MFA FINANCIAL, INC.
Form 10-K
February 18, 2016

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

FORM 10-K

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

For the fiscal year ended December 31, 2015

OR

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

For the transition period from to
Commission File Number: 1-13991
MFA FINANCIAL, INC.
(Exact name of registrant as specified in its charter)

Maryland (State or other jurisdiction of incorporation or organization)	13-3974868 (I.R.S. Employer Identification No.)
350 Park Avenue, 20th Floor, New York, New York (Address of principal executive offices)	10022 (Zip Code)

(212) 207-6400
(Registrant's telephone number, including area code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.01 per share	New York Stock Exchange
7.50% Series B Cumulative Redeemable Preferred Stock, par value $0.01 per share	New York Stock Exchange
8.00% Senior Notes due 2042	New York Stock Exchange

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

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

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

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

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

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

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

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o	Smaller reporting company o

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

On June 30, 2015, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was $2.73 billion based on the closing sales price of our common stock on such date as reported on the New York Stock Exchange.

On February 12, 2016, the registrant had a total of 371,076,243 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's proxy statement to be filed with the Securities and Exchange Commission in connection with the Annual Meeting of Stockholders scheduled to be held on or about May 25, 2016, are incorporated by reference into Part III of this Annual Report on Form 10-K.

Table of Contents

TABLE OF CONTENTS

CAUTIONARY STATEMENT — This Annual Report on Form 10-K includes "forward-looking" statements within the Private Securities Litigation Reform Act of 1995. These forward-looking statements include information about possible or assumed future results with respect to the Company's business, financial condition, liquidity, results of operations, plans and objectives. You can identify forward-looking statements by such words as "will," "believe," expect," "anticipate," "estimate," "plan," "continue," "intend," "should," "could," "would," "may" or similar expressions. We caution t such forward-looking statements made by us are not guarantees of future performance and that actual results may differ materially from these forward-looking statements. We discuss certain factors that affect our business and that may cause our actual results to differ materially from these forward-looking statements under "Item 1A. Risk Factors" of this Annual Report on Form 10-K. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date on which they are made. We undertake no obligation to update or revise any forward-looking statements except as may be required by law.

Table of Contents

In this Annual Report on Form 10-K, references to “we,” “us,” “our” or “the Company” refer to MFA Financial, Inc. and its subsidiaries unless specifically stated otherwise or the context otherwise indicates. The following defines certain of the commonly used terms in this Annual Report on Form 10-K: MBS refers to mortgage-backed securities secured by pools of residential mortgage loans; Agency MBS refers to MBS that are issued or guaranteed by a federally chartered corporation, such as Fannie Mae or Freddie Mac, or an agency of the U.S. Government, such as Ginnie Mae; Non-Agency MBS refers to residential MBS that are not guaranteed by any agency of the U.S. Government or any federally chartered corporation; Legacy Non-Agency MBS refers to MBS issued prior to 2008; RPL/NPL MBS refers to MBS collateralized by re-performing/non-performing loans; Hybrids refer to hybrid mortgage loans that have interest rates that are fixed for a specified period of time and, thereafter, generally adjust annually to an increment over a specified interest rate index; ARMs refer to adjustable-rate mortgage loans and to Hybrids that are past their fixed-rate period, both of which typically have interest rates that adjust annually to an increment over a specified interest rate index; Linked Transactions refer to Non-Agency MBS purchases which were financed with the same counterparty and for periods prior to 2015 considered linked for financial statement reporting purposes and were reported at fair value on a combined basis; and CRT securities refer to credit risk transfer securities which are general obligations of government-sponsored entities (Fannie Mae and Freddie Mac).

PART I

Item 1. Business.

GENERAL

We are primarily engaged in the real estate finance business. We engage in our business through subsidiaries that invest, on a leveraged basis, in residential mortgage assets, including Agency MBS, Non-Agency MBS, residential whole loans and CRT securities. Our principal business objective is to deliver shareholder value through the generation of distributable income and through asset performance linked to residential mortgage credit fundamentals. We selectively invest in residential mortgage assets with a focus on credit analysis, projected prepayment rates, interest rate sensitivity and expected return.

We were incorporated in Maryland on July 24, 1997, and began operations on April 10, 1998. We have elected to be treated as a real estate investment trust (or REIT) for U.S. federal income tax purposes. In order to maintain our qualification as a REIT, we must comply with a number of requirements under federal tax law, including that we must distribute at least 90% of our annual REIT taxable income to our stockholders. We have elected to treat certain of our subsidiaries as a taxable REIT subsidiary (or TRS). In general, a TRS may hold assets and engage in activities that a REIT or qualified REIT subsidiary cannot hold or engage in directly and generally may engage in any real estate or non-real estate related business.

We are a holding company and conduct our real estate finance businesses primarily through wholly-owned subsidiaries, so as to maintain an exemption from registration under the Investment Company Act of 1940, as amended (or the Investment Company Act) by ensuring that less than 40% of the value of our total assets, exclusive of U.S. Government securities and cash items (which we refer to as our adjusted total assets for Investment Company Act purposes), on an unconsolidated basis consist of “investment securities” as defined by the Investment Company Act. We refer to this test as the “40% Test.”

INVESTMENT STRATEGY

As stated above, we primarily invest through subsidiaries in Agency MBS, Non-Agency MBS, residential whole loans and CRT securities.

The mortgages collateralizing our Agency MBS portfolio are predominantly Hybrids, 15-year fixed-rate mortgages and ARMs. Our selection of Agency MBS is largely designed to generate attractive returns relative to interest rate and prepayment risks. The Hybrid loans collateralizing our MBS typically have initial fixed-rate periods at origination of three, five, seven or ten years. At the end of this fixed-rate period, these mortgages become adjustable and their interest rates adjust based on the London Interbank Offered Rate (or LIBOR) or in some cases the one-year constant maturity treasury rate (or CMT). These interest rate adjustments are typically limited by periodic caps (which limit the amount of the interest rate change from the prior rate) and lifetime caps (which are maximum interest rates permitted for the life of the mortgage). As coupons earned on Agency Hybrids and ARMs adjust over time as interest rates change, these assets are generally less sensitive to changes in interest rates than are fixed rate MBS. In general, Hybrid loans and ARMs have 30-year final maturities and they amortize over this 30-year period. While the coupons on 15-year fixed-rate mortgages do not adjust, they amortize according to a 15-year amortization schedule and have a 15-year final maturity. Due to their accelerated amortization and shorter final maturity, these assets are generally less sensitive to changes in long-term interest rates as compared to fixed-rate mortgages with a longer final maturity, such as 30-year mortgages.

Table of Contents

Our Non-Agency MBS portfolio primarily consists of (i) Legacy Non-Agency MBS and (ii) MBS collateralized by re-performing and non-performing loans (or RPL/NPL MBS). In addition to Non-Agency MBS investments, during 2014 we began investing in re-performing and non-performing residential whole loans through our interests in certain consolidated trusts. Our strategy of combining investments in Agency MBS, Non-Agency MBS and residential whole loans is designed to generate attractive returns with less overall sensitivity to changes in the yield curve, the general level of interest rates and prepayments. We expect to continue to seek more credit sensitive assets in 2016, such as residential whole loans, while seeking to minimize sensitivity to interest rates.

Our Legacy Non-Agency MBS have been acquired primarily at discounts to face/par value, which we believe serves to mitigate our exposure to credit risk. A portion of the purchase discount on substantially all of our Legacy Non-Agency MBS is designated as a non-accretable discount (also referred to hereafter as Credit Reserve), which effectively mitigates our risk of loss on the mortgages collateralizing such MBS and is not expected to be accreted into interest income. The portion of the purchase discount that is designated as accretable discount is accreted into interest income over the life of the security. The mortgages collateralizing our Legacy Non-Agency MBS consist primarily of ARMs, 30-year fixed rate mortgages and Hybrids. Legacy Non-Agency ARMs and Hybrids typically exhibit reduced interest rate sensitivity (as compared to fixed-rate Legacy Non-Agency MBS) due to their interest rate adjustments (similar to Agency ARMs and Hybrids). However, yields on Legacy Non-Agency MBS, unlike Agency MBS, also exhibit sensitivity to changes in credit performance. If credit performance improves, the Credit Reserve may be decreased (and accretable discount increased), resulting in a higher yield over the remaining life of the security. Similarly, deteriorating credit performance could increase the Credit Reserve and decrease the yield over the remaining life of the security or other-than-temporary impairment could result. To the extent that higher interest rates in the future are indicative of an improving economy, better employment data and/or higher home prices, it is possible that these factors will improve the credit performance of Legacy Non-Agency MBS and therefore mitigate the interest rate sensitivity of these securities.

Our RPL/NPL MBS were purchased primarily through new issue at prices at or around par and represent the senior tranches of the related securitizations. These RPL/NPL MBS are structured with significant credit enhancement (typically approximately 50%) and the subordinate tranches absorb all credit losses (until those tranches are extinguished) and typically receive no cash flow (interest or principal) until the senior tranche is paid off. Prior to purchase, we analyze the deal structure in order to assess the associated credit risk. Subsequent to purchase, the ongoing credit risk associated with the deal is evaluated by analyzing the extent to which actual credit losses occur that result in a reduction in the amount of subordination enjoyed by our bond. Based on the recent performance of the collateral underlying our RPL/NPL MBS and current subordination levels, we do not believe that we are currently exposed to significant risk of credit loss on these investments. In addition, these deal structures contain an interest rate step-up feature, whereby the original coupon on the senior tranche increases by 300 basis points if the security that we hold has not been redeemed by the issuer after 36 months. We expect that the combination of the priority cash flow of the senior tranche and the 36-month step-up will result in these securities' exhibiting short average lives and, accordingly, reduced interest rate sensitivity. Consequently, we believe that RPL/NPL MBS provide attractive returns given our assessment of the interest rate and credit risk associated with these securities.

In addition, during 2015, we continued to transition to more credit sensitive, less interest sensitive residential mortgage assets by acquiring residential whole loans through certain trusts that are consolidated on our balance sheet for financial reporting purposes. To date, we have focused on purchasing packages of both re-performing and non-performing whole loans. Re-performing loans are typically characterized by borrowers who have experienced payment delinquencies in the past and the amount owed on the mortgage may exceed the value of the property pledged as collateral. These loans are purchased at purchase prices that are discounted (often substantially so) to the contractual loan balance to reflect the credit history of the borrower, the loan-to-value (or LTV) of the loan and the coupon. Non-performing loans are typically characterized by borrowers who have defaulted on their obligations and/or have payment delinquencies of 60 days or more at the time we acquire the loan. These loans are also purchased at purchase prices that are discounted (often substantially so) to the contractual loan balance that reflects primarily the non-performing nature of the loan. Typically, this purchase price is a discount to the expected value of the collateral securing the loan, such value to be realized after foreclosure and liquidation of the property. All of the residential whole loans were purchased by the consolidated trusts on a servicing-released basis, i.e., the sellers of such loans transferred the right to service the loans as part of the sale. Because we do not directly service any loans, we have contracted with loan servicing companies with specific expertise in working with delinquent borrowers in an effort to cure delinquencies through, among other things, loan modification and third-party refinancing. To the extent these efforts are successful, we believe our investments in residential whole loans will yield attractive returns. In addition, to the extent that it is not possible to achieve a successful outcome for a particular borrower and the real property collateral must be foreclosed on and liquidated, we believe that the discounted purchase price at which the asset was acquired, provides us with a level of protection against financial loss.

Table of Contents

FINANCING STRATEGY

Our financing strategy is designed to increase the size of our investment portfolio by borrowing against a substantial portion of the market value of the assets in our portfolio. We primarily use repurchase agreements to finance our holdings of MBS, residential whole loans and CRT securities. We enter into interest rate derivatives to hedge the interest rate risk associated with a portion of our repurchase agreement borrowings. Going forward, in connection with our current and any future investment in residential whole loans, our financing strategy may expand to the use of securitization or other forms of structured financing.

Repurchase agreements, although legally structured as sale and repurchase transactions, are financing contracts (i.e., borrowings) under which we pledge our MBS, residential whole loans and CRT securities as collateral to secure loans with repurchase agreement counterparties (i.e., lenders). Repurchase agreements involve the transfer of the pledged collateral to a lender at an agreed upon price in exchange for such lender's simultaneous agreement to return the same security back to the borrower at a future date (i.e., the maturity of the borrowing) at a higher price. The difference between the sale price that we receive and the repurchase price that we pay represents interest paid to the lender. Our cost of borrowings under repurchase agreements is generally LIBOR based. Under our repurchase agreements, we pledge our securities as collateral to secure the borrowing, which is equal in value to a specified percentage of the fair value of the pledged collateral, while we retain beneficial ownership of the pledged collateral. At the maturity of a repurchase financing, unless the repurchase financing is renewed with the same counterparty, we are required to repay the loan including any accrued interest and concurrently receive back our pledged collateral from the lender. With the consent of the lender, we may renew a repurchase financing at the then prevailing financing terms. Margin calls, whereby, a lender requires that we pledge additional securities or cash as collateral to secure borrowings under our repurchase financing with such lender, are routinely experienced by us when the value of the MBS pledged as collateral declines as a result of principal amortization and prepayments or due to changes in market interest rates, spreads or other market conditions. We also may make margin calls on counterparties when collateral values increase.

In order to reduce our exposure to counterparty-related risk, we generally seek to enter into repurchase agreements and other financing arrangements, and derivatives, with a diversified group of financial institutions. At December 31, 2015, we had outstanding balances under repurchase agreements with 27 separate lenders.

In July 2015, the Company's wholly-owned subsidiary, MFA Insurance, Inc. (or MFA Insurance), became a member of the Federal Home Loan Bank (or FHLB) of Des Moines. At December 31, 2015 and February 16, 2016, MFA Insurance had FHLB advances of approximately $1.500 billion and $1.200 billion, respectively. FHLB advances are secured financing transactions and are carried at their contractual amounts. The ability to borrow from the FHLB is subject to the Company's continued creditworthiness, pledging of sufficient eligible collateral to secure advances, and compliance with certain agreements with the FHLB.

In January, 2016, the Federal Housing Finance Agency (or FHFA) released its final rule amending its regulation on FHLB membership, which, amongst other things, provided termination rules for current captive insurance members. As a result of such regulation, MFA Insurance will not be permitted new advances or renewal of existing advances and will be required to terminate its FHLB membership and repay any outstanding advances within one year of the rule's effective date of February 19, 2016.

In addition to repurchase agreements, FHLB advances, securitized debt and 8% Senior Notes due 2042 (or Senior Notes), we may also use other sources of funding in the future to finance our MBS portfolio, including, but not limited to, other types of collateralized borrowings, loan agreements, lines of credit or the issuance of debt securities.

COMPETITION

We operate in the mortgage REIT industry. We believe that our principal competitors in the business of acquiring and holding residential mortgage assets of the types in which we invest are financial institutions, such as banks, savings and loan institutions, life insurance companies, institutional investors, including mutual funds and pension funds, hedge funds, other mortgage-REITs as well as the U.S. Federal Reserve as part of its monetary policy activities. Some of these entities may not be subject to the same regulatory constraints (i.e., REIT compliance or maintaining an exemption under the Investment Company Act) as us. In addition, many of these entities have greater financial resources and access to capital than us. The existence of these entities, as well as the possibility of additional entities forming in the future, may increase the competition for the acquisition of residential mortgage assets, resulting in higher prices and lower yields on such assets.

EMPLOYEES

At December 31, 2015, we had 50 full-time and three part-time employees. We believe that our relationship with our employees is good. None of our employees are unionized or represented under a collective bargaining agreement.

Table of Contents

AVAILABLE INFORMATION

We maintain a Web site at www.mfafinancial.com. We make available, free of charge, on our Web site our (a) Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K (including any amendments thereto), proxy statements and other information (or, collectively, the Company Documents) filed with, or furnished to, the Securities and Exchange Commission (or SEC), as soon as reasonably practicable after such documents are so filed or furnished, (b) Corporate Governance Guidelines, (c) Code of Business Conduct and Ethics and (d) written charters of the Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee of our Board of Directors (or our Board). Our Company Documents filed with, or furnished to, the SEC are also available at the SEC's Web site at www.sec.gov. We also provide copies of the foregoing materials, free of charge, to stockholders who request them. Requests should be directed to the attention of our General Counsel at MFA Financial, Inc., 350 Park Avenue, 20th Floor, New York, New York 10022.

Table of Contents

Item 1A. Risk Factors.

This section highlights specific risks that could affect our Company and its business. Readers should carefully consider each of the following risks and all of the other information set forth in this Annual Report on Form 10-K. Based on the information currently known to us, we believe the following information identifies the most significant risk factors affecting our Company. However, the risks and uncertainties we face are not limited to those described below. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial may also adversely affect our business.

If any of the following risks and uncertainties develops into actual events or if the circumstances described in the risks and uncertainties occur or continue to occur, these events or circumstances could have a material adverse effect on our business, prospects, financial condition, results of operations, cash flows or liquidity. These events could also have a negative effect on the trading price of our securities.

General

The results of our business operations are affected by a number of factors, many of which are beyond our control, and primarily depend on, among other things, the level of our net interest income, the market value of our assets, which is driven by numerous factors, including the supply and demand for residential mortgage assets in the marketplace, the terms and availability of adequate financing, general economic and real estate conditions (both on a national and local level), the impact of government actions in the real estate and mortgage sector, and the credit performance of our credit sensitive residential mortgage assets. Our net interest income varies primarily as a result of changes in interest rates, the slope of the yield curve (i.e., the differential between long-term and short-term interest rates), borrowing costs (i.e., our interest expense) and prepayment speeds on our MBS, the behavior of which involves various risks and uncertainties. Interest rates and conditional prepayment rates (or CPRs) (which measure the amount of unscheduled principal prepayment on a bond as a percentage of the bond balance), vary according to the type of investment, conditions in the financial markets, competition and other factors, none of which can be predicted with any certainty. Our operating results also depend upon our ability to effectively manage the risks associated with our business operations, including interest rate, prepayment, financing and credit risks, while maintaining our qualification as a REIT.

We may change our investment strategy, operating policies and/or asset allocations without stockholder consent, which could materially adversely affect our results of operations.

We may change our investment strategy, operating policies and/or asset allocation with respect to investments, acquisitions, leverage, growth, operations, indebtedness, capitalization and distributions at any time without the consent of our stockholders. A change in our investment strategy may increase our exposure to interest rate risk, credit risk, default risk and/or real estate market fluctuations. Furthermore, a change in our asset allocation could result in our making investments in asset categories different from our historical investments. These changes could materially adversely affect our financial condition, results of operations, the market price of our common stock or our ability to pay dividends or make distributions.

Credit Risks

Our investments in Non-Agency MBS (including RPL/NPL MBS) involve credit risk, which could materially adversely affect our results of operations.

The holder of a mortgage or MBS assumes the risk that the related borrowers may default on their obligations to make full and timely payments of principal and interest. Under our investment policy, we have the ability to acquire

Non-Agency MBS, residential whole loans and other investment assets of lower credit quality. In general, Legacy Non-Agency MBS and RPL/NPL MBS (which, as of December 31, 2015 represented 48.8% of our total assets) carry greater investment risk than Agency MBS because they are not guaranteed as to principal or interest by the U.S. Government, any federal agency or any federally chartered corporation. Higher-than-expected rates of default and/or higher-than-expected loss severities on the mortgages underlying these investments could adversely affect the value of these assets. Accordingly, defaults in the payment of principal and/or interest on our Legacy Non-Agency MBS, RPL/NPL MBS and other investment assets of less-than-high credit quality would likely result in our incurring losses of income from, and/or losses in market value relating to, these assets, which could materially adversely affect our results of operations.

Our investments in re-performing and non-performing residential whole loans involve credit risks, some of which are different from our Non-Agency MBS, which could materially adversely affect our results of operations.

Our investment in residential whole loans was relatively speaking our fastest growing asset class during 2015, and represented approximately 6.8% of our total assets as of December 31, 2015. We expect that our investment portfolio in residential whole

Table of Contents

loans will continue to increase during 2016, as we seek opportunities in these credit sensitive assets. As a holder of residential whole loans, we are subject to the risk that the related borrowers may default or have defaulted on their obligations to make full and timely payments of principal and interest. If actual results are different from our assumptions in determining the prices paid to acquire such loans, particularly if the market value of the underlying property decreases significantly subsequent to purchase, we may incur significant losses, which could materially adversely affect our results of operations.

A significant portion of our Non-Agency MBS and residential whole loans are secured by properties in a small number of geographic areas and may be disproportionately affected by economic or housing downturns, natural disasters, terrorist events, regulatory changes, adverse climate changes or other adverse events specific to those markets.

A significant number of the mortgages underlying our Non-Agency MBS and residential whole loan investments are concentrated in certain geographic areas. For example, we have significantly higher exposure in California, Florida, New York, Virginia, Maryland and New Jersey. (See "Credit Risk" included under Part II, Item 7A "Quantitative and Qualitative Disclosures About Market Risk" in this Annual Report on Form 10-K.) Certain markets within these states (particularly in California and Florida) experienced significant decreases in residential home values during the financial crisis of 2007-2008 and the years thereafter, although in more recent years some of these markets have experienced a recovery in home prices. Any event that adversely affects the economy or real estate market in any of these states could have a disproportionately adverse effect on our Non-Agency MBS and residential whole loan investments. In general, any material decline in the economy or significant problems in a particular real estate market would likely cause a decline in the value of residential properties securing the mortgages in that market, thereby increasing the risk of delinquency, default and foreclosure of re-performing loans and the loans underlying our Non-Agency MBS. This could, in turn, have a material adverse effect on our credit loss experience on our Non-Agency MBS and residential whole loan investments in the affected market if higher-than-expected rates of default and/or higher-than-expected loss severities on our re-performing loan investments or the mortgages underlying our Non-Agency MBS were to occur.

The occurrence of a natural disaster (such as an earthquake, tornado, hurricane or a flood), terrorist attack or a significant adverse climate change may cause a sudden decrease in the value of real estate in the area or areas affected and would likely reduce the value of the properties securing the mortgages collateralizing our Non-Agency MBS or residential whole loans. Because certain natural disasters are not typically covered by the standard hazard insurance policies maintained by borrowers (such as hurricanes or certain flooding), or the proceeds payable under any such policy is not sufficient to cover the related repairs, the affected borrowers may have to pay for any repairs themselves. Under these circumstances, borrowers may decide not to repair their property or may stop paying their mortgages under those circumstances. This would likely cause defaults and credit loss severities to increase.

Changes in governmental laws and regulations, fiscal policies, property taxes and zoning ordinances can also have a negative impact on property values, which could result in borrowers' deciding to stop paying their mortgages. This circumstance could cause defaults and loss severities to increase, thereby adversely impacting our results of operations.

We have investments in Non-Agency MBS collateralized by Alt A loans and may also have investments collateralized by subprime mortgage loans, which, due to lower underwriting standards, are subject to increased risk of losses.

We have certain investments in Non-Agency MBS backed by collateral pools containing mortgage loans that were originated under underwriting standards that were less strict than those used in underwriting "prime mortgage loans." These lower standards permitted mortgage loans, often with LTV ratios in excess of 80%, to be made to borrowers having impaired credit histories, lower credit scores, higher debt-to-income ratios and/or unverified income. Difficult economic conditions, including increased interest rates and lower home prices, can result in Alt A and subprime mortgage loans having increased rates of delinquency, foreclosure, bankruptcy and loss (including such as during the credit crisis of 2007-2008 and the housing crisis of the last few years), and are likely to otherwise experience delinquency, foreclosure, bankruptcy and loss rates that are higher, and that may be substantially higher, than those experienced by mortgage loans underwritten in a more traditional manner. Thus, because of higher delinquency rates and losses associated with Alt A and subprime mortgage loans, the performance of our Non-Agency MBS that are backed by these types of loans could be correspondingly adversely affected, which could materially adversely impact our results of operations, financial condition and business.

We are subject to counterparty risk and may be unable to seek indemnity or require counterparties to repurchase residential whole loans if they breach representations and warranties, which could cause us to suffer losses.

In connection with our residential whole loan investments, we typically enter into a loan purchase agreement, as buyer, of the loans from a seller. When we invest in mortgage loans , sellers typically make very limited representations and warranties about such loans. Residential mortgage loan purchase agreements may entitle the purchaser of the loans to seek indemnity or demand repurchase or substitution of the loans in the event the seller of the loans breaches a representation or warranty given to

Table of Contents

the purchaser. However, there can be no assurance that a mortgage loan purchase agreement will contain appropriate representations and warranties, that we or the trust that purchases the mortgage loans would be able to enforce a contractual right to repurchase or substitution, or that the seller of the loans will remain solvent or otherwise be able to honor its obligations under its mortgage loan purchase agreements. The inability to obtain or enforce an indemnity or require repurchase of a significant number of loans could require us to absorb the associated losses, and adversely affect our results of operations, financial condition and business.

To the extent that due diligence is conducted on potential assets, such due diligence may not reveal all of the risks associated with such assets and may not reveal other weaknesses in such assets, which could lead to losses.

Before making an investment, we typically, but not always, conduct (either directly or using third parties) certain due diligence. There can be no assurance that we will conduct any specific level of due diligence, or that, among other things, our due diligence processes will uncover all relevant facts, which could result in losses on these assets to the extent we ultimately acquire them, which, in turn, could adversely affect our results of operations, financial condition and business.

We have experienced, and may in the future experience, declines in the market value of certain of our investment securities resulting in our recording impairments, which have had, and may in the future have, an adverse effect on our results of operations and financial condition.

A decline in the market value of our MBS or other investment securities may require us to recognize an "other-than-temporary impairment" (or OTTI) against such assets under GAAP. When the fair value of an available-for-sale (or AFS) investment security is less than its amortized cost at the balance sheet date, the security is considered impaired. We assess our impaired securities on at least a quarterly basis and designate such impairments as either "temporary" or "other-than-temporary." If we intend to sell an impaired security, or it is more likely than not that we will be required to sell the impaired security before any anticipated recovery, then we must recognize an OTTI through charges to earnings equal to the entire difference between the investment's amortized cost and its fair value at the balance sheet date. If we do not expect to sell an other-than-temporarily impaired security, only the portion of the OTTI that is related to credit losses is required to be recognized through charges to earnings with the remainder recognized through accumulated other comprehensive income/(loss) (or AOCI) on our consolidated balance sheets. Impairments recognized through other comprehensive income/(loss) (or OCI) do not impact earnings. Following the recognition of an OTTI through earnings, a new cost basis is established for the security and may not be adjusted for subsequent recoveries in fair value through earnings. However, OTTIs recognized through charges to earnings may be accreted back to the amortized cost basis of the security on a prospective basis through interest income. The determination as to whether an OTTI exists and, if so, the amount of credit impairment recognized in earnings is subjective, as such determinations are based on factual information available at the time of assessment as well as on our estimates of the future performance and cash flow projections. As a result, the timing and amount of OTTIs constitute material estimates that are susceptible to significant change.

Our use of models in connection with the valuation of our assets subjects us to potential risks in the event that such models are incorrect, misleading or based on incomplete information.

As part of our risk management process, we may use models to evaluate, depending on the asset class, house price appreciation and depreciation by county, region, prepayment speeds and foreclosure frequency, cost and timing. Certain assumptions used as inputs to the models may be based on historical trends. These trends may not be indicative of future results. Furthermore, the assumptions underlying the models may prove to be inaccurate, causing the model output also to be incorrect. In the event models and data prove to be incorrect, misleading or incomplete, any decisions made in reliance thereon expose us to potential risks. For example, by relying on incorrect models and data, we may be induced to buy certain assets at prices that are too high, to sell certain other assets at prices that are too low or to miss favorable opportunities altogether, which could have a material adverse impact on our business and growth prospects.

Valuations of some of our assets are subject to inherent uncertainty, may be based on estimates, may fluctuate over short periods of time and may differ from the values that would have been used if a ready market for these assets existed.

While the determination of the fair value of our investment assets takes into consideration valuations provided by third-party dealers and pricing services, the final determination of exit price fair values for our investment assets is based on our judgment, and such valuations may differ from those provided by third-party dealers and pricing services. Valuations of certain assets may be difficult to obtain or may not be reliable. In general, dealers and pricing services heavily disclaim their valuations as such valuations are not intended to be binding bid prices. Additionally, dealers may claim to furnish valuations only as an accommodation and without special compensation, and so they may disclaim any and all liability arising out of any inaccuracy or incompleteness in valuations. Depending on the complexity and illiquidity of an asset, valuations of the same asset can vary substantially from one dealer or pricing service to another.

Table of Contents

Our results of operations, financial condition and business could be materially adversely affected if our fair value determinations of these assets were materially higher than the values that would exist if a ready market existed for these assets.

Mortgage loan modification and refinancing programs and future legislative action may materially adversely affect the value of, and the returns on, our MBS and residential whole loan investments.

The U.S. Government, through the Federal Reserve, the Treasury Department, the Federal Housing Administration (or the FHA) and other agencies implemented a number of federal programs designed to assist homeowners, including the Home Affordable Modification Program (or HAMP), which provides homeowners with assistance in avoiding residential mortgage loan foreclosures, the Hope for Homeowners Program (or H4H Program), which allows certain distressed borrowers to refinance their mortgages into FHA-insured loans in order to avoid foreclosure, and the Home Affordable Refinance Program (or HARP), which allows borrowers who are current on their mortgage payments to refinance and reduce their monthly mortgage payments without new mortgage insurance, up to an unlimited loan-to-value ratio for fixed-rate mortgages. HAMP, the H4H Program and other loss mitigation programs may involve, among other things, the modification of mortgage loans to reduce the principal amount of the loans (through forbearance and/or forgiveness) and/or the rate of interest payable on the loans, or to extend the payment terms of the loans. Especially with our Non-Agency MBS and residential whole loan investments, a continuing number of loan modifications with respect to a given underlying loan, including, but not limited to, those related to principal forgiveness and coupon reduction, could negatively impact the realized yields and cash flows on such investments. These loan modification programs, future legislative or regulatory actions, including possible amendments to the bankruptcy laws, that result in the modification of outstanding residential mortgage loans, as well as changes in the requirements necessary to qualify for refinancing mortgage loans with Fannie Mae, Freddie Mac or Ginnie Mae, may materially adversely affect the value of, and the returns on, these assets.

Our investments in residential whole loans subject us to servicing-related risks, including those associated with foreclosure.

The residential whole loans that have been acquired to date were purchased together with the related mortgage servicing rights. We rely on unaffiliated servicing companies to service and manage the mortgages underlying our residential whole loans. If a servicer is not vigilant in seeing that borrowers make their required monthly payments, borrowers may be less likely to make these payments, resulting in a higher frequency of default. If a servicer takes longer to liquidate non-performing mortgages, our losses related to those loans may be higher than originally anticipated. Any failure by servicers to service these mortgages and related real estate owned (or REO) properties could negatively impact the value of these investments and our financial performance. In addition, while we have contracted with unaffiliated servicing companies to carry out the actual servicing of the loans (including all direct interface with the borrowers), we are nevertheless ultimately responsible, vis-à-vis the borrowers and state and federal regulators, for ensuring that the loans are serviced in accordance with the terms of the related notes and mortgages and applicable law and regulation. (See “Regulatory Risk and Risks Related to the Investment Company Act of 1940 -- Our business is subject to extensive regulation.) In light of the current regulatory environment, such exposure could be significant even though we might have contractual claims against our servicers for any failure to service the loans to the required standard.

When one of our residential whole loans is foreclosed upon, title to the underlying property is taken by a Company subsidiary. The foreclosure process, especially in judicial foreclosure states such as New York, Florida and New Jersey can be lengthy and expensive, and the delays and costs involved in completing a foreclosure, and then liquidating the property through sale, may materially increase any related loss. Finally, at such time as title is taken to a foreclosed property, it may require more extensive rehabilitation than we estimated at acquisition. Thus, a material amount of foreclosed residential mortgage loans, particularly in the states mentioned above, could result in significant losses in our residential whole loan portfolio and could materially adversely affect our results of operations.

The federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government, may materially adversely affect our business.

The payments of principal and interest we receive on our Agency MBS, which depend directly upon payments on the mortgages underlying such securities, are guaranteed by Fannie Mae, Freddie Mac or Ginnie Mae. Fannie Mae and Freddie Mac are U.S. Government-sponsored entities (or GSEs), but their guarantees are not backed by the full faith and credit of the United States (although the FHFA largely controls their actions through its conservatorship of the two GSEs, which occurred in the wake of the 2007-2008 financial crisis). Ginnie Mae is part of a U.S. Government agency and its guarantees are backed by the full faith and credit of the United States.

Although since the financial crisis of 2007-2008 the U.S. Government has undertaken several measures to support the positive net worth of Fannie Mae and Freddie Mac, there is no guarantee of continuing capital support if such support were to become necessary. These uncertainties lead to questions about the availability of, and trading market for, Agency MBS. Despite the steps

Table of Contents

taken by the U.S. Government, Fannie Mae and Freddie Mac could default on their guarantee obligations which would materially and adversely affect the value of our Agency MBS. Accordingly, if these government actions are inadequate in the future and the GSEs were to suffer losses, be significantly reformed, or cease to exist (as discussed below), our business, operations and financial condition could be materially and adversely affected.

In addition, the problems faced by Fannie Mae and Freddie Mac resulting in their being placed into federal conservatorship and receiving significant U.S. Government support have sparked serious debate among federal policy makers regarding the continued role of the U.S. Government in providing liquidity for mortgage loans. In 2011, the Obama administration proposed a plan to wind down the GSEs, and both houses of Congress have considered legislation to reform the GSEs, their functions and their missions. The future roles of Fannie Mae and Freddie Mac may be reduced (perhaps significantly) and the nature of their guarantee obligations could be limited relative to historical measurements. Alternatively, it is still possible that Fannie Mae and Freddie Mac could be dissolved entirely or privatized, and, as mentioned above, the U.S. Government could determine to stop providing liquidity support of any kind to the mortgage market. Any changes to the nature of the GSEs or their guarantee obligations could redefine what constitutes an Agency MBS and could have broad adverse implications for the market and our business, operations and financial condition. If Fannie Mae or Freddie Mac were to be eliminated, or their structures were to change radically (in particular a limitation or removal of the guarantee obligation), we could be unable to acquire additional Agency MBS and our existing Agency MBS could be materially and adversely impacted.

We could be negatively affected in a number of ways depending on the manner in which events unfold for Fannie Mae and Freddie Mac. We rely on our Agency MBS as collateral for a significant portion of our financings under our repurchase agreements. Any decline in their value, or perceived market uncertainty about their value, would make it more difficult for us to obtain financing on our Agency MBS on acceptable terms or at all, or to maintain our compliance with the terms of any financing transactions.

As indicated above, future legislation could, among other things, reform the GSEs and their functions, or nationalize, privatize, or eliminate them entirely. Any law affecting the GSEs may create market uncertainty and have the effect of reducing the actual or perceived credit quality of securities issued or guaranteed by Fannie Mae or Freddie Mac. As a result, such laws could increase the risk of loss on our investments in Agency MBS guaranteed by Fannie Mae and/or Freddie Mac. It also is possible that such laws could adversely impact the market for such securities and the spreads at which they trade. All of the foregoing could materially and adversely affect our business, operations and financial condition.

Government use of eminent domain to seize underwater mortgages could materially adversely affect the value of, and the returns on, our MBS.

The mortgages securing our investments are located in many geographic regions across the United States, with significantly higher exposure in California, Florida, New York, Virginia and Maryland. Several county and municipal governments have discussed using eminent domain to seize from mortgage holders the mortgages of borrowers who are underwater, but not in default. Legislation enacted in 2014 prohibits the FHFA and the Department of Housing and Urban Development from using federal funds to facilitate the seizure of mortgage loans by a state or local municipality. However, if definitive action were to be taken in the future by any local governments, and such actions withstand Constitutional and other legal challenges, resulting in mortgages securing certain of our investments being seized using eminent domain, the consideration received from the seizing authorities for such mortgages may be substantially less than the outstanding principal balance, which would result in a realized loss and a corresponding write-down of the principal balance of those mortgages. The result of these seizures would be that the amounts we receive on our investments would be less than we would otherwise have received if the mortgage loans had not been seized, which may result in a lower return on such assets or require charges for OTTI or loan loss reserves. If governments ultimately adopt such plans and mortgages securing certain of our investments are seized on a widespread scale, it could have a material adverse effect on the value of and/or returns on our assets and our results of operations more generally.

Prepayment and Reinvestment Risk

Prepayment rates on the mortgage loans underlying our MBS may materially adversely affect our profitability or result in liquidity shortfalls that could require us to sell assets in unfavorable market conditions.

The MBS that we acquire are secured by pools of mortgages on residential properties. In general, the mortgages collateralizing our MBS may be prepaid at any time without penalty. Prepayments on our MBS result when borrowers satisfy (i.e., pay off) the mortgage upon selling or refinancing their mortgaged property. When we acquire a particular MBS, we anticipate that the underlying mortgage loans will prepay at a projected rate which, together with expected coupon income, provides us with an expected yield on that MBS. If we purchase MBS at a premium to par value, and borrowers then prepay the underlying mortgage loans at a faster rate than we expected, the increased prepayments on the MBS would result in a yield lower than expected on such securities because we would be required to amortize the related premium on an accelerated basis. Conversely, if we purchase

Table of Contents

MBS at a discount to par value, and borrowers then prepay the underlying mortgage loans at a slower rate than we expected, the decreased prepayments on the MBS would result in a lower yield than expected on such securities and/or may result in OTTI if the fair value of the security is less than its amortized cost.

Prepayment rates on mortgage loans are influenced by changes in mortgage and market interest rates and a variety of economic, geographic, governmental and other factors beyond our control. Consequently, prepayment rates cannot be predicted with certainty and no strategy can completely insulate us from prepayment risks. In periods of declining interest rates, prepayment rates on mortgage loans generally increase. Because of prepayment risk, the market value of our MBS (and in particular our Agency MBS) may benefit less than other fixed income securities from a decline in interest rates. If general interest rates decline at the same time, we would likely not be able to reinvest the proceeds of the prepayments that we receive in assets yielding as much as those yields on the assets that were prepaid.

With respect to Agency MBS, we have, at times, purchased securities that have a higher coupon rate than the prevailing market interest rates. In exchange for a higher coupon rate, we typically pay a premium over par value to acquire such securities. In accordance with U.S. generally accepted accounting principles (or GAAP), we amortize premiums on our MBS over the life of the related MBS. If the underlying mortgage loans securing these securities prepay at a more rapid rate than anticipated, we will be required to amortize the related premiums on an accelerated basis, which could adversely affect our profitability. Defaults on the mortgages underlying Agency MBS typically have the same effect as loan prepayments because of the underlying Agency guarantee. As of December 31, 2015, we had net purchase premiums on our Agency MBS of $172.0 million (or 3.8% of current par value) and net purchase discounts on our Non-Agency MBS of $1.100 billion (or 15.8% of current par value).

Prepayments, which are the primary feature of MBS that distinguishes them from other types of bonds, are difficult to predict and can vary significantly over time. As the holder of MBS, we receive a monthly payment equal to a portion of our investment principal in a particular MBS as the underlying mortgages are prepaid. With respect to Agency MBS, we typically receive notice of monthly principal prepayments on the fifth business day of each month (such day is commonly referred to as “factor day”) and receive the related scheduled payment on a specified later date, which for (a) our Agency ARM-MBS and fixed-rate Agency MBS guaranteed by Fannie Mae is the 25th day of the month (or next business day thereafter), (b) our Agency ARM-MBS guaranteed by Freddie Mac is the 15th day of the following month (or next business day thereafter), (c) our fixed-rate Agency MBS guaranteed by Freddie Mac is the 15th day of the month (or next business day thereafter), and (d) our Agency ARM-MBS guaranteed by Ginnie Mae is the 20th day of that month (or next business day thereafter). With respect to our Non-Agency MBS, we typically receive notice of monthly principal prepayments and the related scheduled payment on the 25th day of each month (or next business day thereafter). In general, on the date each month that principal prepayments are announced (i.e., factor day for Agency MBS), the value of our MBS pledged as collateral under our repurchase agreements is reduced by the amount of the prepaid principal and, as a result, our lenders will typically initiate a margin call that requires us to pledge additional collateral in the form of cash or additional MBS, in an amount equal to the prepaying principal, in order to re-establish the required ratio of borrowing to collateral value under such repurchase agreements. Accordingly, in the case of Agency MBS, the announcement on factor day of principal prepayments occurs prior to our receipt of the related scheduled payment. This timing differential creates a short-term receivable for us in the amount of any such principal prepayments; however, under our repurchase agreements, we may receive a margin call in the amount of the related reduction in value of the Agency MBS and be required to post on or about factor day additional cash or other collateral in the amount of the prepaying principal to be received, which thereby would reduce our liquidity during the period in which the short-term receivable is outstanding. As a result, in order to meet any such margin calls, we might be forced to sell assets in order to maintain adequate liquidity. Forced sales, particularly under adverse market conditions, may result in lower sales prices than sales made under ordinary market conditions in the normal course of business. If our MBS were to be liquidated at prices below our amortized cost (i.e., our cost basis) of such assets, we would incur losses, which could materially adversely affect our earnings. In addition, in order to continue to earn a return on this prepaid principal, we must reinvest it in additional MBS or other assets; however, in a declining interest rate environment, we might earn a lower return on our reinvested funds as compared to the return earned on the MBS that had prepaid.

Prepayments may have a materially negative impact on our financial results, the effects of which depend on, among other things, the timing and amount of the prepayment delay on Agency MBS, the amount of unamortized premium on MBS prepayments, the rate at which prepayments are made on our Non-Agency MBS, the reinvestment lag and the availability of suitable reinvestment opportunities.

Table of Contents

Risks Related to Our Use of Leverage

Our business strategy involves the use of leverage, and we may not achieve what we believe to be optimal levels of leverage or we may become overleveraged, which may materially adversely affect our liquidity, results of operations or financial condition.

Our business strategy involves the use of borrowing or "leverage." Pursuant to our leverage strategy, we borrow against a substantial portion of the market value of our MBS and our residential whole loans and use the borrowed funds to finance our investment portfolio and the acquisition of additional investment assets. We are not required to maintain any particular debt-to-equity ratio. Future increases in the amount by which the collateral value is required to contractually exceed the repurchase transaction loan amount, decreases in the market value of our MBS, increases in interest rate volatility and changes in the availability of acceptable financing could cause us to be unable to achieve the amount of leverage we believe to be optimal. The return on our assets and cash available for distribution to our stockholders may be reduced to the extent that changes in market conditions prevent us from achieving the desired amount of leverage on our investments or cause the cost of our financing to increase relative to the income earned on our leveraged assets. If the interest income on our MBS purchased with borrowed funds fails to cover the interest expense of the related borrowings, we will experience net interest losses and may experience net losses from operations. Such losses could be significant as a result of our leveraged structure. The use of leverage to finance our MBS and other assets involves a number of other risks, including, among other things, the following:

- Adverse developments involving major financial institutions or involving one of our lenders could result in a rapid reduction in our ability to borrow and materially adversely affect our business, profitability and liquidity. As of December 31, 2015, we had amounts outstanding under repurchase agreements with 27 separate lenders. A material adverse development involving one or more major financial institutions or the financial markets in general could result in our lenders reducing our access to funds available under our repurchase agreements or terminating such repurchase agreements altogether. Because all of our repurchase agreements are uncommitted and renewable at the discretion of our lenders, our lenders could determine to reduce or terminate our access to future borrowings at virtually any time, which could materially adversely affect our business and profitability. Furthermore, if a number of our lenders became unwilling or unable to continue to provide us with financing, we could be forced to sell assets, including MBS in an unrealized loss position, in order to maintain liquidity. Forced sales, particularly under adverse market conditions may result in lower sales prices than ordinary market sales made in the normal course of business. If our MBS were liquidated at prices below our amortized cost (i.e., the cost basis) of such assets, we would incur losses, which could adversely affect our earnings.

- Our profitability may be materially adversely affected by a reduction in our leverage. As long as we earn a positive spread between interest and other income we earn on our leveraged assets and our borrowing costs, we believe that we can generally increase our profitability by using greater amounts of leverage. There can be no assurance, however, that repurchase financing will remain an efficient source of long-term financing for our assets. The amount of leverage that we use may be limited because our lenders might not make funding available to us at acceptable rates or they may require that we provide additional collateral to secure our borrowings. If our financing strategy is not viable, we will have to find alternative forms of financing for our assets which may not be available to us on acceptable terms or at acceptable rates. In addition, in response to certain interest rate and investment environments or to changes in market liquidity, we could adopt a strategy of reducing our leverage by selling assets or not reinvesting principal payments as MBS amortize and/or prepay, thereby decreasing the outstanding amount of our related borrowings. Such an action could reduce interest income, interest expense and net income, the extent of which would be dependent on the level of reduction in assets and liabilities as well as the sale prices for which the assets were sold.

•

If we are unable to renew our borrowings at acceptable interest rates, it may force us to sell assets under adverse market conditions, which may materially adversely affect our liquidity and profitability. Since we rely primarily on borrowings under repurchase agreements to finance our MBS, our ability to achieve our investment objectives depends on our ability to borrow funds in sufficient amounts and on acceptable terms, and on our ability to renew or replace maturing borrowings on a continuous basis. Our repurchase agreement credit lines are renewable at the discretion of our lenders and, as such, do not contain guaranteed roll-over terms. Our ability to enter into repurchase transactions in the future will depend on the market value of our MBS pledged to secure the specific borrowings, the availability of acceptable financing and market liquidity and other conditions existing in the lending market at that time. If we are not able to renew or replace maturing borrowings, we could be forced to sell assets, including MBS in an unrealized loss position, in order to maintain liquidity. Forced sales, particularly under adverse market conditions could result in lower sales prices than ordinary market sales made in the normal course of business. If our MBS were liquidated at prices below our amortized cost (i.e., the cost basis) of such assets, we would incur losses, which could materially adversely affect our earnings.

Table of Contents

- A decline in the market value of our assets may result in margin calls that may force us to sell assets under adverse market conditions, which may materially adversely affect our liquidity and profitability. In general, the market value of our MBS is impacted by changes in interest rates, prevailing market yields and other market conditions. A decline in the market value of our MBS may limit our ability to borrow against such assets or result in lenders initiating margin calls, which require a pledge of additional collateral or cash to re-establish the required ratio of borrowing to collateral value, under our repurchase agreements. Posting additional collateral or cash to support our credit will reduce our liquidity and limit our ability to leverage our assets, which could materially adversely affect our business. As a result, we could be forced to sell a portion of our assets, including MBS in an unrealized loss position, in order to maintain liquidity.

- If a counterparty to our repurchase transactions defaults on its obligation to resell the underlying security back to us at the end of the transaction term or if we default on our obligations under the repurchase agreement, we could incur losses. When we engage in repurchase transactions, we generally transfer securities to lenders (i.e., repurchase agreement counterparties) and receive cash from such lenders. Because the cash we receive from the lender when we initially transfer the securities to the lender is less than the value of those securities (this difference is referred to as the "haircut"), if the lender defaults on its obligation to transfer the same securities back to us, we would incur a loss on the transaction equal to the amount of the haircut (assuming there was no change in the value of the securities). See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Annual Report on Form 10-K, for further discussion regarding risks related to exposure to financial institution counterparties in light of recent market conditions. Our exposure to defaults by counterparties may be more pronounced during periods of significant volatility in the market conditions for mortgages and mortgage-related assets as well as the broader financial markets. At December 31, 2015, we had greater than 5% stockholders' equity at risk to the following repurchase agreement counterparties: Credit Suisse (approximately 13.8%), Wells Fargo (approximately 11.3%), RBC (approximately 11.0%), UBS (approximately 7.2%) and Goldman Sachs (approximately 5.1%).

In addition, generally, if we default on one of our obligations under a repurchase transaction with a particular lender, that lender can elect to terminate the transaction and cease entering into additional repurchase transactions with us. In addition, some of our repurchase agreements contain cross-default provisions, so that if a default occurs under any one agreement, the lenders under our other repurchase agreements could also declare a default. Any losses we incur on our repurchase transactions could materially adversely affect our earnings and thus our cash available for distribution to our stockholders.

- Our use of repurchase agreements to borrow money may give our lenders greater rights in the event of bankruptcy. Borrowings made under repurchase agreements may qualify for special treatment under the U.S. Bankruptcy Code. If a lender under one of our repurchase agreements defaults on its obligations, it may be difficult for us to recover our assets pledged as collateral to such lender. In the event of the insolvency or bankruptcy of a lender during the term of a repurchase agreement, the lender may be permitted, under applicable insolvency laws, to repudiate the contract, and our claim against the lender for damages may be treated simply as an unsecured creditor. In addition, if the lender is a broker or dealer subject to the Securities Investor Protection Act of 1970, or an insured depository institution subject to the Federal Deposit Insurance Act, our ability to exercise our rights to recover our securities under a repurchase agreement or to be compensated for any damages resulting from the lender's insolvency may be further limited by those statutes. These claims would be subject to significant delay and, if and when received, may be substantially less than the damages we actually incur. In addition, in the event of our insolvency or bankruptcy, certain repurchase agreements may qualify for special treatment under the Bankruptcy Code, the effect of which, among other things, would be to allow the creditor under the agreement to avoid the automatic stay provisions of the Bankruptcy Code and take possession of, and liquidate, our collateral under our repurchase agreements without delay. Our risks associated with the insolvency or bankruptcy of a lender maybe more pronounced during periods of significant volatility in the market conditions for mortgages and mortgage-related assets as well as the broader financial markets.

An increase in our borrowing costs relative to the interest we receive on our MBS or our re-performing residential whole loans may materially adversely affect our profitability.

Our earnings are primarily generated from the difference between the interest income we earn on our investment portfolio, less net amortization of purchase premiums and discounts, and the interest expense we pay on our borrowings. We rely primarily on borrowings under repurchase agreements to finance the acquisition of MBS which have longer-term contractual maturities. Even though the majority of our investments have interest rates that adjust over time based on changes in corresponding interest rate indexes, the interest we pay on our borrowings may increase at a faster pace than the interest we earn on our investments. In general, if the interest expense on our borrowings increases relative to the interest income we earn on our investments, our profitability may be materially adversely affected, including due to the following reasons:

Table of Contents

- Changes in interest rates, cyclical or otherwise, may materially adversely affect our profitability. Interest rates are highly sensitive to many factors, including fiscal and monetary policies and domestic and international economic and political conditions, as well as other factors beyond our control. In general, we finance the acquisition of our investments through borrowings in the form of repurchase transactions, which exposes us to interest rate risk on the financed assets. The cost of our borrowings is based on prevailing market interest rates. Because the terms of our repurchase transactions typically range from one to six months at inception, the interest rates on our borrowings generally adjust more frequently (as new repurchase transactions are entered into upon the maturity of existing repurchase transactions) than the interest rates on our investments. During a period of rising interest rates, our borrowing costs generally will increase at a faster pace than our interest earnings on the leveraged portion of our investment portfolio, which could result in a decline in our net interest spread and net interest margin. The severity of any such decline would depend on our asset/liability composition, including the impact of hedging transactions, at the time as well as the magnitude and period over which interest rates increase. Further, an increase in short-term interest rates could also have a negative impact on the market value of our MBS portfolio. If any of these events happen, we could experience a decrease in net income or incur a net loss during these periods, which may negatively impact our distributions to stockholders.

- Interest rate caps on the mortgages collateralizing our MBS may materially adversely affect our profitability if short-term interest rates increase. The coupons earned on ARM-MBS adjust over time as interest rates change (typically after an initial fixed-rate period for Hybrids). The financial markets primarily determine the interest rates that we pay on the repurchase transactions used to finance the acquisition of our MBS; however, the level of adjustment to the interest rates earned on our ARM-MBS is typically limited by contract (or in certain cases by state or federal law). The interim and lifetime interest rate caps on the mortgages collateralizing our MBS limit the amount by which the interest rates on such assets can adjust. Interim interest rate caps limit the amount interest rates on a particular ARM can adjust during the next adjustment period. Lifetime interest rate caps limit the amount interest rates can adjust upward from inception through maturity of a particular ARM. Our repurchase transactions are not subject to similar restrictions. Accordingly, in a sustained period of rising interest rates or a period in which interest rates rise rapidly, we could experience a decrease in net income or a net loss because the interest rates paid by us on our borrowings (excluding the impact of hedging transactions) could increase without limitation (as new repurchase transactions are entered into upon the maturity of existing repurchase transactions) while increases in the interest rates earned on the mortgages collateralizing our MBS could be limited due to interim or lifetime interest rate caps.

- Adjustments of interest rates on our borrowings may not be matched to interest rate indexes on our MBS. In general, the interest rates on our repurchase transactions are based on LIBOR, while the interest rates on our ARM-MBS may be indexed to LIBOR or CMT rate. Accordingly, any increase in LIBOR relative to one-year CMT rates will generally result in an increase in our borrowing costs that is not matched by a corresponding increase in the interest earned on our ARM-MBS tied to these other index rates. Any such interest rate index mismatch could adversely affect our profitability, which may negatively impact our distributions to stockholders.

- A flat or inverted yield curve may adversely affect ARM-MBS prepayment rates and supply. Our net interest income varies primarily as a result of changes in interest rates as well as changes in interest rates across the yield curve. When the differential between short-term and long-term benchmark interest rates narrows, the yield curve is said to be “flattening.” In addition, a flatter yield curve generally leads to fixed-rate mortgage rates that are closer to the interest rates available on ARMs, potentially decreasing the supply of ARM-MBS. At times, short-term interest rates may increase and exceed long-term interest rates, causing an inverted yield curve. When the yield curve is inverted, fixed-rate mortgage rates may approach or be lower than mortgage rates on ARMs, further increasing ARM-MBS prepayments and further negatively impacting ARM-MBS supply. Increases in prepayments on our MBS portfolio cause our premium amortization to accelerate, lowering the yield on such assets. If this happens, we could experience a decrease in net income or incur a net loss during these periods, which may negatively impact our distributions to stockholders.

Amendments to the Federal Home Loan Bank membership regulations will require us to terminate our membership with the FHLB, which could adversely affect our ability to finance our operations.

Our captive insurance subsidiary, MFA Insurance, is a member of the Federal Home Loan Bank of Des Moines (or FHLB Des Moines) and obtains advances from the FHLB Des Moines in the form of secured borrowings. On January 12, 2016, the FHFA amended its regulations governing FHLB membership. The amendments exclude captive insurers from the definition of “insurance company,” making MFA Insurance ineligible for FHLB membership, and, MFA Insurance is required to terminate its membership with the FHLB Des Moines by February 19, 2017. It is also required to repay its existing advances from the FHLB Des Moines by February 19, 2017 or, if earlier, the date it terminates its membership with the FHLB Des Moines, and it is prohibited from receiving new advances or renewing existing advances with the FHLB Des Moines. As of December 31, 2015 and February 16, 2016, MFA Insurance had approximately $1.500 billion and $1.200 billion, respectively, in outstanding secured advances from the FHLB Des Moines. There is no guarantee that we will be able to find suitable counterparties, or any counterparties, to replace the advances received by the FHLB Des Moines or that such replacements will be made on comparable terms, which could adversely affect our ability to finance our operations.

Risks Associated With Adverse Developments in the Mortgage Finance and Credit Markets and Financial Markets Generally

Market conditions for mortgages and mortgage-related assets as well as the broader financial markets may materially adversely affect the value of the assets in which we invest.

Our results of operations are materially affected by conditions in the markets for mortgages and mortgage-related assets, including MBS, as well as the broader financial markets and the economy generally. Significant adverse changes in financial market conditions leading to the forced sale of large quantities of mortgage-related and other financial assets, would result in significant volatility in the market for mortgages and mortgage-related assets and potentially significant losses for ourselves and certain other market participants. In addition, concerns over actual or anticipated low economic growth rates higher levels of unemployment or uncertainty regarding future U.S. monetary policy may contribute to increased interest rate volatility. Declines in the value of our investments, or perceived market uncertainty about their value, may make it difficult for us to obtain financing on favorable terms or at all, or maintain our compliance with terms of any financing arrangements already in place. Additionally, increased volatility and/or deterioration in the broader residential mortgage and MBS markets could materially adversely affect the performance and market value of our investments.

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

The assets that comprise our investment portfolio and that we acquire are not traded on an exchange. A portion of our investments are subject to legal and other restrictions on resale and are otherwise generally less liquid than exchange-traded securities. Any illiquidity of our investments may make it difficult for us to sell such investments if the need or desire arises. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our investments. Further, we may face other restrictions on our ability to liquidate an investment in a business entity to the extent that we have or could be attributed with material, non-public information regarding such business entity. As a result, our ability to vary our portfolio in response to changes in economic and other conditions may be relatively limited, which could adversely affect our results of operations and financial condition.

Actions by the U.S. Government designed to stabilize or reform the financial markets may not achieve their intended effect or otherwise benefit our business, and could materially adversely affect our business.

In July 2010, the U.S. Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (or the Dodd-Frank Act), in part to impose significant investment restrictions and capital requirements on banking entities and other organizations that are significant to U.S. financial markets. For instance, the Dodd-Frank Act imposes significant restrictions on the proprietary trading activities of certain banking entities and subjects other systemically significant entities and activities regulated by the U.S. Federal Reserve to increased capital requirements and quantitative limits for engaging in such activities. The Dodd-Frank Act also seeks to reform the asset-backed securitization market (including the MBS market) by requiring the retention of a portion of the credit risk inherent in the pool of securitized assets and by imposing additional registration and disclosure requirements. The Dodd-Frank Act also imposes significant regulatory restrictions on the origination of residential mortgage loans. The Dodd-Frank Act's extensive requirements, and implementation by regulatory agencies such as the Commodity Futures Trading Commission (or CFTC), the Federal Deposit Insurance Corporation (or FDIC), Federal Reserve Board, and the SEC may have a significant effect on the financial markets, and may affect the availability or terms of financing from our lender counterparties and the availability or terms of MBS, both of which could have a material adverse effect on our business.

In addition, the U.S. Government, U.S. Federal Reserve, U.S. Treasury and other governmental and regulatory bodies have taken or are considering taking other actions to continue to address the fallout from the 2007-2008 financial and credit crisis domestically and internationally. International financial regulators are examining standard setting for systemically significant entities, such as those considered by the Third Basel Accords (Basel III) to be incorporated by domestic entities. We cannot predict whether or when such actions may occur or what affect, if any, such actions could have on our business, results of operations and financial condition.

Table of Contents

Deterioration in the condition of European banks and financial institutions could have a material adverse effect on our business.

In the years following the financial and credit crisis of 2007-2008, certain of our repurchase agreement counterparties in the United States and Europe experienced financial difficulty and were either rescued by government assistance or otherwise benefited from accommodative monetary policy of Central Banks. Several European governments implemented measures to attempt to shore up their financial sectors through loans, credit guarantees, capital infusions, promises of continued liquidity funding and interest rate cuts. Additionally, other governments of the world's largest economic countries also implemented interest rate cuts. Although economic and credit conditions have stabilized in the past few years, there is no assurance that these and other plans and programs will be successful in the longer term, and, in particular, when governments and central banks begin to significantly unwind or otherwise reverse these programs and policies. If unsuccessful, this could materially adversely affect our financing and operations as well as those of the entire mortgage sector in general.

Several of our financing counterparties are European banks (or their U.S. based subsidiaries) that, have provided financing to us, particularly repurchase agreement financing for the acquisition of residential mortgage assets. If European banks and financial institutions experienced a deterioration in financial condition, there is the possibility that this would also negatively affect the operations of their U.S. banking subsidiaries. This could adversely affect our financing and operations as well as those of the entire mortgage sector in general.

Any downgrade, or perceived potential of a downgrade, of U.S. sovereign credit ratings or the credit ratings of the GSEs by the various credit rating agencies may materially adversely affect our the value of our Agency MBS and our business more generally.

During the summer of 2011, Standard & Poor's Ratings Services (or S&P), one of the major credit rating agencies, downgraded the U.S. sovereign credit rating in response to the protracted debate over the "U.S. debt ceiling limit" and S&P's perception of the U.S. Government's ability to address its long-term budget deficit. At the same time, S&P also lowered the credit ratings of the GSEs in response to the downgrade in the U.S. sovereign credit rating, as the value of the Agency MBS issued by the GSEs and their ability to meet their obligations under such Agency MBS are largely determined by the support provided to them by the U.S. Government and market perceptions of the strength of such support and the likelihood of its continuity.

We could be adversely affected in a number of ways in the event of a default by the U.S. Government, a further downgrade by S&P or a downgrade of the U.S. sovereign credit rating by another credit rating agency Such adverse effects could include higher financing costs and/or a reduction in the amount of financing provided based on the market value of collateral posted under our repurchase agreements and other financing arrangements. In addition, although the rating agencies have more recently determined that the GSEs' outlook is generally stable, to the extent that the credit rating of any or all of the GSEs were to be downgraded in the future, the value of our Agency MBS could be adversely affected. These outcomes could in turn materially adversely affect our operations and financial condition in a number of ways, including a reduction in the net interest spread between our assets and associated repurchase agreement borrowings or a decrease in our ability to obtain repurchase agreement financing on acceptable terms, or at all.

Regulatory Risk and Risks Related to the Investment Company Act of 1940

Our business is subject to extensive regulation.

Our business is subject to extensive regulation by federal and state governmental authorities, self-regulatory organizations and securities exchanges. We are required to comply with numerous federal and state laws. The laws, rules and regulations comprising this regulatory framework change frequently, as can the interpretation and enforcement of existing laws, rules and regulations. Some of the laws, rules and regulations to which we are subject are intended primarily to safeguard and protect consumers, rather than stockholders or creditors. From time to time, we may receive requests from federal and state agencies for records, documents and information regarding our policies, procedures and practices regarding our business activities. We incur significant ongoing costs to comply with these government regulations.

Although we do not originate or directly service residential mortgage loans, we must comply with various federal and state laws, rules and regulations as a result of owning MBS and residential whole loans. These rules generally focus on consumer protection and include, among others, rules promulgated under the Dodd-Frank Act, and the Gramm-Leach-Bliley Financial Modernization Act of 1999 (or Gramm-Leach-Bliley). These requirements can and do change as statutes and regulations are enacted, promulgated, amended and interpreted, and the recent trend among federal and state lawmakers and regulators has been toward increasing laws, regulations and investigative proceedings in relation to the mortgage industry generally. Although we believe that we have structured our operations and investments to comply with existing legal and regulatory requirements and

Table of Contents

interpretations, changes in regulatory and legal requirements, including changes in their interpretation and enforcement by lawmakers and regulators, could materially and adversely affect our business and our financial condition, liquidity and results of operations.

Maintaining our exemption from registration under the Investment Company Act imposes significant limits on our operations.

We conduct our operations so that neither we nor any of our subsidiaries are required to register as an investment company under the Investment Company Act. Section 3(a)(1)(A) of the Investment Company Act defines an investment company as any issuer that is or holds itself out as being engaged primarily in the business of investing, reinvesting or trading in securities. Section 3(a)(1)(C) of the Investment Company Act defines an investment company as any issuer that is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of the issuer's total assets (exclusive of U.S. Government securities and cash items) on an unconsolidated basis. Excluded from the term "investment securities," among other things, are U.S. Government securities and securities issued by majority-owned subsidiaries that are not themselves investment companies and are not relying on the exception from the definition of investment company for private funds set forth in Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

We are a holding company and conduct our real estate businesses primarily through wholly-owned subsidiaries. We conduct our real estate business so that we do not come within the definition of an investment company because less than 40% of the value of our adjusted total assets on an unconsolidated basis will consist of "investment securities." The securities issued by any wholly-owned or majority-owned subsidiaries that we may form in the future that are excepted from the definition of "investment company" based on Section 3(c)(1) or 3(c)(7) of the Investment Company Act, together with any other investment securities we may own, may not have a value in excess of 40% of the value of our adjusted total assets on an unconsolidated basis. We monitor our holdings to ensure continuing and ongoing compliance with this test. In addition, we believe we will not be considered an investment company under Section 3(a)(1)(A) of the Investment Company Act because we will not engage primarily or hold ourselves out as being engaged primarily in the business of investing, reinvesting or trading in securities. Rather, through our wholly-owned subsidiaries, we will be primarily engaged in the non-investment company businesses of these subsidiaries.

If the value of securities issued by our subsidiaries that are excepted from the definition of "investment company" by Section 3(c)(1) or 3(c)(7) of the Investment Company Act, together with any other investment securities we own, exceeds 40% of our adjusted total assets on an unconsolidated basis, or if one or more of such subsidiaries fail to maintain an exception or exemption from the Investment Company Act, we could, among other things, be required either (a) to substantially change the manner in which we conduct our operations to avoid being required to register as an investment company, (b) effect sales of our assets in a manner that, or at a time when, we would not otherwise choose to do so or (c) to register as an investment company under the Investment Company Act, either of which could have an adverse effect on us and the market price of our securities. If we were required to register as an investment company under the Investment Company Act, we would become subject to substantial regulation with respect to our capital structure (including our ability to use leverage), management, operations, transactions with affiliated persons (as defined in the Investment Company Act), portfolio composition, including restrictions with respect to diversification and industry concentration, and other matters.

We expect that our subsidiaries that invest in residential mortgage loans (whether through a consolidated trust or otherwise) will rely upon the exemption from registration as an investment company under the Investment Company Act pursuant to Section 3(c)(5)(C) of the Investment Company Act, which is available for entities "primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate." This exemption generally requires that at least 55% of these subsidiaries' assets must be comprised of qualifying real estate assets and at least 80% of each of their portfolios must be comprised of qualifying real estate assets and real estate-related assets under the Investment Company Act. Mortgage loans that were fully and exclusively secured by real property are generally qualifying real estate assets for purposes of the exemption. All, or substantially all, of our residential mortgage loans are fully and exclusively secured by real property with a loan-to-value ratio of less than 100%. As a result, we believe our residential mortgage loans that are fully and exclusively secured by real property meet the definition of qualifying real estate assets. To the extent we own any residential mortgage loans with a loan-to-value ratio of greater than 100%, we intend to classify, depending on guidance from the SEC staff, only the portion of the value of such loans that does not exceed the value of the real estate collateral as qualifying real estate assets and the excess as real estate-related assets.

In August 2011, the SEC issued a "concept release" pursuant to which they solicited public comments on a wide range of issues relating to companies engaged in the business of acquiring mortgages and mortgage-related instruments and that rely on Section 3(c)(5)(C) of the Investment Company Act. The concept release and the public comments thereto have not yet resulted in SEC rulemaking or interpretative guidance and we cannot predict what form any such rulemaking or interpretive guidance may take. There can be no assurance, however, that the laws and regulations governing the Investment Company Act status of REITs,

Table of Contents

or guidance from the SEC or its staff regarding the exemption from registration as an investment company on which we rely, will not change in a manner that adversely affects our operations. We expect each of our subsidiaries relying on Section 3(c)(5)(C) to rely on guidance published by the SEC staff or on our analyses of guidance published with respect to other types of assets, if any, to determine which assets are qualifying real estate assets and real estate-related assets. To the extent that the SEC staff publishes new or different guidance with respect to these matters, we may be required to adjust our strategy accordingly. In addition, we may be limited in our ability to make certain investments and these limitations could result in us holding assets we might wish to sell or selling assets we might wish to hold.

Certain of our subsidiaries may rely on the exemption provided by Section 3(c)(6) to the extent that they hold residential mortgage loans through majority owned subsidiaries that rely on Section 3(c)(5)(C). The SEC staff has issued little interpretive guidance with respect to Section 3(c)(6) and any guidance published by the staff could require us to adjust our strategy accordingly.

To the extent that the SEC staff provides more specific guidance regarding any of the matters bearing upon the exceptions we and our subsidiaries rely on from the Investment Company Act, we may be required to adjust our strategy accordingly. Any additional guidance from the SEC staff could provide additional flexibility to us, or it could further inhibit our ability to pursue the strategies we have chosen.

There can be no assurance that the laws and regulations governing the Investment Company Act status of REITs, including the Division of Investment Management of the SEC providing more specific or different guidance regarding these exemptions, will not change in a manner that adversely affects our operations.

Risks Related to Our Use of Hedging Strategies

Our use of hedging strategies to mitigate our interest rate exposure may not be effective.

In accordance with our operating policies, we pursue various types of hedging strategies, including interest rate swap agreements (or Swaps), to seek to mitigate or reduce our exposure to losses from adverse changes in interest rates. Our hedging activity will vary in scope based on the level and volatility of interest rates, the type of assets held and financing sources used and other changing market conditions. No hedging strategy, however, can completely insulate us from the interest rate risks to which we are exposed and there is no guarantee that the implementation of any hedging strategy would have the desired impact on our results of operations or financial condition. Certain of the U.S. federal income tax requirements that we must satisfy in order to qualify as a REIT may limit our ability to hedge against such risks. We will not enter into derivative transactions if we believe that they will jeopardize our qualification as a REIT.

Interest rate hedging may fail to protect or could adversely affect us because, among other things:

- interest rate hedging can be expensive, particularly during periods of rising and volatile interest rates;
- available interest rate hedges may not correspond directly with the interest rate risk for which protection is sought;
- the duration of the hedge may not match the duration of the related liability;
- the credit quality of the party owing money on the hedge may be downgraded to such an extent that it impairs our ability to sell or assign our side of the hedging transaction; and
- the party owing money in the hedging transaction may default on its obligation to pay.

We primarily use Swaps to hedge against future increases in interest rates on our repurchase agreements. Should a Swap counterparty be unable to make required payments pursuant to such Swap, the hedged liability would cease to be hedged for the remaining term of the Swap. In addition, we may be at risk for any collateral held by a hedging counterparty to a Swap, should such counterparty become insolvent or file for bankruptcy. Our hedging transactions, which are intended to limit losses, may actually adversely affect our earnings, which could reduce our cash available for distribution to our stockholders.

We may enter into hedging instruments that could expose us to contingent liabilities in the future, which could materially adversely affect our results of operations.

Subject to maintaining our qualification as a REIT, part of our financing strategy involves entering into hedging instruments that could require us to fund cash payments in certain circumstances (e.g., the early termination of a hedging instrument caused by an event of default or other voluntary or involuntary termination event or the decision by a hedging counterparty to request the posting of collateral that it is contractually owed under the terms of a hedging instrument). With respect to the termination of an existing Swap, the amount due would generally be equal to the unrealized loss of the open Swap position with the hedging counterparty and could also include other fees and charges. These economic losses will be reflected in our financial results of operations and our ability to fund these obligations will depend on the liquidity of our assets and access to capital at the time. Any losses we incur on our hedging instruments could materially adversely affect our earnings and thus our cash available for distribution to our stockholders.

The characteristics of hedging instruments present various concerns, including illiquidity, enforceability, and counterparty risks, which could adversely affect our business and results of operations.

As indicated above, from time to time we enter into Swaps. Entities entering into Swaps are exposed to credit losses in the event of non-performance by counterparties to these transactions. The CFTC, issued new rules that became effective in October 2012 regarding Swaps under the authority granted to it pursuant to the Dodd-Frank Act. Although the new rules do not directly affect the negotiations and terms of individual Swap transactions between counterparties, they do require that the clearing of all Swap transactions through registered derivatives clearing organizations, or swap execution facilities, through standardized documents under which each Swap counterparty transfers its position to another entity whereby the centralized clearinghouse effectively becomes the counterparty to each side of the Swap. It is the intent of the Dodd-Frank Act that the clearing of Swaps in this manner is designed to avoid concentration of swap risk in any single entity by spreading and centralizing the risk in the clearinghouse and its members. In addition to greater initial and periodic margin (collateral) requirements and additional transaction fees both by the swap execution facility and the clearinghouse, the Swap transactions are now subjected to greater regulation by both the CFTC and the SEC. These additional fees, costs, margin requirements, documentation, and regulation could adversely affect our business and results of operations. Additionally, for all Swaps we entered into prior to June 2013, we are not required to clear them through the central clearinghouse and these Swaps are still subject to the risks of non-performance by any of the individual counterparties with whom we entered into these transactions. If the Swap counterparty cannot perform under the terms of a Swap, we would not receive payments due under that agreement, we may lose any unrealized gain associated with the Swap, and the hedged liability would cease to be hedged by the Swap. We may also be at risk for any collateral we have pledged to secure our obligation under the Swap if the counterparty becomes insolvent or files for bankruptcy. Default by a party with whom we enter into a hedging transaction may result in a loss and force us to cover our commitments, if any, at the then-current market price. Although generally we will seek to reserve the right to terminate our hedging positions, it may not always be possible to dispose of or close out a hedging position without the consent of the hedging counterparty and we may not be able to enter into an offsetting contract in order to cover our risk. We cannot assure you that there will always be a liquid secondary market that will exist for hedging instruments purchased or sold and we may be required to maintain a position until exercise or expiration, which could result in losses.

Clearing facilities or exchanges upon which some of our hedging instruments are traded may increase margin requirements on our hedging instruments in the event of adverse economic developments.

In response to events having or expected to have adverse economic consequences or which create market uncertainty, clearing facilities or exchanges upon which some of our hedging instruments (i.e., interest rate swaps) are traded may require us to post additional collateral against our hedging instruments. For example, in response to the U.S. approaching its debt ceiling without resolution and the federal government shutdown, in October 2013, the Chicago Mercantile Exchange announced that it would increase margin requirements by 12% for all over-the-counter interest rate swap portfolios that its clearinghouse guaranteed. This increase was subsequently rolled back shortly thereafter upon the news that Congress passed legislation to temporarily suspend the national debt ceiling and reopen the federal government, and provide a time period for broader negotiations concerning federal budgetary issues. In the event that future adverse economic developments or market uncertainty (including those due to governmental, regulatory, or legislative action or inaction) result in increased margin requirements for our hedging instruments, it could materially adversely affect our liquidity position, business, financial condition and results of operations.

We may fail to qualify for hedge accounting treatment, which could materially adversely affect our results of operations.

We record derivative and hedge transactions in accordance with GAAP, specifically according to the Financial Accounting Standards Board (or FASB) Accounting Standards Codification Topic on Derivatives. Under these standards, we may fail to qualify for hedge accounting treatment for a number of reasons, including if we use instruments that do not meet the definition of a derivative, we fail to satisfy hedge documentation and hedge effectiveness assessment requirements or our instruments are not highly effective. If we fail to qualify for hedge accounting treatment, though the fundamental economic performance of our business would be unaffected, our operating results for financial reporting purposes may be materially adversely affected because losses on the derivatives we enter into would be recorded in net income, rather than AOCI, a component of stockholders' equity.

Table of Contents

Risks Related to Our Taxation as a REIT and the Taxation of Our Assets

If we fail to remain qualified as a REIT, we will be subject to tax as a regular corporation and could face a substantial tax liability, which would reduce the amount of cash available for distribution to our stockholders.

We have elected to qualify as a REIT and intend to comply with the provisions of the Internal Revenue Code of 1986, as amended (or the Code) related to REIT qualification. Accordingly, we will not be subject to U.S. federal income tax to the extent we distribute 100% of our REIT taxable income (which is generally our taxable income, computed without regard to the dividends paid deduction, any net income from prohibited transactions, and any net income from foreclosure property) to stockholders within the timeframe permitted under the Code and provided that we comply with certain income, asset ownership and other tests applicable to REITs. We believe that we currently meet all of the REIT requirements and intend to continue to qualify as a REIT under the provisions of the Code. Many of the REIT requirements however are highly technical and complex. The determination of whether we are a REIT requires an analysis of various factual matters and circumstances, some of which may not be totally within our control and some of which involve interpretation. For example, if we are to qualify as a REIT, annually at least 75% of our gross income must come from, among other sources, interest on obligations secured by mortgages on real property or interests in real property, gain from the disposition of real property, including mortgages or interests in real property (other than sales or dispositions of real property, including mortgages on real property, or securities that are treated as mortgages on real property, that we hold primarily for sale to customers in the ordinary course of a trade or business (i.e., prohibited transactions)), dividends, other distributions on and gains from the disposition of shares in other REITs, commitment fees received for agreements to make real estate loans and certain temporary investment income. In addition, the composition of our assets must meet qualified requirements at the close of each quarter. There can be no assurance that we will be able to satisfy these or other requirements or that the Internal Revenue Service (or IRS) or a court would agree with any conclusions or positions we have taken in interpreting the REIT requirements.

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

We may lose our REIT status if the IRS successfully challenges our characterization of our income from foreign TRSs.

We have elected to treat a Cayman Islands company as a TRS. We will likely be required to include in our income, even without the receipt of actual distributions, earnings from our investment in the foreign TRS. Income inclusions from equity investments in foreign corporations are technically neither actual dividends nor any of the other enumerated categories of qualifying income for the 95% gross income test. However, the IRS, based on discretionary authority granted to it under the Code, has issued private letter rulings to other REITs holding that income inclusions from equity investments in foreign corporations would be treated as qualifying income for purposes of the 95% gross income test. Private letter rulings may be relied upon only by the taxpayers to whom they are issued and the IRS may revoke a private letter ruling. Based on those private letter rulings and advice of counsel, we generally intend to treat such income inclusions as qualifying income for purposes of the 95% gross income test. Nevertheless, no assurance can be provided that the IRS would not successfully challenge our treatment of such income as qualifying income. In the event that such income was determined not to qualify for the 95% gross income test, we could be subject to a penalty tax with respect to such income to the extent it exceeds 5% of our gross income or we could fail to continue to qualify as a REIT.

Table of Contents

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

To maintain our qualification as a REIT, we must distribute at least 90% of our REIT taxable income (determined without regard to the dividends paid deduction and excluding any net capital gain) to our stockholders within the timeframe permitted under the Code. We generally must make these distributions in the taxable year to which they relate, or in the following taxable year if declared before we timely (including extensions) file our tax return for the year and if paid with or before the first regular dividend payment after such declaration. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our taxable income, we will be subject to U.S. federal income tax on our undistributed taxable income. In addition, if we should fail to distribute during each calendar year at least the sum of (a) 85% of our REIT ordinary income for such year, (b) 95% of our REIT capital gain net income for such year, and (c) any undistributed taxable income from prior periods, we would be subject to a non-deductible 4% excise tax on the excess of such required distribution over the sum of (x) the amounts actually distributed, plus (y) the amounts of income we retained and on which we have paid corporate income tax.

The dividend distribution requirement limits the amount of cash we have available for other business purposes, including amounts to fund our growth. Also, it is possible that because of differences in timing between the recognition of taxable income and the actual receipt of cash, we may have to borrow funds on unfavorable terms, sell investments at disadvantageous prices or distribute amounts that would otherwise be invested in future acquisitions to make distributions sufficient to maintain our qualification as a REIT or avoid corporate income tax and the 4% excise tax in a particular year. These alternatives could increase our costs or reduce our stockholders' equity. Thus, compliance with the REIT requirements may hinder our ability to grow, which could adversely affect the value of our common stock.

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

Even if we qualify as a REIT for U.S. federal income tax purposes, we may be required to pay certain federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, excise taxes, state or local income, property and transfer taxes, such as mortgage recording taxes, and other taxes. In addition, in order to meet the REIT qualification requirements, prevent the recognition of certain types of non-cash income, or to avert the imposition of a 100% tax that applies to certain gains derived by a REIT from dealer property or inventory, we may hold some of our assets through TRSs or other subsidiary corporations that will be subject to corporate level income tax at regular rates. In addition, if we lend money to a TRS, the TRS may be unable to deduct all or a portion of the interest paid to us, which could result in an even higher corporate level tax liability. Any of these taxes would reduce our operating cash flow and thus our cash available for distribution to our stockholders.

If our foreign TRSs are subject to U.S. federal income tax at the entity level, it would greatly reduce the amounts those entities would have available to distribute to us and that they would have available to pay their creditors.

There is a specific exemption from regular U.S. federal income tax for non-U.S. corporations that restrict their activities in the United States to trading stock and securities (or any activity closely related thereto) for their own account whether such trading (or such other activity) is conducted by the corporation or its employees through a resident broker, commission agent, custodian or other agent. We intend that our foreign TRS will rely on that exemption or otherwise operate in a manner so that it will not be subject to regular U.S. federal income tax on its net income at the entity level. If the IRS succeeded in challenging that tax treatment, it would greatly reduce the amount that the foreign TRS would have available to pay to their creditors and to distribute to us. In addition, even if our foreign TRS qualifies for that exemption, it may nevertheless be subject to U.S. federal withholding tax on certain types of income.

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

To remain qualified as a REIT for U.S. federal income tax purposes, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts that we distribute to our stockholders and the ownership of our stock. We may be required to make distributions to stockholders at disadvantageous times or when we do not have funds readily available for distribution, and may be unable to pursue investments that would be otherwise advantageous to us in order to satisfy the source-of-income or asset-diversification requirements for qualifying as a REIT. In addition, in certain cases, the modification of a debt instrument could result in the conversion of the instrument from a qualifying real estate asset to a wholly or partially non-qualifying asset that must be contributed to a TRS or disposed of in order for us to qualify or maintain our qualification as a REIT. Thus, compliance with the REIT requirements may hinder our ability to make and, in certain cases, to maintain ownership of, certain attractive investments.

Table of Contents

We may generate taxable income that differs from our GAAP income on our Non-Agency MBS and residential whole loan investments purchased at a discount to par value, which may result in significant timing variances in the recognition of income and losses.

We have acquired and intend to continue to acquire Non-Agency MBS and residential whole loans at prices that reflect significant market discounts on their unpaid principal balances. For financial statement reporting purposes, we generally establish a portion of the purchase discount on Non-Agency MBS as a Credit Reserve. This Credit Reserve is generally not accreted into income for financial statement reporting purposes. For tax purposes, however, we are not permitted to anticipate, or establish a reserve for, credit losses prior to their occurrence. As a result, discount on securities acquired in the primary or secondary market is included in the determination of taxable income and is not impacted by losses until such losses are incurred. Such differences in accounting for tax and GAAP can lead to significant timing variances in the recognition of income and losses. Taxable income on Non-Agency MBS purchased at a discount to their par value may be higher than GAAP earnings in early periods (before losses are actually incurred) and lower than GAAP earnings in periods during and subsequent to when realized credit losses are incurred. Dividends will be declared and paid at the discretion of our Board and will depend on REIT taxable earnings, our financial results and overall financial condition, maintenance of our REIT qualification and such other factors as our Board may deem relevant from time to time.

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

Securitizations by us or our subsidiaries could result in the creation of taxable mortgage pools for U.S. federal income tax purposes. The real estate mortgage investment conduit (or REMIC) provisions of the Code generally provide that REMICs are the only form of pass-through entity permitted to issue debt obligations with two or more maturities if the payments on those obligations bear a relationship to the mortgage obligations held by such entity. If we engage in a non-REMIC securitization transaction, directly or indirectly through a qualified REIT subsidiary (or QRS), in which the assets held by the securitization vehicle consist largely of mortgage loans or MBS, in which the securitization vehicle issues to investors two or more classes of debt instruments that have different maturities, and in which the timing and amount of payments on the debt instruments is determined in large part by the amounts received on the mortgage loans or MBS held by the securitization vehicle, the securitization vehicle will be a taxable mortgage pool. As long as we or another REIT hold a 100% interest in the equity interests in a taxable mortgage pool, either directly, or through a QRS, it will not be subject to tax. A portion of the income that we realize with respect to the equity interest we hold in a taxable mortgage pool will, however, be considered to be excess inclusion income and, as a result, a portion of the dividends that we pay to our stockholders will be considered to consist of excess inclusion income. Such excess inclusion income is treated as unrelated business taxable income (or UBTI) for tax-exempt stockholders, is subject to withholding for foreign stockholders (without the benefit of any treaty reduction), and is not subject to reduction by net operating loss carryovers. In addition to the extent that our stock is owned by tax-exempt "disqualified organizations," such as certain government-related entities and charitable remainder trusts that are not subject to tax on unrelated business income, we may incur a corporate level tax on a portion of our income from the taxable mortgage pool. In that case, we may reduce the amount of our distributions to any disqualified organization whose stock ownership gave rise to the tax. Historically, we have not generated excess inclusion income; however, despite our efforts, we may not be able to avoid creating or distributing excess inclusion income to our stockholders in the future. In addition, we could face limitations in selling equity interests to outside investors in securitization transactions that are taxable mortgage pools or selling any debt securities issued in connection with these securitizations that might be considered to be equity interests for tax purposes. These limitations may prevent us from using certain techniques to maximize our returns from securitization transactions.

We have not established a minimum dividend payment level, and there is no guarantee that we will maintain current dividend payment levels or pay dividends in the future.

In order to maintain our qualification as a REIT, we must comply with a number of requirements under U.S. federal tax law, including that we distribute at least 90% of our REIT taxable income within the timeframe permitted under the Code, which is calculated generally before the dividends paid deduction and excluding net capital gain. Dividends will be declared and paid at the discretion of our Board and will depend on our REIT taxable earnings, our financial results and overall condition, maintenance of our REIT qualification and such other factors as our Board may deem relevant from time to time. We have not established a minimum dividend payment level for our common stock and our ability to pay dividends may be negatively impacted by adverse changes in our operating results. Therefore, our dividend payment level may fluctuate significantly, and, under some circumstances, we may not pay dividends at all.

Our reported GAAP net income may differ from the amount of REIT taxable income and dividend distribution requirements and, therefore, our GAAP results may not be an accurate indicator of future taxable income and dividend distributions.

Generally, the cumulative net income we report over the life of an asset will be the same for GAAP and tax purposes, although the timing of this income recognition over the life of the asset could be materially different. Differences exist in the accounting for GAAP net income and REIT taxable income which can lead to significant variances in the amount and timing of when income and losses are recognized under these two measures. Due to these differences, our reported GAAP financial results could materially differ from our determination of REIT taxable income, and our dividend distribution requirements, and, therefore, our GAAP results may not be an accurate indicator of future taxable income and dividend distributions.

Over time, accounting principles, conventions, rules, and interpretations may change, which could affect our reported GAAP and taxable earnings, and stockholders' equity.

Accounting rules for the various aspects of our business change from time to time. Changes in GAAP, or the accepted interpretation of these accounting principles, can affect our reported income, earnings, and stockholders' equity. In addition, changes in tax accounting rules or the interpretations thereof could affect our REIT taxable income and our dividend distribution requirements. These changes may materially adversely affect our results of operations.

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

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

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

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

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

We may acquire debt instruments in the secondary market for less than their face amount. The discount at which such debt instruments are acquired may reflect doubts about their ultimate collectibility rather than current market interest rates. The amount of such discount will nevertheless generally be treated as “market discount” for U.S. federal income tax purposes. Accrued market discount is reported as income when, and to the extent that, any payment of principal of the debt instrument is made. If we collect less on the debt instrument than our purchase price plus the market discount we had previously reported as income, we may not be able to benefit from any offsetting loss deductions.

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

In addition, we may acquire debt instruments that are subsequently modified by agreement with the borrower. If the amendments to the outstanding instrument are “significant modifications” under the applicable Treasury regulations, the modified instrument will be considered to have been reissued to us in a debt-for-debt exchange with the borrower. In that event, we may be required to recognize taxable gain to the extent the principal amount of the modified instrument exceeds our adjusted tax basis in the unmodified instrument, even if the value of the instrument or the payment expectations have not changed. Following such a taxable modification, we would hold the modified loan with a cost basis equal to its principal amount for federal tax purposes.

Finally, in the event that any debt instruments acquired by us are delinquent as to mandatory principal and interest payments, or in the event payments with respect to a particular instrument are not made when due, we may nonetheless be required to continue to recognize the unpaid interest as taxable income as it accrues, despite doubt as to its ultimate collectibility. Similarly, we may be required to accrue interest income with respect to debt instruments at its stated rate regardless of whether corresponding cash payments are received or are ultimately collectible. In each case, while we would in general ultimately have an offsetting loss deduction available to us when such interest was determined to be uncollectible, the utility of that deduction could depend on our having taxable income in that later year or thereafter.

For these and other reasons, we may have difficulty making distributions sufficient to maintain our qualification as a REIT or avoid corporate income tax and the 4% excise tax in a particular year.

Dividends paid by REITs do not qualify for the reduced tax rates

The maximum regular U.S. federal income tax rate for dividends paid to domestic stockholders that are individuals, trusts and estates is currently 20%. Dividends paid by REITs, however, are generally not eligible for the reduced rates. Although this legislation does not adversely affect the taxation of REITs or dividends paid by REITs, the more favorable rates applicable to regular corporate dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in stock of non-REIT corporations that pay dividends, which could adversely affect the value of the stock of REITs, including our common stock.

We may enter into resecuritization transactions, the tax treatment of which could have a material adverse effect on our results of operations.

We have engaged in and may in the future, engage in resecuritization transactions in which we transfer Non-Agency MBS to a special purpose entity that has formed or will form a securitization vehicle that will issue multiple classes of securities secured by and payable from cash flows on the underlying Non-Agency MBS. To date, we have structured two such transactions as a REMIC securitizations, which, to the extent we have transferred securities in a resecuritization, is viewed as the sale of securities for tax purposes. Although such transactions are treated as sales for tax purposes, they have historically not given rise to any taxable gain so that the prohibited transactions tax rules have not been implicated (i.e., the tax only applies to net taxable gain from sales that are prohibited transactions); however, no assurance can be offered that the IRS will agree with such treatment. In addition, to these REMIC securitization transactions, we have also engaged in two resecuritization transactions that we believe should be treated as financing transactions for tax purposes. If a securitization transaction were to be considered to be a sale of property to customers in the ordinary course of a trade or business, and we recognized a gain on such transaction for tax purposes, then we could risk exposure to the 100% tax on net taxable income from prohibited transactions. Moreover, even if we retained MBS resulting from a resecuritization transaction and then subsequently sold such securities at a tax gain, the gain could, absent an available safe-harbor provision, be characterized as net income from a prohibited transaction. Under these circumstances, our results of operations could be materially adversely affected.

New legislation or administrative or judicial action, in each instance potentially with retroactive effect, could make it more difficult or impossible for us to remain qualified as a REIT.

The present U.S. federal income tax treatment of REITs may be modified, possibly with retroactive effect, by legislative, judicial or administrative action at any time, which could affect the U.S. federal income tax treatment of an investment in us. Revisions in U.S. federal tax laws and interpretations thereof could affect or cause us to change our investments and commitments and affect the tax considerations of an investment in us.

Risks Related to Our Corporate Structure

Our ownership limitations may restrict business combination opportunities.

To qualify as a REIT under the Code, no more than 50% of the value of our outstanding shares of capital stock may be owned, directly or under applicable attribution rules, by five or fewer individuals (as defined by the Code to include certain entities) during the last half of each taxable year. To preserve our REIT qualification, among other things, our charter generally prohibits direct or indirect ownership by any person of more than 9.8% of the number or value of the outstanding shares of our capital stock.

Table of Contents

Generally, shares owned by affiliated owners will be aggregated for purposes of the ownership limit. Any transfer of shares of our capital stock or other event that, if effective, would violate the ownership limit will be void as to that number of shares of capital stock in excess of the ownership limit and the intended transferee will acquire no rights in such shares. Shares issued or transferred that would cause any stockholder to own more than the ownership limit or cause us to become "closely held" under Section 856(h) of the Code will automatically be converted into an equal number of shares of excess stock. All excess stock will be automatically transferred, without action by the prohibited owner, to a trust for the exclusive benefit of one or more charitable beneficiaries that we select, and the prohibited owner will not acquire any rights in the shares of excess stock. The restrictions on ownership and transfer contained in our charter could have the effect of delaying, deferring or preventing a change in control or other transaction in which holders of shares of common stock might receive a premium for their shares of common stock over the then current market price or that such holders might believe to be otherwise in their best interests. The ownership limit provisions also may make our shares of common stock an unsuitable investment vehicle for any person seeking to obtain, either alone or with others as a group, ownership of more than 9.8% of the number or value of our outstanding shares of capital stock.

Provisions of Maryland law and other provisions of our organizational documents may limit the ability of a third party to acquire control of the Company.

Certain provisions of the Maryland General Corporation Law (or MGCL) may have the effect of delaying, deferring or preventing a transaction or a change in control of our company that might involve a premium price for holders of our common stock or otherwise be in their best interests, including:

- "business combination" provisions that, subject to limitations, prohibit certain business combinations between us and an "interested stockholder" (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding voting stock or an affiliate or associate of ours who, at any time within the two-year period immediately prior to the date in question, was the beneficial owner of 10% or more of the voting power of our then outstanding stock) or an affiliate of an interested stockholder for five years after the most recent date on which the stockholder becomes an interested stockholder, and thereafter impose two supermajority stockholder voting requirements to approve these combinations (unless our common stockholders receive a minimum price, as defined under Maryland law, for their shares in the form of cash or other consideration in the same form as previously paid by the interested stockholder for its shares); and

- "control share" provisions that provide that holders of "control shares" of our company (defined as voting shares of stock which, when aggregated with all other shares controlled by the acquiring stockholder, entitle the stockholder to exercise one of three increasing ranges of voting power in electing directors) acquired in a "control share acquisition" (defined as the direct or indirect acquisition of ownership or control of "control shares") have no voting rights except to the extent approved by our stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares.

Our bylaws provide that we are not subject to the "control share" provisions of the MGCL. However, our Board may elect to make the "control share" statute applicable to us at any time, and may do so without stockholder approval.

Title 3, Subtitle 8 of the MGCL permits our Board, without stockholder approval and regardless of what is currently provided in our charter or bylaws, to elect on behalf of our company to be subject to statutory provisions that may have the effect of delaying, deferring or preventing a transaction or a change in control of our company that might involve a premium price for holders of our common stock or otherwise be in their best interest. Our Board may elect to opt in to any or all of the provisions of Title 3, Subtitle 8 of the MGCL without stockholder approval at any time. In addition, without our having elected to be subject to Subtitle 8, our charter and bylaws already (1) provide for a classified board, (2) require the affirmative vote of the holders of at least 80% of the votes entitled to be cast in the election of directors for the removal of any director from our Board, which removal will be allowed only for cause, (3) vest in our Board the exclusive power to fix the number of directorships and (4) require, unless called by our Chairman of the Board, Chief Executive Officer or President or our Board, the written request of stockholders entitled to cast not less than a majority of all votes entitled to be cast at such a meeting to call a special meeting. These provisions may delay or prevent a change of control of our company.

Future offerings of debt securities, which would rank senior to our common stock upon liquidation, and future offerings of equity securities, which would dilute our existing stockholders and may be senior to our common stock for the purposes of dividend and liquidating distributions, may adversely affect the market price of our common stock.

In the future, we may attempt to increase our capital resources by making offerings of debt or additional offerings of equity securities, including commercial paper, senior or subordinated notes and series or classes of preferred stock or common stock. Upon liquidation, holders of our debt securities and shares of preferred stock, if any, and lenders with respect to other borrowings

Table of Contents

will receive a distribution of our available assets prior to the holders of our common stock. Additional equity offerings may dilute the holdings of our existing stockholders or reduce the market price of our common stock, or both. Preferred stock could have a preference on liquidating distributions or a preference on dividend payments or both that could limit our ability to make a dividend distribution to the holders of our common stock. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, holders of our common stock bear the risk of our future offerings reducing the market price of our common stock and diluting their stock holdings in us.

Our Board may approve the issuance of capital stock with terms that may discourage a third party from acquiring the Company.

Our charter permits our Board to issue shares of preferred stock, issuable in one or more classes or series. We may issue a class of preferred stock to individual investors in order to comply with the various REIT requirements or to finance our operations. Our charter further permits our Board to classify or reclassify any unissued shares of preferred or common stock and establish the preferences and rights (including, among others, voting, dividend and conversion rights) of any such shares of stock, which rights may be superior to those of shares of our common stock. Thus, our Board could authorize the issuance of shares of preferred or common stock with terms and conditions that could have the effect of discouraging a takeover or other transaction in which holders of the outstanding shares of our common stock might receive a premium for their shares over the then current market price of our common stock.

Future issuances or sales of shares could cause our share price to decline.

Sales of substantial numbers of shares of our common stock in the public market, or the perception that such sales might occur, could adversely affect the market price of our common stock. In addition, the sale of these shares could impair our ability to raise capital through a sale of additional equity securities. Other issuances of our common stock could have an adverse effect on the market price of our common stock. In addition, future issuances of our common stock may be dilutive to existing stockholders.

Other Business Risks

We are dependent on our executive officers and other key personnel for our success, the loss of any of whom may materially adversely affect our business.

Our success is dependent upon the efforts, experience, diligence, skill and network of business contacts of our executive officers and key personnel. The departure of any of our executive officers and/or key personnel could have a material adverse effect on our operations and performance.

We are dependent on information systems and their failure could significantly disrupt our business.

Our business is highly dependent on our information and communications systems. Any failure or interruption of our systems or cyber-attacks or security breaches of our networks or systems could cause delays or other problems in our securities trading activities, which could have a material adverse effect on operating results, the market price of our common stock and other securities and our ability to pay dividends to our stockholders. In addition, we also face the risk of operational failure, termination or capacity constraints of any of the third parties with which we do business or that facilitate our business activities, including clearing agents or other financial intermediaries we use to facilitate our securities transactions.

Computer malware, viruses, and computer hacking and phishing and cyber attacks have become more prevalent in our industry and may occur on our systems in the future. We rely heavily on financial, accounting and other data processing systems. It is difficult to determine what, if any, negative impact may directly result from any specific interruption or cyber-attacks or security breaches of our networks or systems (or networks or systems of, among other third parties, our lenders) or any failure to maintain performance, reliability and security of our technical infrastructure. As a result, any such computer malware, viruses, and computer hacking and phishing attacks may negatively affect our operations.

Table of Contents

We operate in a highly competitive market for investment opportunities and competition may limit our ability to acquire desirable investments, which could materially adversely affect our results of operations.

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

Table of Contents

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

Office Leases

We pay monthly rent pursuant to two operating leases. Our lease for our corporate headquarters in New York, New York extends through May 31, 2020. The lease provides for aggregate cash payments ranging over time of approximately $2.5 million per year, paid on a monthly basis, exclusive of escalation charges. In addition, as part of this lease agreement, we have provided the landlord a $785,000 irrevocable standby letter of credit fully collateralized by cash. The letter of credit may be drawn upon by the landlord in the event that we default under certain terms of the lease. In addition, we have a lease through December 31, 2016, for our off-site back-up facility located in Rockville Centre, New York, which provides for, among other things, lease payments totaling $30,000, annually.

Item 3. Legal Proceedings.

There are no material legal proceedings to which we are a party or to which any of our assets are subject.

To date, we have not been required to make any payments to the IRS as a penalty for failing to make disclosures required with respect to certain transactions that have been identified by the IRS as abusive or that have a significant tax avoidance purpose.

Item 4. Mine Safety Disclosures.

Not applicable.

Table of Contents

PART II

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

Market Information

Our common stock is listed on the New York Stock Exchange, under the symbol "MFA." On February 12, 2016, the last sales price for our common stock on the New York Stock Exchange was $6.39 per share. The following table sets forth the high and low sales prices per share of our common stock during each calendar quarter for the years ended December 31, 2015 and 2014:

	2015		2014	
Quarter Ended	High	Low	High	Low
March 31	$8.22	$7.68	$7.96	$7.03
June 30	8.04	7.39	8.50	7.65
September 30	7.80	5.78	8.47	7.77
December 31	7.17	6.17	8.45	7.78

Holders

As of February 12, 2016, we had 611 registered holders of our common stock. Such information was obtained through our registrar and transfer agent, based on the results of a broker search.

Dividends

No dividends may be paid on our common stock unless full cumulative dividends have been paid on our preferred stock. We have paid full cumulative dividends on our preferred stock on a quarterly basis through December 31, 2015. We have historically declared cash dividends on our common stock on a quarterly basis. During 2015 and 2014, we declared total cash dividends to holders of our common stock of $296.4 million ($0.80 per share) and $294.8 million ($0.80 per share), respectively. In general, our common stock dividends have been characterized as ordinary income to our stockholders for income tax purposes. However, a portion of our common stock dividends may, from time to time, be characterized as capital gains or return of capital. For the year ended December 31, 2015, a portion of our dividends were deemed to be capital gains. For the year ended December 31, 2014, our common stock dividends were characterized as ordinary income to stockholders. (For additional dividend information, see Notes 13(a) and 13(b) to the consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K.)

We elected to be taxed as a REIT for U.S. federal income tax purposes commencing with our taxable year ended December 31, 1998 and, as such, anticipate distributing at least 90% of our REIT taxable income within the timeframe permitted by the Code. Although we may borrow funds to make distributions, cash for such distributions has generally been, and is expected to continue to be, largely generated from our results of our operations.

Table of Contents

We declared and paid the following dividends on our common stock during the years 2015 and 2014:

Year	Declaration Date	Record Date	Payment Date	Dividend per Share	
2015	December 9, 2015	December 28, 2015	January 29, 2016	$0.20	(1)
	September 17, 2015	September 29, 2015	October 30, 2015	0.20	
	June 15, 2015	June 29, 2015	July 31, 2015	0.20	
	March 13, 2015	March 27, 2015	April 30, 2015	0.20	
2014	December 9, 2014	December 26, 2014	January 30, 2015	$0.20	
	September 17, 2014	September 29, 2014	October 31, 2014	0.20	
	June 13, 2014	June 27, 2014	July 31, 2014	0.20	
	March 10, 2014	March 28, 2014	April 30, 2014	0.20	

(1) At December 31, 2015, the Company had accrued dividends and dividend equivalents payable of $74.6 million related to the common stock dividend declared on December 9, 2015.

Dividends are declared and paid at the discretion of our Board and depend on our cash available for distribution, financial condition, ability to maintain our qualification as a REIT, and such other factors that our Board may deem relevant. We have not established a minimum payout level for our common stock. (See Part I, Item 1A., "Risk Factors", and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations", of this Annual Report on Form 10-K, for information regarding the sources of funds used for dividends and for a discussion of factors, if any, which may adversely affect our ability to pay dividends.)

Purchases of Equity Securities

As previously disclosed, in August 2005, our Board authorized a stock repurchase program (or Repurchase Program), to repurchase up to 4.0 million shares of our outstanding common stock under the Repurchase Program. The Board reaffirmed such authorization in May 2010. In December 2013, our Board increased the number of shares authorized for repurchase to an aggregate of 10.0 million shares (under which approximately 6.6 million shares remain available for repurchase). Such authorization does not have an expiration date and, at present, there is no intention to modify or otherwise rescind such authorization. Subject to applicable securities laws, repurchases of common stock under the Repurchase Program are made at times and in amounts as we deem appropriate (including, in our discretion, through the use of one or more plans adopted under Rule 10b5-1 promulgated under the Securities Exchange Act of 1934, as amended (or 1934 Act)), using available cash resources. Shares of common stock repurchased by us under the Repurchase Program are cancelled and, until reissued by us, are deemed to be authorized but unissued shares of our common stock. The Repurchase Program may be suspended or discontinued by us at any time and without prior notice.

We did not repurchase any shares of our common stock under the Repurchase Program during the years ended December 31, 2015 and 2014.

Table of Contents

We engaged in no share repurchase activity during the fourth quarter of 2015 pursuant to the Repurchase program. We did, however, withhold restricted shares (under the terms of grants under our Equity Compensation Plan (or Equity Plan)) to offset tax withholding obligations that occur upon the vesting and release of restricted stock awards and/or RSUs. The following table presents information with respect to (i) such withheld restricted shares, and (ii) eligible shares remaining for repurchase under the Repurchase Program:

Month	Total Number of Shares Purchased	Weighted Average Price Paid Per Share (1)	Total Number of Shares Repurchased as Part of Publicly Announced Repurchase Program or Employee Plan	Maximum Number of Shares that May Yet be Purchased Under the Repurchase Program or Employee Plan
October 1-31, 2015:				
Repurchase Program (2)	—	$—	—	6,616,355
Employee Transactions (3)	—	—	N/A	N/A
November 1-30, 2015:				
Repurchase Program (2)	—	—	—	6,616,355
Employee Transactions (3)	—	—	N/A	N/A
December 1-31, 2015:				
Repurchase Program (2)	—	—	—	6,616,355
Employee Transactions (3)	266,849	6.77	N/A	N/A
Total Repurchase Program (2)	—	$—	—	6,616,355
Total Employee Transactions (3)	266,849	$6.77	N/A	N/A

(1) Includes brokerage commissions.
(2) As of December 31, 2015, we had repurchased an aggregate of 3,383,645 shares under the Repurchase Program.
(3) Our Equity Plan provides that the value of the shares delivered or withheld be based on the price of our common stock on the date the relevant transaction occurs.

Discount Waiver, Direct Stock Purchase and Dividend Reinvestment Plan

In September 2003, we initiated a Discount Waiver, Direct Stock Purchase and Dividend Reinvestment Plan (or the DRSPP) to provide existing stockholders and new investors with a convenient and economical way to purchase shares of our common stock. Under the DRSPP, existing stockholders may elect to automatically reinvest all or a portion of their cash dividends in additional shares of our common stock and existing stockholders and new investors may make optional cash purchases of shares of our common stock in amounts ranging from $50 (or $1,000 for new investors) to $10,000 on a monthly basis and, with our prior approval, in excess of $10,000. At our discretion, we may issue shares of our common stock under the DRSPP at discounts of up to 5% from the prevailing market price at the time of purchase. Computershare Shareowner Services LLC is the administrator of the DRSPP (or the Plan Agent). Stockholders who own common stock that is registered in their own name and who want to participate in the DRSPP must deliver a completed enrollment form to the Plan Agent. Stockholders who own common stock that is registered in a name other than their own (e.g., broker, bank or other nominee) and who want to participate in the DRSPP must either request such nominee holder to participate on their behalf or request that such nominee holder re-register our common stock in the stockholder's name and deliver a completed enrollment form to the Plan Agent. During the years ended 2015 and 2014, we issued 162,373 and 4,526,855 shares of common stock through the DRSPP generating net proceeds of approximately $1.2 million and $35.6 million, respectively.

Table of Contents

Securities Authorized For Issuance Under Equity Compensation Plans

During 2015, we adopted the Equity Plan, as approved by our stockholders. The Equity Plan amended and restated our 2010 Equity Compensation Plan. (For a description of the Equity Plan, see Note 15(a) to the consolidated financial statements included under Item 8 of this Annual Report on Form 10-K.)

The following table presents certain information with respect to our equity compensation plans as of December 31, 2015:

Award (1)	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights		Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column of this table)	
Restricted Stock Units (or RSUs)	1,875,730				
Total	1,875,730		(2)	9,366,840	(3)

(1) All equity based compensation is granted pursuant to plans that have been approved by our stockholders.
(2) A weighted average exercise price is not applicable for our RSUs, as such equity awards result in the issuance of shares of our common stock provided that such awards vest and, as such, do not have an exercise price. At December 31, 2015, 729,523 RSUs were vested, 584,907 RSUs were subject to time based vesting and 561,300 RSUs will vest subject to achieving a market condition.
(3) Number of securities remaining available for future issuance under equity compensation plans excludes RSUs presented in the table and 110,920 shares of restricted stock, which were issued and outstanding at December 31, 2015.

Table of Contents

Item 6. Selected Financial Data.

Our selected financial data set forth below is derived from our audited financial statements and should be read in conjunction with our consolidated financial statements and the accompanying notes, included under Item 8 of this Annual Report on Form 10-K.

	At or/For the Year Ended December 31,				
(Dollars in Thousands, Except per Share Amounts)	2015	2014	2013	2012	2011
Operating Data:					
Interest Income	$492,143	$463,817	$482,940	$499,157	$496,747
Interest expense	(176,948)	(159,808)	(164,013)	(171,670)	(149,411
Net impairment losses recognized in earnings (1)	(705)	—	—	(1,200)	(10,570
Gain on sales of MBS and U.S. Treasury securities, net (2)	34,900	37,497	25,825	9,001	6,730
Unrealized net gains and net interest income from Linked Transactions	—	17,092	3,225	12,610	3,015
Net gain on residential whole loans held at fair value	17,722	116	—	—	—
Other (loss)/income, net	(1,457)	80	(7,298)	10	1,082
Operating and other expense	(52,429)	(45,290)	(37,970)	(41,069)	(31,179
Net income	$313,226	$313,504	$302,709	$306,839	$316,414
Preferred stock dividends	15,000	15,000	13,750	8,160	8,160
Issuance costs of redeemed preferred stock (3)	—	—	3,947	—	—
Net income available to common stock and participating securities	$298,226	$298,504	$285,012	$298,679	$308,254
Earnings per share — basic and diluted	$0.80	$0.81	$0.78	$0.83	$0.90
Dividends declared per share of common stock (4)	$0.800	$0.800	$1.640	$0.880	$1.005
Dividends declared per share of preferred stock (5)	$1.875	$1.875	$2.136	$2.125	$2.125
Balance Sheet Data:					
MBS and CRT securities	$11,356,643	$10,762,622	$11,371,358	$12,607,625	$10,912,9
Residential whole loans, at carrying value	271,845	207,923	—	—	—
Residential whole loans, at fair value	623,276	143,472	—	—	—
Cash and cash equivalents	165,007	182,437	565,370	401,293	394,022
Linked Transactions	—	398,336	28,181	12,704	55,801
Total assets	13,167,323	12,354,744	12,471,908	13,517,550	11,750,63
Repurchase agreements and other advances	9,388,902	8,267,388	8,339,297	8,752,472	7,813,159
Securitized debt	22,057	110,574	366,205	646,816	875,520
Swaps (in a liability position)	70,526	62,198	28,217	63,034	114,220
Total liabilities	10,200,062	9,151,472	9,329,657	10,206,544	9,252,874
Preferred stock, liquidation preference	200,000	200,000	200,000	96,000	96,000
Total stockholders' equity	2,967,261	3,203,272	3,142,251	3,311,006	2,497,760
Other Data:					
Average total assets	$13,672,737	$12,547,418	$13,192,285	$12,942,171	$11,185,2
Average total stockholders' equity	$3,129,461	$3,230,932	$3,262,458	$2,945,687	$2,701,20
Return on average total assets (6)	2.18%	2.38%	2.16%	2.31%	2.76
Return on average total stockholders' equity (7)	10.01%	9.70%	9.28%	10.42%	11.71
	22.89%	25.75%	24.73%	22.76%	24.18

Total average stockholders’ equity to total average assets (8)					
Dividend payout ratio (9)	1.00	0.99	1.10	1.06	1.09
Book value per share of common stock (10)	$7.47	$8.12	$8.06	$8.99	$6.74

32

Table of Contents

(1) Reflects OTTI recognized through earnings related to Non-Agency MBS.

(2) 2015: We sold Non-Agency MBS for $70.7 million, realizing gross gains of $34.9 million. 2014: We sold Non-Agency MBS for $123.9 million, realizing gross gains of $37.5 million. 2013: We sold Non-Agency MBS for $152.6 million, realizing gross gains of $25.8 million and sold U.S. Treasury securities for $422.2 million, realizing net losses of approximately $24,000. 2012: We sold Agency MBS for $168.9 million, realizing gross gains of $9.0 million. 2011: We sold Agency MBS for $150.6 million, realizing gross gains of $6.7 million.

(3) Issuance costs of redeemed preferred stock represent the original offering costs related to the 8.50% Series A Cumulative Redeemable Preferred Stock ("Series A Preferred Stock"), which was redeemed on May 16, 2013.

(4) 2013: Includes special cash dividends paid totaling $0.78 per share. 2011: Includes a special cash dividend of $0.02 per share.

(5) 2013: Reflects dividends declared per share on Series A Preferred Stock and 7.50% Series B Cumulative Redeemable Preferred Stock ("Series B Preferred Stock") of $0.80 and $1.33, respectively.

(6) Reflects net income available to common stock and participating securities divided by average total assets.

(7) Reflects net income divided by average total stockholders' equity.

(8) Reflects total average stockholders' equity divided by total average assets.

(9) Reflects dividends declared per share of common stock (excluding special dividends) divided by earnings per share.

(10) Reflects total stockholders' equity less the preferred stock liquidation preference divided by total shares of common stock outstanding.

Table of Contents

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

The following discussion should be read in conjunction with our financial statements and accompanying notes included in Item 8 of this Annual Report on Form 10-K.

GENERAL

We are a REIT primarily engaged in the business of investing, on a leveraged basis, in residential mortgage assets, including Agency MBS, Non-Agency MBS, residential whole loans and CRT securities. Our principal business objective is to deliver shareholder value through the generation of distributable income and through asset performance linked to residential mortgage credit fundamentals. We selectively invest in residential mortgage assets with a focus on credit analysis, projected prepayment rates, interest rate sensitivity and expected return.

At December 31, 2015, we had total assets of approximately $13.167 billion, of which $11.173 billion, or 84.9%, represented our MBS portfolio. At such date, our MBS portfolio was comprised of $4.752 billion of Agency MBS and $6.421 billion of Non-Agency MBS which includes $3.795 billion of Legacy Non-Agency MBS and $2.626 billion of RPL/NPL MBS. In addition, at December 31, 2015, we had approximately $895.1 million in residential whole loans acquired through our consolidated trusts, which represented approximately 6.8% of our total assets. Our remaining investment-related assets were primarily comprised of collateral obtained in connection with reverse repurchase agreements, cash and cash equivalents (including restricted cash), CRT securities, MBS-related receivables, derivative instruments, and REO.

The results of our business operations are affected by a number of factors, many of which are beyond our control, and primarily depend on, among other things, the level of our net interest income, the market value of our assets, which is driven by numerous factors, including the supply and demand for residential mortgage assets in the marketplace, the terms and availability of adequate financing, general economic and real estate conditions (both on a national and local level), the impact of government actions in the real estate and mortgage sector, and the credit performance of our credit sensitive residential mortgage assets. Our net interest income varies primarily as a result of changes in interest rates, the slope of the yield curve (i.e., the differential between long-term and short-term interest rates), borrowing costs (i.e., our interest expense) and prepayment speeds on our MBS, the behavior of which involves various risks and uncertainties. Interest rates and conditional prepayment rates (or CPRs) (which measure the amount of unscheduled principal prepayment on a bond as a percentage of the bond balance), vary according to the type of investment, conditions in the financial markets, competition and other factors, none of which can be predicted with any certainty.

With respect to our business operations, increases in interest rates, in general, may over time cause: (i) the interest expense associated with our borrowings to increase; (ii) the value of our MBS portfolio and, correspondingly, our stockholders' equity to decline; (iii) coupons on our ARM-MBS to reset, on a delayed basis, to higher interest rates; (iv) prepayments on our MBS to decline, thereby slowing the amortization of our MBS purchase premiums and the accretion of our purchase discounts; and (v) the value of our derivative hedging instruments and, correspondingly, our stockholders' equity to increase. Conversely, decreases in interest rates, in general, may over time cause: (i) the interest expense associated with our borrowings to decrease; (ii) the value of our MBS portfolio and, correspondingly, our stockholders' equity to increase; (iii) coupons on our ARM-MBS to reset, on a delayed basis, to lower interest rates; (iv) prepayments on our MBS to increase, thereby accelerating the amortization of our MBS purchase premiums and the accretion of our purchase discounts; and (v) the value of our derivative hedging instruments and, correspondingly, our stockholders' equity to decrease. In addition, our borrowing costs and credit lines are further affected by the type of collateral we pledge and general conditions in the credit market.

We are exposed to credit risk in our Non-Agency MBS and residential whole loans, generally meaning that we are subject to credit losses in these portfolios that correspond to the risk of delinquency, default and foreclosure on the underlying real estate collateral. (See Part I, Item 1A., “Risk Factors - Credit Risks”, of this Annual Report on Form 10-K), We believe the discounted purchase prices paid on certain of these investments mitigates our risk of loss in the event that, as we expect on most such investments, we receive less than 100% of the par value of these securities or loans. Our investment process for credit sensitive assets involves analysis focused primarily on quantifying and pricing credit risk.

Table of Contents

The table below presents the composition of our MBS portfolios with respect to repricing characteristics as of December 31, 2015:

Underlying Mortgages	December 31, 2015 Agency MBS Fair Value (1)	Non-Agency MBS Fair Value (2)	Total MBS (1)(2)	Percent of Total	
(In Thousands)					
Hybrids in contractual fixed-rate period	$1,411,282	$ 416,390	$1,827,672	21.4	%
Hybrids in adjustable period	1,489,452	2,104,432	3,593,884	42.1	
15-year fixed rate	1,780,746	7,728	1,788,474	20.9	
Greater than 15-year fixed rate	—	1,206,565	1,206,565	14.1	
Floaters	69,733	59,836	129,569	1.5	
Total	$4,751,213	$ 3,794,951	$8,546,164	100.0	%

(1) Does not include principal payments receivable in the amount of $1.0 million.
(2) Does not reflect $2.626 billion of RPL/NPL MBS, which are re-performing deals with both fixed rate and hybrid re-performing loans. These deal structures contain a coupon step-up of 300 basis points at 36 months or sooner from issuance.

As of December 31, 2015, approximately $7.449 billion, or 66.7%, of our MBS portfolio was in its contractual fixed-rate period or were fixed-rate MBS and approximately $3.723 billion, or 33.3%, was in its contractual adjustable-rate period, or were floating rate MBS with interest rates that reset monthly. Our ARM-MBS in their contractual adjustable-rate period primarily include MBS collateralized by Hybrids for which the initial fixed-rate period has elapsed, such that the interest rate will typically adjust on an annual or semiannual basis.

Premiums arise when we acquire MBS at a price in excess of the principal balance of the mortgages securing such MBS (i.e., par value). Conversely, discounts arise when we acquire MBS at a price below the principal balance of the mortgages securing such MBS or acquire residential whole loans at a price below the principal balance of the mortgage. Premiums paid on our MBS are amortized against interest income and accretable purchase discounts on these investments are accreted to interest income. Purchase premiums on our MBS, which are primarily carried on our Agency MBS, are amortized against interest income over the life of each security using the effective yield method, adjusted for actual prepayment activity. An increase in the prepayment rate, as measured by the CPR, will typically accelerate the amortization of purchase premiums, thereby reducing the internal rate of return (or IRR)/interest income earned on such assets.

CPR levels are impacted by, among other things, conditions in the housing market, new regulations, government and private sector initiatives, interest rates, availability of credit to home borrowers, underwriting standards and the economy in general. In particular, CPR reflects the conditional repayment rate (or CRR), which measures voluntary prepayments of mortgages collateralizing a particular MBS, and the conditional default rate (or CDR), which measures involuntary prepayments resulting from defaults. CPRs on Agency MBS and Legacy Non-Agency MBS may differ significantly. For the year ended December 31, 2015, our Agency MBS portfolio experienced a weighted average CPR of 13.2%, and our Legacy Non-Agency MBS portfolio experienced a CPR of 14.1%. For the year ended December 31, 2014, our Agency MBS portfolio experienced a weighted average CPR of 13.0%, and our Legacy Non-Agency MBS portfolio (including Legacy Non-Agency MBS underlying our Linked Transactions) experienced a CPR of 12.3%. Over the last consecutive eight quarters, ending with December 31, 2015, the monthly fair value weighted average CPR on our Agency and Legacy Non-Agency MBS portfolios ranged from a high of 16.7% experienced during the month ended July 31, 2015 to a low of 10.4%, experienced during each of the months ended March 31, 2015 and March 31, 2014, with an average CPR over such quarters of 13.1%.

Our method of accounting for Non-Agency MBS purchased at significant discounts to par value, requires us to make assumptions with respect to each security. These assumptions include, but are not limited to, future interest rates, voluntary prepayment rates, default rates, mortgage modifications and loss severities. As part of our Non-Agency MBS surveillance process, we track and compare each security's actual performance over time to the performance expected at the time of purchase or, if we have modified our original purchase assumptions, to our revised performance expectations. To the extent that actual performance or our expectation of future performance of our Non-Agency MBS deviates materially from our expected performance parameters, we may revise our performance expectations, such that the amount of purchase discount designated as credit discount may be increased or decreased over time. Nevertheless, credit losses greater than those anticipated or in excess of the recorded purchase discount could occur, which could materially adversely impact our operating results.

Table of Contents

It is our business strategy to hold our MBS as long-term investments. On at least a quarterly basis, we assess our ability and intent to continue to hold each security and, as part of this process, we monitor our securities for other-than-temporary impairment. A change in our ability and/or intent to continue to hold any of our securities that are in an unrealized loss position, or a deterioration in the underlying characteristics of these securities, could result in our recognizing future impairment charges or a loss upon the sale of any such security. At December 31, 2015, we had net unrealized gains of $28.8 million on our Agency MBS, comprised of gross unrealized gains of $69.2 million and gross unrealized losses of $40.4 million, and net unrealized gains on our Non-Agency MBS of $559.0 million, comprised of gross unrealized gains of $587.3 million and gross unrealized losses of $28.4 million. At December 31, 2015, we did not intend to sell any of our MBS that were in an unrealized loss position, and we believe it is more likely than not that we will not be required to sell those securities before recovery of their amortized cost basis, which may be at their maturity.

We rely primarily on borrowings under repurchase agreements to finance our Agency MBS and Non-Agency MBS. Our MBS have longer-term contractual maturities than our borrowings under repurchase agreements. Even though the majority of our MBS have interest rates that adjust over time based on short-term changes in corresponding interest rate indices (typically following an initial fixed-rate period for our Hybrids), the interest rates we pay on our borrowings will typically change at a faster pace than the interest rates we earn on our MBS. In order to reduce this interest rate risk exposure, we may enter into derivative instruments, which at December 31, 2015 were comprised of Swaps.

Our Swap derivative instruments are designated as cash-flow hedges against a portion of our current and forecasted LIBOR-based repurchase agreements. Our Swaps do not extend the maturities of our repurchase agreements; they do, however, lock in a fixed rate of interest over their term for the notional amount of the Swap corresponding to the hedged item. During 2015, we did not enter into any new Swaps and had Swaps with an aggregate notional amount of $710.2 million and a weighted average fixed-pay rate of 1.96% amortize and/or expire. At December 31, 2015, we had Swaps designated in hedging relationships with an aggregate notional amount of $3.050 billion with a weighted average fixed-pay rate of 1.82% and a weighted average variable interest rate received of 0.34%.

Recent Market Conditions and Our Strategy

During 2015, we continued to invest in residential mortgage assets, including both MBS and, through consolidated trusts, residential whole loans. At December 31, 2015, our MBS portfolio was approximately $11.173 billion compared to $12.573 billion (including $1.913 billion MBS reported as components of Linked Transactions) at December 31, 2014.

At December 31, 2015, $6.421 billion, or 57.5% of our MBS portfolios was invested in Non-Agency MBS. During the year ended December 31, 2015, the fair value of our Non-Agency MBS holdings increased by $1.665 billion. The primary components of the change during the year in these Non-Agency MBS include the reclassification of $1.913 billion of Non-Agency MBS that were previously reported as a component of Linked Transactions and $1.734 billion of purchases (at a weighted average purchase price of 99.9%). Partially offsetting these increases were $1.845 billion of principal repayments and other principal reductions, a decrease reflecting Non-Agency MBS price changes of $66.3 million and the sale of Non-Agency MBS with a fair value of $70.8 million.

At December 31, 2015, $4.752 billion, or 42.5% of our MBS portfolio was invested in Agency MBS. During the year ended 2015, the fair value of our Agency MBS decreased by $1.152 billion. This was due to $1.059 billion of principal repayments,$41.2 million of premium amortization and a $51.3 million decrease in net unrealized gains.

In this low interest rate environment, we continue to transition to more credit sensitive, less interest sensitive residential mortgage assets. During the year ended December 31, 2015, we purchased through consolidated trusts residential whole loans of approximately $608.3 million, with an unpaid principal balance of approximately $770.5 million. At December 31, 2015, our total recorded investment in residential whole loans was $895.1 million. Of this amount, $271.8 million is presented as residential whole loans at carrying value and $623.3 million as residential whole loans at fair value in our consolidated balance sheets. For the year ended December 31, 2015, we recognized approximately $16.0 million of income on residential whole loans held at carrying value in Interest Income on our consolidated statement of operations, representing an effective yield of 6.63% (excluding servicing costs). In addition, we recorded net gains on residential whole loans held at fair value of $17.7 million in Other Income, net in our consolidated statement of operations for the year ended December 31, 2015.

We currently expect to continue to seek more credit sensitive, less interest rate sensitive residential mortgage assets during 2016, particularly residential whole loans and Non-Agency MBS (including RPL/NPL MBS). In order to achieve our current investment strategy, we may continue to permit more interest rate sensitive Agency MBS to pay down.

Table of Contents

In addition to our investments in Agency MBS, Non-Agency MBS and residential whole loans, we invest in CRT securities, which are debt obligations issued by Fannie Mae and Freddie Mac. At December 31, 2015, our investments in these securities totaled $183.6 million.

New accounting guidance that was effective at the beginning of the year prospectively eliminated the use of Linked Transaction accounting. Accordingly, on adoption of the new standard on January 1, 2015, we reclassified $1.913 billion of Non-Agency MBS and $4.6 million of CRT securities that were previously reported as a component of Linked Transactions to Non-Agency MBS and CRT securities respectively on the consolidated balance sheets. In addition, liabilities of $1.520 billion that were previously presented as a component of Linked Transactions were reclassified to Repurchase agreements on the consolidated balance sheets. Furthermore, an amount of $4.5 million representing net unrealized gains on securities previously reported as a component of Linked Transactions as of December 31, 2014 was reclassified from Accumulated deficit to AOCI (See Notes 2(t) and 6 to the consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K).

Our book value per common share was $7.47 as of December 31, 2015. Book value per common share decreased from $8.12 as of December 31, 2014 due primarily to the impact of realized gains on sales and discount accretion income on Legacy Non-Agency MBS that was recognized and paid as dividends during the year, the change in the value of our Swaps, and lower unrealized gains on our Agency MBS and Legacy Non-Agency MBS, resulting from lower asset values.

At the end of 2015, the average coupon on mortgages underlying our Agency MBS was lower compared to the end of 2014, due to prepayments on higher yielding assets and downward resets on Hybrid and ARM-MBS within the portfolio. As a result, the coupon yield on our Agency MBS portfolio declined 18 basis points to 2.78% for 2015 from 2.96% for 2014. The net Agency MBS yield decreased to 2.00% for 2015, from 2.23% for 2014. The net yield for our Legacy Non-Agency MBS portfolio was 7.62% for 2015 compared to 7.74% for 2014. The decrease in the net yield on our Legacy Non-Agency MBS portfolio is primarily due to prepayments on higher yielding assets in the portfolio, partially offset by increases in accretable discount due to the impact of credit reserve releases, in the current and prior year, that have occurred as a result of the improved credit performance of loans underlying the Legacy Non-Agency MBS portfolio. The net yield for our RPL/NPL MBS portfolio was 3.68% for the year ended December 31, 2015 compared to 3.69% for the year ended December 31, 2014. In the comparable prior period, the majority of our RPL/NPL MBS were reported as Linked Transactions.

We believe that our $787.5 million Credit Reserve and OTTI appropriately factors in remaining uncertainties regarding underlying mortgage performance and the potential impact on future cash flows for our existing Legacy Non-Agency MBS portfolio. Home price appreciation and underlying mortgage loan amortization have decreased the LTV for many of the mortgages underlying our Legacy Non-Agency MBS portfolio. Home price appreciation during the past few years has generally been driven by a combination of limited housing supply, low mortgage rates, capital flows into own-to-rent foreclosure purchases and demographic-driven U.S. household formation. We estimate that the average LTV of mortgage loans underlying our Legacy Non-Agency MBS has declined from approximately 105% as of January 2012 to approximately 71% as of December 31, 2015. In addition, we estimate that the percentage of non-delinquent loans underlying our Legacy Non-Agency MBS that are underwater (with LTVs greater than 100%), has declined from approximately 52% as of January 2012 to 7% at December 31, 2015. Lower LTVs lessen the likelihood of defaults and simultaneously decrease loss severities. Further, during 2014 and 2015, we have also observed faster voluntary prepayment (i.e. prepayment of loans in full with no loss) speeds than originally projected. The yields on our Legacy Non-Agency MBS that were purchased at a discount are generally positively impacted if prepayment rates on these securities exceed our prepayment assumptions. Based on these current conditions, we have reduced estimated future losses within our Legacy Non-Agency portfolio. As a result, during the year ended 2015, $41.1 million was transferred from Credit Reserve to accretable discount. This increase in accretable discount is expected to increase the interest income realized over the remaining life of our Legacy Non-Agency MBS. The remaining average contractual life of such assets is approximately 20 years, but based on scheduled loan amortization and prepayments (both voluntary and involuntary), loan balances will decline substantially over time. Consequently, we believe that the majority of the impact on interest income from the reduction in Credit Reserve will occur over the next ten years.

At December 31, 2015, we have access to various sources of liquidity which we estimate to be in excess of $571.0 million. This amount includes (i) $165.0 million of cash and cash equivalents; (ii) $241.7 million in estimated financing available from unpledged Agency MBS and from other Agency MBS collateral that is currently pledged in excess of contractual requirements; and (iii) $164.3 million in estimated financing available from unpledged Non-Agency MBS. Consequently, we believe that we are positioned to continue to take advantage of investment opportunities within the residential mortgage marketplace. In 2016, we intend to continue to selectively acquire MBS and residential whole loans. In addition, while the majority of our Legacy Non-Agency MBS will not return their full face value due to loan defaults, we believe that they will deliver attractive loss adjusted yields due to our discounted average amortized cost of 75% of face value at December 31, 2015.

Table of Contents

Repurchase agreement funding for both Agency MBS and Non-Agency MBS continues to be available to us from multiple counterparties. Typically, repurchase agreement funding involving Non-Agency MBS is available from fewer counterparties, at terms requiring higher collateralization and higher interest rates, than for repurchase agreement funding involving Agency MBS. In July 2015, our wholly-owned subsidiary, MFA Insurance, became a member of the FHLB of Des Moines, further diversifying our potential sources of funding for residential mortgage investments. However, in January, 2016, the FHFA released its final rule amending its regulation on FHLB membership, which, amongst other things, provided termination rules for current captive insurance members. As a result of such regulation, MFA Insurance will not be permitted new advances or renewal of existing advances and will be required to terminate its FHLB membership within one year of the rule's effective date of February 19, 2016. At December 31, 2015, our debt consisted of borrowings under repurchase agreements with 27 counterparties, FHLB advances, securitized debt, Senior Notes outstanding and obligation to return securities obtained as collateral, resulting in a debt-to-equity multiple of 3.4 times. (See table on page 55 under Results of Operations that presents our quarterly leverage multiples since March 31, 2014.)

Information About Our Assets

The tables below present certain information about our asset allocation at December 31, 2015.

ASSET ALLOCATION

(Dollars in Thousands)	Agency MBS	Legacy Non-Agency MBS	RPL/NPL MBS (1)	MBS Portfolio	Residential Whole Loans, at Carrying Value (2)	Residential Whole Loans, at Fair Value	Other, net (3)	Total
Fair Value/Carrying Value	$4,752,244	$3,794,951	$2,625,866	$11,173,061	$271,845	$623,276	$479,437	$12,547,6
Less Repurchase Agreements	(2,727,542)	(2,464,982)	(2,080,163)	(7,272,687)	(67,989)	(419,761)	(128,465)	(7,888,90
Less FHLB advances	(1,500,000)	—	—	(1,500,000)	—	—	—	(1,500,00
Less Securitized Debt	—	(22,057)	—	(22,057)	—	—	—	(22,057
Less Senior Notes	—	—	—	—	—	—	(100,000)	(100,000
Equity Allocated	$524,702	$1,307,912	$545,703	$2,378,317	$203,856	$203,515	$250,972	$3,036,66
Less Swaps at Market Value	—	—	—	—	—	—	(69,399)	(69,399
Net Equity Allocated	$524,702	$1,307,912	$545,703	$2,378,317	$203,856	$203,515	$181,573	$2,967,26
Debt/Net Equity Ratio (4)	8.06 x	1.90 x	3.81 x		0.33 x	2.06 x		3.38

(1) Represents private-label MBS issued in 2013, 2014 and 2015 in which the underlying collateral consists of re-performing/non-performing loans that were originated in prior years. Included with the balance of Non-Agency MBS reported on our consolidated balance sheets.

(2) The carrying value of such loans reflects the purchase price, accretion of income, cash received and provision for loan losses since acquisition. At December 31, 2015, the fair value of such loans is estimated to be $289.7 million.

(3) Includes cash and cash equivalents and restricted cash, securities obtained and pledged as collateral, CRT securities, interest receivable, goodwill, prepaid and other assets, obligation to return securities obtained as collateral of $507.4 million, interest payable, dividends payable and accrued expenses and other liabilities.

(4) Represents the sum of borrowings under repurchase agreements, FHLB advances and securitized debt as a multiple of net equity allocated. The numerator of our Total Debt/Net Equity ratio also includes the obligation to return

securities obtained as collateral of $507.4 million, and Senior Notes.

Table of Contents

Agency MBS

The following table presents certain information regarding the composition of our Agency MBS portfolio as of December 31, 2015 and 2014:

December 31, 2015

(Dollars in Thousands)	Current Face	Weighted Average Purchase Price		Weighted Average Market Price		Fair Value (1)	Weighted Average Loan Age (Months) (2)	Weighted Average Coupon (2)		3 Month Average CPR	
15-Year Fixed Rate:											
Low Loan Balance (3)	$1,430,258	104.3	%	103.1	%	$1,475,086	44	2.99	%	8.4	%
HARP (4)	146,821	104.7		103.1		151,387	43	2.98		7.9	
Other (Post June 2009) (5)	144,596	103.9		106.1		153,477	63	4.14		16.1	
Other (Pre June 2009) (6)	745	104.9		106.8		796	79	4.50		28.9	
Total 15-Year Fixed Rate	$1,722,420	104.3	%	103.4	%	$1,780,746	45	3.09	%	9.1	%
Hybrid:											
Other (Post June 2009) (5)	$1,811,007	104.4	%	104.8	%	$1,897,030	56	2.89	%	15.6	%
Other (Pre June 2009) (6)	899,185	101.7		105.7		950,666	109	2.60		9.3	
Total Hybrid	$2,710,192	103.5	%	105.1	%	$2,847,696	73	2.80	%	13.5	%
CMO/Other	$117,791	102.5	%	104.2	%	$122,771	175	2.52	%	12.2	%
Total Portfolio	$4,550,403	103.8	%	104.4	%	$4,751,213	65	2.90	%	11.8	%

December 31, 2014

(Dollars in Thousands)	Current Face	Weighted Average Purchase Price		Weighted Average Market Price		Fair Value (1)	Weighted Average Loan Age (Months) (2)	Weighted Average Coupon (2)		3 Month Average CPR	
15-Year Fixed Rate:											
Low Loan Balance (3)	$1,705,386	104.3	%	104.0	%	$1,773,255	32	3.01	%	7.7	%
HARP (4)	177,193	104.7		104.0		184,192	31	2.99		6.5	
Other (Post June 2009) (5)	192,325	103.9		107.2		206,132	51	4.15		13.0	
Other (Pre June 2009) (6)	1,069	104.9		107.7		1,151	67	4.50		0.8	
Total 15-Year Fixed Rate	$2,075,973	104.3	%	104.3	%	$2,164,730	34	3.12	%	8.1	%
Hybrid:											
Other (Post June 2009) (5)	$2,343,186	104.4	%	105.4	%	$2,469,714	44	3.15	%	17.9	%
Other (Pre June 2009) (6)	1,049,495	101.7		106.8		1,120,830	97	2.82		8.8	
Total Hybrid	$3,392,681	103.6	%	105.8	%	$3,590,544	60	3.04	%	15.1	%
CMO/Other	$141,639	102.5	%	104.8	%	$148,391	163	2.41	%	8.9	%
Total Portfolio	$5,610,293	103.8	%	105.2	%	$5,903,665	53	3.06	%	12.3	%

(1) Does not include principal payments receivable of $1.0 million and $542,000 at December 31, 2015 and 2014, respectively.
(2) Weighted average is based on MBS current face at December 31, 2015 and 2014, respectively.
(3) Low loan balance represents MBS collateralized by mortgages with original loan balance of less than or equal to $175,000.

(4) Home Affordable Refinance Program (or HARP) MBS are backed by refinanced loans with LTVs greater than or equal to 80% at origination.
(5) MBS issued in June 2009 or later. Majority of underlying loans are ineligible to refinance through the HARP program.
(6) MBS issued before June 2009.

Table of Contents

The following table presents certain information regarding our 15-year fixed-rate Agency MBS as of December 31, 2015 and 2014:

December 31, 2015

Coupon	Current Face	Weighted Average Purchase Price	Weighted Average Market Price	Fair Value (1)	Weighted Average Loan Age (Months) (2)	Weighted Average Loan Rate	Low Loan Balance and/or HARP (3)	3 Month Average CPR
(Dollars in Thousands)								
15-Year Fixed Rate:								
2.5%	$834,689	104.0 %	101.5 %	$846,925	36	3.04 %	100 %	6.9 %
3.0%	355,439	105.9	103.4	367,471	42	3.49	100	8.0
3.5%	9,238	103.5	104.9	9,691	62	4.18	100	12.6
4.0%	448,064	103.5	106.4	476,793	61	4.40	79	13.1
4.5%	74,990	105.2	106.5	79,866	65	4.88	33	13.3
Total 15-Year Fixed Rate	$1,722,420	104.3 %	103.4 %	$1,780,746	45	3.57 %	92 %	9.1 %

December 31, 2014

Coupon	Current Face	Weighted Average Purchase Price	Weighted Average Market Price	Fair Value (1)	Weighted Average Loan Age (Months) (2)	Weighted Average Loan Rate	Low Loan Balance and/or HARP (3)	3 Month Average CPR
(Dollars in Thousands)								
15-Year Fixed Rate:								
2.5%	$969,213	104.0 %	102.2 %	$990,328	24	3.04 %	100 %	6.1 %
3.0%	420,623	105.9	104.2	438,377	30	3.49	100	4.4
3.5%	11,990	103.5	106.0	12,706	50	4.17	100	11.7
4.0%	575,040	103.5	107.2	616,662	49	4.40	79	12.4
4.5%	99,107	105.2	107.6	106,657	53	4.88	32	16.9
Total 15-Year Fixed Rate	$2,075,973	104.3 %	104.3 %	$2,164,730	34	3.60 %	91 %	8.1 %

(1) Does not include principal payments receivable of $1.0 million and $542,000 at December 31, 2015 and 2014, respectively.
(2) Weighted average is based on MBS current face at December 31, 2015 and 2014, respectively.
(3) Low Loan Balance represents MBS collateralized by mortgages with an original loan balance less than or equal to $175,000. HARP MBS are backed by refinanced loans with LTVs greater than or equal to 80% at origination.

Table of Contents

The following table presents certain information regarding our Hybrid Agency MBS as of December 31, 2015 and 2014:

December 31, 2015

(Dollars in Thousands)	Current Face	Weighted Average Purchase Price	Weighted Average Market Price	Fair Value (1)	Weighted Average Coupon (2)	Weighted Average Loan Age (Months) (2)	Weighted Average Months to Reset (3)	Interest Only (4)	3 Month Average CPR
Hybrid Post June 2009:									
Agency 5/1	$723,853	104.2 %	105.7 %	$765,426	2.62 %	64	7	23 %	15.6 %
Agency 7/1	838,505	104.5	104.2	873,765	3.04	51	32	22	16.7
Agency 10/1	248,649	104.7	103.7	257,839	3.18	47	72	61	11.5
Total Hybrids Post June 2009	$1,811,007	104.4 %	104.8 %	$1,897,030	2.89 %	56	27	28 %	15.6 %
Hybrid Pre June 2009:									
Coupon < 4.5% (5)	$853,168	101.7 %	105.7 %	$901,870	2.43 %	109	6	59 %	8.9 %
Coupon >= 4.5% (6)	46,017	101.5	106.0	48,796	5.73	102	18	73	17.4
Total Hybrids Pre June 2009	$899,185	101.7 %	105.7 %	$950,666	2.60 %	109	6	60 %	9.3 %
Total Hybrids	$2,710,192	103.5 %	105.1 %	$2,847,696	2.80 %	73	20	39 %	13.5 %

December 31, 2014

(Dollars in Thousands)	Current Face	Weighted Average Purchase Price	Weighted Average Market Price	Fair Value (1)	Weighted Average Coupon (2)	Weighted Average Loan Age (Months) (2)	Weighted Average Months to Reset (3)	Interest Only (4)	3 Month Average CPR
Hybrid Post June 2009:									
Agency 5/1	$953,410	104.2 %	106.4 %	$1,014,865	3.21 %	51	11	22 %	22.9 %
Agency 7/1	1,091,645	104.5	104.7	1,143,315	3.07	40	43	20	14.8
Agency 10/1	298,131	104.7	104.5	311,534	3.22	36	83	59	12.7
Total Hybrids Post June 2009	$2,343,186	104.4 %	105.4 %	$2,469,714	3.15 %	44	35	26 %	17.9 %
Hybrid Pre June 2009:									
Coupon < 4.5% (5)	$864,414	101.8 %	106.7 %	$922,639	2.29 %	99	6	57 %	7.2 %
Coupon >= 4.5% (6)	185,081	101.2	107.1	198,191	5.26	84	13	80	15.6
Total Hybrids Pre June 2009	$1,049,495	101.7 %	106.8 %	$1,120,830	2.82 %	97	7	61 %	8.8 %
Total Hybrids	$3,392,681	103.6 %	105.8 %	$3,590,544	3.04 %	60	26	37 %	15.1 %

(1) Does not include principal payments receivable of $1.0 million and $542,000 at December 31, 2015 and 2014, respectively.
(2) Weighted average is based on MBS current face at December 31, 2015 and 2014, respectively.
(3) Weighted average months to reset is the number of months remaining before the coupon interest rate resets. At reset, the MBS coupon will adjust based upon the underlying benchmark interest rate index, margin and periodic or lifetime caps. The months to reset do not reflect scheduled amortization or prepayments.
(4) Interest only represents MBS backed by mortgages currently in their interest only period. Percentage is based on MBS current face at December 31, 2015 and 2014, respectively.

(5) Agency 3/1, 5/1, 7/1 and 10/1 Hybrid ARM-MBS with coupon less than 4.5%.
(6) Agency 3/1, 5/1, 7/1 and 10/1 Hybrid ARM-MBS with coupon greater than or equal to 4.5%.

Table of Contents

Non-Agency MBS

The following table presents information with respect to our Non-Agency MBS at December 31, 2015 and December 31, 2014. As previously discussed, new accounting guidance that was effective on January 1, 2015 prospectively eliminated the use of Linked Transaction accounting and as a result we did not have any Linked Transactions effective January 1, 2015. Accordingly, on adoption of the new standard on January 1, 2015, we reclassified $1.913 billion of Non-Agency MBS and $4.6 million of CRT securities that had previously been reported as a component of Linked Transactions to Non-Agency MBS and CRT securities, respectively on our consolidated balance sheets. Non-Agency MBS at December 31, 2014 is presented: (i) excluding Linked Transactions and reported in accordance with GAAP; (ii) underlying our Linked Transactions and reflected consistent with GAAP reporting requirements (effective on such date); and (iii) on a combined basis (Non-GAAP).

	December 31,	
(In Thousands)	2015	2014
(i) Non-Agency MBS (GAAP)		
Face/Par	$6,961,493	$5,319,901
Fair Value	6,420,817	4,755,432
Amortized Cost	5,861,843	4,020,241
Purchase Discount Designated as Credit Reserve and OTTI	(787,541) (1)	(900,557) (2)
Purchase Discount Designated as Accretable	(312,182)	(399,564)
Purchase Premiums	73	461
(ii) Non-Agency MBS Underlying Linked Transactions		
Face/Par		$1,922,487
Fair Value		1,913,189
Amortized Cost		1,908,776
Purchase Discount Designated as Credit Reserve		(15,543)
Purchase Discount Designated as Accretable		1,832
(iii) Combined Non-Agency MBS and MBS Underlying Linked Transactions (Non-GAAP)		
Face/Par		$7,242,388
Fair Value		6,668,621
Amortized Cost		5,929,017
Purchase Discount Designated as Credit Reserve and OTTI		(916,100) (3)
Purchase Discount Designated as Accretable		(397,732)
Purchase Premiums		461

(1) Includes discount designated as Credit Reserve of $766.0 million and OTTI of $21.5 million.
(2) Includes discount designated as Credit Reserve of $877.6 million and OTTI of $23.0 million.
(3) Includes discount designated as Credit Reserve of $893.1 million and OTTI of $23.0 million.

Table of Contents

Purchase Discounts on Non-Agency MBS and Securities Underlying Linked Transactions

The following table presents the changes in the components of purchase discount on Non-Agency MBS with respect to purchase discount designated as Credit Reserve and OTTI, and accretable purchase discount for the years ended December 31, 2015 and 2014. As previously discussed, new accounting guidance that was effective for us on January 1, 2015 prospectively eliminated the use of Linked Transaction accounting and as a result we did not have any Linked Transactions effective January 1, 2015. The information presented for the year ended December 31, 2014 includes securities underlying Linked Transactions and is presented on both a GAAP and Non-GAAP basis (effective on such date):

	For the Year Ended December 31,			
	2015		2014	
GAAP Basis	Discount Designated as Credit Reserve and OTTI	Accretable Discount (1)	Discount Designated as Credit Reserve and OTTI	Accretable Discount (1)
(In Thousands)				
Balance at beginning of period	$(900,557)	$(399,564)	$(1,043,037)	$(460,039)
Cumulative effect adjustment on adoption of revised accounting standard for repurchase agreement financing	(15,543)	1,832	—	—
Accretion of discount	—	93,173	—	103,653
Realized credit losses	80,821	—	89,481	—
Purchases	(1,200)	(4,925)	(80,256)	30,003
Sales	8,525	38,420	44,692	20,360
Net impairment losses recognized in earnings	(705)	—	—	—
Unlinking of Linked Transactions	—	—	(6,414)	1,436
Transfers/release of credit reserve	41,118	(41,118)	94,977	(94,977)
Balance at end of period	$(787,541)	$(312,182)	$(900,557)	$(399,564)

Non-GAAP Adjustments	Discount Designated as Credit Reserve and OTTI	Accretable Discount (1)
(In Thousands)		
Balance at beginning of period	$(4,721)	$(3,212)
Accretion of discount	—	1,004
Realized credit losses	783	—
Purchases	(17,801)	4,950
Unlinking of Linked Transactions	6,414	(1,128)
Transfers/release of credit reserve	(218)	218
Balance at end of period	$(15,543)	$1,832

Non-GAAP Basis	Discount Designated as Credit Reserve and OTTI	Accretable Discount (1)
(In Thousands)		

Balance at beginning of period	$(1,047,758)	$(463,251)
Accretion of discount	—	104,657
Realized credit losses	90,264	—
Purchases	(98,057)	34,953
Sales	44,692	20,360
Unlinking of Linked Transactions	—	308
Transfers/release of credit reserve	94,759	(94,759)
Balance at end of period	$(916,100)	$(397,732)

(1) Together with coupon interest, accretable purchase discount is recognized as interest income over the life of the security.

43

Table of Contents

The following table presents information with respect to the yield components of our Non-Agency MBS for the periods presented:

	For the Year Ended December 31,					
	2015		2014		2013	
	Legacy Non-Agency MBS	RPL/NPL MBS	Legacy Non-Agency MBS	RPL/NPL MBS	Legacy Non-Agency MBS	RPL/NPL MBS
Non-Agency MBS						
Coupon Yield (1)	5.08 %	3.61 %	5.19 %	3.55 %	5.63 %	4.56 %
Effective Yield Adjustment (2)	2.54	0.07	2.55	0.14	1.62	—
Net Yield	7.62 %	3.68 %	7.74 %	3.69 %	7.25 %	4.56 %

(1) Reflects coupon interest income divided by the average amortized cost. The discounted purchase price on Legacy Non-Agency MBS causes the coupon yield to be higher than the pass-through coupon interest rate.

(2) The effective yield adjustment is the difference between the net yield, calculated utilizing management's estimates of timing and amount of future cash flows for Legacy Non-Agency MBS and RPL/NPL MBS, less the current coupon yield.

The information presented as of December 31, 2014 in the above tables on pages 42-43, includes certain underlying Non-Agency MBS and the associated repurchase agreement borrowings that were disclosed both separately and/or on a combined basis with our Non-Agency MBS portfolio. Prior to January 1, 2015, for GAAP financial reporting purposes, we were required to account for these items as Linked Transactions. Consequently, the presentation of this information in the above tables constitutes Non-GAAP financial measures within the meaning of Regulation G, as promulgated by the SEC.

In assessing the performance of our Non-Agency MBS portfolio prior to January 1, 2015, we did not view these transactions as linked, but rather viewed the performance of the underlying Non-Agency MBS and the related repurchase agreement borrowings as we would any other Non-Agency MBS that was not part of a linked transaction. Accordingly, as Linked Transaction accounting was discontinued on January 1, 2015, we consider that the Non-GAAP information disclosed in the above table for prior periods provides appropriate comparability to current period disclosures for our Non-Agency MBS portfolio.

Actual maturities of MBS are generally shorter than stated contractual maturities because actual maturities of MBS are affected by the contractual lives of the underlying mortgage loans, periodic payments of principal, and prepayments of principal. The following table presents certain information regarding the amortized costs, weighted average yields and contractual maturities of our MBS at December 31, 2015 and does not reflect the effect of prepayments or scheduled principal amortization on our MBS:

	One to Five Years		Five to Ten Years		Over Ten Years		Total MBS (1)		
(Dollars in Thousands)	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Total Amortized Cost	Total Fair Value	Weighted Average Yield
Agency MBS:									
Fannie Mae	$653	2.60 %	$189,916	3.21 %	$3,638,635	2.13 %	$3,829,204	$3,865,485	2.19 %
Freddie Mac	—	—	130,538	2.80	754,260	2.02	884,798	877,109	2.13
Ginnie Mae	—	—	—	—	9,460	1.71	9,460	9,650	1.71
Total Agency MBS	$653	2.60 %	$320,454	3.04 %	$4,402,355	2.11 %	$4,723,462	$4,752,244	2.18 %

Non-Agency MBS	$358,034	4.08 %	$4,124	8.36 %	$5,499,685	6.05 %	$5,861,843	$6,420,817	5.93 %
Total MBS	$358,687	4.07 %	$324,578	3.11 %	$9,902,040	4.30 %	$10,585,305	$11,173,061	4.25 %

(1) We did not have any MBS with contractual maturities of less than one year at December 31, 2015.

At December 31, 2015, our CRT securities had an amortized cost of $186.3 million, a fair value of $183.6 million, a weighted average yield of 5.09% and weighted average time to maturity of 9.0 years.

44

Table of Contents

Residential Whole Loans

The following table presents the contractual maturities of the residential whole loans held by consolidated trusts at December 31, 2015 and does not reflect estimates of prepayments or scheduled amortization. For residential whole loans at carrying value, amounts presented are estimated based on the underlying loan contractual amounts.

(In Thousands)	Residential Whole Loans at Carrying Value	Residential Whole Loans at Fair Value
Amount due:		
Within one year	$2,319	$5,760
After one year:		
Over one to five years	3,197	5,437
Over five years	266,329	612,079
Total due after one year	$269,526	$617,516
Total residential whole loans	$271,845	$623,276

The following table presents at December 31, 2015, the dollar amount of our residential whole loans at fair value, contractually maturing after one year, and indicates whether the loans have fixed interest rates or adjustable interest rates:

(In Thousands)	Residential Whole Loans at Fair Value (1)
Interest rates:	
Fixed	$342,702
Adjustable	274,814
Total	$617,516

(1) Includes loans on which borrowers have defaulted and are not making payments of principal and/or interest as of December 31, 2015.

Information is not presented for residential whole loans at carrying value as income is recognized based on pools of assets with similar risk characteristics using an estimated yield based on cash flows expected to be collected over the lives of the loans in such pools rather than on the contractual coupons of the underlying loans.

The following table presents additional information regarding our residential whole loans at fair value at December 31, 2015 and 2014:

	Residential Whole Loans at Fair Value	
(Dollars in Thousands)	December 31, 2015	December 31, 2014
Loans 90 days or more past due:		
Number of Loans	2,426	779
Aggregate Amount Outstanding	$493,640	$128,591

Income on residential whole loans at carrying value is recognized based on pools of assets with similar credit risk characteristics using an estimated yield based on cash flows expected to be collected over the lives of the loans in such pools rather than the contractual coupons of the underlying loans. As the unit of account is at the pool level rather than the individual loan level, none of our residential whole loans at carrying value are currently considered 90 days or more past due.

Table of Contents

Exposure to Financial Counterparties

We finance a significant portion of our MBS and CRT securities with repurchase agreements and other advances. In connection with these financing arrangements, we pledge our securities as collateral to secure the borrowing. The amount of collateral pledged will typically exceed the amount of the financing with the extent of over-collateralization ranging from 1%-6% of the amount borrowed (U.S. Treasury and Agency MBS collateral) to up to 64% (Non-Agency MBS collateral). Consequently, while repurchase agreement financing results in us recording a liability to the counterparty in our consolidated balance sheets, we are exposed to the counterparty, if during the term of the repurchase agreement financing, a lender should default on its obligation and we are not able to recover our pledged assets. The amount of this exposure is the difference between the amount loaned to us plus interest due to the counterparty and the fair value of the collateral pledged by us to the lender including accrued interest receivable on such collateral.

In addition, we use interest rate Swaps to manage interest rate risk exposure in connection with our repurchase agreement financings. We will make cash payments or pledge securities as collateral as part of a margin arrangement in connection with interest rate Swaps that are in an unrealized loss position. In the event that a counterparty for a Swap that is not subject to central clearing were to default on its obligation, we would be exposed to a loss to a Swap counterparty to the extent that the amount of cash or securities pledged exceeded the unrealized loss on the associated Swaps and we were not able to recover the excess collateral.

The table below summarizes our exposure to our counterparties at December 31, 2015, by country of domicile:

Country	Number of Counterparties	Repurchase Agreement Financing and Other Advances		Swaps at Fair Value		Exposure (1)	Exposure as a Percentage of MFA Total Assets	
(Dollars in Thousands)								
European Countries: (2)								
Switzerland	2	$2,141,858		$—		$638,992	4.85	%
United Kingdom	2	307,622		—		109,518	0.83	
France	2	259,761		—		42,832	0.33	
Holland	1	245,494		396		12,934	0.10	
Germany	1	—		357		130	—	
Total	8	2,954,735		753		804,406	6.11	%
Other Countries:								
United States (3)	13	$5,141,035		$(70,152	)	$1,032,057	7.62	%
Canada (4)	4	997,405		—		359,307	2.73	
Japan	3	459,332		—		26,371	0.20	
China	1	336,395		—		7,108	0.05	
Total	21	6,934,167		(70,152	)	1,424,843	10.60	%
Total Counterparty Exposure	29	$9,888,902	(5)	$(69,399	)	$2,229,249	16.71	%

(1) Represents for each counterparty the amount of cash and/or securities pledged as collateral less the aggregate of repurchase agreement financing and other advances, Swaps at fair value, and net interest receivable/payable on all such instruments.
(2) Includes European-based counterparties as well as U.S.-domiciled subsidiaries of the European parent entity.
(3) Includes one counterparty that is a central clearing house for our Swaps.
(4) Includes exposure to foreign based affiliates of the Canadian parent entity.

(5) Includes $500.0 million of repurchase agreements entered into in connection with contemporaneous repurchase and reverse repurchase agreements with a single counterparty

At December 31, 2015, we did not use credit default swaps or other forms of credit protection to hedge the exposures summarized in the table above.

Weak economic conditions in Europe could potentially impact our major European financial counterparties, with the possibility that this would also impact the operations of their U.S. domiciled subsidiaries. This could adversely affect our financing and operations as well as those of the entire mortgage sector in general. Management monitors our exposure to our repurchase agreement and Swap counterparties on a regular basis, using various methods, including review of recent rating agency actions or other developments and by monitoring the amount of cash and securities collateral pledged and the associated loan amount under repurchase agreements and/or the fair value of Swaps with our counterparties. We intend to make reverse margin calls on our counterparties to recover excess collateral as permitted by the agreements governing our financing arrangements, or take other necessary actions to reduce the amount of our exposure to a counterparty when such actions are considered necessary.

Tax Considerations

Current period estimated taxable and items expected to impact future taxable income

We estimate that for 2015, our taxable income was approximately $307.5 million. Based on dividends paid or declared during 2015, we have undistributed taxable income of approximately $7.6 million, or $0.02 per share. We have until the filing of our 2015 tax return (due not later than September 15, 2016) to declare the distribution of any 2015 REIT taxable income not previously distributed.

Certain events that are expected to occur over the next few quarters are anticipated to impact the amount of taxable income generated, including (i) the unwind of a resecuritization transaction, which is currently expected to generate taxable income of approximately $0.19 per share, and (ii) the receipt of our share of settlement proceeds in connection with the $8.5 billion settlement of the Bank of America/Countrywide MBS litigation, which is expected to generate taxable income of approximately $0.05 per share.

Key differences between GAAP net income and REIT Taxable Income for Non-Agency MBS and Residential Whole Loans

Our total Non-Agency MBS portfolio for tax differs from our portfolio reported for GAAP primarily due to the fact that for tax purposes; (i) certain of the MBS contributed to the variable interest entities (or VIEs) used to facilitate resecuritization transactions were deemed to be sold; and (ii) the tax portfolio includes certain securities issued by these VIEs. In addition, for our Non-Agency MBS tax portfolio, potential timing differences arise with respect to the accretion of market discount into income and recognition of realized losses for tax purposes as compared to GAAP. Consequently, our REIT taxable income calculated in a given period may differ significantly from our GAAP net income.

The determination of taxable income attributable to Non-Agency MBS and residential whole loans is dependent on a number of factors, including principal payments, defaults, loss mitigation efforts and loss severities. In projecting taxable income for Non-Agency MBS and residential whole loans during the year, management considers estimates of the amount of discount expected to be accreted. Such estimates require significant judgment and actual results may differ from these estimates. Moreover, the deductibility of realized losses from Non-Agency MBS and residential whole loans, and their effect on market discount accretion is analyzed on an asset-by-asset basis and while they will result in a reduction of taxable income, this reduction tends to occur gradually and primarily in periods after the realized losses are reported.

Resecuritization transactions result in differences between GAAP net income and REIT Taxable Income

For tax purposes, depending on the transaction structure, a resecuritization transaction may be treated either as a sale or a financing of the underlying MBS. Income recognized from resecuritization transactions will differ for tax and GAAP. For tax purposes, we own and may in the future acquire interests in resecuritization trusts, in which several of the classes of securities are or will be issued with Original Issue Discount (or OID). As the holder of the retained interests in the trust, we generally will be required to include OID in our current gross interest income over the term of the applicable securities as the OID accrues. The rate at which the OID is recognized into taxable income is calculated using a constant rate of yield to maturity, with realized losses impacting the amount of OID recognized in REIT taxable income once they are actually incurred. For tax purposes, REIT taxable income may be recognized in excess of economic income (i.e., OID) or in advance of the corresponding cash flow from these assets, thereby effecting our dividend distribution requirement to stockholders.

Regulatory Developments

The U.S. Congress, Board of Governors of the Federal Reserve System, U.S. Treasury, FDIC, SEC and other governmental and regulatory bodies have taken and continue to consider additional actions in response to the 2007-2008 financial crisis. In particular, the Dodd-Frank Act created a new regulator, an independent bureau housed within the Federal Reserve System, and known as the Consumer Financial Protection Bureau (or the CFPB). The CFPB has broad authority over a wide range of consumer financial products and services, including mortgage lending. One portion of the Dodd-Frank Act, the Mortgage Reform and Anti-Predatory Lending Act (or Mortgage Reform Act), contains new underwriting and servicing standards for the mortgage industry, as well as restrictions on compensation for mortgage originators. In addition, the Mortgage Reform Act grants broad discretionary regulatory authority to the CFPB to prohibit or condition terms, acts or practices relating to residential mortgage loans that the

Table of Contents

CFPB finds abusive, unfair, deceptive or predatory, as well as to take other actions that the CFPB finds are necessary or proper to ensure responsible affordable mortgage credit remains available to consumers. The Dodd-Frank Act also affects the securitization of mortgages (and other assets) with requirements for risk retention by securitizers and requirements for regulating Rating Agencies.

The Dodd-Frank Act requires that numerous regulations, many of which (including those mentioned above regarding underwriting and mortgage originator compensation) have only recently been implemented and operationalized. As a result, we are unable to fully predict at this time how the Dodd-Frank Act, as well as other laws that may be adopted in the future, will affect our business, results of operations and financial condition, or the environment for repurchase financing and other forms of borrowing, the investing environment for Agency MBS, Non-Agency MBS and/or residential mortgage loans, the securitization industry, Swaps and other derivatives. However, at a minimum, we believe that the Dodd-Frank Act and the regulations promulgated thereunder are likely to continue to increase the economic and compliance costs for participants in the mortgage and securitization industries, including us.

In addition to the regulatory actions being implemented under the Dodd-Frank Act, on August 31, 2011, the SEC issued a concept release under which it is reviewing interpretive issues related to Section 3(c)(5)(C) of the Investment Company Act. Section 3(c)(5)(C) excludes from the definition of “investment company” entities that are primarily engaged in, among other things, “purchasing or otherwise acquiring mortgages and other liens on and interests in real estate.” Many companies that engage in the business of acquiring mortgages and mortgage-related instruments seek to rely on existing interpretations of the SEC Staff with respect to Section 3(c)(5)(C) so as not to be deemed an investment company for the purpose of regulation under the Investment Company Act. In connection with the concept release, the SEC requested comments on, among other things, whether it should reconsider its existing interpretation of Section 3(c)(5)(C). To date the SEC has not taken or otherwise announced any further action in connection with the concept release. (For additional discussion of the SEC’s concept release and its potential impact on us, please see Part I, Item 1A. “Risk Factors” of this Annual Report on Form 10-K.)

Congress may continue to consider legislation that would significantly reform the country’s mortgage finance system, including, among other things, eliminating Freddie Mac and Fannie Mae and replacing them with a single new MBS insurance agency. Many details remain unsettled, including the scope and costs of the agencies’s guarantee and their affordable housing mission, some of which could be addressed even in the absence of large-scale reform. While the likelihood of enactment of major mortgage finance system reform in the short term remains uncertain, it is possible that the adoption of any such reforms could adversely affect the types of assets we can buy, the costs of these assets and our business operations. As the FHFA and both houses of Congress continue to consider various measures intended to dramatically restructure the U.S. housing finance system and the operations of Fannie Mae and Freddie Mac, we expect debate and discussion on the topic to continue throughout 2016.

Results of Operations

Year Ended December 31, 2015 Compared to the Year Ended December 31, 2014

General

For 2015, our net income available to our common stock and participating securities was $298.2 million, or $0.80 per basic and diluted common share, relatively unchanged compared to net income available to common stock and participating securities for 2014 of $298.5 million, or $0.81 per basic and diluted common share.

Net Interest Income

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends primarily upon the volume of interest-earning assets and interest-bearing liabilities and the corresponding interest rates earned or paid. Our net interest income varies primarily as a result of changes in interest rates, the slope of the yield curve (i.e., the differential between long-term and short-term interest rates), borrowing costs (i.e., our interest expense) and prepayment speeds on our MBS. Interest rates and CPRs (which measure the amount of unscheduled principal prepayment on a bond as a percentage of the bond balance) vary according to the type of investment, conditions in the financial markets, and other factors, none of which can be predicted with any certainty.

The changes in average interest-earning assets and average interest-bearing liabilities and their related yields and costs are discussed in greater detail below under “Interest Income” and “Interest Expense.”

For 2015, our net interest spread and margin were 2.33% and 2.65%, respectively, compared to a net interest spread and margin of 2.40% and 2.78%, respectively, for 2014. Our net interest income increased by $11.2 million, or 3.7%, to $315.2 million from $304.0 million for 2014. For 2015, net interest income on RPL/NPL MBS and CRT securities increased by approximately

Table of Contents

$60.3 million. Prior to January 1, 2015, the majority of these assets and associated repurchase agreement financings were reported as components of Linked Transactions with net income reported in Other Income, net in our consolidated statement of operations. This increase was partially offset by the $58.9 million decline in net interest income from Agency and Legacy Non-Agency MBS compared to 2014, primarily due to lower average balances of these MBS and associated Agency repurchase financings. In addition, net interest income for 2015 compared to 2014 was approximately $6.2 million higher due to higher investments in residential whole loans at carrying value and lower outstanding balances of securitized debt.

The net interest spread on our Agency MBS portfolio declined to 0.88% for 2015 compared to 1.08% for 2014. The net interest spread on our Legacy Non-Agency MBS portfolio increased to 4.80% for 2015 compared to 4.73% for 2014. The net interest spread on our RPL/NPL MBS portfolio was 2.01% for 2015 compared to 2.10% for 2014. In the comparable prior period, the majority of our RPL/NPL MBS were reported as Linked Transactions with net interest income reported in Other Income, net.

Table of Contents

Analysis of Net Interest Income

The following table sets forth certain information about the average balances of our assets and liabilities and their related yields and costs for the years ended December 31, 2015, 2014 and 2013. Average yields are derived by dividing interest income by the average amortized cost of the related assets, and average costs are derived by dividing interest expense by the daily average balance of the related liabilities, for the periods shown. The yields and costs include premium amortization and purchase discount accretion which are considered adjustments to interest rates.

	For the Year Ended December 31,								
	2015			2014			2013		
(Dollars in Thousands)	Average Balance	Interest	Average Yield/Cost	Average Balance	Interest	Average Yield/Cost	Average Balance	Interest	Average Yield/Cost
Assets:									
Interest-earning assets:									
Agency MBS (1)	$5,282,198	$105,835	2.00%	$6,388,112	$142,543	2.23%	$6,841,082	$156,046	2.28%
Legacy Non-Agency MBS (1)	3,600,339	274,352	7.62	4,072,237	314,998	7.74	4,507,039	326,749	7.25
RPL/NPL MBS (1)	2,423,808	89,218	3.68	36,065	1,332	3.69	461	21	4.56
Total MBS	11,306,345	469,405	4.15	10,496,414	458,873	4.37	11,348,582	482,816	4.25
CRT securities (1)	133,458	6,572	4.92	16,972	772	4.55	—	—	—
Residential whole loans, at carrying value (2)	241,801	16,036	6.63	58,762	4,083	6.95	—	—	—
Cash and cash equivalents (3)	212,917	130	0.06	358,576	89	0.02	475,287	124	0.03
Total interest-earning assets	11,894,521	492,143	4.14	10,930,724	463,817	4.24	11,823,869	482,940	4.08
Total non-interest-earning assets (2)	1,778,216			1,616,694			1,368,416		
Total assets	$13,672,737			$12,547,418			$13,192,285		
Liabilities and stockholders’ equity:									
Interest-bearing liabilities:									
Agency repurchase agreements (4)	$4,465,949	$51,891	1.16	$5,662,872	$65,128	1.15	$6,116,468	$72,856	1.19
Legacy Non-Agency repurchase agreements (4)	2,629,059	74,062	2.82	2,625,403	79,302	3.01	2,596,663	71,029	2.74
RPL/NPL repurchase agreements	1,928,392	32,246	1.67	17,200	273	1.59	—	—	—
CRT securities repurchase agreements	92,860	1,614	1.74	11,323	189	1.67	—	—	—
Residential whole loan repurchase agreements	222,336	6,108	2.75	16,060	352	2.19	—	—	—
FHLB advances	257,811	997	0.39	—	—	—	—	—	—
	9,596,407	166,918	1.74	8,332,858	145,244	1.74	8,713,131	143,885	1.65

Total repurchase agreements and other advances									
Securitized debt	65,681	1,996	3.04	231,828	6,533	2.82	487,476	12,100	2.48
Senior Notes	100,000	8,034	8.03	100,000	8,031	8.03	100,000	8,028	8.03
Total interest-bearing liabilities	9,762,088	176,948	1.81	8,664,686	159,808	1.84	9,300,607	164,013	1.76
Total non-interest-bearing liabilities	781,188			651,800			629,220		
Total liabilities	10,543,276			9,316,486			9,929,827		
Stockholders’ equity	3,129,461			3,230,932			3,262,458		
Total liabilities and stockholders’ equity	$13,672,737			$12,547,418			$13,192,285		
Net interest income/net interest rate spread (5)		$315,195	2.33%		$304,009	2.40%		$318,927	2.32%
Net interest-earning assets/net interest margin (6)	$2,132,433		2.65%	$2,266,038		2.78%	$2,523,262		2.70%
Ratio of interest-earning assets to interest-bearing liabilities	1.22 x			1.26 x			1.27 x		

(1) Yields presented throughout this Annual Report on Form 10-K are calculated using average amortized cost data for securities which excludes unrealized gains and losses and includes principal payments receivable on securities. For GAAP reporting purposes, purchases and sales are reported on the trade date. Average amortized cost data used to determine yields is calculated based on the settlement date of the associated purchase or sale as interest income is not earned on purchased assets and continues to be earned on sold assets until settlement date. Includes Non-Agency MBS transferred to consolidated VIEs.

(2) Excludes residential whole loans held at fair value that are reported as a component of total non-interest-earning assets.

(3) Includes average interest-earning cash, cash equivalents and restricted cash.

(4) Average cost of repurchase agreements includes the cost of Swaps allocated based on the proportionate share of the overall estimated weighted average portfolio duration.

(5) Net interest rate spread reflects the difference between the yield on average interest-earning assets and average cost of funds.

(6) Net interest margin reflects net interest income divided by average interest-earning assets.

Table of Contents

Rate/Volume Analysis

The following table presents the extent to which changes in interest rates (yield/cost) and changes in the volume (average balance) of interest-earning assets and interest-bearing liabilities have affected our interest income and interest expense during the periods indicated. Information is provided in each category with respect to: (i) the changes attributable to changes in volume (changes in average balance multiplied by prior rate); (ii) the changes attributable to changes in rate (changes in rate multiplied by prior average balance); and (iii) the net change. The changes attributable to the combined impact of volume and rate have been allocated proportionately, based on absolute values, to the changes due to rate and volume.

	Year Ended December 31, 2015 Compared to Year Ended December 31, 2014			Year Ended December 31, 2014 Compared to Year Ended December 31, 2013		
	Increase/(Decrease) due to		Total Net Change in Interest Income/Expense	Increase/(Decrease) due to		Total Net Change in Interest Income/Expense
(In Thousands)	Volume	Rate		Volume	Rate	
Interest-earning assets:						
Agency MBS	$(23,092)	$(13,616)	$ (36,708)	$(10,163)	$(3,340)	$ (13,503)
Legacy Non-Agency MBS	(36,021)	(4,625)	(40,646)	(32,895)	21,123	(11,772)
RPL/NPL MBS (1)	87,884	2	87,886	1,337	(5)	1,332
CRT securities	5,731	69	5,800	772	—	772
Residential whole loans at carrying value (1)	11,872	81	11,953	4,083	—	4,083
Cash and cash equivalents	(5)	46	41	(29)	(6)	(35)
Total net change in income from interest-earning assets	$46,369	$(18,043)	$ 28,326	$(36,895)	$17,772	$ (19,123)
Interest-bearing liabilities:						
Agency repurchase agreements	$(13,900)	$663	$ (13,237)	$(5,275)	$(2,453)	$ (7,728)
Legacy Non-Agency repurchase agreements	110	(5,350)	(5,240)	832	7,441	8,273
RPL/NPL repurchase agreements	31,957	16	31,973	273	—	273
CRT securities repurchase agreements	1,417	8	1,425	189	—	189
Residential whole loan repurchase agreements	5,645	111	5,756	352	—	352
FHLB advances	997	—	997	—	—	—
Securitized debt	(5,013)	476	(4,537)	(7,041)	1,474	(5,567)
Senior Notes	—	3	3	—	3	3
Total net change in expense of interest-bearing liabilities	$21,213	$(4,073)	$ 17,140	$(10,670)	$6,465	$ (4,205)
Net change in net interest income	$25,156	$(13,970)	$ 11,186	$(26,225)	$11,307	$ (14,918)

(1) Excludes residential whole loans held at fair value which are reported as a component of non-interest-earning assets.

Table of Contents

The following table presents certain quarterly information regarding our net interest spread and net interest margin for the quarterly periods presented:

	Total Interest-Earning Assets and Interest-Bearing Liabilities	
Quarter Ended	Net Interest Spread (1)	Net Interest Margin (2)
December 31, 2015	2.22 %	2.54 %
September 30, 2015	2.24	2.58
June 30, 2015	2.33	2.66
March 31, 2015	2.44	2.77
December 31, 2014	2.41	2.76
September 30, 2014	2.32	2.70
June 30, 2014	2.42	2.80
March 31, 2014	2.44	2.84

(1) Reflects the difference between the yield on average interest-earning assets and average cost of funds.
(2) Reflects annualized net interest income divided by average interest-earning assets.

The following table presents the components of the net interest spread earned on our Agency, Legacy Non-Agency MBS and RPL/NPL MBS for the quarterly periods presented:

	Agency MBS			Legacy Non-Agency MBS			RPL /NPL MBS			Total MBS		
Quarter Ended	Net Yield (1)	Cost of Funding (2)	Net Interest Spread (3)	Net Yield (1)	Cost of Funding (2)	Net Interest Spread (3)	Net Yield (1)	Cost of Funding (2)	Net Interest Spread (3)	Net Yield (1)	Cost of Funding (2)	Net Interest Spread (3)
December 31, 2015	2.04 %	1.17 %	0.87 %	7.64 %	2.90 %	4.74 %	3.70 %	1.81 %	1.89 %	4.17 %	1.81 %	2.36 %
September 30, 2015	1.84	1.13	0.71	7.60	2.76	4.84	3.74	1.73	2.01	4.08	1.73	2.35
June 30, 2015	1.89	1.06	0.83	7.59	2.77	4.82	3.66	1.60	2.06	4.09	1.65	2.44
March 31, 2015	2.22	1.13	1.09	7.64	2.85	4.79	3.62	1.52	2.10	4.26	1.69	2.57
December 31, 2014	2.17	1.12	1.05	7.68	2.95	4.73	3.19	1.60	1.59	4.33	1.76	2.57
September 30, 2014	2.09	1.14	0.95	7.70	2.97	4.73	3.53	1.49	2.04	4.28	1.75	2.53
June 30, 2014	2.26	1.13	1.13	7.72	3.11	4.61	4.16	—	4.16	4.36	1.77	2.59
March 31, 2014	2.39	1.21	1.18	7.80	3.04	4.76	4.30	—	4.30	4.50	1.80	2.70

(1) Reflects annualized interest income on MBS divided by average amortized cost of MBS.
(2) Reflects annualized interest expense divided by average balance of repurchase agreements and other advances, including the cost of Swaps allocated based on the proportionate share of the overall estimated weighted average portfolio duration and securitized debt. Agency cost of funding includes 74, 74, 70, 78, 79, 82, 81 and 85 basis

points and Legacy Non-Agency cost of funding includes 69, 66, 68,78, 84, 89, 88 and 74 basis points associated with Swaps to hedge interest rate sensitivity on these assets for the quarters ended December 31, 2015, September 30, 2015, June 30, 2015, March 31, 2015, December 31, 2014, September 30, 2014, June 30, 2014 and March 31, 2014, respectively.

(3) Reflects the difference between the net yield on average MBS and average cost of funds on MBS.

Interest Income

Interest income on our Agency MBS for 2015 decreased by $36.7 million, or 25.8% to $105.8 million from $142.5 million for 2014. This change primarily reflects a $1.106 billion decrease in the average amortized cost of our Agency MBS portfolio to $5.282 billion for 2015 from $6.388 billion for 2014. In addition, the net yield on our Agency MBS decreased to 2.00% for 2015 from 2.23% for 2014. At the end of 2015, the average coupon on mortgages underlying our Agency MBS was lower compared to the end of 2014, as a result of prepayments on higher yielding assets and downward resets on Hybrid and ARM-MBS within the portfolio. As a result, the coupon yield on our Agency MBS portfolio declined 18 basis points to 2.78% for 2015 from 2.96% for 2014. During 2015, our Agency MBS portfolio experienced a 13.2% CPR and we recognized a $41.2 million of net premium

Table of Contents

amortization compared to a CPR of 13.0% and $46.8 million of net premium amortization in 2014. At December 31, 2015, we had net purchase premiums on our Agency MBS of $172.0 million, or 3.8% of current par value, compared to net purchase premiums of $213.3 million, or 3.8% of par value at December 31, 2014.

Interest income on our Non-Agency MBS (which includes Non-Agency MBS transferred to consolidated VIEs) increased $47.2 million, or 14.9%, for 2015 to $363.6 million compared to $316.3 million for 2014. Non-Agency MBS interest income reflected the inclusion of MBS that, prior to January 1, 2015, were accounted for as components of Linked Transactions and income from such securities was reported in Other Income, net in prior periods. In addition, primarily due to the accounting change for Linked Transactions, the average amortized cost of our Non-Agency MBS increased by $1.916 billion or 46.6%, to $6.024 billion for 2015, from $4.108 billion for 2014. Our Legacy Non-Agency MBS portfolio yielded 7.62% for 2015 compared to 7.74% for 2014. The decrease in the yield on our Legacy Non-Agency MBS is primarily due to prepayments on higher yielding assets in the portfolio, partially offset by increases in accretable discount due to the impact of credit reserve releases, in the current and prior year, that have occurred as a result of the improved credit performance of loans underlying the Legacy Non-Agency MBS portfolio. Our RPL/NPL MBS portfolio yielded 3.68% for 2015 compared to 3.69% for 2014. During 2015, we recognized net purchase discount accretion of $92.8 million on our Non-Agency MBS, compared to $103.4 million for 2014. At December 31, 2015, we had net purchase discounts of $1.096 billion, including Credit Reserve and previously recognized OTTI of $787.5 million, on our Legacy Non-Agency MBS, or 25.4% of par value. During 2015 we reallocated $41.1 million of purchased discount designated as Credit Reserve to accretable purchase discount.

The following table presents the components of the coupon yield and net yields earned on our Agency MBS, Legacy Non-Agency MBS and RPL/NPL MBS and weighted average CPR experienced for such MBS for the quarterly periods presented:

	Agency MBS			Legacy Non-Agency MBS			RPL/NPL MBS		
Quarter Ended	Coupon Yield (1)	Net Yield (2)	3 Month Average CPR (3)	Coupon Yield (1)	Net Yield (2)	3 Month Average CPR (3)	Coupon Yield (1)	Net Yield (2)	3 Month Average Bond CPR (4)
December 31, 2015	2.76 %	2.04 %	11.8 %	5.09 %	7.64 %	14.6 %	3.68 %	3.70 %	21.5 %
September 30, 2015	2.74	1.84	15.4	5.10	7.60	16.3	3.62	3.74	29.5
June 30, 2015	2.77	1.89	14.8	5.06	7.59	14.8	3.57	3.66	28.6
March 31, 2015	2.99	2.22	10.9	5.11	7.64	11.1	3.56	3.62	19.6
December 31, 2014	2.91	2.17	12.3	5.13	7.68	12.5	3.91	3.19	17.6
September 30, 2014	2.94	2.09	15.1	5.18	7.70	12.7	3.53	3.53	19.7
June 30, 2014	2.99	2.26	13.0	5.27	7.72	12.1	4.16	4.16	15.8
March 31, 2014	3.01	2.39	11.5	5.19	7.80	11.9	4.30	4.30	16.0

(1) Reflects the annualized coupon interest income divided by the average amortized cost. The discounted purchase price on Legacy Non-Agency MBS causes the coupon yield to be higher than the pass-through coupon interest rate.
(2) Reflects annualized interest income on MBS divided by average amortized cost of MBS.
(3) 3 month average CPR weighted by positions as of the beginning of each month in the quarter.
(4) All principal payments are considered to be prepayments for CPR purposes.

Interest Expense

Our interest expense for 2015 increased by $17.1 million, or 10.7% to $176.9 million, from $159.8 million for 2014. This increase primarily reflects an increase in our average borrowings to finance RPL/NPL MBS (primarily due to the reclassification of repurchase agreements previously reported as a component of Linked Transactions as discussed above), residential whole loans and CRT securities, and utilization of FHLB advances, which was partially offset by a decrease in our average repurchase agreement borrowings to finance Agency MBS, lower financing rates on Legacy Non-Agency MBS, and a decrease in the average balance of securitized debt.

At December 31, 2015, we had repurchase agreement borrowings of $7.889 billion of which $3.050 billion was hedged with Swaps, FHLB advances of $1.500 billion and securitized debt of $22.1 million. At December 31, 2015, our Swaps designated in hedging relationships had a weighted average fixed-pay rate of 1.82% and extended 45 months on average with a maximum remaining term of approximately 92 months.

Table of Contents

The effective interest rate paid on our borrowings decreased to 1.81% for 2015 from 1.84% for 2014. This decrease reflects the lower average balance of Agency repurchase agreements and securitized debt, the lower financing rates associated with our Legacy Non-Agency MBS portfolio (including the allocation of Swap expense), partially offset by the increase in our average balance of repurchase agreements used to finance RPL/NPL MBS.

Payments made and/or received on our Swaps are a component of our borrowing costs and accounted for interest expense of $53.8 million or 57 basis points, for 2015, compared to interest expense of $69.8 million, or 81 basis points, for 2014. The weighted average fixed-pay rate on our Swaps designated as hedges decreased to 1.86% for 2015 from 1.93% for 2014. The weighted average variable interest rate received on our Swaps increased to 0.19% for 2015 from 0.16% for 2014. During 2015, we did not enter into any new Swaps and had Swaps with an aggregate notional amount of $710.2 million and a weighted average fixed-pay rate of 1.96% amortize and/or expire.

We expect that our interest expense and funding costs for 2016 will be impacted by market interest rates, the amount of our borrowings and incremental hedging activity, existing and future interest rates on our hedging instruments and the extent to which we execute additional longer-term structured financing transactions. As a result of these variables, our borrowing costs cannot be predicted with any certainty. (See Notes 6, 8 and 16 to the accompanying consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K.)

OTTI

During 2015 we recognized OTTI charges through earnings of $705,000 against certain of our Non-Agency MBS. These impairment charges reflected changes in our estimated cash flows for such securities based on an updated assessment of the estimated future performance of the underlying collateral, including the expected principal loss over the term of the securities and changes in the expected timing of receipt of cash flows. We did not recognize any OTTI charges through earnings against our Non-Agency MBS during 2014. At December 31, 2015, we had 336 Agency MBS with a gross unrealized loss of $40.4 million, 59 RPL/NPL MBS with a gross unrealized loss of $19.3 million and 58 Legacy Non-Agency MBS with a gross unrealized loss of $9.1 million. Impairments on Agency MBS in an unrealized loss position at December 31, 2015 are considered temporary and not credit related. Unrealized losses on Non-Agency MBS for which no OTTI was recorded during the year are considered temporary based on an assessment of changes in the expected cash flows for such securities, which considers recent bond performance and expected future performance of the underlying collateral. Significant judgment is used both in our analysis of expected cash flows for our Legacy Non-Agency MBS and any determination of the credit component of OTTI. (See “Critical Accounting Policies and Estimates” for more information regarding OTTI.)

Other Income, net

For 2015, Other income, net, decreased by $3.6 million to $51.2 million from $54.8 million for 2014. Other income, net for 2015 primarily reflects $34.9 million of gross gains realized on the sale of $70.7 million Non-Agency MBS, a $17.7 million net gain recorded on residential whole loans held at fair value, and $1.8 million of net losses related to loans transferred to REO during the year. During 2014, we sold Non-Agency MBS for $123.9 million and realized gross gains of $37.5 million. In addition, the year ended 2014 included unrealized net gains and net interest income on Linked Transactions of $17.1 million, which included interest income of $24.4 million on the underlying Non-Agency MBS, interest expense of $8.0 million on borrowings under repurchase agreements and an increase of $677,000 in the fair value of the underlying securities. As previously mentioned, new accounting guidance effective on January 1, 2015 prospectively eliminated the use of Linked Transaction accounting and as a result we did not have any Linked Transactions effective January 1, 2015 (See Note 6 to the accompanying consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K).

Operating and Other Expense

For 2015, we had compensation and benefits and other general and administrative expense of $42.0 million, or 1.34% of average equity, compared to $40.7 million, or 1.26% of average equity, for 2014. Compensation and benefits expense increased $712,000 to $26.3 million for 2015, compared to $25.6 million for 2014, primarily reflecting higher costs associated with our wider residential asset strategy. Our other general and administrative expenses increased by $588,000 to $15.8 million for 2015 compared to $15.2 million for 2014. The increase was primarily due to higher IT development and related costs, data analytics and pricing services related expenses and costs associated with our attaining FHLB membership, partially offset by lower professional services related costs.

Operating and Other Expense during 2015 also includes $10.4 million of loan servicing and other related operating expenses related to our residential whole loan activities. These expenses increased compared to the prior year period by approximately $7.0 million, consistent with the overall growth in this asset class during 2015. The overall increase is primarily due to loan servicing

Table of Contents

and due diligence related expenses associated with acquisitions closed over the past year. Also included in this expense category is the impact of loan loss provisions and non-recoverable REO maintenance and other loan related expenses that are incurred in connection with our investments in this asset class.

Operating and Other Expense for 2014 also included a $1.2 million accrual of interest with respect to prior years undistributed taxable income. No such expense was incurred in 2015.

Selected Financial Ratios

The following table presents information regarding certain of our financial ratios at or for the dates presented:

At or for the Quarter Ended	Return on Average Total Assets (1)	Return on Average Total Stockholders' Equity (2)	Total Average Stockholders' Equity to Total Average Assets (3)	Dividend Payout Ratio (4)	Leverage Multiple (5)	Book Value per Share of Common Stock (6)
December 31, 2015	2.10 %	9.80 %	22.56 %	1.05	3.4	$7.47
September 30, 2015	2.22	10.21	22.85	1.00	3.3	7.70
June 30, 2015	2.16	9.78	23.18	1.00	3.3	7.96
March 31, 2015	2.25	10.26	22.97	0.95	3.3	8.13
December 31, 2014	2.44	9.91	25.78	1.00	2.8	8.12
September 30, 2014	2.41	9.62	26.27	1.00	2.7	8.28
June 30, 2014	2.38	9.25	25.69	1.00	2.8	8.37
March 31, 2014	2.30	9.10	25.27	1.00	2.9	8.20

(1) Reflects annualized net income available to common stock and participating securities divided by average total assets. The decrease for the quarter ended March 31, 2015 compared to the quarter ended December 31, 2014 is primarily due to the reclassification of $1.918 billion of MBS previously reported as a component of Linked Transactions.
(2) Reflects annualized net income divided by average total stockholders' equity.
(3) Reflects total average stockholders' equity divided by total average assets. The decrease for the quarter ended March 31, 2015 compared to the quarter ended December 31, 2014 is primarily due to the reclassification of $1.918 billion of MBS previously reported as a component of Linked Transactions.
(4) Reflects dividends declared per share of common stock divided by earnings per share.
(5) Represents the sum of borrowings under repurchase agreements, FHLB advances, securitized debt, payable for unsettled MBS purchases, and obligations to return securities obtained as collateral and Senior Notes divided by stockholders' equity. The increase in our leverage multiple for the quarter ended March 31, 2015 from the quarter ended December 31, 2014 is primarily due to the reclassification of $1.520 billion of repurchase agreements previously reported as a component of Linked Transactions.
(6) Reflects total stockholders' equity less the preferred stock liquidation preference divided by total shares of common stock outstanding.

Year Ended December 31, 2014 Compared to the Year Ended December 31, 2013

General

For 2014, we had net income available to our common stock and participating securities of $298.5 million, or $0.81 per basic and diluted common share, compared to net income available to common stock and participating securities of $285.0 million, or $0.78 per basic and diluted common share, for 2013. The increase in net income available to our common stock and participating securities, and the increase of this item on a per share basis primarily reflected an increase in unrealized net gains and net interest income from Linked Transactions, higher gains on sales of MBS partially offset by a reduction in net interest income. Yields on Agency MBS were lower for 2014 compared to 2013 and were impacted by lower coupon yields. Non-Agency MBS yields were higher compared to the prior year period due primarily to the impact of credit reserve releases. In addition, during 2013, we had $7.5 million of unrealized losses on forward contracts for the sale of Agency MBS securities on a generic pool, or to-be-announced basis (or TBA short positions), a $3.9 million write-off of issuance costs on the redemption of the Series A Preferred Stock (see Note 13 to the accompanying consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K) and a $2.0 million charge related to the impairment of resecuritization related costs. None of these items re-occurred in 2014.

Table of Contents

Net Interest Income

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends primarily upon the volume of interest-earning assets and interest-bearing liabilities and the corresponding interest rates earned or paid. Our net interest income varies primarily as a result of changes in interest rates, the slope of the yield curve (i.e., the differential between long-term and short-term interest rates), borrowing costs (i.e., our interest expense) and prepayment speeds on our MBS. Interest rates and CPRs (which measure the amount of unscheduled principal prepayment on a bond as a percentage of the bond balance), vary according to the type of investment, conditions in the financial markets, and other factors, none of which can be predicted with any certainty.

The changes in average interest-earning assets and average interest-bearing liabilities and their related yields and costs are discussed in greater detail below under “Interest Income” and “Interest Expense.”

For 2014, our net interest spread and margin were 2.40% and 2.78%, respectively, compared to a net interest spread and margin of 2.32% and 2.70%, respectively, for 2013. Although our net interest spread and margin increased, our net interest income decreased by $14.9 million, or 4.7%, to $304.0 million from $318.9 million for 2013. This decrease primarily reflected the impact of the lower average balance of our MBS portfolio as measured by amortized cost, increased Non-Agency MBS borrowing costs (including the impact of allocated Swap expense), partially offset by higher yielding Non-Agency MBS due to improved credit performance, a decrease in the average balance of securitized debt and lower Agency MBS borrowing costs. It should be noted that our reported net interest income for 2014 and 2013 excluded the interest income on Non-Agency MBS and CRT securities and the interest expense on repurchase agreements financings that had been accounted for as Linked Transactions and for which the net interest income was reported in Other income, net in our consolidated statement of operations. For 2014, the net interest earned on our investments accounted for as Linked Transactions increased by approximately $13.5 million to $16.4 million compared to $2.9 million for 2013. The net interest spread on our Agency MBS portfolio declined slightly to 1.08% for 2014 compared to 1.09% for 2013. The net interest spread on our Non-Agency MBS portfolio increased to 4.70% for 2014 compared to 4.55% for 2013.

The following table presents certain quarterly information regarding our net interest spread and net interest margin for the quarterly periods presented:

	Total Interest-Earning Assets and Interest-Bearing Liabilities	
Quarter Ended	Net Interest Spread (1)	Net Interest Margin (2)
December 31, 2014	2.41 %	2.76 %
September 30, 2014	2.32	2.70
June 30, 2014	2.42	2.80
March 31, 2014	2.44	2.84
December 31, 2013	2.34	2.75
September 30, 2013	2.24	2.63
June 30, 2013	2.38	2.73
March 31, 2013	2.32	2.69

(1) Reflected the difference between the yield on average interest-earning assets and average cost of funds.
(2) Reflected annualized net interest income divided by average interest-earning assets.

56

Table of Contents

The following table presents the components of the net interest spread earned on our Agency and Non-Agency MBS for the quarterly periods presented:

Quarter Ended	Agency MBS Net Yield (1)	Agency MBS Cost of Funding (2)	Agency MBS Net Interest Spread (3)	Non-Agency MBS Net Yield (1)	Non-Agency MBS Cost of Funding (2)	Non-Agency MBS Net Interest Spread (3)	Total MBS Net Yield (1)	Total MBS Cost of Funding (2)	Total MBS Net Interest Spread (3)
December 31, 2014	2.17 %	1.12 %	1.05 %	7.59 %	2.92 %	4.66 %	4.33 %	1.76 %	2.57 %
September 30, 2014	2.09	1.14	0.95	7.68	2.96	4.72	4.28	1.75	2.53
June 30, 2014	2.26	1.13	1.13	7.71	3.11	4.60	4.36	1.77	2.59
March 31, 2014	2.39	1.21	1.18	7.80	2.99	4.81	4.50	1.80	2.70
December 31, 2013	2.37	1.26	1.11	7.77	3.01	4.76	4.48	1.85	2.63
September 30, 2013	2.13	1.12	1.01	7.33	2.91	4.42	4.20	1.74	2.46
June 30, 2013	2.19	1.15	1.04	7.15	2.41	4.74	4.18	1.56	2.62
March 31, 2013	2.42	1.24	1.18	6.80	2.45	4.35	4.17	1.63	2.54

(1) Reflected annualized interest income on MBS divided by average amortized cost of MBS.

(2) Reflected annualized interest expense divided by average balance of repurchase agreements, including the cost of Swaps allocated based on the proportionate share of the overall estimated weighted average portfolio duration, and securitized debt. Agency cost of funding included 79, 82, 81, 85, 86 and 74 basis points and Non-Agency cost of funding included 84, 89, 88, 74, 72 and 57 basis points associated with Swaps to hedge interest rate sensitivity on these assets for the quarters ended December 31, 2014, September 30, 2014, June 30, 2014, March 31, 2014, December 31, 2013 and September 30, 2013, respectively. Agency cost of funding includes 100 and 88 basis points associated with Swaps to hedge interest rate sensitivity on these assets for the quarters ended June 30, 2013 and March 31, 2013, respectively. Non-Agency funding cost did not include any costs associated with Swaps in those periods.

(3) Reflected the difference between the net yield on average MBS and average cost of funds on MBS.

Interest Income

Interest income on our Agency MBS for 2014 decreased by $13.5 million, or 8.7% to $142.5 million from $156.0 million for 2013. This change primarily reflected a $453.0 million decrease in the average amortized cost of our Agency MBS portfolio to $6.388 billion for 2014 from $6.841 billion for 2013 and a decrease in the net yield on our Agency MBS to 2.23% for 2014 from 2.28% for 2013. At the end of 2014, the average coupon on mortgages underlying our Agency MBS was lower compared to the end of 2013, due to acquisition of assets in the marketplace at generally lower coupons and as a result of prepayments on higher yielding assets and downward resets on Hybrid and ARM-MBS within the portfolio. As a result, the coupon yield on our Agency MBS portfolio declined 17 basis points to 2.96% for 2014 from 3.13% for 2013. During 2014, our Agency MBS portfolio experienced a 13.0% CPR and we recognized a $46.8 million of net premium amortization compared to a CPR of 17.9% and $57.9 million of net premium amortization in 2013. At December 31, 2014, we had net purchase premiums on our Agency MBS of $213.3 million, or 3.8% of current par value, compared to net purchase premiums of $226.8 million, or 3.6% of par value at December 31, 2013.

Interest income on our Non-Agency MBS (which includes Non-Agency MBS transferred to consolidated VIEs) decreased $10.4 million, or 3.2%, for 2014 to $316.3 million compared to $326.8 million for 2013, primarily due to the decrease in the amortized cost of our Non-Agency MBS portfolio, partially offset by the increase in the net yield on our Non-Agency MBS portfolio. For 2014, the average amortized cost of our Non-Agency MBS (excluding Non-Agency MBS reported as a component of Linked Transactions) decreased by $399.2 million or 8.9%, to $4.108 billion, from $4.508 billion for 2013. Our Non-Agency MBS portfolio yielded 7.70% for 2014 compared to 7.25% for 2013. The increase in the yield on our Non-Agency MBS was primarily due to the impact of credit reserve releases, in the then current and prior year, that had occurred as a result of the improved credit performance of loans underlying the Legacy Non-Agency MBS portfolio. During 2014, we recognized net purchase discount accretion of $103.4 million on our Non-Agency MBS, compared to $73.2 million for 2013. At December 31, 2014, we had net purchase discounts of $1.300 billion, including Credit Reserve and previously recognized OTTI of $900.6 million, on our Non-Agency MBS, or 24.4% of par value. During 2014 we reallocated $95.0 million of purchased discount designated as Credit Reserve to accretable purchase discount.

Table of Contents

The following table presents the components of the coupon yield and net yields earned on our Agency MBS and Non-Agency MBS and weighted average CPR experienced for such MBS for the quarterly periods presented:

	Agency MBS			Non-Agency MBS			Total MBS		
Quarter Ended	Coupon Yield (1)	Net Yield (2)	3 Month Average CPR	Coupon Yield (1)	Net Yield (2)	3 Month Average CPR	Coupon Yield (1)	Net Yield (2)	3 Month Average CPR
December 31, 2014	2.91 %	2.17 %	12.34 %	5.10 %	7.59 %	12.53 %	3.78 %	4.34 %	12.43 %
September 30, 2014	2.94	2.09	15.11	5.17	7.68	12.71	3.81	4.28	13.94
June 30, 2014	2.99	2.26	13.05	5.27	7.71	12.05	3.87	4.36	12.58
March 31, 2014	3.01	2.39	11.54	5.19	7.80	11.90	3.86	4.50	11.71
December 31, 2013	3.04	2.37	12.87	5.40	7.77	14.16	3.96	4.48	13.42
September 30, 2013	3.07	2.13	19.25	5.59	7.33	18.15	4.07	4.20	18.77
June 30, 2013	3.14	2.19	20.19	5.71	7.15	16.37	4.17	4.18	18.53
March 31, 2013	3.25	2.42	19.08	5.78	6.80	15.06	4.26	4.17	17.34

(1) Reflected the annualized coupon interest income divided by the average amortized cost. The discounted purchase price on Non-Agency MBS causes the coupon yield to be higher than the pass-through coupon interest rate. (Does not include MBS underlying our Linked Transactions. See Note 6 to the accompanying consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K.)
(2) Reflected annualized interest income on MBS divided by average amortized cost of MBS.

Interest Expense

Our interest expense for 2014 decreased by $4.2 million, or 2.6% to $159.8 million, from $164.0 million for 2013. This decrease primarily reflected a decrease in the average balance of securitized debt, a decrease in our average borrowings to finance Agency MBS and the lower effective interest rate paid on borrowings to finance Agency MBS, which was partially offset by higher effective funding costs associated with Non-Agency MBS, including allocated Swap financing costs, and securitized debt.

At December 31, 2014, we had repurchase agreement borrowings of $8.267 billion of which $3.760 billion was hedged with Swaps, and securitized debt of $110.6 million. At December 31, 2014, our Swaps designated in hedging relationships had a weighted average fixed-pay rate of 1.85% and extended 47 months on average with a maximum remaining term of approximately 104 months.

The following table presents information about our securitized debt at December 31, 2014:

	At December 31, 2014	
Benchmark Interest Rate	Securitized Debt	Interest Rate
(Dollars in Thousands)		
Fixed Rate	$57,288	2.85 %
Weighted Average Coupon Rate	53,286	3.82
Total	$110,574	3.31 %

The effective interest rate paid on our borrowings increased to 1.84% for 2014 from 1.76% for 2013. This increase reflected additional higher cost financing (including the impact of allocated Swap expense) associated with our Non-Agency MBS portfolio partially offset by the lower average balance of securitized debt and Agency repurchase agreements. Payments made and/or received on our Swaps are a component of our borrowing costs and accounted for interest expense of $69.8 million or 81 basis points, for 2014, compared to interest expense of $59.0 million, or 63 basis points, for 2013. The weighted average fixed-pay rate on our Swaps decreased to 1.93% for 2014 from 2.08% for 2013. The weighted average variable interest rate received on our Swaps decreased to 0.16% for 2014 from 0.19% for 2013. During 2014, we entered into four new Swaps with an aggregate notional amount of $400.0 million, a weighted average fixed-pay rate of 1.95% with initial maturities ranging from five to seven years, and had Swaps with an aggregate notional amount of $685.0 million and a weighted average fixed-pay rate of 2.28% amortize and/or expire.

Table of Contents

The following table presents our leverage multiples, as measured by debt-to-equity, at the dates presented:

At the Period Ended	GAAP Leverage Multiple (1)	Non-GAAP Leverage Multiple (2)
December 31, 2014	2.8	3.3
September 30, 2014	2.7	3.0
June 30, 2014	2.8	2.9
March 31, 2014	2.9	3.0
December 31, 2013	2.9	3.0
September 30, 2013	3.0	3.1
June 30, 2013	3.1	3.1
March 31, 2013	3.1	3.1

(1) Represented the sum of borrowings under repurchase agreements, securitized debt, payable for unsettled MBS purchases, and obligations to return securities obtained as collateral and Senior Notes divided by stockholders' equity.
(2) The Non-GAAP Leverage Multiple reflected the sum of our borrowings under repurchase agreements, securitized debt, payable for unsettled MBS purchases, obligations to return securities obtained as collateral, Senior Notes and borrowings that were reported on our consolidated balance sheets as a component of Linked Transactions of $1.520 billion, $791.8 million, $387.5 million, $206.0 million, $102.7 million, $82.4 million, $33.2 million and $34.1 million at December 31, 2014, September 30, 2014, June 30, 2014, March 31, 2014, December 31, 2013, September 30, 2013, June 30, 2013 and March 31, 2013 respectively. We presented a Non-GAAP leverage multiple since repurchase agreement borrowings that were a component of Linked Transactions may not be linked in the future and, if no longer linked, would be reported as repurchase agreement borrowings, which would increase our leverage multiple. (See Note 6 to the accompanying consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K.)

OTTI

During 2014 and 2013, we did not recognize any OTTI charges through earnings against our Non-Agency MBS. At December 31, 2014, we had 271 Agency MBS with a gross unrealized loss of $33.6 million and 45 Non-Agency MBS and CRT securities with a gross unrealized loss of $5.8 million. Impairments on Agency MBS in an unrealized loss position at December 31, 2014 are considered temporary and not credit related. Unrealized losses on Non-Agency MBS and CRT securities for which no OTTI was recorded during the year were considered temporary based on an assessment of changes in the expected cash flows for such securities, which considered recent bond performance and expected future performance of the underlying collateral. Significant judgment was used both in the Company's analysis of expected cash flows for its Legacy Non-Agency MBS and any determination of the credit component of OTTI. (See "Critical Accounting Policies and Estimates" for more information regarding OTTI.)

Other Income, net

For 2014, Other income, net, increased by $33.0 million to $54.8 million from $21.8 million for 2013. In 2014 Other income, net primarily reflected $37.5 million of net gains realized on the sale of certain Non-Agency MBS and unrealized net gains and net interest income of $17.1 million on our Linked Transactions. In addition, during 2014 we recorded net gains on residential whole loans held at fair value of $116,000, primarily reflecting changes in market value of the underlying loans since acquisition. During 2014, we sold Non-Agency MBS for $123.9 million, realizing gross gains of $37.5 million. During 2013, we sold Non-Agency MBS for $152.6 million, and realized gross gains of $25.8 million and sold U.S. Treasury securities for $422.2 million, realizing net losses of approximately $24,000. The unrealized net gains and net interest income from Linked Transactions of $17.1 million for 2014 included interest income of $24.4 million on the underlying Non-Agency MBS, interest expense of $8.0 million on the borrowings under repurchase agreements and an increase of $677,000 in the fair value of the underlying securities. The unrealized net gains and net interest income on Linked Transactions of $3.2 million for 2013 included interest income of $3.9 million on the underlying Non-Agency MBS, interest expense of $925,000 on borrowings under repurchase agreements and an increase of $281,000 in the fair value of the underlying securities. During 2014, certain of our Linked Transactions became unlinked, resulting in our recording Non-Agency MBS with a fair value of $86.4 million on our consolidated balance sheets. The $7.5 million of losses realized on TBA short positions for 2013 reflected losses on the sale of $350.0 million notional of TBA securities.

Table of Contents

Operating and Other Expense

For 2014, we had compensation and benefits and other general and administrative expense of $40.7 million, or 1.26% of average equity, compared to $33.7 million, or 1.03% of average equity, for 2013. The $5.3 million increase in our compensation and benefits expense to $25.6 million for 2014, compared to $20.3 million for 2013, primarily reflected increases in equity-based compensation expense, salary and bonus expense, and payroll taxes. Our other general and administrative expenses increased by $1.8 million to $15.2 million for 2014 compared to $13.4 million for 2013. The increase was primarily comprised of increases in professional services, board of director expenses and the cost of data and analytical systems.

During 2014, we recorded $3.4 million of other investment related operating expenses related to our residential whole loan activities. In addition, during 2014, an interest accrual of $1.2 million was recorded, reflecting an additional accrual of interest with respect to prior years undistributed taxable income. During 2013, we recorded an excise tax and interest accrual of $2.0 million reflecting an updated estimate of excise tax payable in respect of undistributed REIT taxable income for the 2012 tax year and an additional accrual of interest with respect to prior years undistributed taxable income and recorded $250,000 reflecting an estimate of excise tax payable in respect of undistributed REIT taxable income for the 2013 tax year. In addition, for 2013, we realized a $2.0 million charge related to the impairment of resecuritization related costs.

Selected Financial Ratios

The following table presents information regarding certain of our financial ratios at or for the dates presented:

At or for the Quarter Ended	Return on Average Total Assets (1)		Return on Average Total Stockholders' Equity (2)		Total Average Stockholders' Equity to Total Average Assets (3)		Dividend Payout Ratio (4)		Book Value per Share of Common Stock (5)
December 31, 2014	2.44	%	9.91	%	25.78	%	1.00		$8.12
September 30, 2014	2.41		9.62		26.27		1.00		8.28
June 30, 2014	2.38		9.25		25.69		1.00		8.37
March 31, 2014	2.30		9.10		25.27		1.00		8.20
December 31, 2013	2.37		9.55		24.80		1.00		8.06
September 30, 2013	2.10		8.71		24.12		1.16	(6)	7.85
June 30, 2013	2.10		8.29		25.35		1.16		8.19
March 31, 2013	2.20		8.92		24.63		1.05	(7)	8.84

(1) Reflected annualized net income available to common stock and participating securities divided by average total assets.
(2) Reflected annualized net income divided by average total stockholders' equity.
(3) Reflected total average stockholders' equity divided by total average assets.
(4) Reflected dividends declared per share of common stock divided by earnings per share.
(5) Reflected total stockholders' equity less the preferred stock liquidation preference divided by total shares of common stock outstanding.
(6) Excluded the special common stock dividend declared on August 1, 2013.
(7) Excluded the special common stock dividend declared on March 4, 2013.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements include our accounts and all majority owned and controlled subsidiaries. In addition, we consolidate the special purpose entities (or SPEs) created to facilitate the resecuritization transactions completed in prior years and the acquisition of residential whole loans. The preparation of consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. In preparing these consolidated financial statements, management has made estimates and judgments of certain amounts included in the consolidated financial statements, giving due consideration to materiality. Application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates.

Our accounting policies are described in Note 2 to the consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K. Management believes the more significant of these to be as follows:

Classifications of Investment Securities and Assessment for Other-Than-Temporary Impairments

Our investments in securities are primarily comprised of Agency MBS and Non-Agency MBS, as discussed and detailed in Notes 2(b) and 3 to the consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K. All of our MBS are designated as available-for-sale (or AFS) and, accordingly, are carried on our consolidated balance sheets at their fair value with unrealized gains and losses excluded from earnings (except when an OTTI is recognized, as discussed below) and reported in AOCI, a component of Stockholders' Equity. We do not intend to hold any of our investment securities for trading purposes; however, if available-for-sale securities were classified as trading securities, there could be substantially greater volatility in our earnings.

When the fair value of an AFS security is less than its amortized cost at the balance sheet date, the security is considered impaired. We assess our impaired securities on at least a quarterly basis and designate such impairments as either "temporary" or "other-than-temporary." If we intend to sell an impaired security, or it is more likely than not that we will be required to sell the impaired security before its anticipated recovery, then we must recognize an OTTI through charges to earnings equal to the entire difference between the investment's amortized cost and its fair value at the balance sheet date. If we do not expect to sell an other-than-temporarily impaired security, only the portion of the OTTI related to credit losses is recognized through charges to earnings with the remainder recognized through AOCI on the consolidated balance sheets.

In making our assessments about OTTIs, we review and consider certain information relating to our financial position and the impaired securities, including the nature of such securities, the contractual collateral requirements impacting us and our investment and leverage strategies, as well as subjective information, including our current and targeted liquidity position, the credit quality and expected cash flows of the underlying assets collateralizing such securities, and current and anticipated market conditions. In determining the OTTI related to credit losses for securities that were purchased at significant discounts to par and/or are considered to be of less than high credit quality, we compare the present value of the remaining cash flows expected to be collected at the purchase date (or last date previously revised) against the present value of the cash flows expected to be collected at the current financial reporting date. The determination as to whether an OTTI exists and, if so, the amount of credit impairment recognized in earnings is subjective, as such determinations are based on factual information available at the time of assessment as well as management's estimates of the future performance and cash flow projections. As a result, the timing and amount of OTTIs constitute material estimates that may be susceptible to significant change.

During 2015, we recognized credit-related OTTI losses through earnings related to our Non-Agency MBS of $705,000. At December 31, 2015, we did not intend to sell any MBS that were in an unrealized loss position, and it is "more likely than not" that we will not be required to sell these MBS before recovery of their amortized cost basis, which may be at their maturity.

Gross unrealized losses on our Agency MBS were $40.4 million at December 31, 2015. Agency MBS are issued by GSEs and enjoy either the implicit or explicit backing of the full faith and credit of the U.S. Government. While our Agency MBS are not rated by any rating agency, they are currently perceived by market participants to be of high credit quality, with risk of default limited to the unlikely event that the U.S. Government would not continue to support the GSEs. Given the credit quality inherent in Agency MBS, we do not consider any of the current impairments on our Agency MBS to be credit related. In assessing whether it is more likely than not that we will be required to sell any impaired security before its anticipated recovery, which may be at its maturity, we consider for each impaired security, the significance of each investment, the amount of impairment, the projected future performance of such impaired securities, as well as our current and anticipated leverage capacity and liquidity position. Based on these analyses, we determined that at December 31, 2015 any unrealized losses on our Agency MBS were temporary.

The payments of principal and interest we receive on our Agency MBS, which depend directly upon payments on the mortgages underlying such securities, are guaranteed by Fannie Mae, Freddie Mac and Ginnie Mae. Fannie Mae and Freddie Mac are GSEs, but their guarantees are not explicitly backed by the full faith and credit of the United States. Ginnie Mae is part of a U.S. Government agency and its guarantees are explicitly backed by the full faith and credit of the United States. We believe that the stronger backing for the guarantors of Agency MBS resulting from the conservatorship of Fannie Mae and Freddie Mac has further strengthened their credit worthiness; however, there can be no assurance that these actions will be adequate for their needs. Accordingly, if these government actions are inadequate and the GSEs suffer losses in the future or cease to exist, our view of the credit worthiness of our Agency MBS could materially change, which may affect our assessment of OTTI for Agency MBS in future periods. (See Part I, Item 1A., Risk Factors, "The federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government, may materially adversely affect our business.")

Unrealized losses on our Non-Agency MBS (including Non-Agency MBS transferred to consolidated VIEs) were $28.4 million, of which $19.3 million were RPL/NPL MBS and $9.1 million were Legacy Non-Agency MBS at December 31, 2015. Based upon the most recent evaluation, we do not consider these unrealized losses to be indicative of OTTI and do not believe

Table of Contents

that these unrealized losses are credit related, but are rather a reflection of current market yields and/or market place bid-ask spreads. We have reviewed our Non-Agency MBS that are in an unrealized loss position to identify those securities with losses that are other-than-temporary based on an assessment of changes in expected cash flows for such securities, which considers recent bond performance, where possible, and expected future performance of the underlying collateral.

Our expectations with respect to our securities in an unrealized loss position may change over time, given, among other things, the dynamic nature of markets and other variables. Future sales or changes in our expectations with respect to securities in an unrealized loss position could result in us recognizing OTTI charges or realizing losses on sales of MBS in the future. (See Notes 2(b) and 3 to the consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K.)

Fair Value Measurements

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels of valuation hierarchy are defined as follows:

Level 1 — inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 — inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 — inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The following describes the valuation methodologies used for our financial instruments measured at fair value on a recurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Securities Obtained and Pledged as Collateral/Obligation to Return Securities Obtained as Collateral

The fair value of U.S. Treasury securities obtained as collateral and the associated obligation to return securities obtained as collateral are based upon prices obtained from a third-party pricing service, which are indicative of market activity. Securities obtained as collateral are classified as Level 1 in the fair value hierarchy.

MBS and CRT Securities

We determine the fair value of our Agency MBS, based upon prices obtained from third-party pricing services, which are indicative of market activity and repurchase agreement counterparties.

For Agency MBS, the valuation methodology of our third-party pricing services incorporate commonly used market pricing methods, trading activity observed in the market place and other data inputs. The methodology also considers the underlying characteristics of each security, which are also observable inputs, including: collateral vintage, coupon, maturity date, loan age, reset date, collateral type, periodic and life cap, geography, and prepayment speeds. Management analyzes pricing data received from third-party pricing services and compares it to other indications of fair value including data received from repurchase agreement counterparties and its own observations of trading activity observed in the market place.

In determining the fair value of our Non-Agency MBS and CRT securities, management considers a number of observable market data points, including prices obtained from pricing services and brokers as well as dialogue with market participants. In valuing Non-Agency MBS, we understand that pricing services use observable inputs that include, in addition to trading activity observed in the market place, loan delinquency data, credit enhancement levels and vintage, which are taken into account to assign pricing factors such as spread and prepayment assumptions. For tranches of Legacy Non-Agency MBS that are cross-collateralized, performance of all collateral groups involved in the tranche are considered. We collect and consider current market intelligence on all major markets, including benchmark security evaluations and bid-lists from various sources, when available.

Our MBS and CRT securities are valued using various market data points as described above, which management considers directly or indirectly observable parameters. Accordingly, our MBS and CRT securities are classified as Level 2 in the fair value hierarchy.

Residential Whole Loans, at Fair Value

We determine the fair value of our residential whole loans held at fair value after considering portfolio valuations obtained from a third-party who specializes in providing valuations of residential mortgage loans and trading activity observed in the market place. The Company's residential whole loans held at fair value are classified as Level 3 in the fair value hierarchy.

Swaps

We determine the fair value of our non-centrally cleared Swaps considering valuations obtained from a third-party pricing service. For Swaps that are cleared by a central clearing house, valuations provided by the clearing house are used. All valuations obtained are tested with internally developed models that apply readily observable market parameters. We consider the creditworthiness of both us and our counterparties, along with collateral provisions contained in each derivative agreement, from the perspective of both us and our counterparties. All of our Swaps are subject either to bilateral collateral arrangements, or for cleared Swaps, to the clearing house's margin requirements. Consequently, no credit valuation adjustment was made in determining the fair value of such instruments. Our Swaps are classified as Level 2 in the fair value hierarchy.

Interest Income on our Non-Agency MBS

Interest income on the Non-Agency MBS that were purchased at a discount to par value and/or are considered to be of less than high credit quality is recognized based on the security's effective interest rate which is the security's IRR. The IRR is determined using management's estimate of the projected cash flows for each security, which are based on our observation of current information and events and include assumptions related to fluctuations in interest rates, prepayment speeds and the timing and amount of credit losses. On at least a quarterly basis, we review and, if appropriate, make adjustments to our cash flow projections based on input and analysis received from external sources, internal models, and our judgment about interest rates, prepayment rates, the timing and amount of credit losses, and other factors. Changes in cash flows from those originally projected, or from those estimated at the last evaluation, may result in a prospective change in the IRR/interest income recognized on these securities or in the recognition of OTTIs.

Based on the projected cash flows for our Non-Agency MBS purchased at a discount to par value, a portion of the purchase discount may be designated as Credit Reserve, which effectively mitigates our risk of loss on the mortgages collateralizing such MBS and is not expected to be accreted into interest income. The amount designated as Credit Reserve may be adjusted over time, based on the actual performance of the security, its underlying collateral, actual and projected cash flow from such collateral, economic conditions and other factors. If the performance of a security with a Credit Reserve is more favorable than forecasted, a portion of the amount designated as Credit Reserve may be reallocated to accretable discount and recognized into interest income over time. Conversely, if the performance of a security with a Credit Reserve is less favorable than forecasted, the amount designated as Credit Reserve may be increased, or impairment charges and write-downs of such securities to a new cost basis could result.

Residential Whole Loans

Residential whole loans included in our consolidated balance sheets are generally comprised of pools of fixed and adjustable rate residential mortgage loans acquired through consolidated trusts in secondary market transactions at discounted purchase prices. The accounting model utilized by us is determined at the time each loan package is initially acquired and is generally based on the delinquency status of the majority of the underlying borrowers in the package at acquisition. The accounting model described below under "Residential Whole Loans at Carrying Value" is typically utilized by us for loans where the underlying borrower has a delinquency status of less than 60 days at the acquisition date. The accounting model described below under “Residential Whole Loans at Fair Value” is typically utilized by us for loans where the underlying borrower has a delinquency status of 60 days or more at the acquisition date. The accounting model initially applied is not subsequently changed.

Our residential whole loans pledged as collateral against repurchase agreements are included in the consolidated balance sheets with the fair value of the loans pledged disclosed parenthetically. Purchases and sales of residential whole loans are recorded on the trade date, with amounts recorded reflecting management’s current estimate of assets that will be acquired or disposed at the closing of the transaction. This estimate is subject to revision at the closing of the transaction, pending the outcome of due diligence performed prior to closing.

Table of Contents

Residential Whole Loans at Carrying Value

Notwithstanding that majority of these loans are considered to be performing substantially in accordance with their current contractual terms and conditions, we have elected to account for these loans as credit impaired as they were acquired at discounted prices that reflect, in part, the impaired credit history of the borrower. Substantially all of the borrowers have previously experienced payment delinquencies and the amount owed on the mortgage loan may exceed the value of the property pledged as collateral. Consequently, we have assessed that these loans have a higher likelihood of default than newly originated mortgage loans with LTVs of 80% or less to credit worthy borrowers. We believe that amounts paid to acquire these loans represent fair market value at the date of acquisition. Such loans are initially recorded at fair value with no allowance for loan losses. Subsequent to acquisition, the recorded amount reflects the original investment amount, plus accretion of interest income, less principal and interest cash flows received. These loans are presented on our consolidated balance sheets at carrying value, which reflects the recorded amount reduced by any allowance for loan losses established subsequent to acquisition.

Under the application of this accounting model we may aggregate into pools loans acquired in the same fiscal quarter that are assessed as having similar risk characteristics. For each pool established, or on an individual loans basis for loans not aggregated into pools, we estimate at acquisition and periodically on at least a quarterly basis, the principal and interest cash flows expected to be collected. The difference between the cash flows expected to be collected and the carrying amount of the loans is referred to as the “accretable yield.” This amount is accreted as interest income over the life of the loans using an effective interest rate (level yield) methodology. Interest income recorded each period reflects the amount of accretable yield recognized and not the coupon interest payments received on the underlying loans. The difference between contractually required principal and interest payments and the cash flows expected to be collected, referred to as the “non-accretable difference,” and includes estimates of both the effect of prepayments and expected credit losses over the life of the underlying loans.

A decrease in expected cash flows in subsequent periods may indicate impairment at the pool and/or individual loan level thus requiring the establishment of an allowance for loan losses by a charge to the provision for loan losses. The allowance for loan losses represents the present value of cash flows expected at acquisition, adjusted for any increases due to changes in estimated cash flows that are subsequently no longer expected to be received at the relevant measurement date. A significant increase in expected cash flows in subsequent periods first reduces any previously recognized allowance for loan losses and then will result in a recalculation in the amount of accretable yield. The adjustment of accretable yield due to a significant increase in expected cash flows is accounted for prospectively as a change in estimate and results in reclassification from non-accretable difference to accretable yield.

Residential Whole Loans at Fair Value

Certain of our residential whole loans are presented at fair value on our consolidated balance sheets as a result of a fair value election made at time of acquisition. Given the significant uncertainty associated with estimating the timing of and amount of cash flows associated with these loans that will be collected, and that the cash flows ultimately collected may be dependent on the value of the property securing the loan, we consider that accounting for these loans at fair value should result in a better reflection over time of the economic returns from these loans. We determine the fair value of our residential whole loans held at fair value after considering portfolio valuations obtained from a third-party who specializes in providing valuations of residential mortgage loans and trading activity observed in the market place. Subsequent changes in fair value are reported in current period earnings and presented in Net gain on residential whole loans held at fair value on our consolidated statements of operations.

Cash received reflecting coupon payments on residential whole loans held at fair value is not included in Interest Income, but rather is presented in Net gain on residential whole loans held at fair value on our consolidated statements of operations.

Hedging Activities

We may use a variety of derivative instruments to economically hedge a portion of our exposure to market risks, including interest rate risk and prepayment risk. The objective of our risk management strategy is to reduce fluctuations in net book value over a range of interest rate scenarios. In particular, we attempt to mitigate the risk of the cost of our variable rate liabilities increasing during a period of rising interest rates. Our derivative instruments are currently comprised of Swaps, which are designated as cash flow hedges against the interest rate risk associated with certain of our borrowings. Prior to 2015, our derivative financial instruments also included Linked Transactions, which were not designated as hedging instruments. New accounting guidance that was effective for us on January 1, 2015 prospectively eliminated the use of Linked Transaction accounting. During 2013, we also entered into TBA short positions which were not designated as hedging instruments.

Table of Contents

Our Swaps designated as hedging transactions have the effect of modifying the repricing characteristics of our repurchase agreements and cash flows for such liabilities. Under each Swap, we agree to pay a fixed rate of interest and receive a variable interest rate, generally based on one-month or three-month LIBOR, on the notional amount of the Swap. We document our risk-management policies, including objectives and strategies, as they relate to our hedging activities and the relationship between the hedging instrument and the hedged liability for all Swaps designated as hedging transactions. We assess, both at inception of a hedge and on a quarterly basis thereafter, whether or not the hedge relationship is "highly effective."

We discontinue hedge accounting on a prospective basis and recognize changes in the fair value of the derivative through earnings when: (i) it is determined that the derivative is no longer effective in offsetting cash flows of a hedged item (including forecasted transactions); (ii) it is no longer probable that the forecasted transaction will occur; or (iii) it is determined that designating the derivative as a hedge is no longer appropriate.

Swaps are carried on our consolidated balance sheets at fair value, as assets, if their fair value is positive, or as liabilities, if their fair value is negative. Changes in the fair value of our Swaps designated in hedging transactions are recorded in OCI provided that the hedge remains effective. Changes in fair value for any ineffective amount of a Swap are recognized in earnings. We have not recognized any change in the value of our existing Swaps designated as hedges through earnings as a result of hedge ineffectiveness.

During 2013, we entered into TBA short positions as a means of managing interest rate risk and MBS basis risk associated with our investment and financing activities. A TBA short position is a forward contract for sale of Agency MBS at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date. The specific Agency MBS that could be delivered into the contract upon the settlement date, published each month by the Securities Industry and Financial Markets Association (or SIFMA), are not known at the time of the transaction.

TBA short positions were accounted for as derivative instruments since we could not assert that it was probable at inception and throughout the term of the TBA contract that we would physically deliver the Agency security upon settlement of the contract. TBA short positions were presented as either derivative assets or liabilities, at fair value on our consolidated balance sheets. Gains and losses associated with TBA short positions were reported in Other income, net on our consolidated statements of operations.

Although permitted under certain circumstances, we do not offset cash collateral receivables or payables against our net derivative positions.

Income Taxes

We believe that we operate in, and intend to continue to operate in, a manner that allows and will continue to allow us to be taxed as a REIT. Provided that we distribute all of our REIT taxable income (including net long-term capital gains) to stockholders in the timeframe permitted by the Code, we do not generally expect to pay corporate level taxes and/or excise taxes. However, such taxes may arise from time to time in the normal course of our business. Many of the REIT requirements, however, are highly technical and complex. In addition, REIT taxable income calculated at the time our financial statements are prepared is based on certain estimates that may be revised as our tax return, which is not required to be filed until September in the following year, is completed. If we were to fail to meet certain of the REIT requirements, we would be subject to U.S. federal, state and local income taxes.

In addition, we have elected to treat certain of our subsidiaries as a TRS. In general, a TRS may hold assets and engage in activities that we cannot hold or engage in directly and generally may engage in any real estate or non-real estate-related business. Generally, a TRS is subject to U.S. federal, state and local corporate income taxes. Since a portion of our business may be conducted through one or more TRS, our income earned by TRS may be subject to corporate income taxation. To maintain our REIT election, no more than 25% (or, for 2018 and subsequent taxable years, 20%) of the value of a REIT's assets at the end of each quarter may consist of stock or securities in a TRS. For purposes of the determination of U. S. federal and state income taxes, the Company's subsidiaries that elected to be treated as a TRS record current or deferred income taxes based on differences (both permanent and timing) between the determination of their taxable income and net income under GAAP. No deferred tax benefit was recorded by the Company in 2015 or 2014, as a valuation allowance for the full amount of the associated deferred tax asset was recognized as its recovery is not considered more likely than not.

Table of Contents

Accounting for Stock-Based Compensation

We expense our equity-based compensation awards that are subject to vesting conditions, ratably over the vesting period of such awards, based upon the fair value of such awards at the grant date. Compensation expense for equity-based awards is recorded net of estimated forfeitures expected to occur over the vesting period. (See Notes 2(l) and 15 to the consolidated financial statements, included under Item 8 of this Annual Report on Form 10-K.)

During 2010, we granted certain RSUs that vested after either two or four years of service and provided that certain criteria were met, which were based on a formula that included changes in our closing stock price over a two- or four-year period and dividends declared on our common stock during those periods. From 2011 through 2013, we granted certain RSUs that vested annually over a one or three-year period, provided that certain criteria were met, which were based on a formula tied to our achievement of average total stockholder return during that three-year period. During 2014 and 2015, we made grants of RSUs certain of which cliff vest after a three-year period and certain of which cliff vest after a three-year period, subject to the achievement of certain performance criteria, based on a formula tied to our achievement of average total stockholder return during that three-year period. The features in these awards related to the attainment of total stockholder return over a specified period constitute a "market condition" which impacts the amount of compensation expense recognized for these awards. Specifically, the uncertainty regarding the achievement of the market condition was reflected in the grant date fair valuation of the RSUs, which in addition to estimates regarding the amount of RSUs expected to be forfeited during the associated service period, determined the amount of compensation expense recognized. The amount of compensation expense recognized was not dependent on whether the market condition was or will be achieved, while differences in actual forfeiture experience relative to estimated forfeitures results in adjustments to the timing and amount of compensation expense recognized.

We have awarded dividend equivalents that may be granted as a separate instrument or may be a right associated with the grant of another equity-based award. Compensation expense for separately awarded dividend equivalents is based on the grant date fair value of such awards and is recognized over the vesting period. Payments pursuant to these dividend equivalents are charged to Stockholders' Equity. Payments pursuant to dividend equivalents that are attached to equity-based awards are charged to Stockholders' Equity to the extent that the attached equity awards are expected to vest. Compensation expense is recognized for payments made for dividend equivalents to the extent that the attached equity awards do not or are not expected to vest and grantees are not required to return payments of dividends or dividend equivalents to the Company.

RECENT ACCOUNTING STANDARDS TO BE ADOPTED IN FUTURE PERIODS

Financial Instruments - Overall - Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued Accounting Standards Update (or ASU) 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (or ASU 2016-01).The amendments in this ASU affect all entities that hold financial assets or owe financial liabilities, and address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The classification and measurement guidance of investments in debt securities and loans are not affected by the amendments in this ASU. ASU 2016-01 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. Early adoption is not permitted for public business entities, except for a provision related to financial statements of fiscal years or interim periods that have not yet been issued, to recognize in other comprehensive income, the change in fair value of a liability resulting from a change in the instrument-specific credit risk measured using the fair value option. Entities should apply the amendments in this ASU by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption. We are currently evaluating the effect that ASU 2016-01 will have on our consolidated financial statements and related disclosures.

Interest - Imputation of Interest - Simplifying the Presentation of Debt Issuance Costs

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs (or ASU 2015-03). The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with the presentation of debt issued at a discount. The recognition and measurement guidance of debt issuance costs are not affected by the amendments in this ASU. ASU 2015-03 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted for financial statements that have not previously been issued and entities should apply the new guidance on a retrospective basis. We do not expect adoption of ASU 2015-03 to have a significant impact on our financial position or financial statement disclosures.

Table of Contents

Consolidation - Amendments to the Consolidation Analysis

In February 2015, the FASB issued ASU 2015-02, Amendments to the Consolidation Analysis (or ASU 2015-02). The amendments in this ASU change the way reporting enterprises evaluate whether (a) they should consolidate limited partnerships and similar entities, (b) fees paid to a decision maker or service provider are variable interests in a VIE, and (c) variable interests in a VIE held by related parties of the reporting enterprise require the reporting enterprise to consolidate the VIE. It also eliminates the VIE consolidation model based on majority exposure to variability that applied to certain investment companies and similar entities. ASU 2015-02 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. At the effective date, all previous consolidation analyses that the guidance affects must be reconsidered. Early adoption is permitted, including adoption in an interim period. If an entity adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. A reporting entity may apply the amendments in this ASU using a modified retrospective approach by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption. A reporting entity also may apply the amendments retrospectively. We are currently evaluating the effect that ASU 2015-02 will have on our consolidated financial statements and related disclosures. While we have not yet selected a transition method, we do not expect adoption of ASU 2015-2 to have a significant impact on our financial position.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (or ASU 2014-09). The ASU requires an entity to recognize revenue in an amount that reflects the consideration to which it expects to be entitled for the transfer of promised goods or services to customers. ASU 2014-09 will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. ASU 2014-09 originally would have been effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2016. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. On April 29, 2015, the FASB proposed a one-year deferral of the effective date for ASU 2014-09. On July 9, 2015 the FASB affirmed its proposal to defer the effective date of the new revenue standard for all entities by one year. As a result, public entities would apply the new revenue standard to annual reporting periods beginning after December 15, 2017 and interim periods therein. The FASB would also permit entities to adopt the standard early, but not before the original public entity effective date. We are currently evaluating the effect that ASU 2014-09 will have on our consolidated financial statements and related disclosures. We have not yet selected a transition method nor have we determined the effect of the standard on our ongoing financial reporting.

Presentation of Financial Statements - Going Concern

In August 2014, the FASB issued ASU 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern (or ASU 2014-15). The amendments in this ASU provide guidance in GAAP about management's responsibility to evaluate whether there is a substantial doubt about an entity's going concern and to provide related footnote disclosures. In connection with preparing financial statements for each annual and interim reporting period, an entity's management should evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or within one year after the date that the financial statements are available to be issued when applicable). The amendments in ASU 2014-15 are effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. We do not expect adoption of ASU 2014-15 to have a significant impact on our financial position or financial statement disclosures.

LIQUIDITY AND CAPITAL RESOURCES

Our principal sources of cash generally consist of borrowings under repurchase agreements and other collateralized financings, payments of principal and interest we receive on our MBS portfolio, cash generated from our operating results and, to the extent such transactions are entered into, proceeds from capital market and structured financing transactions. Our most significant uses of cash are generally to pay principal and interest on our financing transactions, to purchase MBS and residential whole loans, to make dividend payments on our capital stock, to fund our operations and to make other investments that we consider appropriate.

We seek to employ a diverse capital raising strategy under which we may issue capital stock and other types of securities. To the extent we raise additional funds through capital market transactions, we currently anticipate using the net proceeds from such transactions to acquire additional MBS and residential whole loans, consistent with our investment policy, and for working capital, which may include, among other things, the repayment of our financing transactions. There can be no assurance, however, that we will be able to access the capital markets at any particular time or on any particular terms. We have available for issuance an unlimited amount (subject to the terms and limitations of our charter) of common stock, preferred stock, depositary shares representing preferred stock, warrants, debt securities, rights and/or units pursuant to our automatic shelf registration statement and, at December 31, 2015, we had 6.8 million shares of common stock available for issuance pursuant to our DRSPP shelf registration statement. During 2015, we issued 162,373 shares of common stock through our DRSPP, raising net proceeds of approximately $1.2 million.

On April 15, 2013, we completed the issuance of 8.0 million shares of our Series B Preferred Stock with a par value of $0.01 per share and a liquidation preference of $25.00 per share plus accrued and unpaid dividends, in an underwritten public offering. The aggregate net proceeds to us from the offering of the Series B Preferred Stock were approximately $193.3 million, after deducting the underwriting discount and related offering expenses. We used a portion of the net proceeds to redeem all of our outstanding Series A Preferred Stock (as discussed below), and used the remaining net proceeds of the offering for general corporate purposes, including, without limitation, to acquire additional MBS consistent with our investment policy, and for working capital, which included, among other things, the repayment of our repurchase agreements.

On May 16, 2013, we redeemed all 3,840,000 outstanding shares of our Series A Preferred Stock at an aggregate redemption price of approximately $97.0 million, or $25.27153 per share, including all accrued and unpaid dividends to the Redemption Date. The redemption value of the Series A Preferred Stock exceeded its carrying value by $3.9 million, which represents the original offering costs for the Series A Preferred Stock.

Our borrowings under repurchase agreements are uncommitted and renewable at the discretion of our lenders and, as such, our lenders could determine to reduce or terminate our access to future borrowings at virtually any time. The terms of the repurchase transaction borrowings under our master repurchase agreements, as such terms relate to repayment, margin requirements and the segregation of all securities that are the subject of repurchase transactions, generally conform to the terms contained in the standard master repurchase agreement published by SIFMA or the global master repurchase agreement published by SIFMA and the International Capital Market Association. In addition, each lender typically requires that we include supplemental terms and conditions to the standard master repurchase agreement. Typical supplemental terms and conditions, which differ by lender, may include changes to the margin maintenance requirements, required haircuts (as defined below), purchase price maintenance requirements, requirements that all controversies related to the repurchase agreement be litigated in a particular jurisdiction and cross default and setoff provisions.

With respect to margin maintenance requirements for repurchase agreements with Non-Agency MBS as collateral, margin calls are typically determined by our counterparties based on their assessment of changes in the fair value of the underlying collateral and in accordance with the agreed upon haircuts specified in the transaction confirmation with the counterparty. We address margin call requests in accordance with the required terms specified in the applicable repurchase agreement and such requests are typically satisfied by posting additional cash or collateral on the same business day. We review margin calls made by counterparties and assess them for reasonableness by comparing the counterparty valuation against our valuation determination. When we believe that a margin call is unnecessary because our assessment of collateral value differs from the counterparty valuation, we typically hold discussions with the counterparty and are able to resolve the matter. In the unlikely event that resolution cannot be reached, we will look to resolve the dispute based on the remedies available to us under the terms of the repurchase agreement, which in some instances may include the engagement of a third party to review collateral valuations. For other agreements that do not include such provisions, we could resolve the matter by substituting collateral as permitted in accordance with the agreement or otherwise request the counterparty to return the collateral in exchange for cash to unwind the financing.

Table of Contents

The following table presents information regarding the margin requirements, or the percentage amount by which the collateral value is contractually required to exceed the loan amount (this difference is referred to as the "haircut"), on our repurchase agreements at December 31, 2015 and December 31, 2014:

At December 31, 2015	Weighted Average Haircut		Low		High	
Repurchase agreement borrowings secured by:						
Agency MBS	4.67	%	3.00	%	6.00	%
Legacy Non-Agency MBS	25.42		10.00		63.50	
RPL/NPL MBS	21.37		20.00		30.00	
U.S. Treasury securities	1.60		1.00		2.00	
CRT securities	25.04		20.00		30.00	
Residential whole loans	27.69		25.00		36.00	

At December 31, 2014	Weighted Average Haircut		Low		High	
Repurchase agreement borrowings secured by:						
Agency MBS	4.79	%	3.00	%	6.00	%
Legacy Non-Agency MBS	28.88		10.00		60.00	
RPL/NPL MBS	20.00		20.00		20.00	
U.S. Treasury securities	1.62		1.00		2.00	
CRT securities	25.00		25.00		25.00	
Residential whole loans	33.43		30.00		35.00	

The weighted average haircut requirements for the respective underlying collateral types for our repurchase agreements have not significantly changed since December 31, 2014, with the exception of Residential whole loans and Legacy Non-Agency MBS. During 2015, the Company has increased the number of counterparties providing repurchase agreement financing for residential whole loans resulting in a lower overall weighted average haircut. The decrease in the weighted average haircut for Legacy Non-Agency MBS results from the unwind during 2015 of certain re-securitization transactions and subsequent refinancing of the underlying MBS at lower haircut levels.

During 2015, the financial market environment was impacted by continued accommodative monetary policy. Repurchase agreement funding for both Agency MBS and Non-Agency MBS has been available to us at generally attractive market terms from multiple counterparties. Typically, due to the credit risk inherent to Non-Agency MBS, repurchase agreement funding involving Non-Agency MBS is available from fewer counterparties, at terms requiring higher collateralization and higher interest rates, than repurchase agreement funding secured by Agency MBS and U.S. Treasury securities. Therefore, we generally expect to be able to finance our acquisitions of Agency MBS on more favorable terms than financing for Non-Agency MBS.

In July 2015, our wholly-owned subsidiary, MFA Insurance became a member of the FHLB. As a member of the FHLB, MFA Insurance had access to a variety of products and services offered by the FHLB, including secured advances (subject to our continued creditworthiness, pledging of sufficient eligible collateral to secure advances, and compliance with certain agreements with the FHLB). The weighted average haircut on our FHLB advances at December 31, 2015 was 7.00%. However, in January, 2016, the FHFA amended its regulation on FHLB membership, which, among other things, provided termination rules for current captive insurance members. As a result, MFA Insurance will not be permitted new advances or renewal of existing advances and will be required to terminate its FHLB membership and repay any outstanding advances by no later than February 19, 2017. As of December 31, 2015 and February 16, 2016, MFA Insurance had approximately $1.500 billion and $1.200 billion, respectively, in outstanding advances (backed by Agency MBS).

We maintain cash and cash equivalents, unpledged Agency and Non-Agency MBS and collateral in excess of margin requirements held by our counterparties (or collectively, “cash and other unpledged collateral”) to meet routine margin calls and protect against unforeseen reductions in our borrowing capabilities. Our ability to meet future margin calls will be impacted by our ability to use cash or obtain financing from unpledged collateral, which can vary based on the market value of such collateral, our cash position and margin requirements. Our cash position fluctuates based on the timing of our operating, investing and

Table of Contents

financing activities and is managed based on our anticipated cash needs. (See "Interest Rate Risk" included under Item 7A. of this Annual Report on Form 10-K and our Consolidated Statements of Cash Flows, included under Item 8 of this Annual Report on Form 10-K.)

At December 31, 2015, we had a total of $11.339 billion of MBS, U.S. Treasury securities, CRT securities and residential whole loans and $71.5 million of restricted cash pledged against our repurchase agreements and Swaps. In addition, at December 31, 2015, we had $1.612 billion of Agency MBS pledged against our FHLB advances. At December 31, 2015 we have access to various sources of liquidity which we estimate exceeds $571.0 million. This includes (i) $165.0 million of cash and cash equivalents; (ii) $241.7 million in estimated financing available from unpledged Agency MBS and other Agency MBS collateral that is currently pledged in excess of contractual requirements; and (iii) $164.3 million in estimated financing available from unpledged Non-Agency MBS.

The table below presents certain information about our borrowings under repurchase agreements and other advances, and securitized debt:

	Repurchase Agreements and Other Advances			Securitized Debt		
Quarter Ended (1)	Quarterly Average Balance	End of Period Balance	Maximum Balance at Any Month-End	Quarterly Average Balance	End of Period Balance	Maximum Balance at Any Month-End
(In Thousands)						
December 31, 2015	$9,428,224	$9,388,902	$ 9,413,189	$28,252	$22,057	$ 27,927
September 30, 2015	9,422,882	9,475,834	9,475,834	51,021	32,217	50,269
June 30, 2015	9,720,193	9,635,036	9,746,825	80,754	62,320	80,744
March 31, 2015	9,820,548 (2)	9,809,586 (2)	9,863,779 (2)	103,688	91,280	104,299
December 31, 2014	8,190,491	8,267,388	8,271,123	137,503	110,574	138,026
September 30, 2014	8,267,905	8,125,723	8,272,039	190,753	156,276	190,423
June 30, 2014	8,464,135	8,384,101	8,501,978	264,806	214,048	267,740
March 31, 2014	8,412,045	8,606,129	8,606,129	336,893	292,526	338,965
December 31, 2013	8,462,138	8,339,297	8,504,593	399,762	366,205	398,384
September 30, 2013	8,679,410	8,568,171	8,721,573	440,665	419,693	462,207
June 30, 2013	8,842,018	8,909,283	8,909,283	505,409	443,748	508,893
March 31, 2013	8,873,852	8,902,827	8,956,951	606,858	542,014	609,707

(1) The information presented in the table above excludes Senior Notes issued in April 2012. The outstanding balance of Senior Notes has been unchanged at $100.0 million since issuance.
(2) The increase from December 31, 2014 reflects the reclassification of $1.520 billion of repurchase agreements previously presented as components of Linked Transactions. New accounting guidance that was effective on January 1, 2015 prospectively eliminated the use of Linked Transaction accounting and as a result we did not have any Linked Transactions effective January 1, 2015.

Cash Flows and Liquidity For the Year Ended December 31, 2015

Our cash and cash equivalents decreased by $17.4 million during the year ended December 31, 2015, reflecting: $849.7 million used by our financing activities; $550.1 million provided by our investing activities, primarily from payments on our MBS; and $282.2 million provided by our operating activities.

At December 31, 2015, our debt-to-equity multiple was 3.4 times compared to 2.8 times at December 31, 2014. After adjusting the reported debt-to-equity ratio at December 31, 2014 to reflect new accounting standards that became effective January 1, 2015, which eliminated Linked Transaction accounting and resulted in the reclassification of $1.520 billion of liabilities relating to repurchase agreements that had been previously reported as a component of Linked Transactions, the debt to equity ratio at December 31, 2014 would have been 3.3 times. At December 31, 2015, we had borrowings under repurchase agreements of $7.889 billion with 27 counterparties, of which $2.728 billion was secured by Agency MBS, $1.960 billion was secured by Legacy Non-Agency MBS, $2.080 billion was secured by RPL/NPL MBS, $504.8 million was secured by U.S. Treasuries, $128.5 million was secured by CRT securities and $487.8 million were secured by residential whole loans. We continue to have available capacity under our repurchase agreement credit lines. At December 31, 2014, we had borrowings under repurchase agreements of $8.267

Table of Contents

billion with 25 counterparties of which $5.178 billion was secured by Agency MBS, $2.233 billion was secured by Legacy Non-Agency MBS, $130.9 million was secured by RPL/NPL MBS, $507.1 million was secured by U.S. Treasuries, $76.0 million was secured by CRT securities and $142.3 million were secured by residential whole loans.

As of December 31, 2015 and February 16, 2016, we had approximately $1.500 billion and $1.200 billion, respectively, in outstanding secured FHLB advances, which had a weighted average term to maturity of 4.79 years. As a result of the previously mentioned final FHFA rule released in January, 2016, MFA Insurance will be required to terminate its FHLB membership and repay the outstanding advances within one year of the rule's effective date of February 19, 2016.

At December 31, 2015, outstanding securitized debt was $22.1 million, which had a weighted average expected remaining term of 0.35 years. During the year ended December 31, 2015, securitized debt was reduced by principal payments of $88.3 million.

During 2015, we received $550.1 million through our investing activities. We received cash of $2.917 billion from prepayments and scheduled amortization on our MBS, of which $1.857 billion was from Non-Agency MBS and $1.060 billion was attributable to Agency MBS. We purchased $1.734 billion of Non-Agency MBS and $76.3 million of CRT securities funded with cash and repurchase agreement borrowings. While we generally intend to hold our MBS as long-term investments, we may sell certain of our securities in order to manage our interest rate risk and liquidity needs, meet other operating objectives and adapt to market conditions. In addition, during 2015 we sold certain of our Non-Agency MBS for $70.7 million, realizing gross gains of $34.9 million.

In connection with our repurchase agreement borrowings and Swaps, we routinely receive margin calls/reverse margin calls from our counterparties and make margin calls to our counterparties. Margin calls and reverse margin calls, which requirements vary over time, may occur daily between us and any of our counterparties when the value of collateral pledged changes from the amount contractually required. The value of securities pledged as collateral fluctuates reflecting changes in: (i) the face (or par) value of our for MBS; (ii) market interest rates and/or other market conditions; and (iii) the market value of our Swaps. Margin calls/reverse margin calls are satisfied when we pledge/receive additional collateral in the form of additional securities and/or cash.

The table below summarizes our margin activity with respect to our repurchase agreement financings and derivative hedging instruments for the quarterly periods presented:

	Collateral Pledged to Meet Margin Calls			Cash and	
For the Quarter Ended	Fair Value of Securities Pledged	Cash Pledged	Aggregate Assets Pledged For Margin Calls	Securities Received For Reverse Margin Calls	Net Assets Received/(Pledged) For Margin Activity
(In Thousands)					
December 31, 2015	$225,323	$32,200	$257,523	$276,596	$ 19,073
September 30, 2015	397,763	86,300	484,063	433,003	(51,060)
June 30, 2015	391,088	50,700	441,788	408,968	(32,820)
March 31, 2015	309,114	98,000	407,114	350,036	(57,078)

We are subject to various financial covenants under our repurchase agreements and derivative contracts, which include minimum net worth and/or profitability requirements, maximum debt-to-equity ratios and minimum market capitalization requirements. We have maintained compliance with all of our financial covenants through December 31, 2015.

During 2015, we paid $297.4 million for cash dividends on our common stock and dividend equivalents and paid cash dividends of $15.0 million on our preferred stock. On December 9, 2015, we declared our fourth quarter 2015 dividend on our common stock of $0.20 per share; on January 29, 2016, we paid this dividend, which totaled $74.4 million, including dividend equivalents of approximately $263,000.

We believe that we have adequate financial resources to meet our current obligations, including margin calls, as they come due, to fund dividends we declare and to actively pursue our investment strategies. However, should the value of our MBS suddenly decrease, significant margin calls on our repurchase agreement borrowings could result and our liquidity position could be materially and adversely affected. Further, should market liquidity tighten, our repurchase agreement counterparties may increase our margin requirements on new financings, reducing our ability to use leverage. Access to financing may also be negatively impacted by the ongoing volatility in the world financial markets, potentially adversely impacting our current or potential lenders' ability or

Table of Contents

willingness to provide us with financing. In addition, there is no assurance that favorable market conditions will continue to permit us to consummate additional securitization transactions if we determine to seek that form of financing.

OFF-BALANCE SHEET ARRANGEMENTS

We do not have any material off-balance-sheet arrangements.

AGGREGATE CONTRACTUAL OBLIGATIONS

The following table summarizes the effect on our liquidity and cash flows of contractual obligations for the principal and interest amounts due at December 31, 2015:

	Due During the Year Ending December 31,						
(In Thousands)	2016	2017	2018	2019	2020	Thereafter	Total
Repurchase agreements	$7,694,793	$194,109	$—	$—	$—	$—	$7,888,902
Interest expense on repurchase agreements (1)	30,552	10,574	—	—	—	—	41,126
FHLB advances (2)	—	1,500,000	—	—	—	—	1,500,000
Interest expense on FHLB advances (1)(2)	7,501	1,025	—	—	—	—	8,526
Securitized debt (3)	6,219	7,259	7,362	1,217	—	—	22,057
Interest expense on securitized debt (1)	551	356	148	5	—	—	1,060
Senior Notes (4)	—	—	—	—	—	100,000	100,000
Interest expense on Senior Notes (1)	8,000	8,000	8,000	8,000	8,000	171,911	211,911
Long-term lease obligations	2,552	2,522	2,522	2,522	1,050	—	11,168
Total	$7,750,168	$1,723,845	$18,032	$11,744	$9,050	$271,911	$9,784,750

(1) Interest expense based on the interest rate in effect at December 31, 2015.
(2) As a result of the previously mentioned final FHFA rule adopted in January, 2016, MFA Insurance's FHLB membership will terminate one year from the rules effective date of February 19, 2016, requiring any outstanding advances and associated interest to be repaid by February 19, 2017. As a result, the contractual obligations in the table above are reflected as due during the year ended December 31, 2017.
(3) Securitized debt is contractually scheduled to mature by November 2022. However, the weighted average life of the securitized debt is estimated to be 0.35 years assuming a 12.0% weighted average CPR.
(4) Senior Notes mature April 2042 but may be redeemed, in whole or in part, at any time on or after April 15, 2017.

INFLATION

Substantially all of our assets and liabilities are financial in nature. As a result, changes in interest rates and other factors impact our performance far more than does inflation. Our financial statements are prepared in accordance with GAAP and dividends declared are based upon net ordinary income as calculated for tax purposes. In each case, our results of operations and reported assets, liabilities and equity are measured with reference to historical cost or fair value without considering inflation.

72

Table of Contents

CAUTIONARY NOTE REGARDING FORWARD LOOKING STATEMENTS

This Annual Report on Form 10-K includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, which are subject to risks and uncertainties. The forward-looking statements contain words such as “will,” “believe,” “expect,” “anticipate,” “estimate,” “plan,” “continue,” “intend,” “should,” “could,” “would,” “ expressions.

These forward-looking statements include information about possible or assumed future results with respect to our business, financial condition, liquidity, results of operations, plans and objectives. Statements regarding the following subjects, among others, may be forward-looking: changes in interest rates and the market value of our MBS; changes in the prepayment rates on the mortgage loans securing our MBS, an increase of which could result in a reduction of the yield on MBS in our portfolio and an increase of which could require us to reinvest the proceeds received by us as a result of such prepayments in MBS with lower coupons; credit risks underlying our assets, including changes in the default rates and management’s assumptions regarding default rates on the mortgage loans securing our Non-Agency MBS and as related to our residential whole loan portfolio; our ability to borrow to finance our assets and the terms, including the cost, maturity and other terms, of any such borrowings; implementation of or changes in government regulations or programs affecting our business; our estimates regarding taxable income the actual amount of which is dependent on a number of factors, including, but not limited to, changes in the amount of interest income and financing costs, the method elected by us to accrete the market discount on Non-Agency MBS and the extent of prepayments, realized losses and changes in the composition of our Agency MBS and Non-Agency MBS portfolios that may occur during the applicable tax period, including gain or loss on any MBS disposals; the timing and amount of distributions to stockholders, which are declared and paid at the discretion of our Board of Directors and will depend on, among other things, our taxable income, our financial results and overall financial condition and liquidity, maintenance of our REIT qualification and such other factors as the Board deems relevant; our ability to maintain our qualification as a REIT for federal income tax purposes; our ability to maintain our exemption from registration under the Investment Company Act, including statements regarding the concept release issued by the SEC relating to interpretive issues under the Investment Company Act with respect to the status under the Investment Company Act of certain companies that are in engaged in the business of acquiring mortgages and mortgage-related interests; our ability to successfully implement our strategy to grow our residential whole loan portfolio; expected returns on our investments in non-performing residential whole loans (or NPLs), which are affected by, among other things, the length of time required to foreclose upon, sell, liquidate or otherwise reach a resolution of the property underlying the NPL, home price values, amounts advanced to carry the asset (e.g., taxes, insurance, maintenance expenses, etc. on the underlying property) and the amount ultimately realized upon resolution of the asset; and risks associated with investing in real estate assets, including changes in business conditions and the general economy. These and other risks, uncertainties and factors, including those described in the annual, quarterly and current reports that we file with the SEC, could cause our actual results to differ materially from those projected in any forward-looking statements we make. All forward-looking statements are based on beliefs, assumptions and expectations of our future performance, taking into account all information currently available. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date they are made. New risks and uncertainties arise over time and it is not possible to predict those events or how they may affect us. Except as required by law, we are not obligated to, and do not intend to, update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. (See Part I, Item 1A. “Risk Factors” of this Annual Report on Form 10-K)

Table of Contents

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

We seek to manage our risks related to interest rates, liquidity, prepayment speeds, market value and the credit quality of our assets while, at the same time, seeking to provide an opportunity to stockholders to realize attractive total returns through ownership of our capital stock. While we do not seek to avoid risk, we seek, consistent with our investment policies, to: assume risk that can be quantified based on management's judgment and experience and actively manage such risk; earn sufficient returns to justify the taking of such risks; and maintain capital levels consistent with the risks that we undertake.

INTEREST RATE RISK

We generally acquire interest-rate sensitive assets and fund them with interest-rate sensitive liabilities, a portion of which are hedged with Swaps. We are exposed to interest rate risk on our residential mortgage assets, as well as on our liabilities (repurchase agreements, FHLB advances and securitized debt). Changes in interest rates can affect our net interest income and the fair value of our assets and liabilities.
We finance the majority of our investments in Agency, Legacy Non-Agency and RPL/NPL MBS with short-term repurchase agreements. In general, when interest rates change, the borrowing costs of our repurchase agreements (net of the impact of Swaps) change more quickly than the yields on our assets. In a rising interest rate environment the borrowing costs of our repurchase agreements may increase faster than the interest income on our assets, thereby reducing our net income. In order to mitigate compression in net income based on such interest rate movements, we use Swaps and other hedging instruments to lock in a portion of the net interest spread between assets and liabilities.

When interest rates change, the fair value of our residential mortgage assets could change at a different rate than the fair value of our liabilities. We measure the sensitivity of our portfolio to changes in interest rates by estimating the duration of our assets and liabilities. Duration is the approximate percentage change in fair value for a 100 basis point parallel shift in the yield curve. In general, our assets have higher duration than our liabilities and in order to reduce this exposure we use Swaps and other hedging instruments to reduce the gap in duration between our assets and liabilities.

In calculating the duration of our Agency MBS we take into account the characteristics of the underlying mortgage loans including whether the underlying loans are fixed rate, adjustable or hybrid; coupon, expected prepayment rates and lifetime and periodic caps. We use third-party financial models, combined with management's assumptions and observed empirical data when estimating the duration of our Agency MBS.

In analyzing the interest rate sensitivity of our Legacy Non-Agency MBS we take into account the characteristics of the underlying mortgage loans, including credit quality and whether the underlying loans are fixed-rate, adjustable or hybrid. We estimate the duration of our Legacy Non-Agency MBS using management's assumptions.

Our RPL/NPL MBS deal structures contain an interest rate step-up feature whereby the original coupon increases by 300 basis points if the bond is not redeemed by the issuer after 36 months. Therefore, we believe their fair value exhibits little sensitivity to changes in interest rates. We estimate the duration of our RPL/NPL MBS using management's assumptions.

The fair value of our re-performing residential whole loans is dependent on the value of the underlying real estate collateral, past and expected delinquency status of the borrower as well as the level of interest rates. Because the borrower is not delinquent on their mortgage payments but is less likely to prepay the loan due to weak credit history and/or high LTV, we believe our re-performing residential whole loans exhibit positive duration. We estimate the duration of our re-performing residential whole loans using management's assumptions.

The fair value of our non-performing residential whole loans is primarily dependent on the value of the underlying real estate collateral and the time until collateral liquidation. Since neither the value of the collateral nor the liquidation timeline is generally sensitive to interest rates, we believe their fair value exhibits little sensitivity to interest rates. We estimate the duration of our non-performing residential whole loans using management's assumptions.

We use Swaps as part of our overall interest rate risk management strategy. Such derivative financial instruments are intended to act as a hedge against future interest rate increases on our repurchase agreement financings, which rates are typically highly correlated with LIBOR. While our derivatives do not extend the maturities of our borrowings under repurchase agreements, they do, in effect, lock in a fixed rate of interest over their term for a corresponding amount of our repurchase agreement financing that are hedged.

Table of Contents

At December 31, 2015, MFA’s $8.546 billion of Agency MBS and Legacy Non-Agency MBS were backed by Hybrid, adjustable and fixed-rate mortgages. Additional information about these MBS, including average months to reset and three-month average CPR, is presented below:

	Agency MBS			Legacy Non-Agency MBS (1)			Total (1)		
Time to Reset	Fair Value (2)	Average Months to Reset (3)	3 Month Average CPR (4)	Fair Value	Average Months to Reset (3)	3 Month Average CPR (4)	Fair Value (2)	Average Months to Reset (3)	3 Month Average CPR (4)
(Dollars in Thousands)									
< 2 years (5)	$1,977,308	6	12.7 %	$2,580,658	6	13.7 %	$4,557,966	6	13.4 %
2-5 years	772,627	36	15.7	—	—	—	772,627	36	15.7
> 5 years	220,532	75	11.7	—	—	—	220,532	75	11.7
ARM-MBS Total	$2,970,467								