Cherry Hill Mortgage Investment Corp
Form 10-Q
May 09, 2018

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

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FORM 10-Q

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

For the quarterly period ended March 31, 2018

OR

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

For the transition period from ________to ________
Commission file number 001-36099

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CHERRY HILL MORTGAGE INVESTMENT CORPORATION
(Exact name of registrant as specified in its charter)

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N/A
(Former name, former address and former fiscal year, if changed since last report)

| | |
|---|---|
| Maryland | 46-1315605 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |
| 1451 Route 34, Suite 303 | |
| Farmingdale, New Jersey | 07727 |
| (Address of Principal Executive Offices) | (Zip Code) |

(877) 870 – 7005
(Registrant’s Telephone Number, Including Area Code)

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Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was

required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer Accelerated filer

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

Emerging growth company

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

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

As of May 9, 2018, there were 12,721,464 outstanding shares of common stock, $0.01 par value per share, of Cherry Hill Mortgage Investment Corporation.

CHERRY HILL MORTGAGE INVESTMENT CORPORATION

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FORWARD-LOOKING INFORMATION

Cherry Hill Mortgage Investment Corporation (together with its consolidated subsidiaries, the "Company," "we," "our" or "us") makes forward-looking statements in this Quarterly Report on Form 10-Q within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. For these statements, the Company claims the protections of the safe harbor for forward-looking statements contained in such Sections. Forward-looking statements are subject to substantial risks and uncertainties, many of which are difficult to predict and are generally beyond the Company's control. These forward-looking statements include information about possible or assumed future results of the Company's business, financial condition, liquidity, results of operations, plans and objectives. When the Company uses the words "believe," "expect," "anticipate," "estimate," "plan," "continue," "intend," "should," "could," "would," "may," "potential" or the negative of these terms or other comparable termin the Company intends to identify forward-looking statements. Statements regarding the following subjects, among others, may be forward-looking:

- the Company's investment objectives and business strategy;
- the Company's ability to raise capital through the sale of its equity and debt securities and to invest the net proceeds of any such offering in the target assets identified at the time of the offering;
- the Company's ability to obtain future financing arrangements and refinance existing financing arrangements as they mature;
- the Company's expected leverage;
- the Company's expected investments;
- the Company's ability to acquire servicing-related assets and mortgage and real estate-related securities;
- estimates and statements relating to, and the Company's ability to make, future distributions to holders of the Company's securities;
- the Company's ability to compete in the marketplace;
- market, industry and economic trends;
- recent market developments and actions taken and to be taken by the U.S. Government, the U.S. Treasury and the Board of Governors of the Federal Reserve System, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the Government National Mortgage Association and the U.S. Securities and Exchange Commission ("SEC");
- mortgage loan modification programs and future legislative actions;
- the Company's ability to maintain its qualification as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code"), and limitations on the Company's business due to compliance with requirements for maintaining its qualification as a REIT under the Code;
- the Company's ability to maintain its exclusion from regulation as an investment company under the Investment Company Act of 1940, as amended (the "Investment Company Act");
- projected capital and operating expenditures;
- availability of qualified personnel; and
- projected prepayment and/or default rates.

The Company's beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to it or are within its control. If any such change occurs, the Company's business, financial condition, liquidity and results of operations may vary materially from those expressed in, or implied by, the Company's forward-looking statements. These risks, along with, among others, the following factors, could cause actual results to vary from the Company's forward-looking statements:

- the factors discussed under "Part I, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" in this Quarterly Report on Form 10-Q and "Part I, Item 1A. Risk Factors" in the Company's Annual Report on Form 10-K for the year ended December 31, 2017;
- general volatility of the capital markets;

- changes in the Company’s investment objectives and business strategy;
- availability, terms and deployment of capital;
- availability of suitable investment opportunities;
- the Company’s dependence on its external manager, Cherry Hill Mortgage Management, LLC (“the Manager”), and the Company’s ability to find a suitable replacement if the Company or the Manager were to terminate the management agreement the Company has entered into with the Manager;

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- changes in the Company’s assets, interest rates or the general economy;
- increased rates of default and/or decreased recovery rates on the Company’s investments;
- changes in interest rates, interest rate spreads, the yield curve, prepayment rates or recapture rates;
- limitations on the Company’s business due to compliance with requirements for maintaining its qualification as a REIT under the Code and its exclusion from regulation as an investment company under the Investment Company Act;
- the degree and nature of the Company’s competition, including competition for the residential mortgage assets in which the Company invests; and
- other risks associated with acquiring, investing in and managing residential mortgage assets.

Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, it cannot guarantee future results, levels of activity, performance or achievements. These forward-looking statements apply only as of the date of this Quarterly Report on Form 10-Q. The Company is not obligated, and does not intend, to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

Cherry Hill Mortgage Investment Corporation and Subsidiaries
Consolidated Balance Sheets
(in thousands — except share data)

| | (unaudited) March 31, 2018 | December 31, 2017 |
|---|---|---|
| Assets | | |
| RMBS, available-for-sale (including pledged assets of $1,560,765 and $1,728,564, respectively) | $ 1,642,682 | $ 1,840,912 |
| Investments in Servicing Related Assets at fair value (including pledged assets of $188,145 and $122,806, respectively) | 188,145 | 122,806 |
| Cash and cash equivalents | 24,276 | 27,327 |
| Restricted cash | 35,245 | 29,168 |
| Derivative assets | 16,105 | 13,830 |
| Receivables and other assets | 17,724 | 16,642 |
| Total Assets | $ 1,924,177 | $ 2,050,685 |
| Liabilities and Stockholders' Equity | | |
| Liabilities | | |
| Repurchase agreements | $ 1,500,562 | $ 1,666,537 |
| Derivative liabilities | 1,097 | 344 |
| Notes payable | 74,749 | 39,025 |
| Dividends payable | 7,257 | 7,273 |
| Due to affiliates | 4,438 | 3,035 |
| Accrued expenses and other liabilities | 16,777 | 12,014 |
| Total Liabilities | $ 1,604,880 | $ 1,728,228 |
| Stockholders' Equity | | |
| Series A Preferred stock, $0.01 par value, 100,000,000 shares authorized and 2,400,000 shares issued and outstanding as of March 31, 2018 and 100,000,000 shares authorized and 2,400,000 shares issued and outstanding as of December 31, 2017, liquidation preference of $60,000 as of March 31, 2018 and December 31, 2017 | $ 57,917 | $ 57,917 |
| Common stock, $0.01 par value, 500,000,000 shares authorized and 12,721,464 shares issued and outstanding as of March 31, 2018 and 500,000,000 shares authorized and 12,721,464 shares issued and outstanding as of December 31, 2017 | 127 | 127 |
| Additional paid-in capital | 229,679 | 229,642 |
| Retained earnings | 62,573 | 35,238 |
| Accumulated other comprehensive income (loss) | (33,985) | (2,942) |
| Total Cherry Hill Mortgage Investment Corporation Stockholders' Equity | $ 316,311 | $ 319,982 |
| Non-controlling interests in Operating Partnership | 2,986 | 2,475 |
| Total Stockholders' Equity | $ 319,297 | $ 322,457 |
| Total Liabilities and Stockholders' Equity | $ 1,924,177 | $ 2,050,685 |

See accompanying notes to consolidated financial statements.

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Cherry Hill Mortgage Investment Corporation and Subsidiaries
Consolidated Statements of Income
(Unaudited)
(in thousands — except per share data)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Income | | |
| Interest income | $ 13,415 | $ 6,078 |
| Interest expense | 7,543 | 2,431 |
| Net interest income | 5,872 | 3,647 |
| Servicing fee income | 8,650 | 4,574 |
| Servicing costs | 1,712 | 1,227 |
| Net servicing income | 6,938 | 3,347 |
| Other income (loss) | | |
| Realized gain (loss) on RMBS, net | (4,881) | (256) |
| Realized gain on investments in Excess MSRs, net | - | 6,678 |
| Realized gain (loss) on derivatives, net | 13 | (1,017) |
| Unrealized gain on derivatives, net | 19,626 | 1,082 |
| Unrealized gain on investments in MSRs | 12,498 | 12,312 |
| Total Income | 40,066 | 25,793 |
| Expenses | | |
| General and administrative expense | 877 | 975 |
| Management fee to affiliate | 1,315 | 892 |
| Total Expenses | 2,192 | 1,867 |
| Income Before Income Taxes | 37,874 | 23,926 |
| Provision for corporate business taxes | 2,635 | 1,339 |
| Net Income | 35,239 | 22,587 |
| Net (income) loss allocated to noncontrolling interests in Operating Partnership | (456) | (409) |
| Dividends on preferred stock | 1,213 | - |
| Net Income Applicable to Common Stockholders | $ 33,570 | $ 22,178 |
| Net income Per Share of Common Stock | | |
| Basic | $ 2.64 | $ 2.91 |
| Diluted | $ 2.64 | $ 2.90 |
| Weighted Average Number of Shares of Common Stock Outstanding | | |
| Basic | 12,713,265 | 7,634,038 |
| Diluted | 12,721,464 | 7,640,348 |

See accompanying notes to consolidated financial statements.

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Cherry Hill Mortgage Investment Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income (Loss)
(Unaudited)
(in thousands)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Net income | $ 35,239 | $ 22,587 |
| Other comprehensive income (loss): | | |
| Net unrealized gain (loss) on RMBS | (35,924) | 1,416 |
| Reclassification of net realized loss on RMBS included in earnings | 4,881 | 256 |
| Other comprehensive income (loss) | (31,043) | 1,672 |
| Comprehensive income | $ 4,196 | $ 24,259 |
| Comprehensive income attributable to noncontrolling interests in Operating Partnership | 54 | 440 |
| Dividends on preferred stock | 1,213 | - |
| Comprehensive income attributable to common stockholders | $ 2,929 | $ 23,819 |

See accompanying notes to consolidated financial statements.

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Cherry Hill Mortgage Investment Corporation and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity
(Unaudited)
(in thousands — except share data)

| | Common Stock Shares | Common Stock Amount | Preferred Stock Shares | Preferred Stock Amount | Additional Paid-in Capital | Accumulated Other Comprehensive Income (Loss) | Retained Earnings (Deficit) | Non-Controlling Interest in Operating Partnership | Total Stockholders' Equity |
|---|---|---|---|---|---|---|---|---|---|
| Balance, December 31, 2016 | 7,525,348 | $ 75 | - | $ - | $ 148,457 | $ (6,393 ) | $ 12,093 | $ 1,777 | $ 156,009 |
| Issuance of common stock | 5,175,000 | 52 | - | - | 80,863 | - | - | - | 80,915 |
| Net Income (Loss) | - | - | - | - | - | - | 22,178 | 409 | 22,587 |
| Other Comprehensive Income | - | - | - | - | - | 1,672 | - | - | 1,672 |
| LTIP-OP Unit awards | - | - | - | - | - | - | - | 135 | 135 |
| Distribution paid on LTIP-OP Units | - | - | - | - | - | - | - | (91 ) | (91 ) |
| Common dividends declared, $0.49 per share | - | - | - | - | - | - | (3,687 ) | - | (3,687 ) |
| Balance, March 31, 2017 | 12,700,348 | $ 127 | - | $ - | $ 229,320 | $ (4,721 ) | $ 30,584 | $ 2,230 | $ 257,540 |
| | | | | | | | | | |
| Balance, December 31, 2017 | 12,721,464 | $ 127 | 2,400,000 | $ 57,917 | $ 229,642 | $ (2,942 ) | $ 35,238 | $ 2,475 | $ 322,457 |
| Issuance of common stock | - | - | - | - | 37 | - | - | - | 37 |
| Net Income before dividends on preferred stock | - | - | - | - | - | - | 34,783 | 456 | 35,239 |
| Other Comprehensive Income | - | - | - | - | - | (31,043 ) | - | - | (31,043 ) |
| LTIP-OP Unit awards | - | - | - | - | - | - | - | 138 | 138 |
| Distribution paid on LTIP-OP Units | - | - | - | - | - | - | - | (83 ) | (83 ) |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Common dividends declared, $0.49 per share | - | - | - | - | - | - | (6,235 ) | - | (6,235 ) |
| Preferred dividends declared, $0.5125 per share | - | - | - | - | - | - | (1,213 ) | - | (1,213 ) |
| Balance, March 31, 2018 | 12,721,464 | $ 127 | 2,400,000 | $ 57,917 | $ 229,679 | $ (33,985 ) | $ 62,573 | $ 2,986 | $ 319,297 |

See accompanying notes to consolidated financial statements.

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Cherry Hill Mortgage Investment Corporation and Subsidiaries
Consolidated Statements of Cash Flows
(Unaudited)
(in thousands)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Cash Flows From Operating Activities | | |
| Net income | $ 35,239 | $ 22,587 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | |
| Realized loss on RMBS, net | 4,881 | 256 |
| Realized gain (loss) on investments in Excess MSRs, net | - | (6,678 ) |
| Amortization of premiums on investment securities | 3,460 | 1,419 |
| Change in fair value of investments in Servicing Related Assets | (12,498 ) | (12,312 ) |
| Unrealized (gain) loss on derivatives, net | (19,626 ) | (1,082 ) |
| Realized (gain) loss on derivatives, net | (13 ) | 1,017 |
| LTIP-OP Unit awards | 138 | 135 |
| Changes in: | | |
| Receivables and other assets | (1,082 ) | 2,012 |
| Due to affiliates | 1,403 | 443 |
| Payables for unsettled trades | - | 251,590 |
| Accrued expenses and other liabilities | 4,747 | (425 ) |
| Net cash provided by (used in) operating activities | 16,649 | $ 258,962 |
| Cash Flows From Investing Activities | | |
| Purchase of RMBS | (40,556 ) | (491,869 ) |
| Principal paydown of RMBS | 41,644 | 17,104 |
| Proceeds from sale of RMBS | 157,758 | 7,610 |
| Proceeds from sale of Excess MSRs | - | 35,905 |
| Acquisition of MSRs | (52,841 ) | (32,350 ) |
| Purchase of derivatives | (842 ) | (408 ) |
| Sale of derivatives | 32 | - |
| Net cash provided by (used in) investing activities | 105,195 | $ (464,008 ) |
| Cash Flows From Financing Activities | | |
| Changes in restricted cash | (6,077 ) | 15,384 |
| Borrowings under repurchase agreements | 1,904,638 | 784,497 |
| Repayments of repurchase agreements | (2,070,613 ) | (605,795 ) |
| Proceeds from derivative financing | 18,927 | - |
| Proceeds from bank loans | 36,195 | 2,000 |
| Principal paydown of bank loans | (471 ) | (8,886 ) |
| Dividends paid | (7,448 ) | (3,687 ) |
| LTIP-OP Units distributions paid | (83 ) | (91 ) |
| Issuance of common stock, net of offering costs | 37 | 80,915 |
| Net cash provided by (used in) financing activities | $ (124,895 ) | $ 264,337 |
| Net Increase (Decrease) in Cash and Cash Equivalents | (3,051 ) | $ 59,291 |
| Cash and Cash Equivalents, Beginning of Period | 27,327 | 15,824 |
| Cash and Cash Equivalents, End of Period | 24,276 | $ 75,115 |
| Supplemental Disclosure of Cash Flow Information | | |
| Cash paid during the period for interest expense | 8,800 | $ 1,800 |
| Dividends declared but not paid | $ 7,257 | $ 3,687 |

See accompanying notes to consolidated financial statements.

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Cherry Hill Mortgage Investment Corporation and Subsidiaries

Notes to Consolidated Financial Statements

March 31, 2018

(Unaudited)

Note 1 — Organization and Operations

Cherry Hill Mortgage Investment Corporation (together with its consolidated subsidiaries, the “Company”) was organized in the state of Maryland on October 31, 2012 to invest in residential mortgage assets in the United States. Under the Company’s charter, the Company is authorized to issue up to 500,000,000 shares of common stock and 100,000,000 shares of preferred stock, each with a par value of $0.01 per share.

The accompanying interim consolidated financial statements include the accounts of the Company’s subsidiaries, Cherry Hill Operating Partnership, LP (the “Operating Partnership”), Cherry Hill QRS I, LLC, Cherry Hill QRS II, LLC, Cherry Hill QRS III, LLC (“QRS III”), Cherry Hill QRS IV, LLC (“QRS IV”), CHMI Solutions, Inc. (“CHMI Solutions”) and Aurora Financial Group, Inc. (“Aurora”).

On October 9, 2013, the Company completed an initial public offering (the “IPO”) and a concurrent private placement of its common stock. The Company did not conduct any activity prior to the IPO and the concurrent private placement. Substantially all of the net proceeds from the IPO and the concurrent private placement were used to invest in excess mortgage servicing rights on residential mortgage loans (“Excess MSRs”) and residential mortgage-backed securities (“RMBS” or “securities”), the payment of principal and interest on which is guaranteed by a U.S. government agency or a U.S. government sponsored enterprise (“Agency RMBS”).

On March 29, 2017, the Company issued and sold 5,175,000 shares of its common stock, par value $0.01 per share, raising approximately $81.1 million after underwriting discounts and commissions but before expenses of approximately $229,000. All of the net proceeds were invested in RMBS.

On August 17, 2017, the Company issued and sold 2,400,000 shares of its 8.20% Series A Cumulative Redeemable Preferred Stock, par value $0.01 per share (the “Series A Preferred Stock”), raising approximately $58.1 million after underwriting discounts and commissions but before expenses of approximately $193,000. All of the net proceeds from the Series A Preferred Stock offering were also invested in RMBS. The Company anticipates that a significant portion of the net proceeds received from paydowns of these RMBS will be deployed into the acquisition of mortgage servicing rights (“MSRs”). The Company may also sell certain of these RMBS and deploy the net proceeds from such sales to the extent necessary to fund the purchase price of MSRs.

The Company is party to a management agreement (the “Management Agreement”) with Cherry Hill Mortgage Management, LLC (the “Manager”), a Delaware limited liability company established by Mr. Stanley Middleman. The Manager is a party to a Services Agreement with Freedom Mortgage Corporation (“Freedom Mortgage”), which is owned and controlled by Mr. Middleman. The Manager is owned by a “blind trust” for the benefit of Mr. Middleman. For a further discussion of the Management Agreement, see Note 7.

The Company has elected to be taxed as a real estate investment trust (“REIT”), as defined under the Internal Revenue Code of 1986, as amended (the “Code”), commencing with its short taxable year ended December 31, 2013. As long as the Company continues to comply with a number of requirements under federal tax law and maintains its qualification as a REIT, the Company generally will not be subject to U.S. federal income taxes to the extent that the Company distributes its taxable income to its stockholders on an annual basis and does not engage in prohibited transactions.

However, certain activities that the Company may perform may cause it to earn income that will not be qualifying income for REIT purposes.

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Note 2 — Basis of Presentation and Significant Accounting Policies

Basis of Accounting

The accompanying interim consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. The interim consolidated financial statements include the accounts of the Company and its consolidated subsidiaries. All significant intercompany transactions and balances have been eliminated. The Company consolidates those entities in which it has an investment of 50% or more and has control over significant operating, financial and investing decisions of the entity. The interim consolidated financial statements reflect all necessary and recurring adjustments for fair presentation of the results for the interim periods presented herein.

Emerging Growth Company Status

On April 5, 2012, the Jumpstart Our Business Startups Act (the "JOBS Act") was signed into law. The JOBS Act contains provisions that, among other things, reduce certain reporting requirements for qualifying public companies. Because the Company qualifies as an "emerging growth company," it may, under Section 7(a)(2)(B) of the Securities Act of 1933, as amended (the "Securities Act"), delay adoption of new or revised accounting standards applicable to public companies until such standards would otherwise apply to private companies. The Company has elected to take advantage of this extended transition period until the first to occur of the date that it (i) is no longer an "emerging growth company" or (ii) affirmatively and irrevocably opts out of this extended transition period. As a result, the consolidated interim financial statements may not be comparable to those of other public companies that comply with such new or revised accounting standards. Until the date that the Company is no longer an "emerging growth company" (expected to occur as of October 9, 2018) or affirmatively and irrevocably opts out of the extended transition period, upon issuance of a new or revised accounting standard that applies to the consolidated interim financial statements and that has a different effective date for public and private companies, the Company will disclose the date on which adoption is required for non-emerging growth public companies and the date on which it will adopt the new or revised accounting standard.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make a number of significant estimates and assumptions. These include estimates of: the fair value of Excess MSRs and MSRs (collectively, "Servicing Related Assets"); RMBS and derivatives; credit losses, including the period of time during which the Company anticipates an increase in the fair values of RMBS sufficient to recover unrealized losses on those RMBS; and other estimates that affect the reported amounts of certain assets, revenues, liabilities and expenses as of the date of, and for the periods covered by, the consolidated interim financial statements. It is likely that changes in these estimates will occur in the near term. The Company's estimates are inherently subjective in nature. Actual results could differ from the Company's estimates, and the differences may be material.

Risks and Uncertainties

In the normal course of business, the Company encounters primarily two significant types of economic risk: credit and market. Credit risk is the risk of default on the Company's investments in RMBS, Servicing Related Assets and derivatives that results from a borrower's or derivative counterparty's inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of investments in RMBS, Servicing Related Assets and derivatives due to changes in interest rates, spreads or other market factors, including prepayment speeds on the Company's RMBS and Servicing Related Assets. The Company is subject to the risks involved with real estate and real estate-related debt instruments. These include, among others, the risks normally associated with changes in the

general economic climate, changes in the mortgage market, changes in tax laws, interest rate levels, and the availability of financing.

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The Company also is subject to certain risks relating to its status as a REIT for U.S. federal income tax purposes. If the Company were to fail to qualify as a REIT in any taxable year, the Company would be subject to U.S. federal income tax on its REIT income, which could be material. Unless entitled to relief under certain statutory provisions, the Company would also be disqualified from treatment as a REIT for the four taxable years following the year during which qualification is lost.

Investments in RMBS

Classification – The Company classifies its investments in RMBS as securities available for sale. Although the Company generally intends to hold most of its securities until maturity, it may, from time to time, sell any of its securities as part of its overall management of its portfolio. Securities available for sale are carried at fair value with the net unrealized gains or losses reported as a separate component of accumulated other comprehensive income (loss), to the extent impairment losses, if any, are considered temporary. Unrealized losses on securities are charged to earnings if they reflect a decline in value that is other-than-temporary, as described below.

Fair value is determined under the guidance of Accounting Standards Codification ("ASC") 820, Fair Value Measurements and Disclosures ("ASC 820"). The Company determines fair value of its RMBS investments based upon prices obtained from third-party pricing providers. The third-party pricing providers use pricing models that generally incorporate such factors as coupons, primary and secondary mortgage rates, rate reset periods, issuer, prepayment speeds, credit enhancements and expected life of the security. Management's judgment is used to arrive at the fair values of RMBS, taking into account prices obtained from third-party pricing providers and other applicable market data. The Company's application of ASC 820 guidance is discussed in further detail in Note 9.

Investment securities transactions are recorded on the trade date. At disposition, the net realized gain or loss is determined on the basis of the cost of the specific investment and is included in earnings. All RMBS purchased and sold in the three month period ended March 31, 2018 were settled prior to period-end. All RMBS purchased and sold in the year ended December 31, 2017 were settled prior to year-end.

Revenue Recognition – Interest income from coupon payments is accrued based on the outstanding principal amount of the RMBS and their contractual terms. Premiums and discounts associated with the purchase of the RMBS are accreted into interest income over the projected lives of the securities using the effective interest method. The Company's policy for estimating prepayment speeds for calculating the effective yield is to evaluate historical performance, consensus on prepayment speeds, and current market conditions. Adjustments are made for actual prepayment activity. Approximately $5.1 million and $5.7 million in interest income was receivable at March 31, 2018 and December 31, 2017, respectively, and has been classified within "Receivables and other assets" on the consolidated balance sheets. For further discussion on Receivables and other assets, see Note 13.

Impairment – The Company evaluates its RMBS on a quarterly basis to assess whether a decline in the fair value below the amortized cost basis is an other-than-temporary impairment ("OTTI"). The presence of OTTI is based upon a fair value decline below a security's amortized cost basis and a corresponding adverse change in expected cash flows due to credit related factors as well as non-credit factors, such as changes in interest rates and market spreads. Impairment is considered other-than-temporary if the Company (i) intends to sell the security, (ii) will more likely than not be required to sell the security before recovering its cost basis, or (iii) does not expect to recover the security's entire amortized cost basis, even if the Company does not intend to sell the security, or the Company believes it is more likely than not that it will be required to sell the security before recovering its cost basis. Under these scenarios, the impairment is other-than-temporary and the full amount of impairment is recognized currently in earnings and the cost basis of the security is adjusted. However, if the Company does not intend to sell the impaired security and it is more likely than not that it will not be required to sell before recovery, the OTTI is separated into (i) the estimated amount relating to credit loss, or the credit component, and (ii) the amount relating to all other factors, or the non-credit component. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss

recognized in accumulated other comprehensive income (loss). The difference between the new amortized cost basis and the cash flows expected to be collected is accreted into interest income in accordance with the effective interest method. The Company recorded approximately $45,000 of OTTI charges during the three month period ended March 31, 2018. The Company did not record any OTTI charges during the three month period ended March 31, 2017. OTTI has been classified within “Realized gain (loss) on RMBS, net” on the consolidated statements of income.



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Investments in Excess MSRs

As a result of the Company's sale of its remaining Excess MSRs in February 2017, there were no Excess MSRs at March 31, 2018.

Classification – The Company had elected the fair value option to record its investments in Excess MSRs in order to provide users of the consolidated interim financial statements with better information regarding the effects of prepayment risk and other market factors on the Excess MSRs. Under this election, the Company recorded a valuation adjustment on its investments in Excess MSRs on a quarterly basis to recognize the changes in fair value of its Excess MSRs in net income as described below. In determining the valuation of Excess MSRs in accordance with ASC 820, management used internally developed models that were primarily based on observable market-based inputs but which also included unobservable market data inputs. The Company's application of ASC 820 guidance is discussed in further detail in Note 9.

Revenue Recognition – Investments in Excess MSRs were aggregated into pools, and each pool of Excess MSRs was accounted for in the aggregate. Interest income for Excess MSRs was accreted into interest income on an effective yield or "interest" method, based upon the expected excess mortgage servicing amount over the expected life of the underlying mortgages. Changes to expected cash flows resulted in a cumulative retrospective adjustment, which was recorded in the period in which the change in expected cash flows occurred. Under the retrospective method, the interest income recognized for a reporting period is measured as the difference between the amortized cost basis at the end of the period and the amortized cost basis at the beginning of the period, plus any cash received during the period. The amortized cost basis was calculated as the present value of estimated future cash flows using an effective yield, which was the yield that equated all past actual and estimated future cash flows to the initial investment. The difference between the fair value of Excess MSRs and their amortized cost basis was recorded on the consolidated statements of income as "Unrealized gain (loss) on investments in Excess MSRs." Fair value was generally determined by discounting the expected future cash flows using discount rates that incorporated the market risks and liquidity premium specific to the Excess MSRs and, therefore, may have differed from their effective yields. The sale of investments in Excess MSRs was recognized upon the settlement date. There was no Excess MSR cash flow receivable at March 31, 2018 or December 31, 2017.

In connection with the sale of its Excess MSRs, the Company elected a settlement date accounting policy to account for the gain on sale from that transaction. For a further discussion of the Company's sale of its Excess MSRs, see Note 7.

Investments in MSRs

Classification – The Company's MSRs represent the contractual right to service mortgage loans. The Company has elected the fair value option to record its investments in MSRs in order to provide users of the consolidated interim financial statements with better information regarding the effects of prepayment risk and other market factors on the MSRs. Under this election, the Company records a valuation adjustment on its investments in MSRs on a quarterly basis to recognize the changes in fair value of its MSRs in net income as described below. Although transactions in MSRs are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels, costs to service and discount rates). Changes in the fair value of MSRs as well as servicing fee income and servicing expenses are reported on the consolidated statements of income. In determining the valuation of MSRs in accordance with ASC 820, management uses internally developed models that are primarily based on observable market-based inputs but which also include unobservable market data inputs. The Company's application of ASC 820 guidance is discussed in further detail in Note 9. For reporting purposes, conventional conforming loans are aggregated into one category and government conforming loans are aggregated into a separate category.

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Revenue Recognition – Mortgage servicing fee income represents revenue earned for servicing mortgage loans. The servicing fees are based on a contractual percentage of the outstanding principal balance and recognized as revenue as the related mortgage payments are collected. Corresponding costs to service are charged to expense as incurred. As an owner and manager of MSRs, the Company may be obligated to fund advances of principal and interest payments due to third-party owners of the loans, but not yet received from the individual borrowers. These advances are reported as servicing advances within the “Receivables and other assets” line item on the consolidated balance sheets. Approximately $4.9 million and $5.9 million in reimbursable servicing advances were receivable at March 31, 2018 and December 31, 2017, respectively, and have been classified within “Receivables and other assets” on the consolidated balance sheets. Although advances on Federal National Mortgage Association (“Fannie Mae”) and Federal Home Loan Mortgage Corporation (“Freddie Mac”) MSRs made in accordance with the relevant guidelines are generally recoverable, the recoverability of similar advances made on Government National Mortgage Association (“Ginnie Mae”) MSRs may be limited under the rules and regulations of the U.S. Department of Housing and Urban Development, the Department of Veterans Affairs (the “VA”) and the Federal Housing Administration (“FHA”). Because the Company acquired its Ginnie Mae MSRs in February 2017 and the Company expects to recover advances on its Fannie Mae and Freddie Mac MSRs, the Company has determined that no reserves for unrecoverable advances are necessary at March 31, 2018 and December 31, 2017. For further discussion on the Company’s receivables and other assets, including the Company’s servicing advances, see Note 13.

Servicing fee income received and servicing expenses incurred are reported on the consolidated statements of income (loss). The difference between the fair value of MSRs and their amortized cost basis is recorded on the consolidated statements of income as “Unrealized gain (loss) on investments in MSRs.” Fair value is generally determined by discounting the expected future cash flows using discount rates that incorporate the market risks and liquidity premium specific to the MSRs and, therefore, may differ from their effective yields.

As a result of the Company’s investments in MSRs, it is obligated from time to time to repurchase an underlying loan from the applicable agency for which it is being serviced due to an alleged breach of a representation or warranty. Loans acquired in this manner are recorded at the purchase price less any principal recoveries and are then offered for sale in the scratch and dent market.

Derivatives and Hedging Activities

Derivative transactions include swaps, swaptions, Treasury futures and “to-be-announced” securities (“TBAs”). Swaps and swaptions are entered into by the Company solely for interest rate risk management purposes. TBAs and Treasury futures are used for duration risk and basis risk management purposes. The decision as to whether or not a given transaction/position (or portion thereof) is economically hedged is made on a case-by-case basis, based on the risks involved and other factors as determined by senior management, including restrictions imposed by the Code on REITs. In determining whether to economically hedge a risk, the Company may consider whether other assets, liabilities, firm commitments and anticipated transactions already offset or reduce the risk. All transactions undertaken as economic hedges are entered into with a view towards minimizing the potential for economic losses that could be incurred by the Company. Generally, derivatives entered into are not intended to qualify as hedges under GAAP, unless specifically stated otherwise.

The Company’s bi-lateral derivative financial instruments contain credit risk to the extent that its bank counterparties may be unable to meet the terms of the agreements. The Company reduces such risk by limiting its exposure to any one counterparty. In addition, the potential risk of loss with any one party resulting from this type of credit risk is monitored. The Company’s interest rate swaps are required to be cleared on an exchange, which further mitigates, but does not eliminate, credit risk. Management does not expect any material losses as a result of default by other parties to its derivative financial instruments.

Classification – All derivatives are recognized as either assets or liabilities on the consolidated balance sheets and measured at fair value. Due to the nature of these instruments, they may be in a receivable/asset position or a payable/liability position at the end of an accounting period. Derivative amounts payable to, and receivable from, the same party under a contract may be offset as long as the following conditions are met: (i) each of the two parties owes the other determinable amounts; (ii) the reporting party has the right to offset the amount owed with the amount owed by the other party; (iii) the reporting party intends to offset; and (iv) the right to offset is enforceable by law. The Company reports the fair value of derivative instruments gross of cash paid or received pursuant to credit support agreements, and fair value may be reflected on a net counterparty basis when the Company believes a legal right of offset exists under an enforceable master netting agreement. For further discussion on offsetting assets and liabilities, see Note 8.

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Revenue Recognition – With respect to derivatives that have not been designated as hedges, any payments under, or fluctuations in the fair value of, such derivatives have been recognized currently in “Realized and unrealized gains (losses) on derivatives, net” in the consolidated statements of income.

Cash and Cash Equivalents and Restricted Cash

The Company considers all highly liquid short-term investments with maturities of 90 days or less when purchased to be cash equivalents. Substantially all amounts on deposit with major financial institutions exceed insured limits. Restricted cash represents the Company’s cash held by counterparties (i) as collateral against the Company’s derivatives ($1.9 million and $549,000 at March 31, 2018 and December 31, 2017, respectively) and (ii) as collateral for borrowings under its repurchase agreements (approximately $33.4 million and $28.6 million at March 31, 2018 December 31, 2017, respectively).

The Company’s centrally cleared interest rate swaps require that the Company posts an “initial margin” amount determined by the clearing exchange, which is generally intended to be set at a level sufficient to protect the exchange from the interest rate swap’s maximum estimated single-day price movement. The Company also exchanges “variation margin” based upon daily changes in fair value, as measured by the exchange. As a result of amendments to rules governing certain central clearing activities, the exchange of variation margin is a settlement of the interest rate swap, as opposed to pledged collateral. Accordingly, beginning in the first quarter of 2018 and in subsequent periods, the Company will account for the receipt or payment of variation margin as a direct reduction to the carrying value of the interest rate swap asset or liability. At March 31, 2018, $18.9 million of variation margin was reported as a reduction to interest rate swaps, at fair value. As of December 31, 2017, variation margin pledged or received is netted on a counterparty basis and classified within restricted cash, due from counterparties, or due to counterparties on the Company’s consolidated balance sheets.

Due to Affiliates

The sum under “Due to affiliates” on the consolidated balance sheets represents amounts due to the Manager pursuant to the Management Agreement. For further information on the Management Agreement, see Note 7.

Income Taxes

The Company elected to be taxed as a REIT under Code Sections 856 through 860 beginning with its short taxable year ended December 31, 2013. As a REIT, the Company generally will not be subject to U.S. federal income tax to the extent that it distributes its taxable income to its stockholders and does not engage in prohibited transactions. The Company’s taxable REIT subsidiaries (“TRSs”), CHMI Solutions and Aurora, are subject to U.S. federal income taxes on their taxable income. To maintain qualification as a REIT, the Company must distribute at least 90% of its annual REIT taxable income to its stockholders and meet certain other requirements such as assets it may hold, income it may generate and its stockholder composition.

The Company accounts for income taxes in accordance with ASC 740, Income Taxes. ASC 740 requires the recording of deferred income taxes that reflect the net tax effect of temporary differences between the carrying amounts of the Company’s assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, including operating loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in earnings in the period that includes the enactment date. The Company assesses its tax positions for all open tax years and determines if it has any material unrecognized liabilities in accordance with ASC 740. The Company records these liabilities to the extent it deems them more-likely-than-not to be incurred. The Company records interest and penalties related to income taxes within the provision for income taxes in the consolidated statements of income. The Company has not incurred

any interest or penalties.



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Realized Gain (Loss) on Investments, Net

The following table presents gains and losses on sales of the specified categories of investments for the periods indicated (dollars in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Realized gain (loss) on RMBS, net | | |
| Loss on RMBS | $ (4,881) | $ (256) |
| Net realized gain (loss) on RMBS | (4,881) | (256) |
| Realized gain (loss) on derivatives, net | 13 | (1,017) |
| Unrealized gain (loss) on derivatives, net | 19,626 | 1,082 |
| Realized gain on Excess MSRs, net | - | 6,678 |
| Unrealized gain (loss) on MSRs, net | 12,498 | 12,312 |
| Total | $ 27,256 | $ 18,799 |

Repurchase Agreements and Interest Expense

The Company finances its investments in RMBS with short-term borrowings under master repurchase agreements. Borrowings under the repurchase agreements are generally short-term debt due within one year. These borrowings generally bear interest rates of a specified margin over one-month LIBOR. The repurchase agreements represent uncommitted financing. Borrowings under these agreements are treated as collateralized financing transactions and are carried at their contractual amounts, as specified in the respective agreements. Interest is recorded at the contractual amount on an accrual basis.

Dividends Payable

Because the Company is organized as a REIT under the Code, it is required by law to distribute annually at least 90% of its REIT taxable income, which it does in the form of quarterly dividend payments. The Company accrues the dividend payable on the accounting date, which causes an offsetting reduction in retained earnings.

Comprehensive Income

Comprehensive income is defined as the change in equity of a business enterprise during a period resulting from transactions and other events and circumstances, excluding those resulting from investments by and distributions to owners. For the Company’s purposes, comprehensive income represents net income, as presented in the consolidated statements of income, adjusted for unrealized gains or losses on RMBS, which are designated as available for sale.

Recent Accounting Pronouncements

Revenue Recognition – In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers (“ASU 2014-09”), which supersedes the revenue recognition requirements in ASC 605, Revenue Recognition, and most industry-specific guidance throughout the Industry Topics of the Codification. Under the new revenue recognition guidance, entities are required to identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract and recognize revenue when (or as) the entity satisfies a performance obligation. In April 2015, the FASB voted for a one-year deferral of the effective date, resulting in this new guidance being effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017. Adoption of this guidance is delayed until the first SEC filing after the Company loses its emerging growth company status, which is expected to be December 31, 2018. Subsequent to the

initial issuance, the FASB has continued to issue updates to this guidance to provide additional clarification and implementation instructions to issuers regarding (i) principal versus agent considerations, (ii) identifying performance obligations, (iii) licensing, and (iv) narrow-scope improvements and practical expedients relating to assessing collectability, presentation of sales taxes, non-cash consideration, and completed contracts and contract modifications at transition. Entities have the option of using either a full retrospective or a modified approach to adopt the guidance in ASU 2014-09. The Company evaluated the new guidance and determined that interest income, gains and losses on financial instruments and income from servicing residential mortgage loans are outside the scope of ASU 2014-09. For income from servicing residential mortgage loans, the Company considered that the FASB Transition Resource Group members generally agreed that an entity should look to ASC 860, Transfers and Servicing ("ASC 860"), to determine the appropriate accounting for these fees and ASU 2014-09 contains a scope exception for contracts that fall under ASC 860. As a result, the Company does not expect the adoption of ASU 2014-09 to have a material impact on its consolidated financial statements.

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Credit Losses – In June 2016, the FASB issued ASU 2016-13, Financial Instruments—Credit Losses, an accounting standards update that changes the impairment model for most financial assets and certain other instruments. Allowances for credit losses on Available-for-Sale debt securities will be recognized, rather than direct reductions in the amortized cost of the investments. The new model also requires the estimation of lifetime expected credit losses and corresponding recognition of allowance for losses on trade and other receivables, held-to-maturity debt securities, loans, and other instruments held at amortized cost. This guidance requires certain recurring disclosures and is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2019, with early adoption permitted for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. The Company is evaluating the adoption of this ASU.

Statement of Cash Flows – In August 2016, the FASB issued ASU 2016-15, Classification of Certain Cash Receipts and Cash Payments, an accounting standards update that amends the guidance on the classification of certain cash receipts and cash payments presented within the statement of cash flows to reduce the existing diversity in practice. This guidance is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. Adoption of this guidance is delayed until the first SEC filing after the Company loses its emerging growth company status, which is expected to be December 31, 2018. The Company is currently evaluating the effect that this guidance will have on its consolidated financial statements.

Income Taxes – In October 2016, the FASB issued ASU 2016-16, Income Taxes, an accounting standards update that amends the guidance on the classification of income taxes related to the intra-entity transfer of assets other than inventory. This guidance is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. Adoption of this guidance is delayed until the first SEC filing after the Company loses its emerging growth company status, which is expected to be December 31, 2018. The Company is currently evaluating the effect that this guidance will have on its consolidated financial statements. However, the significance of adoption is dependent on the nature of the transactions and corresponding tax laws in effect at the time of adoption.

Restricted Cash – In November 2016, the FASB issued ASU 2016-18, Restricted Cash, an accounting standards update that amends the guidance on restricted cash within the statement of cash flows. The update amends the classification of restricted cash and cash equivalents to be included within cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts. This guidance is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. Adoption of this guidance is delayed until the first SEC filing after the Company loses its emerging growth company status, which is expected to be December 31, 2018. The adoption will impact the presentation of the cash flows, but will not otherwise have a material impact on the consolidated results of operations or financial condition of the Company.

Note 3 — Segment Reporting

The Company conducts its business through the following segments: (i) investments in RMBS; (ii) investments in Servicing Related Assets; and (iii) "All Other," which consists primarily of general and administrative expenses, including fees paid to the Company's directors and management fees and reimbursements paid to the Manager pursuant to the Management Agreement (See Note 7). For segment reporting purposes, the Company does not allocate interest income on short-term investments or general and administrative expenses.

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Summary financial data with respect to the Company's segments is given below, together with a reconciliation to the same data for the Company as a whole (dollars in thousands):

| | Servicing Related Assets | RMBS | All Other | Total |
|---|---|---|---|---|
| Income Statement | | | | |
| Three Months Ended March 31, 2018 | | | | |
| Interest income | $ - | $13,415 | $ - | $13,415 |
| Interest expense | 213 | 7,330 | - | 7,543 |
| Net interest income | (213) | 6,085 | - | 5,872 |
| Servicing fee income | 8,650 | - | - | 8,650 |
| Servicing costs | 1,712 | - | - | 1,712 |
| Net servicing income | 6,938 | - | - | 6,938 |
| Other income | 12,498 | 14,758 | - | 27,256 |
| Other operating expenses | - | - | 2,192 | 2,192 |
| Provision for corporate business taxes | 2,635 | - | - | 2,635 |
| Net income (loss) | $ 16,588 | $20,843 | $ (2,192) | $35,239 |
| Three Months Ended March 31, 2017 | | | | |
| Interest income | $ 523 | $5,555 | $ - | $6,078 |
| Interest expense | 114 | 2,317 | - | 2,431 |
| Net interest income | 409 | 3,238 | - | 3,647 |
| Servicing fee income | 4,574 | - | - | 4,574 |
| Servicing costs | 1,227 | - | - | 1,227 |
| Net servicing income | 3,347 | - | - | 3,347 |
| Other income | 18,990 | (191) | - | 18,799 |
| Other operating expenses | - | - | 1,867 | 1,867 |
| Provision for corporate business taxes | 1,339 | - | - | 1,339 |
| Net income (loss) | $ 21,407 | $3,047 | $ (1,867) | $22,587 |
| | | | | |
| Balance Sheet | | | | |
| March 31, 2018 | | | | |
| Investments | $ 188,145 | $1,642,682 | $ - | $1,830,827 |
| Other assets | 7,746 | 56,436 | 29,168 | 93,350 |
| Total assets | 195,891 | 1,699,118 | 29,168 | 1,924,177 |
| Debt | 74,749 | 1,500,562 | - | 1,575,311 |
| Other liabilities | 12,348 | 4,060 | 13,161 | 29,569 |
| Total liabilities | 87,097 | 1,504,622 | 13,161 | 1,604,880 |
| GAAP book value | $ 108,794 | $194,496 | $ 16,007 | $319,297 |

| December 31, 2017 | | | | |
|---|---|---|---|---|
| Investments | $122,806 | $1,840,912 | $- | $1,963,718 |
| Other assets | 8,281 | 48,631 | 30,055 | 86,967 |
| Total assets | 131,087 | 1,889,543 | 30,055 | 2,050,685 |
| Debt | 39,025 | 1,666,537 | - | 1,705,562 |
| Other liabilities | 6,575 | 4,385 | 11,706 | 22,666 |
| Total liabilities | 45,600 | 1,670,922 | 11,706 | 1,728,228 |
| Book value | $85,487 | $218,621 | $18,349 | $322,457 |

Note 4 — Investments in RMBS

All of the Company’s RMBS are classified as available for sale and are, therefore, reported at fair value with changes in fair value recorded in other comprehensive income (loss) except for securities that are OTTI (dollars in thousands):

Summary of RMBS Assets

As of March 31, 2018

| | Original | | Gross Unrealized | | | Number | Weighted Average | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Asset Type | Original Face Value | Book Value | Gains | Losses | Carrying Value(A) | Number of Securities | Rating | Coupon | Yield(C) | Maturity (Years)(D) |
| RMBS | | | | | | | | | | |
| Fannie Mae | $1,218,762 | $1,136,907 | $85 | $(28,746) | $1,108,246 | 145 | (B) | 3.80 % | 3.61 % | 26 |
| Freddie Mac | 502,220 | 452,615 | - | (11,859) | 440,756 | 59 | (B) | 3.73 % | 3.56 % | 27 |
| CMOs | 98,325 | 87,145 | 6,535 | - | 93,680 | 20 | Unrated | 5.80 % | 4.93 % | 11 |
| Total/Weighted Average | $1,819,307 | $1,676,667 | $6,620 | $(40,605) | $1,642,682 | 224 | | 3.90 % | 3.67 % | 25 |

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As of December 31, 2017

| Asset Type | Original Face Value | Book Value | Gross Unrealized Gains | Gross Unrealized Losses | Carrying Value(A) | Number of Securities | Weighted Average Rating | Weighted Average Coupon | Weighted Average Yield(C) | Weighted Average Maturity (Years)(D) |
|---|---|---|---|---|---|---|---|---|---|---|
| RMBS | | | | | | | | | | |
| Fannie Mae | $1,306,823 | $1,241,027 | $1,427 | $(8,755) | $1,233,699 | 154 | (B) | 3.80% | 3.61% | 26 |
| Freddie Mac | 556,204 | 515,475 | 864 | (2,795) | 513,544 | 64 | (B) | 3.74% | 3.57% | 27 |
| CMOs | 98,325 | 87,353 | 6,343 | (27) | 93,669 | 20 | Unrated | 5.26% | 4.88% | 12 |
| Total/Weighted Average | $1,961,352 | $1,843,855 | $8,634 | $(11,577) | $1,840,912 | 238 | | 3.86% | 3.66% | 25 |

(A) See Note 9 regarding the estimation of fair value, which approximates carrying value for all securities.
(B) The Company used an implied AAA rating for the Fannie Mae and Freddie Mac securities, other than collateralized mortgage obligations ("CMOs"), which are unrated.
(C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the book value of settled securities.
(D) The weighted average maturity is based on the timing of expected principal reduction on the assets.

Summary of RMBS Assets by Maturity

As of March 31, 2018

| Years to Maturity | Original Face Value | Book Value | Gross Unrealized Gains | Gross Unrealized Losses | Carrying Value(A) | Number of Securities | Weighted Average Rating | Weighted Average Coupon | Weighted Average Yield(C) | Weighted Average Maturity (Years)(D) |
|---|---|---|---|---|---|---|---|---|---|---|
| 5-10 Years | $3,500 | $2,778 | $323 | $- | $3,101 | 2 | (B) | 6.12% | 5.56% | 7 |
| Over 10 Years | 1,815,807 | 1,673,889 | 6,297 | (40,605) | 1,639,581 | 222 | (B) | 3.89% | 3.66% | 25 |
| Total/Weighted Average | $1,819,307 | $1,676,667 | $6,620 | $(40,605) | $1,642,682 | 224 | | 3.90% | 3.67% | 25 |

As of December 31, 2017

| Years to Maturity | Original Face Value | Book Value | Gross Unrealized Gains | Gross Unrealized Losses | Carrying Value(A) | Number of Securities | Weighted Average Rating | Weighted Average Coupon | Weighted Average Yield(C) | Weighted Average Maturity (Years)(D) |
|---|---|---|---|---|---|---|---|---|---|---|
| 5-10 Years | $16,069 | $15,483 | $324 | $(312) | $15,495 | 3 | (B) | 4.33% | 4.06% | 7 |
| Over 10 Years | 1,945,283 | 1,828,372 | 8,310 | (11,265) | 1,825,417 | 235 | (B) | 3.85% | 3.65% | 26 |
| Total/Weighted Average | $1,961,352 | $1,843,855 | $8,634 | $(11,577) | $1,840,912 | 238 | | 3.86% | 3.66% | 25 |

(A) See Note 9 regarding the estimation of fair value, which approximates carrying value for all securities.
(B) The Company used an implied AAA rating for the Fannie Mae and Freddie Mac securities, other than CMOs, which are unrated.
(C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the book value of settled securities.
(D) The weighted average maturity is based on the timing of expected principal reduction on the assets.

At March 31, 2018 and December 31, 2017, the Company pledged Agency RMBS with a carrying value of approximately $1,560.8 million and $1,728.6 million, respectively, as collateral for borrowings under repurchase agreements. At March 31, 2018 and December 31, 2017, the Company did not have any securities purchased from and financed with the same counterparty that did not meet the conditions of ASC 860 to be considered linked transactions and, therefore, classified as derivatives.

Based on management's analysis of the Company's securities, the performance of the underlying loans and changes in market factors, management determined that unrealized losses as of the balance sheet date on the Company's securities were primarily the result of changes in market factors, rather than issuer-specific credit impairment, and such losses were considered temporary. The Company performed analyses in relation to such securities, using management's best estimate of their cash flows, which support its belief that the carrying values of such securities were fully recoverable over their expected holding periods. Such market factors include changes in market interest rates and credit spreads and certain macroeconomic events, none of which will directly impact the Company's ability to collect amounts contractually due. Management continually evaluates the credit status of each of the Company's securities and the collateral supporting those securities. This evaluation includes a review of the credit of the issuer of the security (if applicable), the credit rating of the security (if applicable), the key terms of the security (including credit support), debt service coverage and loan to value ratios, the performance of the pool of underlying loans and the estimated value of the collateral supporting such loans, including the effect of local, industry and broader economic trends and factors. Significant judgment is required in this analysis. In connection with the above, the Company weighs the fact that all of its investments in RMBS are guaranteed by U.S. government agencies or U.S. government sponsored enterprises.

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Unrealized losses that are considered OTTI are recognized in earnings. The Company recorded approximately $45,000 of OTTI during the three month period ended March 31, 2018. The Company did not record any OTTI charges during the three month period ended March 31, 2017.

The following tables summarize the Company's securities in an unrealized loss position as of the dates indicated (dollars in thousands):

RMBS Unrealized Loss Positions

As of March 31, 2018

| Duration in Loss Position | Original Face Value | Book Value | Gross Unrealized Losses | Carrying Value(A) | Number of Securities | Weighted Average Rating | Weighted Average Coupon | Weighted Average Yield(C) | Weighted Average Maturity (Years)(D) |
|---|---|---|---|---|---|---|---|---|---|
| Less than Twelve Months | $1,403,123 | $1,317,506 | $(30,085) | $1,287,421 | 160 | (B) | 3.81 % | 3.63 % | 26 |
| Twelve or More Months | 287,634 | 251,176 | (10,520) | 240,656 | 41 | (B) | 3.59 % | 3.38 % | 26 |
| Total/Weighted Average | $1,690,757 | $1,568,682 | $(40,605) | $1,528,077 | 201 | | 3.78 % | 3.59 % | 26 |

As of December 31, 2017

| Duration in Loss Position | Original Face Value | Book Value | Gross Unrealized Losses | Carrying Value(A) | Number of Securities | Weighted Average Rating | Weighted Average Coupon | Weighted Average Yield(C) | Weighted Average Maturity (Years)(D) |
|---|---|---|---|---|---|---|---|---|---|
| Less than Twelve Months | $1,026,911 | $1,005,352 | $(5,378) | $999,974 | 111 | (B) | 3.81 % | 3.63 % | 26 |
| Twelve or More Months | 323,858 | 289,599 | (6,199) | 283,400 | 45 | (B) | 3.61 % | 3.40 % | 25 |
| Total/Weighted Average | $1,350,769 | $1,294,951 | $(11,577) | $1,283,374 | 156 | | 3.76 % | 3.58 % | 26 |

(A) See Note 9 regarding the estimation of fair value, which approximates carrying value for all securities.

(B) The Company used an implied AAA rating for the Fannie Mae and Freddie Mac securities, other than CMOs, which are unrated.

(C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the book value of settled securities.

(D) The weighted average maturity is based on the timing of expected principal reduction on the assets. Except for the security for which the Company has recognized OTTI, the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost bases which may be maturity.

Note 5 — Investments in Servicing Related Assets

Excess MSRs

In 2013 and 2014, the Company acquired Excess MSRs from Freedom Mortgage and entered into recapture agreements with Freedom Mortgage. For reporting purposes, these Excess MSRs were aggregated into three pools: Excess MSR Pool 1, Excess MSR Pool 2 and Excess MSR Pool 2014.

Excess MSR Pool 1 and Excess MSR Pool 2014 were sold to Freedom Mortgage on November 15, 2016, and Excess MSR Pool 2 was sold to Freedom Mortgage on February 1, 2017. Each recapture agreement between the Company and Freedom Mortgage was terminated at the time the related pool was sold. See Note 7.

MSRs

On May 29, 2015, in conjunction with the acquisition of Aurora, the Company acquired MSRs on conventional mortgage loans with an aggregate unpaid principal balance ("UPB") of approximately $718.4 million at the time of acquisition.

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Subsequently, Aurora acquired portfolios of Fannie Mae, Freddie Mac and Ginnie Mae MSRs with an aggregate UPB of approximately $16.9 billion as of the respective acquisition dates. See Note 7 for a description of the Company's acquisition of MSRs from Freedom Mortgage in connection with the sale by the Company of its Excess MSRs to Freedom Mortgage.

In June 2016, Aurora entered into a joint marketing recapture agreement with Freedom Mortgage. Pursuant to this agreement, Freedom Mortgage attempts to refinance certain mortgage loans underlying Aurora's MSR portfolio as directed by Aurora. See Note 7.

The following is a summary of the Company's Servicing Related Assets as of the dates indicated (dollars in thousands):

Servicing Related Assets Summary
As of March 31, 2018

| | Unpaid Principal Balance | Cost Basis | | Carrying Value(A) | Weighted Average Coupon | | Weighted Average Maturity (Years)(B) | Changes in Fair Value Recorded in Other Income (Loss) |
|---|---|---|---|---|---|---|---|---|
| MSRs | | | | | | | | |
| Conventional | $11,809,591 | $134,991 | (C) | $145,001 | 4.01 | % | 26.6 | $ 10,010 |
| Government | 3,864,093 | 40,656 | (C) | 43,144 | 3.36 | % | 27.5 | 2,488 |
| Total / Weighted Average | $15,673,684 | $175,647 | | $188,145 | 3.85 | % | 26.8 | $ 12,498 |

As of December 31, 2017

| | Unpaid Principal Balance | Cost Basis | | Carrying Value(A) | Weighted Average Coupon | | Weighted Average Maturity (Years)(B) | Changes in Fair Value Recorded in Other Income (Loss) |
|---|---|---|---|---|---|---|---|---|
| MSRs | | | | | | | | |
| Conventional | $7,724,397 | $81,499 | (C) | $82,150 | 3.89 | % | 25.2 | $ 651 |
| Government | 3,986,254 | 32,148 | (C) | 40,656 | 3.36 | % | 27.8 | 8,508 |
| Total / Weighted Average | $11,710,651 | $113,647 | | $122,806 | 3.71 | % | 26.1 | $ 9,159 |

(A) Carrying value represents the fair value of the pools or recapture agreements, as applicable (see Note 9).
(B) The weighted average maturity represents the weighted average expected timing of the receipt of cash flows of each investment.
(C) MSR cost basis consists of the carrying value of the prior period, adjusted for any purchases, sales and principal paydowns of the underlying mortgage loans.

The tables below summarize the geographic distribution for the states representing 5% or greater of the underlying residential mortgage loans of the Servicing Related Assets as of the dates indicated:

Geographic Concentration of Servicing Related Assets
As of March 31, 2018

| | Percentage of Total Outstanding Unpaid Principal Balance | |
|---|---|---|
| California | 17.0 | % |
| New Jersey | 5.7 | % |
| New York | 5.5 | % |
| Florida | 5.0 | % |
| All other | 66.8 | % |
| Total | 100.0 | % |

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As of December 31, 2017

| | Percentage of Total Outstanding Unpaid Principal Balance | |
|---|---|---|
| California | 13.7 | % |
| New Jersey | 7.2 | % |
| Florida | 5.3 | % |
| All other | 73.8 | % |
| Total | 100.0 | % |

Geographic concentrations of investments expose the Company to the risk of economic downturns within the relevant states. Any such downturn in a state where the Company holds significant investments could affect the underlying borrower's ability to make the mortgage payment and, therefore, could have a meaningful, negative impact on the Company's Servicing Related Assets.

Note 6 — Equity and Earnings per Common Share

Equity Incentive Plan

During 2013, the board of directors approved and the Company adopted the Cherry Hill Mortgage Investment Corporation 2013 Equity Incentive Plan (the "2013 Plan"). The 2013 Plan provides for the grant of options to purchase shares of the Company's common stock, stock awards, stock appreciation rights, performance units, incentive awards and other equity-based awards, including long term incentive plan units ("LTIP-OP Units") of the Operating Partnership.

LTIP-OP Units are a special class of partnership interest in the Operating Partnership. LTIP-OP Units may be issued to eligible participants for the performance of services to or for the benefit of the Operating Partnership. Initially, LTIP-OP Units do not have full parity with the Operating Partnership's common units of limited partnership interest ("OP Units") with respect to liquidating distributions; however, LTIP-OP Units receive, whether vested or not, the same per-unit distributions as OP Units and are allocated their pro-rata share of the Operating Partnership's net income or loss. Under the terms of the LTIP-OP Units, the Operating Partnership will revalue its assets upon the occurrence of certain specified events, and any increase in the Operating Partnership's valuation from the time of grant of the LTIP-OP Units until such event will be allocated first to the holders of LTIP-OP Units to equalize the capital accounts of such holders with the capital accounts of the holders of OP Units. Upon equalization of the capital accounts of the holders of LTIP-OP Units with the other holders of OP Units, the LTIP-OP Units will achieve full parity with OP Units for all purposes, including with respect to liquidating distributions. If such parity is reached, vested LTIP-OP Units may be converted into an equal number of OP Units at any time and, thereafter, enjoy all the rights of OP Units, including redemption rights. Each LTIP-OP Unit awarded is deemed equivalent to an award of one share of the Company's common stock under the 2013 Plan and reduces the 2013 Plan's share authorization for other awards on a one-for-one basis.

An LTIP-OP Unit and a share of common stock of the Company have substantially the same economic characteristics in as much as they effectively share equally in the net income or loss of the Operating Partnership. Holders of LTIP-OP Units that have reached parity with OP Units have the right to redeem their LTIP-OP Units, subject to certain restrictions. The redemption is required to be satisfied in cash, or at the Company's option, the Company may purchase the OP Units for common stock, calculated as follows: one share of the Company's common stock, or cash equal to the fair value of a share of the Company's common stock at the time of redemption, for each LTIP-OP Unit. When an LTIP-OP Unit holder redeems an OP Unit (as described above), non-controlling interest in the Operating Partnership is reduced and the Company's equity is increased.

LTIP-OP Units vest ratably over the first three annual anniversaries of the grant date. The fair value of each LTIP-OP Unit was determined based on the closing price of the Company's common stock on the applicable grant date in all other cases.

The following table sets forth the number of shares of the Company's common stock and the values thereof (based on the closing prices on the respective dates of grant) granted to the Company's independent directors under the 2013 Plan. Except as otherwise indicated, all shares are fully vested.

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The following tables present certain information about the 2013 Plan as of the dates indicated:

Equity Incentive Plan Information

| | LTIP-OP Units | | | Shares of Common Stock | | Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans | Issuance Price |
|---|---|---|---|---|---|---|---|
| | Issued | Forfeited | Converted | Issued | Forfeited | | |
| December 31, 2016 | (140,350) | 916 | - | (28,503) | 3,155 | 1,335,218 | |
| Number of securities issued or to be issued upon exercise | - | - | - | - | - | - | |
| March 31, 2017 | (140,350) | 916 | - | (28,503) | 3,155 | 1,335,218 | |
| Number of securities issued or to be issued upon exercise | (38,150) | - | - | (8,199) | - | (46,349) | $ 18.30 |
| June 30, 2017 | (178,500) | 916 | - | (36,702) | 3,155 | 1,288,869 | |
| Number of securities issued or to be issued upon exercise | - | - | 12,917 | (12,917) | - | - | $ 18.44 |
| September 30, 2017 | (178,500) | 916 | 12,917 | (49,619) | 3,155 | 1,288,869 | |
| Number of securities issued or to be issued upon exercise | - | - | - | - | - | - | |
| December 31, 2017 | (178,500) | 916 | 12,917 | (49,619) | 3,155 | 1,288,869 | |
| Number of securities issued or to be issued upon exercise | - | - | - | - | - | - | |
| March 31, 2018 | (178,500) | 916 | 12,917 | (49,619) | 3,155 | 1,288,869 | |

The Company recognized approximately $138,000 and $135,000 in share-based compensation expense in the three month period ended March 31, 2018 and March 31, 2017, respectively. There was approximately $762,000 and $900,000 of total unrecognized share-based compensation expense as of March 31, 2018 and December 31, 2017, respectively, all of which was related to unvested LTIP-OP Units. This unrecognized share-based compensation expense is expected to be recognized ratably over the remaining vesting period of up to three years. The aggregate expense related to the LTIP-OP Unit grants is presented as “General and administrative expense” in the Company’s consolidated statements of income.

Non-Controlling Interests in Operating Partnership

Non-controlling interests in the Operating Partnership in the accompanying consolidated financial statements relate to LTIP-OP Units and OP Units issued upon conversion of LTIP-OP Units, in either case, held by parties other than the Company.

As of March 31, 2018, the non-controlling interest holders in the Operating Partnership owned 164,667 LTIP-OP Units, or approximately 1.3% of the units of the Operating Partnership. Pursuant to ASC 810, Consolidation, changes in a parent’s ownership interest (and transactions with non-controlling interest unit holders in the Operating Partnership) while the parent retains its controlling interest in its subsidiary should be accounted for as equity transactions. The carrying amount of the non-controlling interest will be adjusted to reflect the change in its ownership interest in the subsidiary, with the offset to equity attributable to the Company.

Preferred Stock

The Company is authorized to issue up to 100,000,000 shares of preferred stock, $0.01 par value per share, of which 97,470,000 shares were undesignated and 2,530,000 shares were designated as Series A Preferred Stock as of March 31, 2018.

On August 17, 2017, the Company completed an offering of 2,400,000 shares of Series A Preferred Stock for net proceeds of $58.1 million after underwriting discounts and commissions but before expenses of approximately $193,000.

The Series A Preferred Stock ranks senior to the Company's common stock with respect to rights to the payment of dividends and the distribution of assets upon the Company's liquidation, dissolution or winding up. The Series A Preferred Stock has no stated maturity, is not subject to any sinking fund or mandatory redemption and will remain outstanding indefinitely unless repurchased or redeemed by the Company or converted by the holders of the Series A Preferred Stock into the Company's common stock in connection with certain changes of control. The Series A Preferred Stock is not redeemable by the Company prior to August 17, 2022, except under circumstances intended to preserve the Company's qualification as a REIT for U.S. federal income tax purposes and except upon the occurrence of certain changes of control. On and after August 17, 2022, the Company may, at its option, redeem the Series A Preferred Stock, in whole or in part, at any time or from time to time, for cash at a redemption price equal to $25.00 per share, plus any accumulated and unpaid dividends to, but not including, the date fixed for redemption. If the Company does not exercise its rights to redeem the Series A Preferred Stock upon certain changes in control, the holders of the Series A Preferred Stock have the right to convert some or all of their shares of Series A Preferred Stock into a number of shares of the Company's common stock based on a defined formula, subject to a share cap, or alternative consideration. The share cap on each share of Series A Preferred Stock is 2.62881 shares of common stock, subject to certain adjustments. The Company pays cumulative cash dividends at the rate of 8.20% per annum of the $25.00 per share liquidation preference (equivalent to $2.05 per annum per share) on the Series A Preferred Stock, in arrears, on or about the $15^{th}$ day of January, April, July and October of each year.

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On April 5, 2018, the Company filed Articles Supplementary with the State Department of Assessments and Taxation of Maryland to classify and designate 1,270,000 shares of the Company's authorized but unissued preferred stock, par value $0.01 per share, as shares of Series A Preferred Stock, with the terms and conditions of the Series A Preferred Stock described above. The Articles Supplementary became effective upon filing on April 5, 2018, and upon such effectiveness, the Company was authorized to issue an aggregate of 3,800,000 shares of Series A Preferred Stock. See Note 16.

Earnings per Common Share

The Company is required to present both basic and diluted earnings per common share ("EPS"). Basic EPS is calculated by dividing net income (loss) applicable to common stockholders by the weighted average number of shares of common stock outstanding during each period. Diluted EPS is calculated by dividing net income (loss) applicable to common stockholders by the weighted average number of shares of common stock outstanding plus the additional dilutive effect of common stock equivalents during each period. In accordance with ASC 260, Earnings Per Share, if there is a loss from continuing operations, the common stock equivalents are deemed anti-dilutive and earnings (loss) per share is calculated excluding the potential common shares.

The following table presents basic earnings per share of common stock for the periods indicated (dollars in thousands, except per share data):

Earnings per Common Share Information

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Numerator: | | |
| Net income allocable to common stockholders | $ 35,239 | $ 22,587 |
| Net (income) loss allocated to noncontrolling interests in Operating Partnership | (456 ) | (409 ) |
| Dividends on preferred stock | 1,213 | - |
| Net income attributable to common stockholders | $ 33,570 | $ 22,178 |
| Denominator: | | |
| Weighted average common shares outstanding | 12,713,265 | 7,634,038 |
| Weighted average diluted shares outstanding | 12,721,464 | 7,640,348 |
| Basic and Diluted: | | |
| Basic earnings per share | $ 2.64 | $ 2.91 |
| Diluted earnings per share | $ 2.64 | $ 2.90 |

There were no participating securities or equity instruments outstanding that were anti-dilutive for purposes of calculating EPS for the periods presented.

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Note 7 — Transactions with Affiliates and Affiliated Entities

Manager

The Company has entered into the Management Agreement with the Manager, pursuant to which the Manager provides for the day-to-day management of the Company's operations. The Management Agreement requires the Manager to manage the Company's business affairs in conformity with the policies that are approved and monitored by the Company's board of directors. The term of the Management Agreement will expire on October 22, 2020 and will be automatically renewed for a one-year term on such date and on each anniversary of such date thereafter unless terminated or not renewed as described below. Either we or our Manager may elect not to renew the Management Agreement upon expiration of its initial term or any renewal term by providing written notice of non-renewal at least 180 days, but not more than 270 days, before expiration. In the event we elect not to renew the term, we will be required to pay our Manager a termination fee equal to three times the average annual management fee amount earned by the Manager during the two four-quarter periods ending as of the end of the most recently completed fiscal quarter prior to the non-renewal. We may terminate the Management Agreement at any time for cause effective upon 30 days prior written notice of termination from us to our Manager, in which case no termination fee would be due. Our board of directors will review our Manager's performance prior to the automatic renewal thereof and, as a result of such review, upon the affirmative vote of at least two-thirds of the members of our board of directors or of the holders of a majority of our outstanding common stock, we may terminate the Management Agreement based upon unsatisfactory performance by our Manager that is materially detrimental to us or a determination by our independent directors that the management fees payable to our Manager are not fair, subject to the right of our Manager to prevent such a termination by agreeing to a reduction of the management fees payable to our Manager. Upon any termination of the Management Agreement based on unsatisfactory performance or unfair management fees, we are required to pay our Manager the termination fee described above. Our Manager may terminate the Management Agreement, without payment of the termination fee, in the event we become regulated as an investment company under the Investment Company Act of 1940, as amended. Our Manager may also terminate the Management Agreement upon 60 days' written notice if we default in the performance of any material term of the Management Agreement and the default continues for a period of 30 days after written notice to us, whereupon we would be required to pay our Manager the termination fee described above. Pursuant to the Management Agreement, the Manager, under the supervision of the Company's board of directors, formulates investment strategies, arranges for the acquisition of assets, arranges for financing, monitors the performance of the Company's assets and provides certain advisory, administrative and managerial services in connection with the operations of the Company. For performing these services, the Company pays the Manager the management fee which is payable in cash quarterly in arrears, in an amount equal to 1.5% per annum of the Company's stockholders' equity (as defined in the Management Agreement).

The Manager is a party to a services agreement (the "Services Agreement") with Freedom Mortgage, pursuant to which Freedom Mortgage provides to the Manager the personnel, services and resources needed by the Manager to carry out its obligations and responsibilities under the Management Agreement. The Company is a named third-party beneficiary to the Services Agreement and, as a result, has, as a non-exclusive remedy, a direct right of action against Freedom Mortgage in the event of any breach by the Manager of any of its duties, obligations or agreements under the Management Agreement that arise out of or result from any breach by Freedom Mortgage of its obligations under the Services Agreement. The Services Agreement will terminate upon the termination of the Management Agreement. Pursuant to the Services Agreement, the Manager will make certain payments to Freedom Mortgage in connection with the services provided. The Management Agreement between the Company and the Manager was negotiated between related parties, and the terms, including fees payable, may not be as favorable to the Company as if it had been negotiated with an unaffiliated third party. At the time the Management Agreement was negotiated, both the Manager and Freedom Mortgage were controlled by Mr. Stanley Middleman, who is also a shareholder of the Company. Ownership of the Manager has been transferred to CHMM Blind Trust, a grantor trust for the benefit of Mr. Middleman.

The Management Agreement provides that the Company will reimburse the Manager for (i) various expenses incurred by the Manager or its officers, and agents on the Company's behalf, including costs of software, legal, accounting, tax, administrative and other similar services rendered for the Company by providers retained by the Manager and (ii) the allocable portion of the compensation paid to specified officers dedicated to the Company. The amounts under "Due to affiliates" on the consolidated balance sheets consisted of the following for the periods indicated (dollars in thousands):

Management Fees and Compensation Reimbursement to Affiliate

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Management fees | $ 1,124 | $ 701 |
| Compensation reimbursement | 191 | 191 |
| Total | $ 1,315 | $ 892 |

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Subservicing Agreement

Freedom Mortgage is directly servicing the majority of the Company's portfolio of Fannie Mae and Freddie Mac MSRs and all of its Ginnie Mae MSRs pursuant to a subservicing agreement entered into on June 10, 2015. The agreement has an initial term of three years, expiring on September 1, 2018, and is subject to automatic renewal for additional three year terms unless either party chooses not to renew. The agreement may be terminated without cause by either party by giving notice as specified in the agreement. Under that agreement, Freedom Mortgage agrees to service the applicable mortgage loans in accordance with applicable law and the requirements of the applicable agency and the Company pays customary fees to Freedom Mortgage for specified services.

Joint Marketing Recapture Agreement

In June 2016, Aurora entered into a joint marketing recapture agreement with Freedom Mortgage. Pursuant to this agreement, Freedom Mortgage attempts to refinance certain mortgage loans underlying Aurora's MSR portfolio subserviced by Freedom Mortgage as directed by Aurora. If a loan is refinanced, Aurora will pay Freedom Mortgage a fee for its origination services. Freedom Mortgage will be entitled to sell the loan for its own benefit and will transfer the related MSR to Aurora. The agreement had an initial term of one year, subject to automatic renewals of one year each and subject to termination by either party upon 60 days prior notice. All new loans must qualify for sale to Fannie Mae or Freddie Mac or be eligible for pooling with Ginnie Mae, as applicable, and meet other conditions set forth in the agreement. During the three month period ended March 31, 2018, MSRs on 48 loans with an aggregate UPB of approximately $10.3 million had been received from Freedom Mortgage which generated approximately $15,300 in fees due to Freedom Mortgage. During the year ended December 31, 2017, MSRs on 116 loans with an aggregate UPB of approximately $27.6 million had been received from Freedom Mortgage which generated approximately $43,000 in fees due to Freedom Mortgage.

Sale of Excess MSRs

On November 15, 2016, the Company sold the Excess MSRs in Excess MSR Pool 1 and the Excess MSRs in Excess MSR Pool 2014 to Freedom Mortgage. At the closing, the Company received cash proceeds of approximately $38.0 million, repaid $12.0 million of outstanding borrowings drawn on the Company's $25 million term loan facility with NexBank SSB (the "NexBank term loan") with a portion of the cash proceeds and released the Company's security interests in the underlying MSRs. The Company invested the remaining cash proceeds in Agency RMBS. The Company sold the Excess MSRs in Excess MSR Pool 2 to Freedom Mortgage on February 1, 2017. In connection with the sale of the Excess MSRs in Excess MSR Pool 2 to Freedom Mortgage, Freedom Mortgage transferred to Aurora Ginnie Mae MSRs with a weighted average servicing fee of approximately 30 basis points at the time of acquisition. The Ginnie Mae MSRs relate to a pool consisting primarily of newly originated Ginnie Mae conforming mortgage loans that had an aggregate UPB of approximately $4.5 billion as of January 31, 2017. At the closing of the sale of the Excess MSRs in Excess MSR Pool 2, the Company repaid the remaining outstanding borrowings drawn on the NexBank term loan with cash on hand. In addition, the acknowledgment agreement that the Company and Freedom Mortgage entered into with Ginnie Mae at the time of the IPO was terminated.

In connection with the sale transactions, Freedom Mortgage made 12 monthly yield maintenance payments to the Company from December 2016 to November 2017 aggregating $3.0 million.

See Note 10 for a discussion of the now terminated acknowledgment agreement among the Company, Freedom Mortgage and Ginnie Mae.

Other Transactions with Affiliated Entities

In March 2017, the Company waived the forfeiture provisions of LTIP-OP Units previously granted to Mr. Middleman that otherwise would have been triggered once he no longer was a member of the Company’s board of directors.

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Note 8 — Derivative Instruments

Interest Rate Swap Agreements, Swaptions, TBAs and Treasury Futures

In order to help mitigate exposure to higher short-term interest rates in connection with borrowings under its repurchase agreements, the Company enters into interest rate swap agreements and swaption agreements. Interest rate swap agreements establish an economic fixed rate on related borrowings because the variable-rate payments received on the interest rate swap agreements largely offset interest accruing on the related borrowings, leaving the fixed-rate payments to be paid on the interest rate swap agreements as the Company's effective borrowing rate, subject to certain adjustments including changes in spreads between variable rates on the interest rate swap agreements and actual borrowing rates. A swaption is an option granting its owner the right but not the obligation to enter into an underlying swap. The Company's interest rate swap agreements and swaptions have not been designated as qualifying hedging instruments for GAAP purposes.

In order to help mitigate duration risk and manage basis risk, the Company utilizes Treasury futures and forward-settling purchases and sales of RMBS where the underlying pools of mortgage loans are TBAs. Pursuant to these TBA transactions, the Company agrees to purchase or sell, for future delivery, RMBS with certain principal and interest terms and certain types of underlying collateral, but the particular RMBS to be delivered is not identified until shortly before the TBA settlement date. Unless otherwise indicated, references to Treasury futures include options on Treasury futures.

The following table summarizes the outstanding notional amounts of derivative instruments as of the dates indicated (dollars in thousands):

| Derivatives | March 31, 2018 | December 31, 2017 |
|---|---|---|
| Notional amount of interest rate swaps | $ 1,141,750 | $ 1,067,950 |
| Notional amount of swaptions | 180,000 | 155,000 |
| Notional amount of TBAs, net | (50,300) | 26,900 |
| Notional amount of Treasury futures | (111,400) | - |
| Total notional amount | $ 1,160,050 | $ 1,249,850 |

The following table presents information about the Company's interest rate swap agreements as of the dates indicated (dollars in thousands):

| | Notional Amount | Weighted Average Pay Rate | Weighted Average Receive Rate | Weighted Average Years to Maturity |
|---|---|---|---|---|
| March 31, 2018 | $1,141,750 | 1.90 % | 1.89 % | 4.9 |
| December 31, 2017 | $1,067,950 | 1.83 % | 1.44 % | 4.9 |

The following table presents information about the Company's interest rate swaption agreements as of the dates indicated (dollars in thousands):

| | Notional Amount | Weighted Average Pay Rate | Weighted Average Receive Rate[(A)] | Weighted Average Years to Maturity |
|---|---|---|---|---|
| March 31, 2018 | $180,000 | 2.93 % | LIBOR-BBA % | 10.5 |
| December 31, 2017 | $155,000 | 2.88 % | LIBOR-BBA % | 10.8 |

Floats in accordance with LIBOR.

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The following table presents information about realized gain (loss) on derivatives, which is included on the consolidated statements of income for the periods indicated (dollars in thousands):

Realized Gains (Losses) on Derivatives

| Derivatives | Consolidated Statements of Income (Loss) Location | Three Months Ended March 31, 2018 | 2017 |
|---|---|---|---|
| Interest rate swaps | Realized gain (loss) on derivatives, net | $ (422) | $ (159) |
| Swaptions | Realized gain (loss) on derivatives, net | (274) | (69) |
| TBAs | Realized gain (loss) on derivatives, net | (29) | (112) |
| Treasury futures | Realized gain (loss) on derivatives, net | 738 | (677) |
| Total | | $ 13 | $ (1,017) |

Offsetting Assets and Liabilities

The Company has netting arrangements in place with all of its derivative counterparties pursuant to standard documentation developed by the International Swap and Derivatives Association. Under GAAP, if the Company has a valid right of offset, it may offset the related asset and liability and report the net amount. The Company presents interest rate swaps, swaptions and Treasury futures assets and liabilities on a gross basis in its consolidated balance sheets. The Company presents TBA assets and liabilities on a net basis in its consolidated balance sheets. The Company presents repurchase agreements in this section even though they are not derivatives because they are subject to master netting arrangements. However, repurchase agreements are presented on a gross basis. Additionally, the Company does not offset financial assets and liabilities with the associated cash collateral on the consolidated balance sheets.

The following tables present information about the Company's assets and liabilities that are subject to master netting arrangements or similar agreements and can potentially be offset on the Company's consolidated balance sheets as of the dates indicated (dollars in thousands):

Offsetting Assets and Liabilities
As of March 31, 2018

| | Gross Amounts of Recognized Assets or Liabilities | Gross Amounts Offset in the Consolidated Balance Sheet | Net Amounts of Assets Presented in the Consolidated Balance Sheet | Gross Amounts Not Offset in the Consolidated Balance Sheet: Financial Instruments | Cash Collateral Received (Pledged) | Net Amount |
|---|---|---|---|---|---|---|
| Assets | | | | | | |
| Interest rate swaps | $ 13,438 | $ - | $ 13,438 | $ (13,438) | $ - | $ - |
| Swaptions | 2,474 | - | 2,474 | (2,474) | - | - |
| TBAs | 193 | - | 193 | (193) | - | - |
| Total Assets | $ 16,105 | $ - | $ 16,105 | $ (16,105) | $ - | $ - |
| Liabilities | | | | | | |
| Repurchase agreements | $ 1,500,562 | $ - | $ 1,500,562 | $ (1,467,185) | $ (33,377) | $ - |
| Interest rate swaps | 57 | - | 57 | (57) | - | - |
| Treasury futures | 1,040 | - | 1,040 | 828 | (1,868) | - |
| Total Liabilities | $ 1,501,659 | $ - | $ 1,501,659 | $ (1,466,414) | $ (35,245) | $ - |

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As of December 31, 2017

| | Gross Amounts of Recognized Assets or Liabilities | Gross Amounts Offset in the Consolidated Balance Sheet | Net Amounts of Assets Presented in the Consolidated Balance Sheet | Gross Amounts Not Offset in the Consolidated Balance Sheet | | |
|---|---|---|---|---|---|---|
| | | | | Financial Instruments | Cash Collateral Received (Pledged) | Net Amount |
| Assets | | | | | | |
| Interest rate swaps | $ 12,994 | $ - | $ 12,994 | $ (12,994) | $ - | $ - |
| Swaptions | 802 | - | 802 | (802) | - | - |
| TBAs | 34 | - | 34 | (34) | - | - |
| Total Assets | $ 13,830 | $ - | $ 13,830 | $ (13,830) | $ - | $ - |
| | | | | | | |
| Liabilities | | | | | | |
| Repurchase agreements | $ 1,666,537 | $ - | $ 1,666,537 | $ (1,637,922) | $ (28,615) | $ - |
| Interest rate swaps | 342 | - | 342 | 32 | (374) | - |
| Treasury futures | 2 | - | 2 | 177 | (179) | - |
| Total Liabilities | $ 1,666,881 | $ - | $ 1,666,881 | $ (1,637,713) | $ (29,168) | $ - |

Note 9 – Fair Value

Fair Value Measurements

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 clarifies that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy gives the highest priority to quoted prices available in active markets (i.e., observable inputs) and the lowest priority to data lacking transparency (i.e., unobservable inputs). Additionally, ASC 820 requires an entity to consider all aspects of nonperformance risk, including the entity's own credit standing, when measuring the fair value of a liability.

ASC 820 establishes a three level hierarchy to be used when measuring and disclosing fair value. An instrument's categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation. Following is a description of the three levels:

Level 1 inputs are quoted prices in active markets for identical assets or liabilities as of the measurement date under current market conditions. Additionally, the entity must have the ability to access the active market and the quoted prices cannot be adjusted by the entity.

Level 2 inputs include quoted prices in active markets for similar assets or liabilities; quoted prices in inactive markets for identical or similar assets or liabilities; or inputs that are observable or can be corroborated by observable market data by correlation or other means for substantially the full-term of the assets or liabilities.

Level 3 unobservable inputs are supported by little or no market activity. The unobservable inputs represent the assumptions that management believes market participants would use to price the assets and liabilities, including risk. Generally, Level 3 assets and liabilities are valued using pricing models, discounted cash flow methodologies, or similar techniques that require significant judgment or estimation.

Recurring Fair Value Measurements

The following is a description of the methods used to estimate the fair values of the Company's assets and liabilities measured at fair value on a recurring basis, as well as the basis for classifying these assets and liabilities as Level 2 or 3 within the fair value hierarchy. The Company's valuations consider assumptions that it believes a market participant would consider in valuing the assets and liabilities, the most significant of which are disclosed below. The Company reassesses and periodically adjusts the underlying inputs and assumptions used in the valuations for recent historical experience, as well as for current and expected relevant market conditions.

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RMBS

The Company holds a portfolio of RMBS that are classified as available for sale and are carried at fair value in the consolidated balance sheets. The Company determines the fair value of its RMBS based upon prices obtained from third-party pricing providers. The third-party pricing providers use pricing models that generally incorporate such factors as coupons, primary and secondary mortgage rates, rate reset period, issuer, prepayment speeds, credit enhancements and expected life of the security. As a result, the Company classified 100% of its RMBS as Level 2 fair value assets at March 31, 2018 and December 31, 2017.

Excess MSRs

The Company held a portfolio of Excess MSRs that were reported at fair value in the consolidated balance sheet at December 31, 2016. The Company used a discounted cash flow model to estimate the fair value of these assets. Although Excess MSR transactions are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels and discount rates). As a result, the Company classified 100% of its Excess MSRs as Level 3 fair value assets at December 31, 2016. The Company did not hold any Excess MSRs at December 31, 2017.

MSRs

The Company holds a portfolio of MSRs that are reported at fair value in the consolidated balance sheets. The Company uses a discounted cash flow model to estimate the fair value of these assets. Although MSR transactions are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels, costs to service and discount rates). As a result, the Company classified 100% of its MSRs as Level 3 fair value assets at March 31, 2018 and December 31, 2017.

Derivative Instruments

The Company enters into a variety of derivative instruments as part of its economic hedging strategies. The Company executes interest rate swaps, swaptions, TBAs and treasury futures. The Company utilizes third-party pricing providers to value its derivative instruments. As a result, the Company classified 100% of its derivative instruments as Level 2 fair value assets and liabilities at March 31, 2018 and December 31, 2017.

Both the Company and the derivative counterparties under their netting arrangements are required to post cash collateral based upon the net underlying market value of the Company’s open positions with the counterparties. Posting of cash collateral typically occurs daily, subject to certain dollar thresholds. Due to the existence of netting arrangements, as well as frequent cash collateral posting at low posting thresholds, credit exposure to the Company and/or counterparties is considered materially mitigated. The Company’s interest rate swaps are required to be cleared on an exchange, which further mitigates, but does not eliminate, credit risk. Based on the Company’s assessment, there is no requirement for any additional adjustment to derivative valuations specifically for credit.

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The following tables present the Company's assets and liabilities measured at fair value on a recurring basis as of the dates indicated (dollars in thousands).

Recurring Fair Value Measurements

As of March 31, 2018

| | Level 1 | Level 2 | Level 3 | Carrying Value |
|---|---|---|---|---|
| Assets | | | | |
| RMBS | | | | |
| Fannie Mae | $ - | $1,108,246 | $- | $ 1,108,246 |
| Freddie Mac | - | 440,756 | - | 440,756 |
| CMOs | - | 93,680 | - | 93,680 |
| RMBS total | - | 1,642,682 | - | 1,642,682 |
| Derivative assets | | | | |
| Interest rate swaps | - | 13,438 | - | 13,438 |
| Interest rate swaptions | - | 2,474 | - | 2,474 |
| TBAs | - | 193 | - | 193 |
| Derivative assets total | - | 16,105 | - | 16,105 |
| Servicing related assets | - | - | 188,145 | 188,145 |
| Total Assets | $ - | $1,658,787 | $188,145 | $ 1,846,932 |
| Liabilities | | | | |
| Derivative liabilities | | | | |
| Treasury futures | - | 1,040 | - | 1,040 |
| Derivative liabilities total | - | 1,097 | - | 1,097 |
| Total Liabilities | $ - | $1,097 | $- | $ 1,097 |

As of December 31, 2017

| | Level 1 | Level 2 | Level 3 | Carrying Value |
|---|---|---|---|---|
| Assets | | | | |
| RMBS | | | | |
| Fannie Mae | $ - | $1,233,699 | $- | $ 1,233,699 |
| Freddie Mac | - | 513,544 | - | 513,544 |
| CMOs | - | 93,669 | - | 93,669 |
| RMBS total | - | 1,840,912 | - | 1,840,912 |
| Derivative assets | | | | |
| Interest rate swaps | - | 12,994 | - | 12,994 |
| Interest rate swaptions | - | 802 | - | 802 |
| TBAs | - | 34 | - | 34 |
| Derivative assets total | - | 13,830 | - | 13,830 |
| Servicing related assets | - | - | 122,806 | 122,806 |
| Total Assets | $ - | $1,854,742 | $122,806 | $ 1,977,548 |
| Liabilities | | | | |
| Derivative liabilities | | | | |
| Interest rate swaps | - | 342 | - | 342 |
| Treasury futures | - | 2 | - | 2 |
| Derivative liabilities total | - | 344 | - | 344 |
| Total Liabilities | $ - | $344 | $- | $ 344 |

The Company may be required to measure certain assets or liabilities at fair value from time to time. These periodic fair value measures typically result from application of certain impairment measures under GAAP. These items would constitute nonrecurring fair value measures under ASC 820. As of March 31, 2018 and December 31, 2017, the Company did not have any assets or liabilities measured at fair value on a nonrecurring basis in the periods presented.

Level 3 Assets and Liabilities

The valuation of Level 3 assets and liabilities requires significant judgment by the third-party pricing providers and management. The third-party pricing providers and management rely on inputs such as market price quotations from market makers (either market or indicative levels), original transaction price, recent transactions in the same or similar instruments, and changes in financial ratios or cash flows to determine fair value. Level 3 instruments may also be discounted to reflect illiquidity and/or non-transferability, with the amount of such discount estimated by third-party pricing providers and management in the absence of market information. Assumptions used by third-party pricing providers and management due to lack of observable inputs may significantly impact the resulting fair value and, therefore, the Company’s consolidated financial statements. The Company’s management reviews all valuations that are based on pricing information received from third-party pricing providers. As part of this review, prices are compared against other pricing or input data points in the marketplace, along with internal valuation expertise, to ensure the pricing is reasonable.

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In connection with the above, the Company estimates the fair value of its Servicing Related Assets based on internal pricing models rather than quotations, and compares the results of these internal models against the results from models generated by third-party valuation specialists. The determination of estimated cash flows used in pricing models is inherently subjective and imprecise.

Changes in market conditions, as well as changes in the assumptions or methodology used to determine fair value, could result in a significant change to estimated fair values. It should be noted that minor changes in assumptions or estimation methodologies can have a material effect on these derived or estimated fair values, and that the fair values reflected below are indicative of the interest rate and credit spread environments as of March 31, 2018 and December 31, 2017 and do not take into consideration the effects of subsequent changes in market or other factors.

The tables below present the reconciliation for the Company's Level 3 assets (Servicing Related Assets) measured at fair value on a recurring basis as of the dates indicated (dollars in thousands):

Level 3 Fair Value Measurements

As of March 31, 2018

| | Level 3 [A] MSRs |
|---|---|
| Balance at December 31, 2017 | $ 122,806 |
| Purchases, sales and principal paydowns: | |
| Purchases | 52,962 |
| Other changes [B] | (121) |
| Purchases, sales and principal paydowns: | $ 52,841 |
| Changes in Fair Value due to: | |
| Changes in valuation inputs or assumptions used in valuation model | 14,991 |
| Other changes in fair value [C] | (2,493) |
| Unrealized gain (loss) included in Net Income | $ 12,498 |
| Balance at March 31, 2018 | $ 188,145 |

As of December 31, 2017

| | Level 3 [A] Excess MSRs Pool 2 | MSRs | Total |
|---|---|---|---|
| Balance at December 31, 2016 | $29,392 | $31,871 | $61,263 |
| Purchases, sales and principal paydowns: | | | |
| Purchases | - | 83,586 | 83,586 |
| Sales | (35,905) | - | (35,905) |
| Other changes [B] | 6,513 | (1,810) | 4,703 |
| Purchases, sales and principal paydowns: | $(29,392) | $81,776 | $52,384 |
| Changes in Fair Value due to: | | | |
| Changes in valuation inputs or assumptions used in valuation model | - | 16,375 | 16,375 |
| Other changes in fair value [C] | - | (7,216) | (7,216) |
| Unrealized gain (loss) included in Net Income | $- | $9,159 | $9,159 |
| Balance at December 31, 2017 | $- | $122,806 | $122,806 |

(A) Includes the recapture agreement for each respective pool.
(B) Represents purchase price adjustments, principally contractual prepayment protection, and changes due to the Company's repurchase of the underlying collateral.
(C) Represents changes due to realization of expected cash flows.

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The tables below present information about the significant unobservable inputs used in the fair value measurement of the Company’s Servicing Related Assets classified as Level 3 fair value assets as of the dates indicated (dollars in thousands):

Fair Value Measurements

As of March 31, 2018

| | Fair Value | Valuation Technique | Unobservable Input [A] | Range | Weighted Average | |
|---|---|---|---|---|---|---|
| MSRs | | | | | | |
| Conventional | $ 145,001 | Discounted cash flow | Constant prepayment speed | 5.4% - 24.6 % | 8.6 | % |
| | | | Uncollected payments | 0.2% - 1.5 % | 0.8 | % |
| | | | Discount rate | | 9.3 | % |
| | | | Annual cost to service, per loan | | $ 71 | |
| Government | $ 43,144 | Discounted cash flow | Constant prepayment speed | 6.0% - 17.0 % | 7.4 | % |
| | | | Uncollected payments | 0.4% - 5.2 % | 3.3 | % |
| | | | Discount rate | | 12.0 | % |
| | | | Annual cost to service, per loan | | $ 96 | |
| TOTAL | $ 188,145 | Discounted cash flow | | | | |

As of December 31, 2017