary of key inputs used in the valuation and assessment for impairment of the Company's MSRs at period end and the effect on fair value from adverse changes in those inputs (weighted averages are based upon UPB):

	June 30, 2017		December 31, 2016	
	Fair value	Amortized cost	Fair value	Amortized cost
	(Carrying value, unpaid principal balance of underlying mortgage loans and effect on fair value amounts in thousands)			
MSR and pool characteristics:				
Carrying value	\$ 678,441	\$ 1,273,158	\$ 515,925	\$ 1,111,747
Unpaid principal balance of underlying mortgage loans	\$ 56,775,177	\$ 100,448,732	\$ 43,667,165	\$ 85,509,941
Weighted average note interest rate	4.0%	3.7%	4.1%	3.7%
Weighted average servicing fee rate (in basis points)	32	30	32	31
Key inputs:				
Pricing spread (1):				
Range	10.0% – 14.3%	7.6% – 14.3%	7.6% – 14.9%	7.6% – 14.9%
Weighted average	10.6%	10.6%	10.1%	10.7%
Effect on fair value of (2):				
5% adverse change	\$ (12,381)	\$ (25,059)	\$ (9,097)	\$ (22,382)
10% adverse change	\$ (24,302)	\$ (49,154)	\$ (17,872)	\$ (43,889)
20% adverse change	\$ (46,865)	\$ (94,654)	\$ (34,516)	\$ (84,464)
Prepayment speed (3):				
Range	7.6% – 70.8%	7.3% – 43.2%	7.0% – 46.7%	6.6% – 43.9%
Weighted average	10.6%	9.2%	10.3%	8.7%
Average life (in years):				
Range	3.5 – 8.2	2.0 – 8.9	1.3 – 8.6	1.6 – 9.4
Weighted average	6.8	7.8	6.7	8.1
Effect on fair value of (2):				
5% adverse change	\$ (11,403)	\$ (20,003)	\$ (8,818)	\$ (16,636)
10% adverse change	\$ (22,421)	\$ (39,356)	\$ (17,336)	\$ (32,750)
20% adverse change	\$ (43,374)	\$ (76,236)	\$ (33,533)	\$ (63,513)
Annual per-loan cost of servicing:				
Range	\$78 – \$98	\$79 – \$98	\$78 – \$101	\$79 – \$101
Weighted average	\$89	\$89	\$92	\$92

Effect on fair value of (2):

5% adverse change	\$ (6,645)	\$ (9,965)	\$ (5,612)	\$ (8,890)
10% adverse change	\$ (13,290)	\$ (19,230)	\$ (11,225)	\$ (17,781)
20% adverse change	\$ (26,580)	\$ (39,858)	\$ (22,450)	\$ (35,562)

---

- (1) The Company applies a pricing spread to the United States Dollar LIBOR curve for purposes of discounting cash flows relating to MSRs.
- (2) For MSRs carried at fair value, an adverse change in one of the above-mentioned key inputs is expected to result in a reduction in fair value which will be recognized in income. For MSRs carried at lower of amortized cost or fair value, an adverse change in one of the above-mentioned key inputs may result in recognition of MSR impairment. The extent of the recognized MSR impairment will depend on the relationship of fair value to the carrying value of such MSRs.
- (3) Prepayment speed is measured using Life Total CPR.

42

---

Table of Contents

The preceding sensitivity analyses are limited in that they were performed at a particular point in time; only contemplate the movements in the indicated inputs; do not incorporate changes to other inputs; are subject to the accuracy of various models and inputs used; and do not incorporate other factors that would affect the Company's overall financial performance in such events, including operational adjustments made by management to account for changing circumstances. For these reasons, the preceding estimates should not be viewed as earnings forecasts.

## Excess Servicing Spread Financing at Fair Value

The Company categorizes ESS as a "Level 3" fair value liability. Because the ESS is a claim to a portion of the cash flows from MSR, the fair value measurement of the ESS is similar to that of MSR. The Company uses the same discounted cash flow approach to measuring the ESS as used to measure MSR except that certain inputs relating to the cost to service the mortgage loans underlying the MSR and certain ancillary income are not included as these cash flows do not accrue to the holder of the ESS. The key inputs used in the estimation of ESS fair value include pricing spread (discount rate) and prepayment speed. Significant changes to either of those inputs in isolation could result in a significant change in the fair value of ESS. Changes in these key inputs are not necessarily directly related.

ESS is generally subject to fair value increases when mortgage interest rates increase. Increasing mortgage interest rates normally slow mortgage refinancing activity. Decreased refinancing activity increases the life of the mortgage loans underlying the ESS, thereby increasing its fair value, which is owed to PMT. Increases in the fair value of ESS decrease income and are included in Net mortgage loan servicing fees—Change in fair value of excess servicing spread payable to PennyMac Mortgage Investment Trust.

Following are the key inputs used in estimating the fair value of ESS financing:

	June 30, 2017	December 31, 2016
Carrying value (in thousands)	\$261,796	\$288,669
ESS and pool characteristics:		
Unpaid principal balance of underlying mortgage loans (in thousands)	\$29,716,891	\$32,376,359
Average servicing fee rate (in basis points)	34	34
Average excess servicing spread (in basis points)	19	19
Key inputs:		
Pricing spread (1):		
Range	3.8% – 4.4%	3.8% – 4.8%
Weighted average	4.2%	4.4%
Annualized prepayment speed (2):		

Range	7.7% – 70.9%	7.0% – 41.3%
Weighted average	10.7%	10.5%
Average life (in years):		
Range	0.7 – 8.1	1.4 – 8.6
Weighted average	6.6	6.8

---

(1)The Company applies a pricing spread to the United States Dollar LIBOR curve for purposes of discounting cash flows relating to ESS.

(2)Prepayment speed is measured using Life Total CPR.

### Mortgage Servicing Liabilities

MSLs are categorized as “Level 3” fair value liabilities. The Company uses a discounted cash flow approach to estimate the fair value of MSLs. This approach consists of projecting net servicing cash flows discounted at a rate that management believes market participants would use in their determinations of fair value. The key inputs used in the estimation of the fair value of MSLs include the applicable pricing spread (discount rate), the prepayment rates of the underlying mortgage loans, and the per-loan annual cost to service the respective mortgage loans. Changes in the fair value of MSLs are included in Net servicing fees—Amortization, impairment and change in fair value of mortgage servicing rights and mortgage servicing liabilities in the consolidated statements of income.

Table of Contents

Following are the key inputs used in determining the fair value of MSLs:

	June 30, 2017	December 31, 2016
MSL and pool characteristics:		
Carrying value (in thousands)	\$ 18,295	\$ 15,192
Unpaid principal balance of underlying mortgage loans (in thousands)	\$ 1,698,588	\$ 2,074,896
Weighted average servicing fee rate (in basis points)	25	25
Key inputs:		
Pricing spread (1)	7.8%	8.0%
Prepayment speed (2)	32.3%	31.7%
Average life (in years)	3.6	3.7
Annual per-loan cost of servicing	\$ 443	\$ 497

- 
- (1) The Company applies a pricing spread to the United States Dollar LIBOR curve for purposes of discounting cash flows relating to MSLs.
- (2) Prepayment speed is measured using Life Total CPR.

#### Note 9—Mortgage Servicing Rights and Mortgage Servicing Liabilities

##### Carried at Fair Value

The activity in MSRs carried at fair value is as follows:

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Balance at beginning of period	\$ 506,916	\$ 594,403	\$ 515,925	\$ 660,247
Additions:				
Purchases	183,586	—	183,789	11
Mortgage servicing rights resulting from mortgage loan sales	7,945	4,820	13,929	9,288
	191,531	4,820	197,718	9,299
Change in fair value due to:				
Changes in valuation inputs used in valuation model				
(1)	(1,588)	(51,855)	404	(100,731)
Other changes in fair value (2)	(18,418)	(21,074)	(35,606)	(42,521)
Total change in fair value	(20,006)	(72,929)	(35,202)	(143,252)
Balance at end of period	\$ 678,441	\$ 526,294	\$ 678,441	\$ 526,294
		December		
	June 30,	31,		
	2017	2016		
	(in thousands)			
Fair value of mortgage servicing rights pledged to secure Assets sold under agreements to repurchase and Notes payable	\$ 468,138	\$ 509,847		

(1) Principally reflects changes in discount rates and prepayment speed inputs, primarily due to changes in market interest rates, and changes in expected borrower performance and servicer losses given default.

(2) Represents changes due to realization of cash flows.

Table of Contents

Carried at Lower of Amortized Cost or Fair Value

The activity in MSRs carried at the lower of amortized cost or fair value is summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Amortized cost:				
Balance at beginning of period	\$ 1,299,093	\$ 866,989	\$ 1,206,694	\$ 798,925
Mortgage servicing rights resulting from mortgage loan sales	128,927	127,652	259,145	223,966
Amortization	(43,279)	(33,050)	(81,098)	(61,300)
Balance at end of period	1,384,741	961,591	1,384,741	961,591
Valuation allowance:				
Balance at beginning of period	(80,948)	(124,310)	(94,947)	(47,237)
Reductions (additions)	(30,635)	(72,647)	(16,636)	(149,720)
Balance at end of period	(111,583)	(196,957)	(111,583)	(196,957)
Mortgage servicing rights, net at end of period	\$ 1,273,158	\$ 764,634	\$ 1,273,158	\$ 764,634
Fair value of mortgage servicing rights at beginning of period	\$ 1,227,077	\$ 743,062	\$ 1,112,302	\$ 766,345
Fair value of mortgage servicing rights at end of period	\$ 1,273,364	\$ 764,634	\$ 1,273,364	\$ 764,634
		December		
	June 30,	31,		
	2017	2016		
	(in thousands)			
Fair value of mortgage servicing rights pledged to secure assets sold under agreements to repurchase and note payable	\$ 1,267,981	\$ 1,107,824		

The following table summarizes the Company's estimate of future amortization of its existing MSRs. This estimate was developed with the inputs applicable to the June 30, 2017 valuation of MSRs. The inputs underlying the following estimate will change as market conditions and portfolio composition and behavior change, causing both actual and projected amortization levels to change over time.

Twelve month period ending June 30,	Estimated MSR amortization
-------------------------------------	----------------------------



	(in thousands)
2018	\$ 162,473
2019	145,784
2020	131,122
2021	117,708
2022	105,638
Thereafter	722,016
	\$ 1,384,741

Table of Contents

## Mortgage Servicing Liabilities Carried at Fair Value

The activity in MSLs carried at fair value is summarized below:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands)			
Balance at beginning of period	\$ 15,994	\$ 6,747	\$ 15,192	\$ 1,399
Mortgage servicing liabilities resulting from mortgage loan sales	3,810	—	7,869	5,409
Changes in fair value due to:				
Changes in valuation inputs used in valuation model (1)	4,705	—	7,995	—
Other changes in fair value (2)	(6,214)	(2,066)	(12,761)	(2,127)
Total change in fair value	(1,509)	(2,066)	(4,766)	(2,127)
Balance at end of period	\$ 18,295	\$ 4,681	\$ 18,295	\$ 4,681

(1) Principally reflects changes in expected borrower performance and servicer losses given default.

(2) Represents changes due to realization of cash flows.

Servicing fees relating to MSRs and MSLs are recorded in Net mortgage loan servicing fees—Mortgage loan servicing fees—From non-affiliates on the consolidated statements of income; late charges and other ancillary fees relating to MSRs and MSLs are recorded in Net mortgage loan servicing fees—Mortgage loan servicing fees—Ancillary and other fees on the Company's consolidated statements of income. Such amounts are summarized below:

Quarter ended June 30,

Six months ended June 30,

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

	2017	2016	2017	2016
	(in thousands)			
Contractual servicing fees	\$ 112,348	\$ 92,770	\$ 218,815	\$ 184,097
Ancillary and other fees:				
Late charges	5,905	1,424	12,589	3,044
Other	1,101	488	2,026	883
	\$ 119,354	\$ 94,682	\$ 233,430	\$ 188,024

Note 10—Carried Interest Due from Investment Funds

The activity in the Company's Carried Interest due from Investment Funds is summarized as follows:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands)		2017	
Balance at beginning of period	\$ 70,778	\$ 70,519	\$ 70,906	\$ 69,926
Carried Interest recognized during the period	241	244	113	837
Balance at end of period	\$ 71,019	\$ 70,763	\$ 71,019	\$ 70,763

The amount of the Carried Interest that will be received by the Company depends on the Investment Funds' future performance. As a result, the amount of Carried Interest recorded by the Company is based on the cash flows that would be produced assuming termination of the Investment Funds at period end and may be reduced in future periods based on the performance of the Investment Funds in those periods. However, the Company is not required to pay guaranteed returns to the Investment Funds and the amount of any reduction to Carried Interest will be limited to the amounts previously recognized.

During the quarter ended June 30, 2017, the Investment Funds entered into agreements to sell their remaining assets to a non-affiliate. If the sale settles as anticipated, the Company expects to collect a substantial portion of the Carried Interest during 2017 and the remaining balance during 2018. The sale agreements are subject to continuing due diligence and closing conditions. There can be no assurance regarding the size of the transaction or whether the transaction will be completed at all.

Table of Contents

## Note 11—Borrowings

The borrowing facilities described throughout this Note 11 contain various covenants, including financial covenants governing the Company's net worth, debt-to-equity ratio, profitability and liquidity. Management believes that the Company was in compliance with these covenants as of June 30, 2017.

## Assets Sold Under Agreement to Repurchase

The Company has multiple borrowing facilities in the form of asset sales under agreements to repurchase. These borrowing facilities are secured by mortgage loans held for sale at fair value or participation certificates backed by MSR. Eligible mortgage loans and participation certificates backed by MSRs and servicing advances are sold at advance rates based on the fair value of the assets sold. Interest is charged at a rate based on the buyer's overnight cost of funds rate or on LIBOR depending on the terms of the respective agreements. Mortgage loans and MSRs financed under these agreements may be re-pledged by the lenders.

Assets sold under agreements to repurchase are summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(dollars in thousands)			
Average balance of assets sold under agreements to repurchase	\$ 2,082,668	\$ 1,352,401	\$ 1,801,138	\$ 1,195,987
Weighted average interest rate (1)	3.13 %	3.06 %	3.11 %	2.87 %
Total interest expense	\$ 19,101	\$ 12,252	\$ 33,046	\$ 20,912
Maximum daily amount outstanding	\$ 3,617,164	\$ 1,803,371	\$ 3,617,164	\$ 1,863,455
			June 30,	December 31,
			2017	2016
			(dollars in thousands)	
Carrying value:				
Unpaid principal balance			\$ 3,023,288	\$ 1,736,922
Unamortized debt issuance costs			(1,960)	(1,808)
			\$ 3,021,328	\$ 1,735,114
Weighted average interest rate			2.91 %	3.02 %
Available borrowing capacity (2) (3):				
Committed			\$ 142,723	\$ 347,487

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Uncommitted	1,338,989	857,591
	\$ 1,481,712	\$ 1,205,078
Fair value of assets securing repurchase agreements:		
Mortgage loans held for sale	\$ 2,766,171	\$ 1,422,255
Servicing advances	\$ 72,010	\$ 81,306
Mortgage servicing rights	\$ 1,202,483	\$ 1,479,322
Assets purchased from PennyMac Mortgage Investment Trust under agreements to resell	\$ 150,000	\$ 150,000
Margin deposits placed with counterparties (4)	\$ 5,250	\$ 3,000

- 
- (1) Excludes the effect of amortization of commitment fees totaling \$2.6 million and \$1.8 million for the quarters ended June 30, 2017 and 2016, respectively, and \$4.9 million and \$3.6 million for the six months ended June 30, 2017 and 2016, respectively.
- (2) The amount the Company is able to borrow under asset repurchase agreements is tied to the fair value of unencumbered assets eligible to secure those agreements and the Company's ability to fund the agreements' margin requirements relating to the assets sold.
- (3) At June 30, 2017, available borrowing capacity includes \$500 million of temporary increases in credit facility limits expiring on various dates through September 30, 2017.
- (4) Margin deposits are included in Other assets on the Company's consolidated balance sheet.

Table of Contents

Following is a summary of maturities of outstanding advances under repurchase agreements by maturity date:

Remaining maturity at June 30, 2017	Balance (dollars in thousands)
Within 30 days	\$ 591,929
Over 30 to 90 days	1,973,532
Over 180 days to one year	457,827
Total loans sold under agreements to repurchase	\$ 3,023,288
Weighted average maturity (in months)	3.1

The amount at risk (the fair value of the assets pledged plus the related margin deposit, less the amount advanced by the counterparty and interest payable) relating to the Company's assets sold under agreements to repurchase is summarized by counterparty below as of June 30, 2017:

Counterparty	Amount at risk (in thousands)	Weighted average maturity of advances under repurchase agreement	Facility maturity
Credit Suisse First Boston Mortgage Capital LLC	\$ 91,587	April 27, 2018	April 27, 2018
Credit Suisse First Boston Mortgage Capital LLC	\$ 48,987	August 1, 2017	April 27, 2018
Bank of America, N.A.	\$ 69,343	September 19, 2017	May 25, 2018
JP Morgan Chase Bank, N.A.	\$ 41,179	August 19, 2017	October 13, 2017
Barclays Bank PLC	\$ 13,758	September 19, 2017	December 1, 2017
Citibank, N.A.	\$ 10,631	August 2, 2017	March 2, 2018
Morgan Stanley Bank, N.A.	\$ 9,914	August 17, 2017	August 25, 2017
Royal Bank of Canada	\$ 7,406	September 12, 2017	September 18, 2017

The Company is subject to margin calls during the period the agreements are outstanding and therefore may be required to repay a portion of the borrowings before the respective agreements mature if the fair value (as determined by the applicable lender) of the assets securing those agreements decreases.

#### Mortgage Loan Participation and Sale Agreements

Certain of the borrowing facilities secured by mortgage loans held for sale are in the form of mortgage loan participation and sale agreements. Participation certificates, each of which represents an undivided beneficial

ownership interest in mortgage loans that have been pooled with Fannie Mae, Freddie Mac or Ginnie Mae, are sold to the lender pending the securitization of the mortgage loans and sale of the resulting securities. A commitment to sell the securities resulting from the pending securitization between the Company and a non-affiliate is also assigned to the lender at the time a participation certificate is sold.

The purchase price paid by the lender for each participation certificate is based on the trade price of the security, plus an amount of interest expected to accrue on the security to its anticipated delivery date, minus a present value adjustment, any related hedging costs and a holdback amount that is based on a percentage of the purchase price. The holdback amount is not required to be paid to the Company until the settlement of the security and its delivery to the lender.

The mortgage loan participation and sale agreements are summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(dollars in thousands)			
Average balance	\$ 180,968	\$ 189,363	\$ 193,326	\$ 178,460
Weighted average interest rate (1)	2.32 %	1.69 %	2.12 %	1.68 %
Total interest expense	\$ 1,164	\$ 917	\$ 2,296	\$ 1,698
Maximum daily amount outstanding	\$ 286,138	\$ 737,319	\$ 719,434	\$ 737,319

(1) Excludes the effect of amortization of facility fees totaling \$102,000 and \$107,000 for the quarters ended June 30, 2017 and 2016, respectively, and \$231,000 and \$185,000 for the six months ended June 30, 2017 and 2016, respectively.

Table of Contents

	June 30, 2017		December 31, 2016	
	(dollars in thousands)			
Carrying value:				
Unpaid principal balance	\$ 243,707		\$ 671,562	
Unamortized debt issuance costs	(346)		(136)	
	\$ 243,361		\$ 671,426	
Weighted average interest rate	2.48	%	2.02	%
Fair value of mortgage loans pledged to secure mortgage loan participation and sale agreements	\$ 252,917		\$ 702,919	

## Notes Payable

On February 16, 2017, the Company, through the Issuer Trust, issued an aggregate principal amount of \$400 million in Term Notes to qualified institutional buyers under Rule 144A of the Securities Act of 1933, as amended. The Term Notes bear interest at a rate equal to one-month LIBOR plus 4.75% per annum. The Term Notes will mature on February 25, 2020 or, if extended pursuant to the terms of the related indenture supplement, February 25, 2021 (unless earlier redeemed in accordance with the terms of the Term Notes). The Term Notes rank pari passu with the VFN issued by Issuer Trust to PLS and are secured by certain participation certificates relating to Ginnie Mae MSR and ESS that are financed pursuant to the GNMA MSR Facility.

The Company entered into a revolving credit agreement, dated as of December 30, 2015, pursuant to which the lenders agreed to make revolving loans in an amount not to exceed \$100 million. On November 18, 2016, the credit agreement was amended and restated. Pursuant to the amended and restated credit agreement (“Credit Agreement”), the lenders have agreed to make revolving loans in an amount not to exceed \$150 million. The proceeds of the loans are to be used solely for working capital and general corporate purposes of the Company and its subsidiaries. Interest on the loans shall accrue at a per annum rate of interest equal to, at an election of the Company, either LIBOR plus the applicable margin or an alternate base rate (as defined in the Credit Agreement). During the existence of certain events of default, interest shall accrue at a higher rate. The maturity date of the loans is 364 days following the date of the Credit Agreement.

During December 2015, the Company entered into a note payable which is secured by MSRs relating to certain mortgage loans in the Company’s servicing portfolio. Interest is charged at a rate based on LIBOR plus the applicable contract margin.

Notes payable are summarized below:



	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(dollars in thousands)			
Average balance	\$ 461,365	\$ 121,941	\$ 378,638	\$ 103,554
Weighted average interest rate (1)	5.79 %	4.53 %	5.78 %	4.47 %
Total interest expense	\$ 8,059	\$ 2,291	\$ 12,999	\$ 3,889
Maximum daily amount outstanding	\$ 471,868	\$ 128,849	\$ 546,868	\$ 128,849

---

(1) Excluding the effect of amortization of debt issuance costs totaling \$1.1 million and \$0.9 million for the quarters ended June 30, 2017 and 2016, respectively, and \$2.0 million and \$1.5 million for the six months ended June 30, 2017 and 2016, respectively.

Table of Contents

	June 30, 2017		December 31, 2016	
	(dollars in thousands)			
Carrying value:				
Unpaid principal balance	\$ 433,865		\$ 151,935	
Unamortized debt issuance costs	(4,173)		(993)	
	\$ 429,692		\$ 150,942	
Weighted average interest rate	4.87	%	4.67	%
Unused amount	\$ 246,135		\$ 98,065	
Assets pledged to secure notes payable:				
Cash	\$ 50,458		\$ 91,788	
Carried Interest	\$ 71,019		\$ 70,906	
Mortgage servicing rights	\$ 533,636		\$ 138,349	

## Obligations under Capital Lease

In December 2015, the Company entered into a capital lease transaction secured by certain fixed assets and capitalized software. The capital lease matures on November 3, 2019 and bears interest at a spread over one-month LIBOR.

Obligations under capital lease are summarized below:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30, 2017	2016
	(dollars in thousands)			
Average balance	\$ 29,053	\$ 17,566	\$ 25,739	\$ 15,641
Weighted average interest rate	2.69	% 2.44	% 2.69	% 2.44
Total interest expense	\$ 221	\$ 161	\$ 380	\$ 224
Maximum daily amount outstanding	\$ 30,044	\$ 24,720	\$ 30,044	\$ 24,720

	June 30, 2017		December 31, 2016	
	(in thousands)			
Unpaid principal balance	\$ 26,641		\$ 23,424	
Weighted average interest rate	2.70	%	2.48	%

Assets pledged to secure obligations under capital lease:

Furniture, fixtures and equipment	\$ 27,476	\$ 25,134
Capitalized software	\$ 1,797	\$ 515

#### Excess Servicing Spread Financing

In conjunction with the Company's purchase from non-affiliates of certain MSRs on pools of Agency-backed residential mortgage loans, the Company has entered into sale and assignment agreements with PMT. Under these agreements, the Company sold to PMT the right to receive ESS cash flows relating to certain MSRs. The Company retained all ancillary income associated with servicing the loans and a fixed base servicing fee. The Company continues to be the servicer of the mortgage loans and retains all servicing obligations, including responsibility to make servicing advances. The agreements are treated as financings and are carried at fair value with changes in fair value recognized in current period income.

Table of Contents

Following is a summary of ESS:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Balance at beginning of period	\$ 277,484	\$ 321,976	\$ 288,669	\$ 412,425
Issuances of excess servicing spread to PennyMac Mortgage Investment Trust	1,380	1,690	2,953	3,601
Accrual of interest	4,366	5,713	9,013	12,728
Repayment	(14,278)	(17,400)	(28,910)	(38,281)
Settlement (1)	—	—	—	(59,045)
Change in fair value	(7,156)	(17,428)	(9,929)	(36,877)
Balance at end of period	\$ 261,796	\$ 294,551	\$ 261,796	\$ 294,551

(1) On February 29, 2016, the Company and PMT terminated the 2/1/13 Spread Acquisition Agreement and all amendments thereto. In connection with the termination of the 2/1/13 Spread Acquisition Agreement, the Company reacquired from PMT all of its right, title and interest in and to all of the Fannie Mae ESS previously sold by the Company to PMT under the 2/1/13 Spread Acquisition Agreement and then subject to such 2/1/13 Spread Acquisition Agreement. On February 29, 2016, the Company also reacquired from PMT all of its right, title and interest in and to all of the Freddie Mac ESS previously sold to PMT by the Company.

#### Note 12—Liability for Losses Under Representations and Warranties

Following is a summary of the Company's liability for losses under representations and warranties:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Balance at beginning of period	\$ 19,436	\$ 22,209	\$ 19,067	\$ 20,611
Provision for losses on mortgage loans sold:				
Resulting from sales of mortgage loans	1,296	2,286	2,698	4,368
Reduction in liability due to change in estimate	(1,020)	—	(1,892)	—
Incurred losses	(144)	(218)	(305)	(702)
Balance at end of period	\$ 19,568	\$ 24,277	\$ 19,568	\$ 24,277
Unpaid principal balance of mortgage loans subject to representations and warranties at end of period	\$ 106,284,973	\$ 72,151,175		

Note 13—Income Taxes

The Company's effective tax rates were 12.4% and 11.8% for the quarters ended June 30, 2017 and 2016, respectively, and 12.4% and 11.9% for the six months ended June 30, 2017 and 2016, respectively. The difference between the Company's effective tax rate and the statutory rate is primarily due to the allocation of earnings to the noncontrolling interest unitholders. As the noncontrolling interest unitholders convert their ownership units into the Company's shares, the portion of the Company's income that will be subject to corporate federal and state statutory tax rates will increase, which will in turn increase the Company's effective income tax rate.

Table of Contents

## Note 14—Noncontrolling Interest

Net income attributable to the Company's common stockholders and the effects of changes in noncontrolling ownership interest in PennyMac are summarized below:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30, 2017	2016
	(in thousands)			
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 10,479	\$ 14,475	\$ 21,358	\$ 19,650
Increase in the Company's additional paid-in capital for exchanges of Class A units of Private National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	\$ 8,164	\$ 2,039	\$ 16,927	\$ 2,640
Shares of Class A common stock of PennyMac Financial Services, Inc. issued pursuant to exchange of Class A units of Private National Mortgage Acceptance Company, LLC	555	90	1,046	93
			June 30, 2017	December 31, 2016
Percentage of noncontrolling interest in Private National Mortgage Acceptance Company, LLC			69.4 %	70.6 %

## Note 15—Net Gains on Mortgage Loans Held for Sale

Net gains on mortgage loans held for sale at fair value is summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Cash (loss) gain:				
Mortgage loans	\$ 1,904	\$ 20,830	\$ (56,777)	\$ 42,231
Hedging activities	5,317	(77,593)	6,424	(150,133)

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

	7,221	(56,763)	(50,353)	(107,902)
Non-cash gain:				
From non-affiliates:				
Mortgage servicing rights and mortgage servicing liabilities resulting from mortgage loan sales	133,062	132,472	265,205	227,845
Provision for losses relating to representations and warranties:				
Pursuant to mortgage loan sales	(1,296)	(2,286)	(2,698)	(4,368)
Reduction in liability due to change in estimate	1,020	—	1,892	—
Change in fair value relating to mortgage loans and hedging derivatives held at period end:				
Interest rate lock commitments	(19,849)	18,377	(13,234)	46,488
Mortgage loans	(13,326)	11,669	(5,930)	31,517
Hedging derivatives	(7,235)	28,649	(6,634)	32,014
	99,597	132,118	188,248	225,594
Recapture payable to PennyMac Mortgage Investment Trust	(1,506)	(1,915)	(3,201)	(3,867)
	\$ 98,091	\$ 130,203	\$ 185,047	\$ 221,727

Table of Contents

## Note 16—Net Interest Expense

Net interest expense is summarized below:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands)			
Interest income:				
From non-affiliates:				
Short-term investments	\$ 657	\$ 284	\$ 994	\$ 456
Mortgage loans held for sale at fair value	23,714	13,262	40,329	23,743
Placement fees relating to custodial funds	8,577	4,786	13,679	6,060
	32,948	18,332	55,002	30,259
From PennyMac Mortgage Investment Trust—Financings receivable	2,025	2,222	3,830	3,824
	34,973	20,554	58,832	34,083
Interest expense:				
To non-affiliates:				
Assets sold under agreements to repurchase	19,101	12,252	33,046	20,912
Mortgage loan participation and sale agreements	1,164	917	2,296	1,698
Notes payable	8,059	2,291	12,999	3,889
Obligations under capital lease	221	161	380	224
Interest shortfall on repayments of mortgage loans serviced for Agency securitizations	3,304	3,422	6,927	5,527
Interest on mortgage loan impound deposits	662	710	1,690	1,475
	32,511	19,753	57,338	33,725
To PennyMac Mortgage Investment Trust—Excess servicing spread financing at fair value	4,366	5,713	9,013	12,728
	36,877	25,466	66,351	46,453
	\$ (1,904)	\$ (4,912)	\$ (7,519)	\$ (12,370)

## Note 17—Stock-based Compensation

Following is a summary of the stock-based compensation expense by type of instrument awarded:



	Quarter ended		Six months ended	
	June 30,		June 30,	
	2017	2016	2017	2016
	(in thousands)			
Performance-based RSUs	\$ 2,409	\$ 1,644	\$ 5,712	\$ 4,433
Stock options	1,163	1,423	2,439	2,503
Time-based RSUs	1,294	641	2,239	1,348
Exchangeable PNMAC units	—	18	—	43
	\$ 4,866	\$ 3,726	\$ 10,390	\$ 8,327

Following is a summary of equity award activity:

	Quarter ended June 30, 2017		
	Performance based RSUs	Stock options	Time-based RSUs
	(in thousands)		
March 31, 2017	3,160	3,571	646
Granted	—	—	—
Vested units and exercised options	(446)	(5)	(22)
Forfeited or canceled	(308)	(17)	(6)
June 30, 2017	2,406	3,549	618

Table of Contents

	Quarter ended June 30, 2016		
	Performance	Stock	Time-based
	based		
	RSUs	options	RSUs
	(in thousands)		
March 31, 2016	2,686	2,799	454
Granted	—	—	—
Vested units and exercised options	—	—	(49)
Forfeited or canceled	(13)	(13)	(7)
June 30, 2016	2,673	2,786	398
	Six months ended June 30, 2017		
	Performance	Stock	Time-based
	based		
	RSUs	options	RSUs
	(in thousands)		
December 31, 2016	2,475	2,738	382
Granted	694	861	405
Vested units and exercised options	(446)	(25)	(160)
Forfeited or canceled	(317)	(25)	(9)
June 30, 2017	2,406	3,549	618
	Six months ended June 30, 2016		
	Performance	Stock	Time-based
	based		
	RSUs	options	RSUs
	(in thousands)		
December 31, 2015	2,351	1,845	271
Granted	813	962	251
Vested units and exercised options	—	—	(115)
Forfeited or canceled	(491)	(21)	(9)
June 30, 2016	2,673	2,786	398

Note 18—Supplemental Cash Flow Information

	Six months ended	
	June 30,	
	2017	2016
	(in thousands)	
Cash paid for interest	\$ 68,884	\$ 44,065
Cash paid for income taxes	\$ 36	\$ 43
Non-cash investing activity:		
Mortgage servicing rights resulting from mortgage loan sales	\$ 273,074	\$ 233,254
Mortgage servicing liabilities resulting from mortgage loan sales	\$ 7,869	\$ 5,409
Unsettled portion of MSR acquisitions	\$ 24,323	\$ —
Non-cash financing activity:		
Transfer of excess servicing spread pursuant to a recapture agreement with PennyMac Mortgage Investment Trust	\$ 2,953	\$ 3,601
Issuance of common stock in settlement of director fees	\$ 169	\$ 149

#### Note 19—Regulatory Capital and Liquidity Requirements

The Company, through PLS and PennyMac, is required to maintain specified levels of capital and liquidity to remain a seller/servicer in good standing with the Agencies. Such requirements generally are tied to the size of the Company's loan servicing portfolio or loan origination volume.

Table of Contents

The Agencies' capital and liquidity requirements, the calculations of which are specified by each Agency, are summarized below:

Agency—company subject to requirement	June 30, 2017		December 31, 2016	
	Actual (1)	Requirement	Actual (1)	Requirement
	(dollars in thousands)			
<b>Capital</b>				
Fannie Mae & Freddie Mac - PLS	\$ 1,395,498	\$ 407,095	\$ 1,289,464	\$ 335,883
Ginnie Mae - PLS	\$ 1,164,514	\$ 612,896	\$ 1,085,549	\$ 455,542
Ginnie Mae - PennyMac	\$ 1,356,831	\$ 674,186	\$ 1,261,565	\$ 501,097
HUD - PLS	\$ 1,164,514	\$ 2,500	\$ 1,085,549	\$ 2,500
<b>Liquidity</b>				
Fannie Mae & Freddie Mac - PLS	\$ 217,281	\$ 55,623	\$ 179,230	\$ 45,930
Ginnie Mae - PLS	\$ 217,281	\$ 143,568	\$ 179,230	\$ 115,304
<b>Tangible net worth / Total assets ratio</b>				
Fannie Mae and Freddie Mac – PLS	22	%	6	%
	26	%	6	%

(1) Calculated in compliance with the respective Agency's requirements.

Noncompliance with an Agency's requirements can result in such Agency taking various remedial actions up to and including terminating PennyMac's ability to sell loans to and service loans on behalf of the respective Agency.

#### Note 20—Commitments and Contingencies

##### Litigation

The business of the Company involves the collection of numerous accounts, as well as the validation of liens and compliance with various state and federal lending and servicing laws. Accordingly, the Company may be involved in proceedings, claims, and legal actions arising in the ordinary course of business. As of June 30, 2017, the Company was not involved in any legal proceedings, claims, or actions that in management's view would be reasonably likely to have a material adverse effect on the Company.

##### Commitments to Purchase and Fund Mortgage Loans

	June 30, 2017 (in thousands)
Commitments to purchase mortgage loans from PennyMac Mortgage Investment Trust	\$ 1,973,346
Commitments to fund mortgage loans	2,026,415
	\$ 3,999,761

Table of Contents

## Leases

The Company leases office facilities. Rent expense was \$4.2 million and \$2.6 million for the quarters ended June 30, 2017 and 2016, respectively and \$7.6 million and \$5.0 million for the six months ended June 30, 2017 and 2016, respectively.

The following table provides a summary of future minimum lease payments required under lease agreements, which may also contain renewal options as of June 30, 2017:

Twelve months ended June 30:	Future minimum lease payments (in thousands)
2018	\$ 12,158
2019	14,296
2020	14,650
2021	13,185
2022	10,633
Thereafter	37,033
	\$ 101,955

## Commitment to Make Distributions to PennyMac Owners

Under the terms of its Limited Liability Company Agreement, PennyMac is required to make cash distributions to the Company's noncontrolling interest holders in amounts sufficient to allow such noncontrolling interest holders to pay federal and state taxes on their allocable share of PennyMac taxable income. Such distributions are calculated and, if required, made quarterly.

## Note 21—Stockholders' Equity

In June 2017, the Company's Board of Directors authorized a stock repurchase program ("Repurchase Program") under which the Company may repurchase up to \$50 million of its outstanding Class A common stock. The Company did not repurchase any of its Class A common stock during the quarter and six months ended June 30, 2017.

Note 22—Segments and Related Information

The Company operates in three segments: loan production, loan servicing and investment management.

Two of the segments are in the mortgage banking business: loan production and loan servicing. The loan production segment performs mortgage loan origination, acquisition and sale activities. The loan servicing segment performs servicing of newly originated mortgage loans, execution and management of early buyout transactions and servicing of mortgage loans sourced and managed by the investment management segment for the Advised Entities, including executing the loan resolution strategy identified by the investment management segment relating to distressed mortgage loans.

The investment management segment represents the activities of the Company's investment manager, which include sourcing, performing diligence, bidding and closing investment asset acquisitions, managing correspondent production activities for PMT and managing the acquired assets for the Advised Entities.

Table of Contents

Financial performance and results by segment are as follows:

	Quarter ended June 30, 2017			Investment Management	Total
	Mortgage Banking Production (in thousands)	Servicing	Total		
Revenue: (1)					
Net gains on mortgage loans held for sale at fair value	\$ 74,706	\$ 23,385	\$ 98,091	\$ —	\$ 98,091
Mortgage loan origination fees	30,193	—	30,193	—	30,193
Fulfillment fees from PennyMac Mortgage Investment Trust	21,107	—	21,107	—	21,107
Net mortgage loan servicing fees	—	46,913	46,913	—	46,913
Management fees	—	—	—	6,007	6,007
Carried Interest from Investment Funds	—	—	—	241	241
Net interest income (expense):	—	—	—	—	—
Interest income	15,279	19,694	34,973	—	34,973
Interest expense	11,330	25,534	36,864	13	36,877
	3,949	(5,840)	(1,891)	(13)	(1,904)
Other	531	446	977	96	1,073
Total net revenue	130,486	64,904	195,390	6,331	201,721
Expenses	63,780	76,117	139,897	3,864	143,761
Income before provision for income taxes	\$ 66,706	\$ (11,213)	\$ 55,493	\$ 2,467	\$ 57,960
Segment assets at period end (2)	\$ 2,732,947	\$ 3,574,239	\$ 6,307,186	\$ 94,525	\$ 6,401,711

(1) All revenues are from external customers.

(2) Excludes parent Company assets, which consist primarily of working capital of \$3.0 million.

	Quarter ended June 30, 2016			Investment Management	Total
	Mortgage Banking Production (in thousands)	Servicing	Total		
Revenue: (1)					
Net gains on mortgage loans held for sale at fair value	\$ 115,894	\$ 14,309	\$ 130,203	\$ —	\$ 130,203



Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Mortgage loan origination fees	28,907	—	28,907	—	28,907
Fulfillment fees from PennyMac Mortgage Investment Trust	19,111	—	19,111	—	19,111
Net mortgage loan servicing fees	—	26,555	26,555	—	26,555
Management fees	—	—	—	5,730	5,730
Carried Interest from Investment Funds	—	—	—	244	244
Net interest income (expense):					
Interest income	11,528	9,026	20,554	—	20,554
Interest expense	6,825	18,625	25,450	16	25,466
	4,703	(9,599)	(4,896)	(16)	(4,912)
Other	849	851	1,700	268	1,968
Total net revenue	169,464	32,116	201,580	6,226	207,806
Expenses	64,959	53,085	118,044	5,504	123,548
Income (loss) before provision for income taxes	\$ 104,505	\$ (20,969)	\$ 83,536	\$ 722	\$ 84,258
Segment assets at period end (2)	\$ 2,222,007	\$ 2,289,922	\$ 4,511,929	\$ 95,141	\$ 4,607,070

(1) All revenues are from external customers.

(2) Excludes parent Company assets, which consist primarily of Deferred tax asset of \$4.9 million and working capital of \$4.4 million.

Table of Contents

	Six months ended June 30, 2017			Investment Management	Total
	Mortgage Banking Production (in thousands)	Servicing	Total		
Revenue: (1)					
Net gains (losses) on mortgage loans held for sale at fair value	\$ 137,543	\$ 47,504	\$ 185,047	\$ —	\$ 185,047
Loan origination fees	55,767	—	55,767	—	55,767
Fulfillment fees from PennyMac Mortgage Investment Trust	37,677	—	37,677	—	37,677
Net servicing fees	—	121,076	121,076	—	121,076
Management fees	—	—	—	11,381	11,381
Carried Interest from Investment Funds	—	—	—	113	113
Net interest income (expense):	—	—	—	—	—
Interest income	28,215	30,617	58,832	—	58,832
Interest expense	20,152	46,175	66,327	24	66,351
Other	8,063	(15,558)	(7,495)	(24)	(7,519)
Other	1,476	917	2,393	259	2,652
Total net revenue	240,526	153,939	394,465	11,729	406,194
Expenses	126,316	151,736	278,052	8,150	286,202
Income before provision for income taxes	\$ 114,210	\$ 2,203	\$ 116,413	\$ 3,579	\$ 119,992
Segment assets at period end (2)	\$ 2,732,947	\$ 3,574,239	\$ 6,307,186	\$ 94,525	\$ 6,401,711

(1) All revenues are from external customers.

(2) Excludes parent Company assets, which consist primarily of working capital of \$3.0 million.

	Six months ended June 30, 2016			Investment Management	Total
	Mortgage Banking Production (in thousands)	Servicing	Total		
Revenue: (1)					
Net gains on mortgage loans held for sale at fair value	\$ 194,108	\$ 27,619	\$ 221,727	\$ —	\$ 221,727
Loan origination fees	51,341	—	51,341	—	51,341
Fulfillment fees from PennyMac Mortgage Investment Trust	32,046	—	32,046	—	32,046
Net servicing fees	—	44,074	44,074	—	44,074
Management fees	—	—	—	11,642	11,642

Carried Interest from Investment Funds	—	—	—	837	837
Net interest income (expense):					
Interest income	19,905	14,177	34,082	1	34,083
Interest expense	11,708	34,769	46,477	26	46,503
	8,197	(20,592)	(12,395)	(25)	(12,420)
Other	1,088	619	1,707	204	1,911
Total net revenue	286,780	51,720	338,500	12,658	351,158
Expenses	113,867	112,151	226,018	10,792	236,810
Income before provision for income taxes and non-segment activities	172,913	(60,431)	112,482	1,866	114,348
Non-segment activities (2)	—	—	—	—	49
Income before provision for income taxes	\$ 172,913	\$ (60,431)	\$ 112,482	\$ 1,866	\$ 114,397
Segment assets at period end (3)	\$ 2,222,007	\$ 2,289,922	\$ 4,511,929	\$ 95,141	\$ 4,607,070

(1) All revenues are from external customers.

(2) Relates to parent Company interest expenses eliminated in consolidation.

Table of Contents

- (3) Excludes parent Company assets, which consist primarily of deferred tax asset of \$4.9 million and working capital of \$4.4 million.

Note 23—Recently Issued Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers (Subtopic 606) (“ASU 2014-09”), which supersedes the guidance in the Revenue Recognition topic of the ASC. ASU 2014-09 clarifies the principles for recognizing revenue in order to improve comparability of revenue recognition practices across entities and industries with certain scope exceptions including financial instruments, leases, and guarantees. ASU 2014-09 provides guidance intended to assist in the identification of contracts with customers and separate performance obligations within those contracts, the determination and allocation of the transaction price to those identified performance obligations and the recognition of revenue when a performance obligation has been satisfied. ASU 2014-09 also requires disclosures regarding the nature, amount, timing, and uncertainty of revenues and cash flows from contracts with customers.

Upon adoption, ASU 2014-09 provides for transition through either a full retrospective approach requiring the restatement of all presented prior periods or a modified retrospective approach, which allows the new recognition standard to be applied to only those contracts that are not completed at the date of transition. If the modified retrospective approach is adopted, a cumulative-effect adjustment to retained earnings is performed with additional disclosures required including the amount by which each line item is affected by the transition as compared to the guidance in effect before adoption and an explanation of the reasons for significant changes in these amounts.

The FASB has issued several amendments to the new revenue standard ASU 2014-09, including:

- In August 2015, ASU 2015-14, Revenue From Contracts With Customers (“ASU 2015-14”). This update deferred the initial effective date of ASU 2014-09. As a result of the issuance of ASU 2015-14, ASU 2014-09 is effective for annual reporting periods beginning on or after December 15, 2017, and interim periods within those annual periods. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period.
- In March 2016, ASU 2016-08, Principal Versus Agent Considerations (Reporting Revenue Gross versus Net). The amendments to this update are intended to improve the implementation guidance on principal versus agent considerations in ASU 2014-09 by clarifying how an entity should identify the unit of accounting (i.e. the specified good or service) and how an entity should apply the control principle to certain types of arrangements.
- In May 2016, ASU 2016-12, Narrow-Scope Improvements and Practical Expedients. The amendments to this update clarify certain core recognition principles and provide practical expedients available at transition. The improvements address collectability, sales tax presentation, noncash consideration, contract modifications and completed contracts at transition.
- In December 2016, ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers. The amendments to this update:
  - o Clarify that guarantee fees within the scope of the Guarantees topic of the ASC (other than product or service warranties) are not within the scope of the Revenue from Contracts with Customers topic of the ASC. Entities should see the Derivatives and Hedging topic, for guarantees accounted for as derivatives.
  - o Clarify guidance contained in the Other Assets and Deferred Costs—Contracts with Customers subtopic of the ASC that when performing impairment testing an entity should (a) consider expected contract renewals and extensions and (b) include both the amount of consideration it already has received but has not recognized as revenue and the amount it expects to receive in the future.
  - o Clarify the interaction of impairment testing with guidance in other ASC topics that impairment testing first should be performed on assets not within the scope of the Other Assets and Deferred Costs,

Intangibles-Goodwill and Other or the Property, Plant, and Equipment topics of the ASC (such as assets within the Inventory topic of the ASC), then assets within the scope of the Other Assets and Deferred Costs topic of the ASC, then asset groups and reporting units within the scope of the Other Assets and Deferred Costs, Intangibles-Goodwill and Other and the Property, Plant, and Equipment topics of the ASC.

Table of Contents

- o Clarify that all contracts within the scope of the Financial Services – Insurance topic are of the ASC excluded from the scope of the Revenue from Contracts with Customers topic.
  - o Provide optional exemptions from the disclosure requirement for remaining performance obligations for specific situations in which an entity need not estimate variable consideration to recognize revenue and expands the information that is required to be disclosed when an entity applies one of the optional exemptions.
  - o Clarify that the disclosure of revenue recognized from performance obligations satisfied (or partially satisfied) in previous periods applies to all performance obligations and is not limited to performance obligations with corresponding contract balances.
  - o Align the cost-capitalization guidance for advisors to both public funds and private funds in the Financial Services— Investment Companies—Other Expenses subtopic of the ASC.
  - In February 2017, ASU 2017-05, Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20) (“ASU 2017-05”). The amendments to this update clarify the scope of the Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets subtopic of the ASC, and add guidance for partial sales of nonfinancial assets. ASU 2017-05 clarifies that:
    - o A financial asset is within the scope of the Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets subtopic of the ASC if it meets the definition of an in substance nonfinancial asset and defines the term in substance nonfinancial asset, in part, as a financial asset promised to a counterparty in a contract if substantially all of the fair value of the assets (recognized and unrecognized) that are promised to the counterparty in the contract is concentrated in nonfinancial assets.
    - o It excludes all businesses and nonprofit activities from the scope of the Other Income – Gains and Losses from the Derecognition of Nonfinancial Assets subtopic of the ASC. Derecognition of all businesses and nonprofit activities should be accounted for in accordance with the Consolidation—Overall subtopic of the ASC.
    - o An entity should identify each distinct nonfinancial asset or in substance nonfinancial asset promised to a counterparty and derecognize each asset when a counterparty obtains control of it.
    - o An entity should allocate consideration to each distinct asset by applying the guidance in the Revenue from Contracts with Customers topic of the ASC on allocating the transaction price to performance obligations.
    - o An entity must derecognize a distinct nonfinancial asset or distinct in substance nonfinancial asset in a partial sale transaction when it (1) does not have (or ceases to have) a controlling financial interest in the legal entity that holds the asset in accordance with the Consolidations topic of the ASC and (2) transfers control of the asset in accordance with the Revenue from Contracts with Customers topic of the ASC. Once an entity transfers control of a distinct nonfinancial asset or distinct in substance nonfinancial asset, it is required to measure any noncontrolling interest it receives (or retains) at fair value.
- The Company’s revenues from contracts with customers that are subject to ASU 2014-09 include fulfillment fees, mortgage servicing fees, management fees, Carried Interest and certain reimbursed overhead costs. The Company has concluded that:
- The recognition and measurement of fulfillment fees, mortgage servicing fees and management fees is not expected to change as a result of the Company’s adoption of ASU 2014-09.



Table of Contents

- The Company's Carried Interest arrangements with the Investment Funds represent capital allocations to the Company. As a result, the Company has concluded as part of its assessment of the effect of the adoption of ASU 2014-09 that its Carried Interest represents an equity method investment subject to the Investments – Equity Method and Joint Ventures topic of the ASC. Therefore, effective January 1, 2018, the Company will recharacterize its Carried Interest as financial instruments under the equity method of accounting. This change is not expected to change the timing or amount of the Company's recognition of Carried Interest.
- The effect of the adoption of ASU 2014-09 on the presentation of overhead reimbursements will be to increase Other income and the Company's overhead expense categories by offsetting amounts. Under the Management Agreement, PMT is required to pay its pro rata portion of rent, telephone, utilities, office furniture, equipment, machinery and other office, internal and overhead expenses of the Company and its affiliates required for PMT's and its subsidiaries' operations. These expenses are allocated based on the ratio of PMT's proportion of gross assets compared to all remaining gross assets managed by the Company as calculated at each fiscal quarter end. The Company recognizes such reimbursements as expense offsets in its consolidated statements of income. ASU 2014-09 requires such reimbursements to be treated as revenues. The Company included \$1.6 million and \$2.4 million and \$3.0 million and \$5.0 million of such common overhead as expense offsets in the quarter and six month periods ended June 30, 2017 and 2016, respectively.

The Company intends to adopt ASU 2014-09 using the modified retrospective method. The Company does not expect to record a cumulative effect adjustment to its beginning retained earnings as a result of adoption of ASU 2014-09.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments—Overall: Recognition and Measurement of Financial Assets and Financial Liabilities (“ASU 2016-01”). ASU 2016-01 affects the accounting for equity investments, financial liabilities under the fair value option, the presentation and disclosure requirements for financial instruments, and the valuation allowance assessment when recognizing deferred tax assets resulting from unrealized losses on available-for-sale debt securities.

ASU 2016-01 requires that:

- All equity investments in unconsolidated entities (other than those accounted for using the equity method of accounting) with readily determinable fair values will generally be measured at fair value through earnings.
- When the fair value option has been elected for financial liabilities, changes in fair value due to instrument-specific credit risk will be recognized separately in other comprehensive income. The accumulated gains and losses due to these changes will be reclassified from accumulated other comprehensive income to earnings if the financial liability is settled before maturity.
- For financial instruments measured at amortized cost, public business entities will be required to use the exit price when measuring the fair value of financial instruments for disclosure purposes.
- Financial assets and financial liabilities shall be presented separately in the notes to the financial statements, grouped by measurement category (e.g., fair value, amortized cost, lower of cost or fair value) and form of financial asset (e.g., loans, securities).
- Public business entities will no longer be required to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost.
- Entities will have to assess the realizability of a deferred tax asset related to a debt security classified as available for sale in combination with the entity's other deferred tax assets.

The classification and measurement guidance will be effective for public business entities in fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption of the provision to record fair value changes for financial liabilities under the fair value option resulting from instrument-specific credit risk in other comprehensive income is permitted and can be elected for all financial statements of fiscal years and interim periods that have not yet been issued or that have not yet been made available for issuance. The adoption of ASU



2016-01 is not expected to have an effect on the Company's consolidated financial statements.

61

---

Table of Contents

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (“ASU 2016-02”). ASU 2016-02 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e. lessees and lessors) and supersedes previous leasing standards. ASU 2016-02 requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether the lease is effectively a financed purchase of the leased asset by the lessee. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification.

ASU 2016-02 is effective for the Company for reporting periods beginning after December 15, 2018, with early adoption permitted. The Company is currently assessing the potential impact that the adoption of ASU 2016-02 will have on its consolidated financial statements. As shown in Note 20 - Commitments and Contingencies, the Company had approximately \$102.0 million in future minimum lease payment commitments as of March 31, 2017. Were the Company to adopt ASU 2016-02 as of June 30, 2017, it would be required to recognize a right-of-use asset and a corresponding liability based on the present value of such obligation as of June 30, 2017. The Company does not expect to recognize a significant cumulative effect adjustment to its stockholders’ equity as a result of adopting ASU 2016-02.

In March 2016, the FASB issued ASU 2016-09, Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU 2016-09”). ASU 2016-09 simplifies several aspects of the accounting for share-based payment award transactions, including:

- Modifies the accounting for income taxes relating to share-based payments. All excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) will be recognized as income tax expense or benefit in the consolidated income statement. The tax effects of exercised or vested awards will be treated as discrete items in the reporting period in which they occur. An entity will recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period. Under current GAAP, excess tax benefits are recognized in additional paid-in capital; tax deficiencies are recognized either as an offset to accumulated excess tax benefits, if any, or in the consolidated income statement in the period they reduce income taxes payable.
- Changes the classification of excess tax benefits on the consolidated statement of cash flows. In the consolidated statement of cash flows, excess tax benefits will be classified along with other income tax cash flows as an operating activity. Under current GAAP, excess tax benefits are separated from other income tax cash flows and classified as a financing activity.
- Changes the requirement to estimate the number of awards that are expected to vest. Under ASU 2016-09, an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest as presently required or account for forfeitures when they occur. Under current GAAP, accruals of compensation cost are based on the number of awards that are expected to vest.

- Changes the tax withholding requirements for share-based payment awards to qualify for equity accounting. The threshold to qualify for equity classification permits withholding up to the maximum statutory tax rates in the applicable jurisdictions. Under current GAAP, for an award to qualify for equity classification is that an entity cannot partially settle the award in cash in excess of the employer's minimum statutory withholding requirements.
- Establishes GAAP for the classification of employee taxes paid when an employer withholds shares for tax withholding purposes. Cash paid by an employer when directly withholding shares for tax- withholding purposes should be classified as a financing activity. This guidance establishes GAAP related to the classification of withholding taxes in the statement of cash flows as there is no such guidance under current GAAP.

ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted for any organization in any interim or annual period. The adoption of ASU 2016-09 did not have a significant effect on the Company's consolidated financial statements.

Table of Contents

Note 24—Subsequent Events

The Company has evaluated the impacts of events that have occurred subsequent to June 30, 2017 through the filing date of the Consolidated Financial Statements with the SEC. Based on this evaluation, the Company has determined none of these events were required to be recognized or disclosed in the Consolidated Financial Statements and related Notes.

Table of Contents

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

Cautionary Statement Regarding Forward-Looking Statements

The following discussion and analysis of financial condition and results of operations should be read with the consolidated financial statements and the related notes of PennyMac Financial Services, Inc. ("PFSI") included within this Quarterly Report on Form 10-Q.

Statements contained in this Quarterly Report on Form 10-Q may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements involve known and unknown risks, uncertainties and other factors, which may cause actual results to be materially different from those expressed or implied in such statements. You can identify these forward-looking statements by words such as "may," "will," "should," "expect," "anticipate," "believe," "estimate," "intend," "plan" and other similar expressions. You should consider our forward-looking statements in light of the risks discussed under the heading "Risk Factors," as well as our consolidated financial statements, related notes, and the other financial information appearing elsewhere in this Quarterly Report on Form 10-Q and our other filings with the United States Securities and Exchange Commission ("SEC"). The forward-looking statements contained in this Quarterly Report on Form 10-Q are made as of the date hereof and we assume no obligation to update or supplement any forward-looking statements.

Overview

The following discussion and analysis provides information that we believe is relevant to an assessment and understanding of our consolidated results of operations and financial condition. Unless the context indicates otherwise, references in this Quarterly Report on Form 10-Q to the words "we," "us," "our" and the "Company" refer to PFSI.

Our Company

We are a specialty financial services firm with a comprehensive mortgage platform and integrated business primarily focused on the production and servicing of U.S. residential mortgage loans (activities which we refer to as mortgage banking) and the management of investments related to the U.S. mortgage market. We believe that our operating capabilities, specialized expertise, access to long-term investment capital, and our management's experience across all aspects of the mortgage business will allow us to profitably grow these activities and capitalize on other related opportunities as they arise in the future.

We operate and control all of the business and affairs of Private National Mortgage Acceptance Company, LLC (“PennyMac”) and are its sole managing member. PennyMac was founded in 2008 by members of our executive leadership team and two strategic partners, BlackRock Mortgage Ventures, LLC and HC Partners, LLC, formerly known as Highfields Capital Investments, LLC, together with its affiliates.

We conduct our business in three segments: loan production, loan servicing (together, these two activities comprise our mortgage banking activities) and investment management. Our principal mortgage banking subsidiary, PennyMac Loan Services, LLC (“PLS”), is a non-bank producer and servicer of mortgage loans in the United States. PLS is a seller/servicer for the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Corporation (“Freddie Mac”), each of which is a government-sponsored entity (“GSE”). It is also an approved issuer of securities guaranteed by the Government National Mortgage Association (“Ginnie Mae”), a lender of the Federal Housing Administration (“FHA”), a lender/servicer of the Veterans Administration (“VA”) and the U.S. Department of Agriculture (“USDA”), and a servicer for the Home Affordable Modification Program (“HAMP”). We refer to each of Fannie Mae, Freddie Mac, Ginnie Mae, FHA, VA and USDA as an “Agency” and collectively as the “Agencies.” PLS is able to service mortgage loans in all 50 states, the District of Columbia, Guam and the U.S. Virgin Islands, and originate mortgage loans in 49 states and the District of Columbia, either because PLS is properly licensed in a particular jurisdiction or exempt or otherwise not required to be licensed in that jurisdiction.

Our investment management subsidiary, PNMAC Capital Management, LLC (“PCM”), is a Delaware limited liability company registered with the Securities and Exchange Commission (“SEC”) as an investment adviser under the Investment Advisors Act of 1940, as amended. PCM manages PennyMac Mortgage Investment Trust (“PMT”), a mortgage real estate investment trust, listed on the New York Stock Exchange under the ticker symbol PMT, PNMAC Mortgage Opportunity Fund, LLC and PNMAC Mortgage Opportunity Fund, LP, both registered under the Investment

Table of Contents

Company Act of 1940 (“Investment Company Act”), as amended, an affiliate of these Funds and PNMAC Mortgage Opportunity Fund Investors, LLC. We refer to these funds collectively as our “Investment Funds” and, together with PMT, as our “Advised Entities.”

## Results of Operations

Our results of operations are summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Revenues:				
Net gains on mortgage loans held for sale at fair value	\$ 98,091	\$ 130,203	\$ 185,047	\$ 221,727
Mortgage loan origination fees	30,193	28,907	55,767	51,341
Fulfillment fees from PennyMac Mortgage Investment Trust	21,107	19,111	37,677	32,046
Net mortgage loan servicing fees	46,913	26,555	121,076	44,074
Management fees & Carried Interest	6,248	5,974	11,494	12,479
Net interest expense	(1,904)	(4,912)	(7,519)	(12,370)
Other	1,073	1,968	2,652	1,910
Total net revenue	201,721	207,806	406,194	351,207
Expenses	143,761	123,548	286,202	236,810
Provision for income taxes	7,214	9,963	14,860	13,559
Net income	\$ 50,746	\$ 74,295	\$ 105,132	\$ 100,838
Income before provision for income taxes by segment:				
Mortgage banking:				
Production	\$ 66,706	\$ 104,505	\$ 114,210	\$ 172,913
Servicing	(11,213)	(20,969)	2,203	(60,431)
Total mortgage banking	55,493	83,536	116,413	112,482
Investment management	2,467	722	3,579	1,866
Non-segment activities (1)	—	—	—	49
	\$ 57,960	\$ 84,258	\$ 119,992	\$ 114,397
During the period:				
Interest rate lock commitments issued	\$ 13,489,651	\$ 12,924,700	\$ 24,595,550	\$ 21,665,118
Fair value of mortgage loans purchased and originated for sale:				
Government-insured or guaranteed loans acquired from PennyMac Mortgage Investment Trust	\$ 11,227,406	\$ 9,933,264	\$ 21,244,194	\$ 16,783,840

Mortgage loans originated through consumer direct channel	1,292,687	1,513,858	2,353,899	2,736,621
	\$ 12,520,093	\$ 11,447,122	\$ 23,598,093	\$ 19,520,461
Unpaid principal balance of mortgage loans fulfilled for PennyMac Mortgage Investment Trust	\$ 5,918,027	\$ 5,174,020	\$ 10,549,933	\$ 8,433,383
Unpaid principal balance of mortgage loan servicing portfolio at period end:				
Owned:				
Mortgage servicing rights	\$ 157,223,909	\$ 117,036,803		
Mortgage servicing liabilities	1,698,588	751,193		
Mortgage loans held for sale	2,915,346	1,971,903		
	161,837,843	119,759,899		
Subserviced for Advised Entities	67,125,932	51,958,636		
	\$ 228,963,775	\$ 171,718,535		
Net assets of Advised Entities:				
PennyMac Mortgage Investment Trust	\$ 1,454,832	\$ 1,360,826		
Investment Funds	144,744	201,490		
	\$ 1,599,576	\$ 1,562,316		

(1) Relates to parent Company interest expense eliminated in consolidation.

Net income decreased \$23.5 million during the quarter ended June 30, 2017 compared to the same period in 2016 and increased \$4.3 million during the six months ended June 30, 2017 compared to the same period in 2016. These changes reflect the effects on our mortgage banking activities of higher market interest rates during the six months ended June 30, 2017 compared to the same period in 2016.

The decrease for the quarter ended in June 30, 2017 was primarily due to a decrease in Net gains on mortgage loans held for sale at fair value resulting from a decrease in our profit margin that more than offset an increase in mortgage loan production volume. The decrease in Net gains on mortgage loans held for sale at fair value was partially



Table of Contents

offset by an increase in Net mortgage loan servicing fees which reflects both growth in the our servicing portfolio and reduced fair value adjustments net of hedging losses.

The increase in net income for the six months ended in June 30, 2017 was primarily due to an increase in Net mortgage loan servicing fees resulting from lower amortization and losses in change in fair value of MSRs due to less adverse interest rate movements along with an increase in mortgage loan servicing fees from a larger servicing portfolio that was partially offset by a decrease in Net gains on mortgage loans held for sale at fair value and an increase in expenses due to the larger scale of our business.

Net Gains on Mortgage Loans Held for Sale at Fair Value

Most of our mortgage loan production is centered in government-insured or guaranteed mortgage loans. We source the majority of our government-insured or guaranteed mortgage loan production through PMT. PMT is not approved by Ginnie Mae as an issuer of Ginnie Mae-guaranteed securities which are backed by government-insured or guaranteed mortgage loans. We purchase the government-insured or guaranteed mortgage loans that PMT acquires through its correspondent lending activities and pay PMT a sourcing fee ranging from two to three and one-half basis points on the UPB of such mortgage loans.

During the quarter and six months ended June 30, 2017, we recognized Net gains on mortgage loans held for sale at fair value totaling \$98.1 million and \$185.1 million, respectively, a decrease of \$32.1 million and \$36.7 million, respectively, compared to the same periods in 2016. The decrease was primarily due to a decrease in our profit margin on mortgage loan production partially offset by growth in our mortgage loan production volume.

Table of Contents

Our net gains on mortgage loans held for sale are summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
From non affiliates:				
Cash gain (loss) :				
Mortgage loans	\$ 1,904	\$ 20,830	\$ (56,777)	\$ 42,231
Hedging activities	5,317	(77,593)	6,424	(150,133)
	7,221	(56,763)	(50,353)	(107,902)
Non-cash gain:				
Mortgage servicing rights and mortgage servicing liabilities resulting from mortgage loan sales	133,062	132,472	265,205	227,845
Provision for losses relating to representations and warranties:				
Pursuant to mortgage loan sales	(1,296)	(2,286)	(2,698)	(4,368)
Reduction in liability due to change in estimate	1,020	—	1,892	—
Change in fair value of mortgage loans and derivative financial instruments outstanding at period end:				
Interest rate lock commitments	(19,849)	18,377	(13,234)	46,488
Mortgage loans	(13,326)	11,669	(5,930)	31,517
Hedging derivatives	(7,235)	28,649	(6,634)	32,014
	99,597	132,118	188,248	225,594
From PennyMac Mortgage Investment Trust - Recapture payable	(1,506)	(1,915)	(3,201)	(3,867)
	\$ 98,091	\$ 130,203	\$ 185,047	\$ 221,727
During the period:				
Unpaid principal balance of mortgage loans sold	\$ 12,017,983	\$ 10,766,503	\$ 23,474,792	\$ 18,381,560
Interest rate lock commitments issued:				
Conventional mortgage loans	\$ 804,501	\$ 847,051	\$ 1,473,086	\$ 1,394,368
Government-insured or guaranteed mortgage loans	12,685,150	12,077,649	23,122,464	20,270,750
	\$ 13,489,651	\$ 12,924,700	\$ 24,595,550	\$ 21,665,118
At period end:				

Mortgage loans held for sale at fair value	\$ 3,037,602	\$ 2,097,138
Commitments to fund and purchase mortgage loans	\$ 3,999,761	\$ 3,868,230

Provision for Losses on Representations and Warranties

We record our estimate of the losses that we expect to incur in the future as a result of claims against us in connection with the representations and warranties we provide to the purchasers and insurers of the mortgage loans we sell in our Net gains on sale of mortgage loans held for sale at fair value. The representations and warranties require adherence to purchaser and insurer origination and underwriting guidelines, including but not limited to the validity of the lien securing the mortgage loan, property eligibility, borrower credit, income and asset requirements, and compliance with applicable federal, state and local law.

In the event of a breach of our representations and warranties, we may be required to either repurchase the mortgage loans with identified defects or indemnify the purchaser or insurer against future credit losses. In such cases, we bear any subsequent credit loss on the mortgage loans. Our credit loss may be reduced by any recourse we have to correspondent originators that sold such mortgage loans and breached similar or other representations and warranties. In such event, we have the right to seek a recovery of related repurchase losses from that correspondent seller.

Table of Contents

The method we use to estimate our losses on representations and warranties is a function of our estimate of future defaults, mortgage loan repurchase rates, the severity of loss in the event of defaults and the probability of reimbursement by the correspondent mortgage loan seller. We establish a liability at the time loans are sold and review our liability estimate on a periodic basis.

We recorded provisions for losses under representations and warranties as a component of Net gains on mortgage loans held for sale at fair value totaling \$276,000 and \$806,000 during the quarter and six months ended June 30, 2017, respectively, compared to \$2.3 million and \$4.4 million during the quarter and six months ended June 30, 2016. The decrease in provision for losses under representations and warranties during the quarter and six months ended June 30, 2017 compared to the same periods in 2016 was primarily due to a \$1.0 million and \$1.9 million, respectively, reduction in the liability estimate resulting from changes in estimates relating to better-than anticipated credit performance of seasoned mortgage loan pools along with additional reductions relating to mortgage loans meeting previously announced limitations on pursuit by the Agencies of claims on mortgage loans with certain performance histories.

Following is a summary of mortgage loan repurchase activity and the UPB of mortgage loans subject to representations and warranties:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
During the period:				
Indemnification activity				
Mortgage loans indemnified by				
PFSI at beginning of period	\$ 6,288	\$ 3,540	\$ 5,599	\$ 3,470
New indemnifications	723	1,716	1,412	1,855
Indemnified mortgage loans				
repaid or refinanced	214	384	214	453
Mortgage loans indemnified by				
PFSI at end of period	\$ 6,797	\$ 4,872	\$ 6,797	\$ 4,872
Repurchase activity				
Total mortgage loans				
repurchased by PFSI	\$ 6,217	\$ 4,486	\$ 11,520	\$ 11,399
Less:				
Mortgage loans repurchased by				
correspondent lenders	4,827	3,075	7,410	6,340
Mortgage loans repaid by				
borrowers or resold with				
defects resolved	2,332	814	5,551	1,141
Net mortgage loans (repaid or	\$ (942)	\$ 597	\$ (1,441)	\$ 3,918
resold) repurchased by PFSI				
with losses chargeable to				

liability for representations and warranties				
Net losses charged to liability for representations and warranties	\$ 144	\$ 218	\$ 305	\$ 702
At period end:				
Unpaid principal balance of mortgage loans subject to representations and warranties	\$ 106,284,973	\$ 72,151,175		
Liability for representations and warranties	\$ 19,568	\$ 24,277		

During the quarter and six months ended June 30, 2017, we repurchased mortgage loans totaling \$6.2 million and \$11.5 million, respectively, in UPB. We recorded losses of \$144,000 and \$305,000, respectively, net of recoveries from correspondent sellers as a result of these repurchases during the quarter and six months ended June 30, 2017. As the outstanding balance of mortgage loans we purchase and sell subject to representations and warranties increases and the loans sold continue to season, we expect that the level of repurchase activity may increase.

The level of the liability for losses under representations and warranties is difficult to estimate and requires considerable management judgment. The level of mortgage loan repurchase losses is dependent on economic factors,

Table of Contents

purchaser or insurer loss mitigation strategies, and other external conditions that may change over the lives of the underlying mortgage loans. Our estimate of the liability for representations and warranties is developed by our credit administration staff and approved by our senior management credit committee which includes our senior executives and senior management in our loan production, loan servicing and credit risk management areas.

Our representations and warranties are generally not subject to stated limits of exposure. However, we believe that the current UPB of mortgage loans sold by us to date represents the maximum exposure to repurchases related to representations and warranties.

## Other mortgage loan production-related revenues

Mortgage loan origination fees increased \$1.3 million and \$4.4 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016 primarily due to growth in the volume of correspondent purchases in our loan production activities.

Fulfillment fees from PMT, which represent fees we collect for services we perform on behalf of PMT in connection with its acquisition, packaging and sale of mortgage loans, are calculated as a percentage of the UPB of the mortgage loans we fulfill for PMT. Fulfillment fees increased \$2.0 million and \$5.6 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016 due to increased mortgage loan production volume during 2017 as compared to 2016.

Summarized below are our fulfillment fees:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Fulfillment fee revenue	\$ 21,107	\$ 19,111	\$ 37,677	\$ 32,046
Unpaid principal balance of mortgage loans fulfilled	\$ 5,918,027	\$ 5,174,020	\$ 10,549,933	\$ 8,433,383
Average fulfillment fee rate (in basis points)	36	37	36	38

## Net mortgage loan servicing fees

Our net mortgage loan servicing fees are summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Net mortgage loan servicing fees:				
Mortgage loan servicing fees:				
From non-affiliates	\$ 112,348	\$ 92,770	\$ 218,815	\$ 184,097
From PennyMac Mortgage Investment Trust	10,099	16,427	20,585	27,880
From Investment Funds	543	723	1,039	1,424
Ancillary and other fees	11,202	10,818	23,068	22,270
	134,192	120,738	263,507	235,671
Amortization, impairment and change in fair value of mortgage servicing rights and excess servicing spread financing net of hedging results	(87,279)	(94,183)	(142,431)	(191,597)
Net mortgage loan servicing fees	\$ 46,913	\$ 26,555	\$ 121,076	\$ 44,074
Average mortgage loan servicing portfolio	\$ 212,671,694	\$ 167,966,390	\$ 206,055,588	\$ 165,413,607

Table of Contents

Amortization, impairment and change in fair value of mortgage servicing rights and mortgage servicing liabilities are summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Amortization and realization of cash flows	\$ (55,482)	\$ (51,092)	\$ (103,942)	\$ (97,767)
Other changes, in fair value of, and reversal of (provision for) impairment of mortgage servicing rights and mortgage servicing liabilities	(36,927)	(125,467)	(24,226)	(254,375)
Change in fair value of excess servicing spread	7,156	17,428	9,929	36,877
Hedging results	(2,026)	64,948	(24,192)	123,668
Total fair value adjustments, net of hedging results	(31,797)	(43,091)	(38,489)	(93,830)
Total amortization, impairment and change in fair value of mortgage servicing rights, mortgage servicing liabilities and excess servicing spread	\$ (87,279)	\$ (94,183)	\$ (142,431)	\$ (191,597)
Average mortgage servicing rights balances:				
Carried at lower of amortized cost or fair value	\$ 1,235,077	\$ 772,734	\$ 1,199,327	\$ 759,286
Carried at fair value	551,740	571,074	534,918	595,124
	\$ 1,786,817	\$ 1,343,808	\$ 1,734,245	\$ 1,354,410
Average mortgage servicing liabilities	\$ 15,241	\$ 5,286	\$ 15,084	\$ 4,130
Mortgage servicing rights at period end:				
Carried at lower of amortized cost or fair value	\$ 1,273,158	\$ 764,634		
Carried at fair value	678,441	526,294		
	\$ 1,951,599	\$ 1,290,928		
Mortgage servicing liabilities at period end	\$ 18,295	\$ 4,681		

Following is a summary of our mortgage loan servicing portfolio in UPB:

	June 30, 2017	December 31, 2016
	(in thousands)	
Mortgage loans serviced		
Prime servicing:		
Owned:		
Mortgage servicing rights		
Originated	\$ 105,296,264	\$ 89,516,155
Acquired	51,927,645	39,660,951
	157,223,909	129,177,106



Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

Mortgage servicing liabilities	1,698,588	2,074,896
Mortgage loans held for sale	2,915,346	2,101,283
	161,837,843	133,353,285
Subserviced for Advised Entities	64,924,592	58,327,748
Total prime servicing	226,762,435	191,681,033
Special servicing – Subserviced for Advised Entities	2,201,340	2,558,969
Total mortgage loans serviced	\$ 228,963,775	\$ 194,240,002

Net mortgage loan servicing fees increased \$20.4 million and \$77.0 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The increases were due to a combination of increased mortgage loan servicing fees and decreased net losses in fair value and impairment of MSRs and MSLs, net of hedging results. Mortgage loan servicing fees increased \$13.5 million and \$27.8 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016 reflecting increases in our average servicing portfolio of 26.6% and 24.6% for the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The increase was partially offset by decreasing mortgage loan servicing fees from the Advised Entities due to activity fees we earned relating to sale of distressed mortgage loans during 2016 that have not occurred

Table of Contents

during 2017 and as their distressed mortgage loan portfolios continue to liquidate. The Investment Funds' investment period ended December 31, 2011 and PMT has not acquired any distressed mortgage loans since 2015. The decrease of \$6.9 million and \$49.2 million in amortization, impairment and MSR, MSL and ESS valuation adjustments during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016 reflect the effect of interest rates, which did not decline as steeply during 2017 compared to 2016. Higher interest rates discourage refinancings which contribute to increased fair value of MSRs.

## Management fees and Carried Interest

Management fees and Carried Interest are summarized below:

	Quarter ended June 30,		Six months ended	
	2017	2016	June 30,	2016
	(in thousands)		2017	2016
PennyMac Mortgage Investment Trust:				
Base management	\$ 5,334	\$ 5,199	\$ 10,342	\$ 10,551
Performance incentive	304	—	304	—
	5,638	5,199	10,646	10,551
Investment Funds	369	531	735	1,091
Total management fees	6,007	5,730	11,381	11,642
Carried Interest	241	244	113	837
Total management fees and Carried Interest	\$ 6,248	\$ 5,974	\$ 11,494	\$ 12,479
	June 30,	December 31,		
	2017	2016		
	(in thousands)			
Net assets of Advised Entities at period end:				
PennyMac Mortgage Investment Trust	\$ 1,454,832	\$ 1,351,114		
Investment Funds	144,744	197,550		
	\$ 1,599,576	\$ 1,548,664		

Base management fees from PMT increased \$135,000 and decreased \$209,000 during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The changes were due to fluctuations in PMT's average shareholders' equity, upon which its base management fees are calculated. The increase of PMT's average shareholders' equity during the quarter ended June 30, 2017 compared to the same period in 2016 is primarily due to an issuance of additional equity by PMT. The performance incentive fees increased \$304,000 during the quarter and six months ended June 30, 2017 resulting from an increase in PMT's net income during the period over which incentive fees are calculated.

Management fees from the Investment Funds decreased \$162,000 and \$356,000, respectively, during the quarter and six months ended June 30, 2017, compared to the same periods in 2016. The decreases were due to a reduction in the Investment Funds' net asset values as a result of continued distributions to the Investment Funds' investors following the end of the Investment Funds' commitment period.

Carried Interest income from Investment Funds decreased \$3,000 and \$724,000 during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The decreases were due to a decline in the performance of the Funds compared to the same periods in 2016, and to a shrinking investment base on which returns are generated.

Table of Contents

## Other revenues

Net interest expense decreased \$3.0 million and \$4.9 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The decrease is primarily due to an increase in interest income on mortgage loans held for sale as a result of an increase in average mortgage loan inventory and an increase in the placement fees we receive relating to the custodial funds that we manage, partially offset by an increase in interest expense incurred to fund the growth in our average inventory of mortgage loans held for sale and to finance our MSR.

Change in fair value of investment in and dividends received from PMT decreased \$153,000 during the quarter ended June 30, 2017 compared to the same period in 2016 and increased \$72,000 during the six months ended June 30, 2017, compared to the same period in 2016. The changes reflect the share price fluctuations in our investment in PMT. We held 75,000 common shares of PMT during each of the periods ended June 30, 2017 and 2016, with fair value of \$1.4 million and \$1.2 million, respectively, at the end of each period.

## Expenses

## Compensation

Our compensation expense is summarized below:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)			
Salaries and wages	\$ 55,971	\$ 50,110	\$ 112,874	\$ 98,223
Incentive compensation	12,100	19,421	23,628	25,751
Taxes and benefits	10,031	8,663	21,315	17,545
Stock and unit-based compensation	4,865	4,953	10,390	9,926
	\$ 82,967	\$ 83,147	\$ 168,207	\$ 151,445
Head count:				
Average	2,912	2,636	2,944	2,594
Period end	2,976	2,682		

Compensation expense decreased \$180,000 during the quarter ended June 30, 2017 compared to the same period in 2016 and increased \$16.8 million during the six months ended June 30, 2017 compared to the same period in 2016.

The increase was primarily due to an increase in base salaries due to increased average head count resulting from the growth in our mortgage banking activities partially offset by a decrease in incentive compensation due to lower than expected attainment of profitability targets during the six months ended June 30, 2017 compared to the same period in 2016.

#### Servicing

Servicing expense increased \$11.3 million and \$17.2 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016. The increases were primarily due to increased early buyouts of delinquent mortgage loans from Ginnie Mae guaranteed pools for the quarter and six months ended June 30, 2017 as compared to the same periods in 2016. The early buyout program reduces the ultimate cost of servicing such mortgage loan pools when we purchase and either sell the defaulted mortgage loans to third-party investors or finance them with debt at interest rates below the Ginnie Mae MBS pass-through rate at which we would otherwise be required to advance. Such purchases accelerate loss recognition when the mortgage loans are purchased. However, anticipated losses relating to such servicing advances are contemplated in the valuation of our MSRs and therefore the early buyout of delinquent mortgage loans included in Ginnie Mae guaranteed pools has an offsetting positive effect on our MSR valuation.

#### Technology

Technology expense increased \$3.8 million and \$8.4 million during the quarter and six months ended June 30, 2017, respectively, compared to the same periods in 2016 primarily due to our continued investment in loan production and servicing infrastructure.

Table of Contents

## Expenses Allocated to PMT

We are reimbursed by PMT for other expenses, including common overhead expenses we have incurred on PMT's behalf, in accordance with the terms of the Management Agreement with PMT. We present the expense amounts in the consolidated statements of income net of these allocations.

Common overhead expense amounts allocated to PMT are summarized below:

	Quarter ended		Six months ended	
	June 30, 2017	2016	June 30, 2017	2016
	(in thousands)			
Technology	\$ 424	\$ 1,125	\$ 881	\$ 2,270
Occupancy	443	512	822	1,085
Depreciation and amortization	396	407	804	806
Other	330	391	520	835
Total expenses	\$ 1,593	\$ 2,435	\$ 3,027	\$ 4,996

## Provision for Income Taxes

Our effective tax rates were 12.4% during the quarter and six months ended June 30 2017, compared to 11.8% and 11.9% during the same periods in 2016, respectively. The difference between our effective tax rate and the statutory rate is primarily due to the allocation of earnings to the noncontrolling interest unitholders. As the noncontrolling interest unitholders convert their ownership units into our shares, we expect an increase in allocated earnings that will be subject to corporate federal and state statutory tax rates, which will in turn increase our effective income tax rate.

## Balance Sheet Analysis

Following is a summary of key balance sheet items as of the dates presented:

June 30, 2017	December 31, 2016
------------------	----------------------

	(in thousands)	
<b>ASSETS</b>		
Cash and short-term investments	\$ 221,418	\$ 185,331
Mortgage loans held for sale at fair value	3,037,602	2,172,815
Servicing advances, net	291,907	348,306
Investments in and advances to affiliates	170,427	168,863
Carried Interest due from Investment Funds	71,019	70,906
Mortgage servicing rights	1,951,599	1,627,672
Mortgage loans eligible for repurchase	462,487	382,268
Other	198,279	177,741
Total assets	\$ 6,404,738	\$ 5,133,902
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Borrowings	\$ 3,721,022	\$ 2,580,906
Payable to affiliates	482,825	555,052
Liability for mortgage loans eligible for repurchase	462,487	382,268
Other	227,152	216,320
Total liabilities	4,893,486	3,734,546
Stockholders' equity	1,511,252	1,399,356
Total liabilities and stockholders' equity	\$ 6,404,738	\$ 5,133,902

Table of Contents

Total assets increased \$1.3 billion from \$5.1 billion at December 31, 2016 to \$6.4 billion at June 30, 2017. The increase was primarily due to an increase of \$864.8 million in mortgage loans held for sale at fair value resulting from growth in our mortgage loan production inventory, an increase of \$323.9 million in our investment in MSRs reflecting continued additions from our mortgage loan production activities and servicing portfolio acquisitions and an \$80.2 million increase in mortgage loans eligible for repurchase, partially offset by a \$56.4 million decrease in servicing advances.

Total liabilities increased by \$1.2 billion from \$3.7 billion as of December 31, 2016 to \$4.9 billion as of June 30, 2017. The increase was primarily attributable to an increase in borrowings to fund growth in our inventory of mortgage loans held for sale at fair value and to finance our MSRs.

## Cash Flows

Our cash flows for the six months ended June 30, 2017 and 2016 are summarized below:

	Six months ended June 30,		Change
	2017	2016	
	(in thousands)		
Operating	\$ (853,044)	\$ (958,795)	\$ 105,751
Investing	(274,348)	109,802	(384,150)
Financing	1,104,003	887,236	216,767
Net (decrease) increase in cash	\$ (23,389)	\$ 38,243	\$ (61,632)

Our cash flows resulted in a net decrease in cash of \$23.4 million during the six months ended June 30, 2017 as discussed below.

## Operating activities

Net cash used in operating activities totaled \$853.0 million and \$958.8 million during the six months ended June 30, 2017 and 2016, respectively, primarily due to the growth of our inventory of mortgage loans held for sale at fair value.

## Investing activities



Net cash used in investing activities during the six months ended June 30, 2017 totaled \$274.3 million primarily due to purchases of MSRs totaling \$181.6 million. Net cash provided by investing activities during the six months ended June 30, 2016 totaled \$109.8 million primarily due to \$138.8 million in net settlements of derivative financial instruments received in our hedging of MSRs partially offset by acquisitions of fixed assets and capitalized software.

#### Financing activities

Net cash provided by financing activities totaled \$1.1 billion and \$887.2 million during the six months ended June 30, 2017 and 2016, respectively, primarily to finance the growth in our inventory of mortgage loans held for sale at fair value and our investments in MSRs.

#### Liquidity and Capital Resources

Our liquidity reflects our ability to meet our current obligations (including our operating expenses and, when applicable, the retirement of, and margin calls relating to, our debt, margin calls relating to hedges, tax receivable agreement payments to exchanged Private National Mortgage Acceptance Company LLC unitholders and tax distributions to noncontrolling interest holders), fund new originations and purchases, and make investments as we identify them. We expect our primary sources of liquidity to be through cash flows from business activities, proceeds from borrowings and/or additional equity offerings. We believe that our liquidity is sufficient to meet our current liquidity needs.

Our current leverage strategy is to finance our assets where we believe such borrowing is prudent, appropriate and available. Our borrowing activities are in the form of assets sold under agreements to repurchase, sales of mortgage loan participation certificates, notes payable, the Credit Agreement, ESS and a capital lease. While the GMSR term note,

Table of Contents

ESS and the capital lease have intermediate to long-term maturities, most of our borrowings have short-term maturities and provide for terms of approximately one year. We will continue to finance most of our assets on a short-term basis until longer-term financing becomes more available. Because a significant portion of our current debt facilities consists of short-term borrowings, we expect to renew these facilities in advance of their maturity dates in order to ensure our ongoing liquidity and access to capital or otherwise allow ourselves sufficient time to replace any necessary financing.

Our repurchase agreements represent the sales of assets together with agreements for us to buy back the respective assets at a later date. The table below presents the average outstanding, maximum and ending balances:

	Quarter ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)		(in thousands)	
Repurchase agreements outstanding:				
Average balance	\$ 2,082,668	\$ 1,352,401	\$ 1,801,138	\$ 1,195,987
Maximum daily balance	\$ 3,617,164	\$ 1,803,371	\$ 3,617,164	\$ 1,863,455
Balance at end of period	\$ 3,023,288	\$ 1,591,047		

Our secured financing agreements at PLS require us to comply with various financial covenants. The most significant financial covenants specific to PLS currently include the following:

- positive net income for any calendar quarter;
  - a minimum in unrestricted cash and cash equivalents of \$40 million;
- a minimum tangible net worth of \$500 million;
- a maximum ratio of total liabilities to tangible net worth of 10:1; and
- at least one other warehouse or repurchase facility that finances amounts and assets similar to those being financed under one of our existing secured financing agreements.

With respect to servicing performed for PMT, PLS is also subject to certain covenants under its debt agreements. Covenants of PLS in PMT's debt agreements are at least equal to, or less restrictive, than the covenants described above.

In addition to the covenants noted above, our Credit Agreement (classified as a note payable) and capital lease contain additional financial covenants specific to PennyMac including, but not limited to,

- a minimum of cash and carried interest equal to the amount borrowed under the Credit Agreement;

- a minimum of unrestricted cash and cash equivalents equal to \$40 million;
- a minimum tangible net worth of \$500 million;
- a minimum asset coverage ratio (the ratio of the total asset amount to the total commitment) of 2.5; and
- a maximum ratio of total indebtedness to tangible net worth of 5:1.

Although these financial covenants limit the amount of indebtedness that we may incur and affect our liquidity through minimum cash reserve requirements, we believe that these covenants currently provide us with sufficient flexibility to successfully operate our business and obtain the financing necessary to achieve that purpose.

Our debt financing agreements also contain margin call provisions that, upon notice from the applicable lender at its option, require us to transfer cash or, in some instances, additional assets in an amount sufficient to eliminate any margin deficit. A margin deficit will generally result from any decline in the market value (as determined by the applicable lender) of the assets subject to the related financing agreement. Upon notice from the applicable lender, we will generally be required to satisfy the margin call on the day of such notice or within one business day thereafter, depending on the timing of the notice.

Table of Contents

We are also subject to liquidity and net worth requirements established by FHFA for Agency seller/servicers and Ginnie Mae for single-family issuers. FHFA and Ginnie Mae have established minimum liquidity and net worth requirements for approved non-depository single-family sellers/servicers in the case of FHFA, and for approved single-family issuers in the case of Ginnie Mae, as summarized below:

- FHFA liquidity requirement is equal to 0.035% (3.5 basis points) of total Agency servicing UPB plus an incremental 200 basis points of the amount by which total nonperforming Agency servicing UPB exceeds 6% of the applicable Agency servicing UPB; allowable assets to satisfy liquidity requirement include cash and cash equivalents (unrestricted), certain investment-grade securities that are available for sale or held for trading including Agency mortgage-backed securities, obligations of Fannie Mae or Freddie Mac, and U.S. Treasury obligations, and unused and available portions of committed servicing advance lines;
- FHFA net worth requirement is a minimum net worth of \$2.5 million plus 25 basis points of UPB for total 1-4 unit residential mortgage loans serviced and a tangible net worth/total assets ratio greater than or equal to 6%;
- Ginnie Mae single-family issuer minimum liquidity requirement is equal to the greater of \$1.0 million or 0.10% (10 basis points) of the issuer's outstanding Ginnie Mae single-family securities, which must be met with cash and cash equivalents; and
- Ginnie Mae net worth requirement is equal to \$2.5 million plus 0.35% (35 basis points) of the issuer's outstanding Ginnie Mae single-family obligations.

We believe that we are currently in compliance with the applicable Agency requirements.

We have purchased portfolios of MSRs and have financed them in part through the sale to PMT of the right to receive ESS. The outstanding amount of the ESS financing is based on the current valuation of such ESS and amounts received on the underlying mortgage loans.

The Repurchase Program allows us to repurchase up to \$50 million of the Company's Class A common stock using open market stock purchases or privately negotiated transactions in accordance with applicable rules and regulations. The Repurchase Program does not have an expiration date and the authorization does not obligate us to acquire any particular amount of Class A common stock. We intend to finance the Repurchase Program through cash on hand. We did not repurchase any of our Class A common stock during the quarter and six months ended June 30, 2017.

We continue to explore a variety of means of financing our continued growth, including debt financing through bank warehouse lines of credit, bank loans, repurchase agreements, securitization transactions and corporate debt. However,

there can be no assurance as to how much additional financing capacity such efforts will produce, what form the financing will take or whether such efforts will be successful.

#### Off-Balance Sheet Arrangements and Aggregate Contractual Obligations

#### Off-Balance Sheet Arrangements and Guarantees

As of June 30, 2017, we have not entered into any off-balance sheet arrangements.

#### Contractual Obligations

As of June 30, 2017, we had contractual obligations aggregating \$8.3 billion, comprised of borrowings, commitments to purchase and originate mortgage loans, a payable to exchanged Private National Mortgage Acceptance Company, LLC unitholders under a tax receivable agreement, and anticipated payments related to excess servicing spread financing. We also lease our office facilities and license certain software to support our loan servicing operations.

All agreements to repurchase assets and mortgage loan participation and sale agreements that matured between June 30, 2017 and the date of this Report have been renewed, extended or repaid and are described in Note 11—Borrowings in the accompanying consolidated financial statements.

Table of Contents

Payment obligations under these agreements are summarized below:

Contractual obligations	Payments due by period				
	Total (in thousands)	Less than 1 year	1-3 years	3-5 years	More than 5 years
Commitments to purchase and originate mortgage loans	\$ 3,999,761	\$ 3,999,761	\$ —	\$ —	\$ —
Assets sold under agreements to repurchase	3,023,288	3,023,288	—	—	—
Mortgage loan participation and sale agreements	243,707	243,707	—	—	—
Notes payable	433,865	33,865	400,000	—	—
Obligations under capital lease	26,641	12,475	14,166	—	—
Excess servicing spread financing at fair value payable to PennyMac Mortgage Investment Trust (1)	261,796	—	—	—	261,796
Payable to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement	73,084	1,078	18,051	10,906	43,049
Anticipated interest payments related to excess servicing spread financing at fair value	98,511	15,073	24,322	18,160	40,956
Software licenses (2)	35,423	15,181	20,242	—	—
Office leases	101,955	12,158	28,946	23,818	37,033
<b>Total</b>	<b>\$ 8,298,031</b>	<b>\$ 7,356,586</b>	<b>\$ 505,727</b>	<b>\$ 52,884</b>	<b>\$ 382,834</b>

- (1) The ESS financing obligation payable to PMT does not have a stated contractual maturity date and will pay down as the underlying MSR's receive the excess servicing fee due to PMT.
- (2) Software licenses include both volume and activity based fees that are dependent on the number of loans serviced during each period and include a base fee of approximately \$1.3 million per month. Estimated payments for software licenses above are based on the number of loans currently serviced by us, which totaled approximately 1.0 million at June 30, 2017. Future amounts due may significantly fluctuate based on changes in the number of loans serviced by us. For the six months ended June 30, 2017, software license fees totaled \$9.9 million.

The amount at risk (the fair value of the assets pledged plus the related margin deposit, less the amount advanced by the counterparty and accrued interest) relating to our assets sold under agreements to repurchase is summarized by counterparty below as of June 30, 2017:

Counterparty	Amount at risk (in thousands)	Weighted average maturity of advances under repurchase agreement	Facility Maturity
Credit Suisse First Boston Mortgage Capital LLC	\$ 91,587	April 27, 2018	April 27, 2018
Credit Suisse First Boston Mortgage Capital LLC	\$ 48,987	August 1, 2017	April 27, 2018
Bank of America, N.A.	\$ 69,343	September 19, 2017	May 25, 2018
JP Morgan Chase Bank, N.A.	\$ 41,179	August 19, 2017	October 13, 2017
Barclays Bank PLC	\$ 13,758	September 19, 2017	December 1, 2017
Citibank, N.A.	\$ 10,631	August 2, 2017	March 2, 2018
Morgan Stanley Bank, N.A.	\$ 9,914	August 17, 2017	August 25, 2017
Royal Bank of Canada	\$ 7,406	September 12, 2017	September 18, 2017

#### Debt Obligations

As described further above in “Liquidity and Capital Resources,” we currently finance certain of our assets through borrowings with major financial institution counterparties in the form of sales of assets under agreements to repurchase, mortgage loan participation and sale agreements, two notes payable, ESS and a capital lease. The borrower under each of these facilities is PLS with the exception of the Credit Agreement, which is classified as a note payable, and the capital lease, in each case where the borrower is PennyMac. All PLS obligations as previously noted are guaranteed by PennyMac.

Table of Contents

Under the terms of these agreements, PLS is required to comply with certain financial covenants, as described further above in “Liquidity and Capital Resources,” and various non-financial covenants customary for transactions of this nature. As of June 30, 2017, we were in compliance in all material respects with these covenants.

The agreements also contain margin call provisions that, upon notice from the applicable lender, require us to transfer cash or, in some instances, additional assets in an amount sufficient to eliminate any margin deficit. Upon notice from the applicable lender, we will generally be required to satisfy the margin call on the day of such notice or within one business day thereafter, depending on the timing of the notice.

In addition, the agreements contain events of default (subject to certain materiality thresholds and grace periods), including payment defaults, breaches of covenants and/or certain representations and warranties, cross-defaults, guarantor defaults, servicer termination events and defaults, material adverse changes, bankruptcy or insolvency proceedings and other events of default customary for these types of transactions. The remedies for such events of default are also customary for these types of transactions and include the acceleration of the principal amount outstanding under the agreements and the liquidation by our lenders of the mortgage loans or other collateral then subject to the agreements.

The borrowings have maturities as follows:

Lender	Outstanding indebtedness (1)	Total facility size (2)	Committed facility (2)	Maturity date (2)
(dollar amounts in thousands)				
Assets sold under agreements to repurchase				
Credit Suisse First Boston Mortgage Capital LLC	\$ 773,496	\$ 850,000	\$ 293,000	April 27, 2018
Credit Suisse First Boston Mortgage Capital LLC (3)	\$ 457,827	\$ 650,000	\$ 407,000	April 27, 2018
Bank of America, N.A. (5)	\$ 766,544	\$ 800,000	\$ 225,000	May 25, 2018
Morgan Stanley Bank, N.A.	\$ 131,399	\$ 500,000	\$ 175,000	August 25, 2017
JP Morgan Chase Bank, N.A.	\$ 489,474	\$ 500,000	\$ 50,000	October 13, 2017
Citibank, N.A.	\$ 175,878	\$ 700,000	\$ 275,000	March 2, 2018
Barclays Bank PLC (4)	\$ 135,757	\$ 370,000	\$ —	December 1, 2017
Royal Bank of Canada	\$ 92,913	\$ 135,000	\$ 75,000	September 18, 2017
Mortgage loan participation and sale agreements				
Bank of America, N.A.	\$ 243,707	\$ 250,000	\$ —	May 25, 2018



Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

JP Morgan Chase Bank, N.A. Notes payable	\$ —	\$ 500,000	\$ —	October 31, 2017
GMSR 2017-GT Term Note	\$ 400,000	\$ 400,000	\$ —	February 25, 2020
Barclays Bank PLC (4)	\$ 33,865	\$ 130,000	\$ 130,000	December 1, 2017
Credit Suisse AG	\$ —	\$ 150,000	\$ 150,000	November 17, 2017
Obligations under capital lease Banc of America Leasing and Capital LLC	\$ 26,641	\$ —	\$ —	March 22, 2020

---

- (1) Outstanding indebtedness as of June 30, 2017.
- (2) Total facility size, committed facility and maturity date include contractual changes through the date of this Report.
- (3) The Credit Suisse First Boston Mortgage Capital LLC facility size is a total of \$1.5 billion that the Company can allocate as needed. The borrowing of \$458 million is in the form of a sale of a variable funding note under an agreement to repurchase, with a maximum allowable borrowing of \$650 million through September 28, 2017, declining to a maximum allowable borrowing of \$407 million thereafter.
- (4) Pursuant to amendments of a master repurchase agreement and a loan and security agreement, each dated as of June 16, 2017, Barclays Bank PLC agreed to temporarily increase the maximum aggregate facility amount to \$500 million from \$300 million until September 30, 2017 of which \$130 million represents the maximum amount for MSRs. The aggregate facility amount will be reset to \$300 million after September 30, 2017.

Table of Contents

- (5) Pursuant to an amendment of a master repurchase agreement dated as of May 23, 2017, Bank of America, N.A. agreed to temporarily increase the maximum aggregate principal amount to \$800 million from \$500 million until August 31, 2017, at which time the aggregate principal amount will be reset to \$500 million.

## Quantitative and Qualitative Disclosures About Market Risk

Market risk is the exposure to loss resulting from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices, real estate values and other market based risks. The primary market risks that we are exposed to are credit risk, interest rate risk, prepayment risk, inflation risk and fair value risk.

The following sensitivity analyses are limited in that they were performed at a particular point in time; only contemplate the movements in the indicated variables; do not incorporate changes to other variables; are subject to the accuracy of various models and assumptions used; and do not incorporate other factors that would affect our overall financial performance in such scenarios, including operational adjustments made by management to account for changing circumstances. For these reasons, the following estimates should not be viewed as earnings forecasts.

## Mortgage Servicing Rights

The following tables summarize the estimated change in fair value of MSRs accounted for using the amortization method as of June 30, 2017, given several shifts in pricing spreads, prepayment speed and annual per-loan cost of servicing:

Pricing spread shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 1,384,405	\$ 1,326,599	\$ 1,299,443	\$ 1,248,305	\$ 1,224,210	\$ 1,178,710
Change in fair value:						
\$	\$ 111,041	\$ 53,235	\$ 26,078	\$ (25,059)	\$ (49,154)	\$ (94,654)
%	8.7	% 4.2	% 2.0	% (2.0)	% (3.9)	% (7.4)
Prepayment speed shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 1,360,597	\$ 1,315,460	\$ 1,294,052	\$ 1,253,361	\$ 1,234,008	\$ 1,197,128
Change in fair value:						

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

	\$ 87,233	\$ 42,095	\$ 20,687	\$ (20,003)	\$ (39,356)	\$ (76,236)
	6.9	% 3.3	% 1.6	% (1.6)	% (3.1)	% (6.0)
-loan servicing cost shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
r value	\$ 1,313,222	\$ 1,293,293	\$ 1,283,329	\$ 1,263,400	\$ 1,253,435	\$ 1,233,506
Change in fair value:	\$ 39,858	\$ 19,929	\$ 9,964	\$ (9,965)	\$ (19,930)	\$ (39,858)
	3.1	% 1.6	% 0.8	% (0.8)	% (1.6)	% (3.1)

The following tables summarize the estimated change in fair value of MSR's accounted for using the fair value method as of June 30, 2017, given several shifts in pricing spreads, prepayment speed and annual per loan cost of servicing:

Pricing spread shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 733,094	\$ 704,682	\$ 691,305	\$ 666,060	\$ 654,138	\$ 631,576
Change in fair value:	\$ 54,654	\$ 26,242	\$ 12,865	\$ (12,381)	\$ (24,302)	\$ (46,865)
\$	8.1	% 3.9	% 1.9	% (1.8)	% (3.6)	% (6.9)
%						

Table of Contents

Prepayment speed shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 728,344	\$ 702,487	\$ 690,250	\$ 667,037	\$ 656,019	\$ 635,066
Change in fair value:						
\$	\$ 49,903	\$ 24,047	\$ 11,809	\$ (11,403)	\$ (22,421)	\$ (43,374)
%	7.4	% 3.5	% 1.7	% (1.7)	% (3.3)	% (6.4)

Per-loan servicing cost shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 705,020	\$ 691,730	\$ 685,085	\$ 671,795	\$ 665,150	\$ 651,860
Change in fair value:						
\$	\$ 26,580	\$ 13,290	\$ 6,645	\$ (6,645)	\$ (13,290)	\$ (26,580)
%	3.9	% 2.0	% 1.0	% (1.0)	% (2.0)	% (3.9)

## Excess Servicing Spread Financing

The following tables summarize the estimated change in fair value of our ESS accounted for using the fair value method as of June 30, 2017, given several shifts in pricing spreads and prepayment speed (decrease in the liabilities' values increases net income):

Pricing spread shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 271,706	\$ 266,661	\$ 264,207	\$ 259,427	\$ 257,100	\$ 252,567
Change in fair value:						
\$	\$ 9,910	\$ 4,866	\$ 2,411	\$ (2,369)	\$ (4,696)	\$ (9,229)
%	3.8	% 1.9	% 0.9	% (0.9)	% (1.8)	% (3.5)

Prepayment speed shift in %	-20%	-10%	-5%	+5%	+10%	+20%
	(dollar amounts in thousands)					
Fair value	\$ 288,188	\$ 274,418	\$ 267,972	\$ 255,873	\$ 250,190	\$ 239,488
Change in fair value:						

\$	\$ 26,392	\$ 12,622	\$ 6,176	\$ (5,922)	\$ (11,606)	\$ (22,308)
%	10.1 %	4.8 %	2.4 %	(2.3) %	(4.4) %	(8.5) %

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

In response to this Item 3, the information set forth on pages 79 and 80 of this Report is incorporated herein by reference.

### Item 4. Controls and Procedures

#### Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures. However, no matter how well a control system is designed and operated, it can provide only reasonable, not absolute, assurance that it will detect or uncover failures within the Company to disclose material information otherwise required to be set forth in our periodic reports.

Our management has conducted an evaluation, with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Report as required by paragraph (b) of Rule 13a-15 under the Exchange Act. Based on our evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were

Table of Contents

effective, as of the end of the period covered by this Report, to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the applicable rules and forms, and that it is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting during the six months ended June 30, 2017 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we may be involved in various legal actions, claims and proceedings arising in the ordinary course of business. As of June 30, 2017, we were not involved in any such legal proceedings, claims or actions that management believes would be reasonably likely to have a material adverse effect on us.

Item 1A. Risk Factors

There have been no material changes from the risk factors set forth under Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016, filed with the SEC on March 9, 2017 and our Quarterly Reports on Form 10-Q filed thereafter.

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

Repurchases of our Common Stock

The following table summarizes the stock repurchase activity for the three months ended June, 2017 and the approximate dollar value of shares that may yet be purchased pursuant to our stock repurchase program.

In June 2017, the our Board of Directors authorized a stock repurchase program under which we may repurchase up to \$50 million of our outstanding Class A common stock. We did not repurchase any of our Class A common stock during the three months ended June 30, 2017.

Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased	Approximate Dollar Value of Shares that
---	---------------------------------------	---	--

				as Part of Publicly Announced Plans or Program (1)	May Yet Be Purchased Under the Plans or Program (1)
April 1, 2017 – April 30, 2017	—	\$	—	—	\$ 50,000,000
May 1, 2017 – May 31, 2017	—	\$	—	—	\$ 50,000,000
June 1, 2017 – June 30, 2017	—	\$	—	—	\$ 50,000,000
Total	—	\$	—	—	\$ 50,000,000

(1) As disclosed in our current report on Form 8-K filed on June 21, 2017, our Board of Directors approved a stock repurchase program authorizing us to repurchase up to \$50.0 million of our outstanding common stock. We have not conducted any repurchases of shares of our common stock under the stock repurchase program. The stock repurchase program does not require us to purchase a specific number of shares, and the timing and amount of any shares repurchased are based on market conditions and other factors, including price, regulatory requirements and capital availability. Stock repurchases may be effected through negotiated transactions or open market purchases, including pursuant to a trading plan implemented pursuant to Rule 10b5-1 of the Securities Exchange Act of 1934, as amended. The stock repurchase program does not have an expiration date but may be suspended, modified or discontinued at any time without prior notice.

### Item 3. Defaults Upon Senior Securities

None.

### Item 4. Mine Safety Disclosures

Not applicable.

### Item 5. Other Information

None.





Table of Contents

Item 6. Exhibits

Exhibit Number	Exhibit Description
3.1	Amended and Restated Certificate of Incorporation of PennyMac Financial Services, Inc. (incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
3.2	Amended and Restated Bylaws of PennyMac Financial Services, Inc. (incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on August 19, 2013).
4.1	Specimen Class A Common Stock Certificate (incorporated by reference to Exhibit 4.1 of the Registrant's Amendment No. 4 to Form S-1 Registration Statement as filed with the SEC on April 29, 2013).
10.1	Fourth Amended and Restated Limited Liability Company Agreement of Private National Mortgage Acceptance Company, LLC, dated as of May 8, 2013 (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.2	Exchange Agreement, dated as of May 8, 2013, between PennyMac Financial Services, Inc. and Private National Mortgage Acceptance Company, LLC and the Company Unitholders (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.3	Tax Receivable Agreement, dated as of May 8, 2013, between PennyMac Financial Services, Inc. Private National Mortgage Acceptance Company, LLC and each of the Members (incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.4	Registration Rights Agreement, dated as of May 8, 2013, between PennyMac Financial Services, Inc. and the Holders (incorporated by reference to Exhibit 10.4 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.5	Stockholder Agreement, dated as of May 8, 2013, between PennyMac Financial Services, Inc. and BlackRock Mortgage Ventures, LLC (incorporated by reference to Exhibit 10.5 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.6	Stockholder Agreement, dated as of May 8, 2013, between PennyMac Financial Services, Inc. and HC Partners LLC (incorporated by reference to Exhibit 10.6 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.7†	PennyMac Financial Services, Inc. 2013 Equity Incentive Plan (incorporated by reference to Exhibit 99.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 14, 2013).
10.8†	PennyMac Financial Services, Inc. 2013 Equity Incentive Plan Form of Restricted Stock Unit Award Agreement for Non-Employee Directors (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 16, 2013).
10.9†	

Edgar Filing: PENNYMAC FINANCIAL SERVICES, INC. - Form 10-Q

PennyMac Financial Services, Inc. 2013 Equity Incentive Plan Form of Restricted Stock Unit Award Agreement for Executive Officers (incorporated by reference to Exhibit 10.9 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015).

- 10.10† PennyMac Financial Services, Inc. 2013 Equity Incentive Plan Form of Restricted Stock Unit Award Agreement for Other Eligible Participants (incorporated by reference to Exhibit 10.10 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015).
- 10.11† PennyMac Financial Services, Inc. 2013 Equity Incentive Plan Form of Stock Option Award Agreement (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on June 17, 2013).

Table of Contents

Exhibit Number	Exhibit Description
10.12†	Form of PennyMac Financial Services, Inc. Indemnification Agreement (incorporated by reference to Exhibit 10.8 of the Registrant’s Amendment No. 2 to Form S-1 Registration Statement as filed with the SEC on April 5, 2013).
10.13†	Employment Agreement, dated December 8, 2015, among Stanford L. Kurland, Private National Mortgage Acceptance Company, LLC and PennyMac Financial Services, Inc. (incorporated by reference to Exhibit 10.5 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 14, 2015).
10.14†	First Amendment to Employment Agreement, dated as of April 5, 2017, by and among Private National Mortgage Acceptance Company, LLC, PennyMac Financial Services, Inc. and Stanford L. Kurland (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on April 7, 2017).
10.15†	Employment Agreement, dated December 8, 2015, among David A. Spector, Private National Mortgage Acceptance Company, LLC and PennyMac Financial Services, Inc. (incorporated by reference to Exhibit 10.6 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 14, 2015).
10.16†	First Amendment to Employment Agreement, dated as of April 5, 2017, by and among Private National Mortgage Acceptance Company, LLC, PennyMac Financial Services, Inc. and David A. Spector (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K filed with the SEC on April 7, 2017).
10.17	Second Amended and Restated Management Agreement, dated as of September 12, 2016, by and among PennyMac Mortgage Investment Trust, PennyMac Operating Partnership, L.P. and PNMAC Capital Management, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on September 12, 2016).
10.18	Third Amended and Restated Flow Servicing Agreement, dated as of September 12, 2016, by and between PennyMac Operating Partnership, L.P. and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K as filed with the SEC on September 12, 2016).
10.19	Amended and Restated Mortgage Banking Services Agreement, dated as of September 12, 2016, by and between PennyMac Loan Services, LLC and PennyMac Corp. (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K as filed with the SEC on September 12, 2016).
10.20	Amendment No. 1 to Amended and Restated Mortgage Banking Services Agreement, dated as of May 25, 2017, by and between PennyMac Loan Services, LLC and PennyMac Corp.
10.21	Amended and Restated MSR Recapture Agreement, dated as of September 12, 2016, by and between PennyMac Loan Services, LLC and PennyMac Corp. (incorporated by reference to Exhibit 10.4 of the Registrant’s Current Report on Form 8-K as filed with the SEC on September 12, 2016).
10.22	Amended and Restated Underwriting Fee Reimbursement Agreement, dated as of February 1, 2013, by and among PennyMac Mortgage Investment Trust, PennyMac Operating Partnership, L.P. and PNMAC

Capital Management, LLC (incorporated by reference to Exhibit 10.13 of the Registrant's Form S-1 Registration Statement as filed with the SEC on February 7, 2013).

- 10.23 Master Spread Acquisition and MSR Servicing Agreement, dated as of December 19, 2014, among PennyMac Loan Services, LLC, PennyMac Operating Partnership, L.P., and PennyMac Holdings, LLC (incorporated by reference to Exhibit 1.01 of the Registrant's Current Report on Form 8-K as filed with the SEC on December 24, 2014).

Table of Contents

Exhibit Number	Exhibit Description
10.24	Amendment No. 1 to Master Spread Acquisition and MSR Servicing Agreement, dated as of March 3, 2015, among PennyMac Loan Services, LLC, PennyMac Operating Partnership, L.P., and PennyMac Holdings, LLC (incorporated by reference to Exhibit 10.38 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 31, 2015).
10.25	Second Amended and Restated Master Spread Acquisition and MSR Servicing Agreement, dated as of December 19, 2016, by and between PennyMac Loan Services, LLC, and PennyMac Holdings, LLC (incorporated by reference to Exhibit 10.7 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.26	Second Amended and Restated Flow Servicing Agreement, dated as of August 1, 2008, as amended effective as of January 1, 2012, by and between PNMAC Mortgage Opportunity Fund Investors, LLC and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.15 of the Registrant’s Form S-1 Registration Statement as filed with the SEC on February 7, 2013).
10.27	Amendment No. 1 to the Second Amended and Restated Flow Servicing Agreement, dated as of December 5, 2014, by and among PennyMac Loan Services, LLC and PNMAC Mortgage Opportunity Fund Investors, LLC (incorporated by reference to Exhibit 10.43 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).
10.28	Amended and Restated Flow Servicing Agreement, by and between PNMAC Mortgage Co., LLC and PennyMac Loan Services, LLC, dated August 1, 2010 (incorporated by reference to Exhibit 10.14 of the Registrant’s Amendment No. 1 to Form S-1 Registration Statement as filed with the SEC on March 26, 2013).
10.29	Amendment No. 1 to the Amended and Restated Flow Servicing Agreement, dated as of December 4, 2014, by and among PennyMac Loan Services, LLC and PNMAC Mortgage Co., LLC (incorporated by reference to Exhibit 10.41 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).
10.30	Amended and Restated Flow Servicing Agreement, dated as of August 1, 2010, by and between PNMAC Mortgage Opportunity Fund, LP and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.27 of the Registrant’s Amendment No. 1 to Form S-1 Registration Statement as filed with the SEC on March 26, 2013).
10.31	Amendment No. 1 to the Amended and Restated Flow Servicing Agreement, dated as of December 4, 2014, by and among PennyMac Loan Services, LLC and PNMAC Mortgage Opportunity Fund, L.P. (incorporated by reference to Exhibit 10.45 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).
10.32	Investment Management Agreement, dated as of August 1, 2008, between PNMAC Mortgage Opportunity Fund Investors, LLC and PNMAC Capital Management, LLC (incorporated by reference to Exhibit 10.17 of the Registrant’s Form S-1 Registration Statement as filed with the SEC on February 7, 2013).
10.33	

Investment Management Agreement, as amended and restated May 26, 2011, by and between PNMAC Mortgage Opportunity Fund, L.P. and PNMAC Capital Management, LLC (incorporated by reference to Exhibit 10.16 of the Registrant's Form S-1 Registration Statement as filed with the SEC on February 7, 2013).

- 10.34 Master Repurchase Agreement, dated as of March 17, 2011, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.18 of the Registrant's Form S-1 Registration Statement as filed with the SEC on February 7, 2013).

Table of Contents

Exhibit Number	Exhibit Description
10.35	Amendment No. 1 to Master Repurchase Agreement, dated as of July 21, 2011, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibits 10.19 of the Registrant’s Amendment No. 3 to Form S-1 Registration Statement as filed with the SEC on April 22, 2013).
10.36	Amendment No. 2 to Master Repurchase Agreement, dated as of March 23, 2012, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibits 10.19 of the Registrant’s Amendment No. 3 to Form S-1 Registration Statement as filed with the SEC on April 22, 2013).
10.37	Amendment No. 3 to Master Repurchase Agreement, dated as of August 28, 2012, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibits 10.19 of the Registrant’s Amendment No. 3 to Form S-1 Registration Statement as filed with the SEC on April 22, 2013).
10.38	Amendment No. 4 to Master Repurchase Agreement, dated as of January 3, 2013, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibits 10.19 of the Registrant’s Amendment No. 3 to Form S-1 Registration Statement as filed with the SEC on April 22, 2013).
10.39	Amendment No. 5 to Master Repurchase Agreement, dated as of March 28, 2013, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibits 10.19 of the Registrant’s Amendment No. 3 to Form S-1 Registration Statement as filed with the SEC on April 22, 2013).
10.40	Amendment No. 6 to Master Repurchase Agreement, dated as of January 31, 2014, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on February 6, 2014).
10.41	Amendment No. 7 to Master Repurchase Agreement, dated as of March 27, 2014, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.44 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).
10.42	Amendment No. 8 to Master Repurchase Agreement, dated as of August 13, 2014, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.48 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2014).
10.43	Amendment No. 9 to Master Repurchase Agreement, dated as of January 30, 2015, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.49 of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2014).
10.44	



Amendment No. 10 to Master Repurchase Agreement, dated as of March 29, 2016, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.62 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2016).

- 10.45 Amendment No. 11 to Master Repurchase Agreement, dated as of May 23, 2017, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed with the SEC on May 30, 2017).

Table of Contents

Exhibit Number	Exhibit Description
10.46	Guaranty, dated as of March 17, 2011, by Private National Mortgage Acceptance Company, LLC in favor of Bank of America, N.A (incorporated by reference to Exhibit 10.50 of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2014).
10.47	Amended and Restated Master Repurchase Agreement, dated as of March 3, 2017, among Citibank, N.A. and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on March 8, 2017).
10.48	Amendment Number One to Amended and Restated Master Repurchase Agreement, dated as of June 19, 2017, between Citibank, N.A. and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.4 of the Registrant’s Current Report on Form 8-K filed with the SEC on June 21, 2017).
10.49	Guaranty Agreement, dated as of June 26, 2012, by Private National Mortgage Acceptance Company, LLC in favor of Citibank, N.A (incorporated by reference to Exhibit 10.61 of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2014).
10.50	Amended and Restated Master Spread Participation Agreement, dated as of November 10, 2015, by and among PennyMac Loan Services, LLC and PennyMac Loan Services, LLC as the Initial Participant (incorporated by reference to Exhibit 10.189 of the Registrant’s Annual Report on Form 10-K for the quarter ended December 31, 2015).
10.51	Master Repurchase Agreement (Participation Certificates and Servicing), dated as of November 10, 2015, among Credit Suisse First Boston Mortgage Capital LLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on November 16, 2015).
10.52	Amendment No. 1 to Master Repurchase Agreement, dated as of December 19, 2016, among Credit Suisse First Boston Mortgage Capital LLC, Credit Suisse AG, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.74 of the Registrant’s Annual Report on Form 10-K filed with the SEC on March 9, 2017).
10.53	Third Amended and Restated Guaranty (Participation Certificates and Servicing), dated as of November 10, 2015, by Private National Mortgage Acceptance Company, LLC in favor of Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K as filed with the SEC on November 16, 2015).
10.54	Third Amended and Restated Master Repurchase Agreement, dated as of April 28, 2017, by and among Credit Suisse First Boston Mortgage Capital LLC, Credit Suisse AG, Alpine Securitization LTD, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on May 3, 2017).
10.55	Amendment No. 1 to Third Amended and Restated Master Repurchase Agreement, dated as of June 1, 2017, by and among Credit Suisse First Boston Mortgage Capital LLC, Credit Suisse AG, Alpine Securitization LTD, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC.

- 10.56 Amended and Restated Guaranty, dated as of April 28, 2017, by Private National Mortgage Acceptance LLC in favor of Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 3, 2017).
- 10.57 Master Repurchase Agreement, dated as of July 2, 2013, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 1.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on July 8, 2013).

Table of Contents

Exhibit Number	Exhibit Description
10.58	Amendment Number One to the Master Repurchase Agreement, dated as of August 26, 2013, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.49 of the Registrant’s Form S-1 Registration Statement as filed with the SEC on October 1, 2013).
10.59	Amendment Number Two to the Master Repurchase Agreement, dated as of January 28, 2014, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.63 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).
10.60	Amendment Number Three to the Master Repurchase Agreement, dated as of June 30, 2014, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.70 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2014).
10.61	Amendment Number Four to the Master Repurchase Agreement, dated as of June 29, 2015, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.98 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).
10.62	Amendment Number Five to the Master Repurchase Agreement, dated as of July 27, 2015, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on July 27, 2015).
10.63	Amendment Number Six to the Master Repurchase Agreement, dated as of November 9, 2015, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.118 of the Registrant’s Annual Report on Form 10-K for the quarter ended December 31, 2015).
10.64	Amendment Number Seven to the Master Repurchase Agreement, dated July 26, 2016, by and between PennyMac Loan Services, LLC and Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 10.91 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2016).
10.65	Amendment Number Eight to the Master Repurchase Agreement, dated August 26, 2016, by and between PennyMac Loan Services, LLC, Morgan Stanley Bank, N.A. and Morgan Stanley Mortgage Capital Holdings LLC (incorporated by reference to Exhibit 10.84 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended September 31, 2016).
10.66	Amendment Number Nine to the Master Repurchase Agreement, dated June 20, 2017, by and between PennyMac Loan Services, LLC, Morgan Stanley Bank, N.A. and Morgan Stanley Mortgage Capital Holdings LLC (incorporated by reference to Exhibit 10.5 of the Registrant’s Current Report on Form 8-K as filed with the SEC on June 21, 2017).
10.67	Guaranty Agreement, dated as of July 2, 2013, by Private National Mortgage Acceptance Company, LLC in favor of Morgan Stanley Bank, N.A. (incorporated by reference to Exhibit 1.2 of the Registrant’s Current Report on Form 8-K as filed with the SEC on July 8, 2013).
10.68	Mortgage Loan Participation Purchase and Sale Agreement, dated as of August 13, 2014, by and among PennyMac Loan Services, LLC, Private National Mortgage Acceptance Company, LLC and Bank of America, N.A. (incorporated by reference to Exhibit 10.72 of the Registrant’s Quarterly Report on Form

10-Q for the quarter ended June 30, 2014).

- 10.69 Amendment No. 1 to Mortgage Loan Participation Purchase and Sale Agreement, dated as of January 30, 2015, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.84 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2014).

Table of Contents

Exhibit Number	Exhibit Description
10.70	Amendment No. 2 to Mortgage Loan Participation Purchase and Sale Agreement, dated as of December 22, 2015, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.122 of the Registrant's Annual Report on Form 10-K for the quarter ended December 31, 2015).
10.71	Amendment No. 3 to Mortgage Loan Participation Purchase and Sale Agreement, dated as of March 29, 2016, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.96 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016).
10.72	Amendment No. 4 to Mortgage Loan Participation Purchase and Sale Agreement, dated as of March 28, 2017, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC.
10.73	Amendment No. 5 to Mortgage Loan Participation Purchase and Sale Agreement, dated as of May 23, 2017, by and among Bank of America, N.A., PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC.
10.74	Amended and Restated Guaranty, dated as of August 13, 2014, by Private National Mortgage Acceptance Company, LLC in favor of Bank of America, N.A. (incorporated by reference to Exhibit 10.73 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2014).
10.75	Mortgage Loan Purchase Agreement, dated as of September 25, 2012, by and between PennyMac Loan Services, LLC and PennyMac Corp. (incorporated by reference to Exhibit 10.124 of the Registrant's Annual Report on Form 10-K for the quarter ended December 31, 2015).
10.76	Flow Sale Agreement, dated as of June 16, 2015, by and between PennyMac Corp. and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.104 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).
10.77	Amended and Restated Flow Commercial Mortgage Loan Purchase Agreement, dated as of June 1, 2016, by and between PennyMac Loan Services, LLC and PennyMac Corp. (incorporated by reference to Exhibit 10.100 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016).
10.78	Servicing Agreement, dated as of July 13, 2015, between PennyMac Corp., PennyMac Holdings, LLC, any other parties signing this Agreement as owner of Mortgage Loans listed in Schedule I and any New Owners, PennyMac Loan Services, LLC, and Midland Loan Services, a division of PNC Bank, National Association (incorporated by reference to Exhibit 10.127 of the Registrant's Annual Report on Form 10-K for the quarter ended December 31, 2015).
10.79	Amended and Restated Commercial Mortgage Servicing Oversight Agreement, dated as of June 1, 2016, among PennyMac Corp., PennyMac Holdings, LLC, and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.102 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016).
10.80	

Master Repurchase Agreement, dated as of December 4, 2015, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on December 10, 2015).

- 10.81 Amendment Number One to Master Repurchase Agreement, dated as of September 29, 2016, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.97 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 31, 2016).

Table of Contents

Exhibit Number	Exhibit Description
10.82	Amendment Number Two to Master Repurchase Agreement, dated as of December 2, 2016, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.101 of the Registrant’s Annual Report on Form 10-K filed with the SEC on March 9, 2017).
10.83	Amendment Number Three to Master Repurchase Agreement, dated as of May 3, 2017, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on May 5, 2017).
10.84	Amendment Number Four to Master Repurchase Agreement, dated as of June 16, 2017, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on June 21, 2017).
10.85	Mortgage Loan Participation Purchase and Sale Agreement, dated as of December 4, 2015, between PennyMac Loan Services, LLC and Barclays Bank PLC (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 10, 2015).
10.86	Amendment Number One to Mortgage Loan Participation Purchase and Sale Agreement, dated as of December 2, 2016, between PennyMac Loan Services, LLC and Barclays Bank PLC (incorporated by reference to Exhibit 10.103 of the Registrant’s Annual Report on Form 10-K filed with the SEC on March 9, 2017).
10.87	Amendment Number Two to Mortgage Loan Participation Purchase and Sale Agreement, dated as of May 3, 2017, between PennyMac Loan Services, LLC and Barclays Bank PLC (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K filed with the SEC on May 5, 2017).
10.88	Amendment Number Three to Mortgage Loan Participation Purchase and Sale Agreement, dated as of June 16, 2017, between PennyMac Loan Services, LLC and Barclays Bank PLC (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K filed with the SEC on June 21, 2017).
10.89	Loan and Security Agreement, dated as of December 4, 2015, among PennyMac Loan Services, LLC, Private National Mortgage Acceptance Company, LLC and Barclays Bank PLC (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 10, 2015).
10.90	Amendment Number One to the Loan and Security Agreement, dated as of February 26, 2016, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on March 3, 2016).
10.91	Amendment Number Two to the Loan and Security Agreement, dated as of December 2, 2016, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.106 of the Registrant’s Annual Report on Form



10-K filed with the SEC on March 9, 2017).

- 10.92 Amendment Number Three to the Loan and Security Agreement, dated as of January 30, 2017, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.107 of the Registrant's Annual Report on Form 10-K filed with the SEC on March 9, 2017).

Table of Contents

Exhibit Number	Exhibit Description
10.93	Amendment Number Four to the Loan and Security Agreement, dated as of June 16, 2017, among Barclays Bank PLC, PennyMac Loan Services, LLC and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K filed with the SEC on June 21, 2017).
10.94	Master Lease Agreement No. 30350-90000, dated as of December 9, 2015, among Private National Mortgage Acceptance Company, LLC and Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 14, 2015).
10.95	Addendum to Master Lease Agreement No. 30350-90000, dated as of December 9, 2015, among Private National Mortgage Acceptance Company, LLC and Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 14, 2015).
10.96	Schedule Number 001 to Master Lease Agreement, dated as of December 9, 2015, among Private National Mortgage Acceptance Company, LLC and Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 14, 2015).
10.97	Schedule Number 002 to Master Lease Agreement, dated as of May 4, 2016, among Private National Mortgage Acceptance Company, LLC and Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.140 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 31, 2016).
10.98	Schedule Number 003 to Master Lease Agreement, dated as of November 3, 2016, among Private National Mortgage Acceptance Company, LLC and Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K as filed with the SEC on November 4, 2016).
10.99	Schedule Number 004 to Master Lease Agreement, dated as of March 23, 2017, among Private National Mortgage Acceptance Company, LLC and Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on March 27, 2017).
10.100	Guaranty, dated as of December 9, 2015, by PennyMac Loan Services, LLC in favor of Banc of America Leasing & Capital, LLC (incorporated by reference to Exhibit 10.4 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 14, 2015).
10.101	Amended and Restated Credit Agreement, dated November 18, 2016, by and among Private National Mortgage Acceptance Company, LLC, the lenders that are parties thereto, Credit Suisse AG and Credit Suisse Securities (USA) LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on November 22, 2016).
10.102	Amended and Restated Collateral and Guaranty Agreement, dated November 18, 2016, by and among Private National Mortgage Acceptance Company, LLC, Credit Suisse AG, Cayman Islands Branch,

PennyMac Financial Services, Inc., PNMAC Capital Management, LLC, PennyMac Loan Services, LLC and PNMAC Opportunity Fund Associates, LLC (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on November 22, 2016).

- 10.103 Master Repurchase Agreement, dated as of August 19, 2016, between PennyMac Loan Services, LLC and JPMorgan Chase Bank, N.A. (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on August 23, 2016).

Table of Contents

Exhibit Number	Exhibit Description
10.104	First Amendment to Master Repurchase Agreement, dated as of May 23, 2017, between PennyMac Loan Services, LLC and JPMorgan Chase Bank, N.A. (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on May 30, 2017).
10.105	Guaranty, dated as of August 19, 2016, by Private National Mortgage Acceptance Company, LLC in favor of JPMorgan Chase Bank, N.A. (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K as filed with the SEC on August 23, 2016).
10.106	Master Repurchase Agreement, dated as of September 19, 2016, between Royal Bank of Canada and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on September 22, 2016).
10.107	Amendment No. 1 to Master Repurchase Agreement, dated as of May 3, 2017, between Royal Bank of Canada and PennyMac Loan Services, LLC.
10.108	Base Indenture, dated as of December 19, 2016, by and among PNMAC GMSR ISSUER TRUST, Citibank, N.A., PennyMac Loan Services, LLC, Credit Suisse First Boston Mortgage Capital LLC, and Pentalpha Surveillance LLC (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.109	Amended and Restated Base Indenture, dated as of February 16, 2017, by and among PNMAC GMSR ISSUER TRUST, Citibank, N.A., PennyMac Loan Services, LLC, Credit Suisse First Boston Mortgage Capital LLC, and Pentalpha Surveillance LLC (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K as filed with the SEC on February 23, 2017).
10.110	Series 2016-MSRVF1 Indenture Supplement to Indenture, dated as of December 19, 2016, by and among PNMAC GMSR ISSUER TRUST, Citibank, N.A., PennyMac Loan Services, LLC, and Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.111	Series 2016-MBSADV1 Indenture Supplement to Indenture, dated as of December 19, 2016, by and among PNMAC GMSR ISSUER TRUST, Citibank, N.A., PennyMac Loan Services, LLC, and Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.122 of the Registrant's Annual Report on Form 10-K filed with the SEC on March 9, 2017).
10.112	Omnibus Amendment No. 1 to the Series 2016-MSRVF1 Indenture Supplement and Series 2016-MBSADV1 Indenture Supplement, dated as of February 16, 2017, by and among PNMAC GMSR ISSUER TRUST, Citibank, N.A., PennyMac Loan Services, LLC, and Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K as filed with the SEC on February 23, 2017).
10.113	Series 2017-GT1 Indenture Supplement, dated as of February 16, 2017, to Amended and Restated Base Indenture, dated as of February 16, 2017, by and among PNMAC GMSR ISSUER TRUST, Citibank, N.A., PennyMac Loan Services, LLC, Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K as filed with the SEC on February 23, 2017).

- 10.114 Master Repurchase Agreement, dated as of December 19, 2016, by and among PNMAC GMSR ISSUER TRUST, PennyMac Loan Services, LLC, and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K as filed with the SEC on December 21, 2016).

Table of Contents

Exhibit Number	Exhibit Description
10.115	Amendment No. 1 to Master Repurchase Agreement, dated as of February 16, 2017, by and among PNM MAC GMSR ISSUER TRUST, PennyMac Loan Services, LLC, and Private National Mortgage Acceptance Company, LLC and consented to by Citibank, N.A., Credit Suisse AG, Cayman Islands Branch, and Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.4 of the Registrant’s Current Report on Form 8-K as filed with the SEC on February 23, 2017).
10.116	Guaranty, dated as of December 19, 2016, made by Private National Mortgage Acceptance Company, LLC, in favor of PNM MAC GMSR ISSUER TRUST (incorporated by reference to Exhibit 10.4 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.117	Amendment No. 1 to Guaranty, dated as of February 16, 2017, by and between PNM MAC GMSR ISSUER TRUST and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.5 of the Registrant’s Current Report on Form 8-K as filed with the SEC on February 23, 2017).
10.118	Master Repurchase Agreement, dated as of December 19, 2016, by and among PennyMac Holdings, LLC, PennyMac Loan Services, LLC, and PennyMac Mortgage Investment Trust, (incorporated by reference to Exhibit 10.5 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.119	Guaranty, dated as of December 19, 2016, by PennyMac Mortgage Investment Trust, in favor of PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.6 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.120	Subordination, Acknowledgment and Pledge Agreement, dated as of December 19, 2016, between PNM MAC GMSR ISSUER TRUST and PennyMac Holdings, LLC (incorporated by reference to Exhibit 10.8 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.121	Master Repurchase Agreement, dated as of December 19, 2016, by and among, Credit Suisse First Boston Mortgage Capital LLC, Credit Suisse AG, Cayman Islands Branch, and PennyMac Loan Services, LLC (incorporated by reference to Exhibit 10.8 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.122	Guaranty, dated as of December 19, 2016, by Private National Mortgage Acceptance Company, LLC in favor of Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.9 of the Registrant’s Current Report on Form 8-K as filed with the SEC on December 21, 2016).
10.123	Master Repurchase Agreement, dated as of November 1, 2016, among JPMorgan Chase Bank, National Association, PennyMac Loan Services, LLC, and Private National Mortgage Acceptance Company, LLC (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K as filed with the SEC on November 4, 2016).
10.124	Guaranty, dated as of November 1, 2016, by Private National Mortgage Acceptance Company, LLC, in favor of JPMorgan Chase Bank, National Association (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K as filed with the SEC on November 4, 2016).
31.1	Certification of David A. Spector pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

- 31.2 Certification of Andrew S. Chang pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1\* Certification of David A. Spector pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Table of Contents

Exhibit Number	Exhibit Description
32.2*	Certification of Andrew S. Chang pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Balance Sheets as of June 30, 2017 and December 31, 2016 (ii) the Consolidated Statements of Income for the quarters ended June 30, 2017 and June 30, 2016, (iii) the Consolidated Statements of Changes in Stockholders' Equity for the quarters ended June 30, 2017 and June 30, 2016, (iv) the Consolidated Statements of Cash Flows for the quarters ended June 30, 2017 and June 30, 2016 and (v) the Notes to the Consolidated Financial Statements.
*	The certifications attached hereto as Exhibits 32.1 and 32.2 are furnished to the SEC pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933, except as shall be expressly set forth by specific reference in such filing.
†	Indicates management contract or compensatory plan or arrangement.



Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

PENNYMAC FINANCIAL  
SERVICES, INC.  
(Registrant)

Dated: August 7, 2017 By: /s/ DAVID A. SPECTOR  
David A. Spector  
President and Chief Executive Officer

Dated: August 7, 2017 By: /s/ ANDREW S. CHANG  
Andrew S. Chang  
Chief Financial Officer