

Edgar Filing: AG Mortgage Investment Trust, Inc. - Form 10-Q

AG Mortgage Investment Trust, Inc.
Form 10-Q
May 03, 2019
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2019

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 001-35151

AG MORTGAGE INVESTMENT TRUST, INC.

Maryland 27-5254382
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)
245 Park Avenue, 26th Floor 10167
New York, New York
(Address of Principal Executive Offices) (Zip Code)
(212) 692-2000
(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 and 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 such files). Yes No

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

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

Title of each class:	Trading Symbols:	Name of each exchange on which registered:
Common Stock, \$0.01 par value per share	MITT	New York Stock Exchange (NYSE)

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8.25% Series A Cumulative Redeemable Preferred Stock	MITT PrA	New York Stock Exchange (NYSE)
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8.00% Series B Cumulative Redeemable Preferred Stock	MITT PrB	New York Stock Exchange (NYSE)
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As of April 23, 2019, there were 32,709,397 outstanding shares of common stock of AG Mortgage Investment Trust, Inc.

AG MORTGAGE INVESTMENT TRUST, INC.
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PART I

ITEM 1. FINANCIAL STATEMENTS

AG Mortgage Investment Trust, Inc. and Subsidiaries
 Consolidated Balance Sheets (Unaudited)
 (in thousands, except per share data)

	March 31, 2019	December 31, 2018
Assets		
Real estate securities, at fair value:		
Agency - \$2,240,880 and \$1,934,562 pledged as collateral, respectively	\$2,287,981	\$1,988,280
Non-Agency - \$640,396 and \$605,243 pledged as collateral, respectively (1)	659,340	625,350
ABS - \$12,594 and \$13,346 pledged as collateral, respectively	20,199	21,160
CMBS - \$266,689 and \$248,355 pledged as collateral, respectively	276,403	261,385
Residential mortgage loans, at fair value - \$117,830 and \$99,283 pledged as collateral, respectively	202,047	186,096
Commercial loans, at fair value - \$2,467 and \$- pledged as collateral, respectively	110,223	98,574
Single-family rental properties, net	137,886	138,678
Investments in debt and equity of affiliates	102,099	84,892
Excess mortgage servicing rights, at fair value	24,301	26,650
Cash and cash equivalents	50,779	31,579
Restricted cash	37,266	52,779
Other assets	98,617	33,503
Total Assets	\$4,007,141	\$3,548,926
Liabilities		
Financing arrangements, net	\$3,214,909	\$2,822,505
Securitized debt, at fair value	10,515	10,858
Dividend payable	16,352	14,372
Other liabilities	33,729	45,180
Total Liabilities	3,275,505	2,892,915
Commitments and Contingencies (Note 14)		
Stockholders' Equity		
Preferred stock - \$0.01 par value; 50,000 shares authorized:		
8.25% Series A Cumulative Redeemable Preferred Stock, 2,070 shares issued and outstanding (\$51,750 aggregate liquidation preference)	49,921	49,921
8.00% Series B Cumulative Redeemable Preferred Stock, 4,600 shares issued and outstanding (\$115,000 aggregate liquidation preference)	111,293	111,293
Common stock, par value \$0.01 per share; 450,000 shares of common stock authorized and 32,703 and 28,744 shares issued and outstanding at March 31, 2019 and December 31, 2018, respectively	327	287
Additional paid-in capital	661,561	595,412
Retained earnings/(deficit)	(91,466)	(100,902)
Total Stockholders' Equity	731,636	656,011
Total Liabilities & Stockholders' Equity	\$4,007,141	\$3,548,926

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

(1) See Note 3 for details related to variable interest entities.

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AG Mortgage Investment Trust, Inc. and Subsidiaries
 Consolidated Statements of Operations (Unaudited)
 (in thousands, except per share data)

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Net Interest Income		
Interest income	\$41,490	\$39,357
Interest expense	23,341	15,326
Total Net Interest Income	18,149	24,031
Other Income/(Loss)		
Rental income	3,397	—
Net realized gain/(loss)	(20,610)	(11,839)
Net interest component of interest rate swaps	1,781	(1,470)
Unrealized gain/(loss) on real estate securities and loans, net	46,753	(36,155)
Unrealized gain/(loss) on derivative and other instruments, net	(10,086)	37,090
Other income	596	—
Total Other Income/(Loss)	21,831	(12,374)
Expenses		
Management fee to affiliate	2,345	2,439
Other operating expenses	3,830	3,223
Equity based compensation to affiliate	126	51
Excise tax	92	375
Servicing fees	371	62
Property depreciation and amortization	1,447	—
Property operating expenses	1,843	—
Total Expenses	10,054	6,150
Income/(loss) before equity in earnings/(loss) from affiliates	29,926	5,507
Equity in earnings/(loss) from affiliates	(771)	2,740
Net Income/(Loss)	29,155	8,247
Dividends on preferred stock	3,367	3,367
Net Income/(Loss) Available to Common Stockholders	\$25,788	\$4,880
Earnings/(Loss) Per Share of Common Stock		
Basic	\$0.84	\$0.17
Diluted	\$0.84	\$0.17
Weighted Average Number of Shares of Common Stock Outstanding		
Basic	30,551	28,196
Diluted	30,581	28,217

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

AG Mortgage Investment Trust, Inc. and Subsidiaries
 Consolidated Statements of Stockholders' Equity (Unaudited)
 (in thousands)

	Common Stock		8.25 % Series A Cumulative Redeemable Preferred Stock	8.00 % Series B Cumulative Redeemable Preferred Stock	Additional Paid-in Capital	Retained Earnings/(Deficit)	Total
	Shares	Amount					
Balance at January 1, 2018	28,193	\$ 282	\$ 49,921	\$ 111,293	\$ 585,530	\$ (32,767)	\$ 714,259
Net proceeds from issuance of common stock	—	—	—	—	(63)	—	(63)
Grant of restricted stock and amortization of equity based compensation	3	—	—	—	143	—	143
Common dividends declared	—	—	—	—	—	(13,393)	(13,393)
Preferred Series A dividends declared	—	—	—	—	—	(1,067)	(1,067)
Preferred Series B dividends declared	—	—	—	—	—	(2,300)	(2,300)
Net Income/(Loss)	—	—	—	—	—	8,247	8,247
Balance at March 31, 2018	28,196	\$ 282	\$ 49,921	\$ 111,293	\$ 585,610	\$ (41,280)	\$ 705,826
Balance at January 1, 2019	28,744	\$ 287	\$ 49,921	\$ 111,293	\$ 595,412	\$ (100,902)	\$ 656,011
Net proceeds from issuance of common stock	3,953	40	—	—	65,924	—	65,964
Grant of restricted stock and amortization of equity based compensation	6	—	—	—	225	—	225
Common dividends declared	—	—	—	—	—	(16,352)	(16,352)
Preferred Series A dividends declared	—	—	—	—	—	(1,067)	(1,067)
Preferred Series B dividends declared	—	—	—	—	—	(2,300)	(2,300)
Net Income/(Loss)	—	—	—	—	—	29,155	29,155
Balance at March 31, 2019	32,703	\$ 327	\$ 49,921	\$ 111,293	\$ 661,561	\$ (91,466)	\$ 731,636

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

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AG Mortgage Investment Trust, Inc. and Subsidiaries
 Consolidated Statements of Cash Flows (Unaudited)
 (in thousands)

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Cash Flows from Operating Activities		
Net income/(loss)	\$ 29,155	\$ 8,247
Adjustments to reconcile net income/(loss) to net cash provided by (used in) operating activities:		
Net amortization of premium/(discount)	(1,656)	(959)
Net realized (gain)/loss	20,610	11,839
Unrealized (gain)/loss on real estate securities and loans, net	(46,753)	36,155
Unrealized (gain)/loss on derivative and other instruments, net	10,086	(37,090)
Property depreciation and amortization	1,447	—
Equity based compensation to affiliate	126	51
Equity based compensation expense	99	92
(Income)/loss from investments in debt and equity of affiliates in excess of distributions received	1,635	2,127
Change in operating assets/liabilities:		
Other assets	(1,025)	(152)
Other liabilities	(4,004)	4,542
Net cash provided by (used in) operating activities	9,720	24,852
Cash Flows from Investing Activities		
Purchase of real estate securities	(645,249)	(686,020)
Purchase of residential mortgage loans	(19,745)	—
Origination of commercial loans	(11,748)	—
Purchase of commercial loans	(10,118)	—
Purchase of U.S. Treasury securities	—	(249,659)
Purchase of excess mortgage servicing rights	—	(7,604)
Investments in debt and equity of affiliates	(20,734)	(39,216)
Proceeds from sales of real estate securities	213,027	728,366
Proceeds from sales of residential mortgage loans	75	—
Proceeds from sales of U.S. treasury securities	—	249,227
Principal repayments/return of basis on real estate securities and excess mortgage servicing rights	63,995	112,743
Principal repayments on commercial loans	10,471	—
Principal repayments on residential mortgage loans	4,007	183
Distributions received in excess of income from investments in debt and equity of affiliates	1,893	6,460
Net proceeds from/(payments made) on reverse repurchase agreements	11,487	24,695
Net proceeds from/(payments made) on sales of securities borrowed under reverse repurchase agreements	(11,437)	(24,032)
Net settlement of interest rate swaps and other instruments	(31,268)	6,504
Net settlement of TBAs	(431)	373
Cash flows provided by/(used in) other investing activities	(1,151)	1,224
Net cash provided by/(used in) investing activities	(446,926)	123,244

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Cash Flows from Financing Activities		
Net proceeds from issuance of common stock	65,964	(63)
Borrowings under financing arrangements	10,167,128	13,806,248
Repayments of financing arrangements	(9,774,724)	(13,950,356)
Net collateral received from/(paid to) derivative counterparty	(599)	27,207
Net collateral received from/(paid to) repurchase counterparty	863	384
Dividends paid on common stock	(14,372)	(13,391)
Dividends paid on preferred stock	(3,367)	(3,367)
Net cash provided by/(used in) financing activities	440,893	(133,338)
Net change in cash, cash equivalents and restricted cash	3,687	14,758
Cash, cash equivalents, and restricted cash, Beginning of Period	84,358	52,815
Cash, cash equivalents, and restricted cash, End of Period	\$ 88,045	\$ 67,573

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	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Supplemental disclosure of cash flow information:		
Cash paid for interest on financing arrangements	\$ 24,847	\$ 14,513
Cash paid for excise and income taxes	\$ 1,396	\$ 1,379
Supplemental disclosure of non-cash financing and investing activities:		
Receivable on unsettled trades	\$ 68,389	\$ 104,654
Payable on unsettled trades	\$ —	\$ 117,356
Principal repayments on real estate securities not yet received	\$ —	\$ 1,018
Common stock dividends declared but not paid	\$ 16,352	\$ 13,393
Decrease in securitized debt	\$ 317	\$ 994
Transfer from residential mortgage loans to other assets	\$ 628	\$ —
Transfer from non-agency to investments in debt and equity of affiliates	\$ —	\$ 44,970
Transfer from financing arrangements to investments in debt and equity of affiliates	\$ —	\$ 33,720

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the consolidated balance sheets that sum to the total of the same such amounts shown in the consolidated statements of cash flows:

	March 31, 2019	March 31, 2018
Cash and cash equivalents	\$50,779	\$25,294
Restricted cash	37,266	42,279
Total cash, cash equivalents and restricted cash shown in the consolidated statements of cash flows	\$88,045	\$67,573

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

AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
March 31, 2019

1. Organization

AG Mortgage Investment Trust, Inc. (the "Company") was incorporated in the state of Maryland on March 1, 2011. The Company is a hybrid mortgage REIT that opportunistically invests in a diversified portfolio of residential mortgage-backed securities, or RMBS, residential and commercial mortgage assets, financial assets and real estate. RMBS include securities issued or guaranteed by a U.S. government-sponsored entity such as Fannie Mae or Freddie Mac (collectively, "GSEs"), or any agency of the U.S. Government such as Ginnie Mae (collectively, "Agency RMBS"). Residential and commercial mortgage assets, financial assets and real estate include Non-Agency RMBS, ABS, CMBS, excess mortgage servicing rights ("Excess MSRs"), loans, and single-family rental properties, each as described below.

Non-Agency RMBS represent fixed- and floating-rate RMBS issued by entities or organizations other than a GSE or agency of the U.S. government, including investment grade (AAA through BBB) and non-investment grade classes (BB and below). The mortgage loan collateral for Non-Agency RMBS consists of residential mortgage loans that do not generally conform to underwriting guidelines issued by U.S. government agencies or U.S. government-sponsored entities.

Asset Backed Securities ("ABS") are securitized investments for which the underlying assets are diverse, not only representing real estate related assets.

Commercial Mortgage Backed Securities ("CMBS") represent investments of fixed- and floating-rate CMBS, including investment grade (AAA through BBB) and non-investment grade classes (BB and below), secured by, or evidencing an ownership interest in, a single commercial mortgage loan or a pool of commercial mortgage loans.

Collectively, the Company refers to Agency RMBS, Non-Agency RMBS, ABS and CMBS asset types as "real estate securities" or "securities."

Commercial loans are secured by an interest in commercial real estate and represent a contractual right to receive money on demand or on fixed or determinable dates. Residential mortgage loans refer to performing, re-performing and non-performing loans secured by a first lien mortgage on residential mortgaged property located in any of the 50 states of the United States or in the District of Columbia. The Company refers to its residential and commercial mortgage loans as "mortgage loans" or "loans."

Single-family rental properties represent equity interests in residential properties held for the purpose of owning, leasing, and operating as single-family rental properties.

The Company conducts its business through the following segments: (i) Securities and Loans and (ii) Single-Family Rental Properties.

The Company is externally managed by AG REIT Management, LLC, a Delaware limited liability company (the "Manager"), a wholly-owned subsidiary of Angelo, Gordon & Co., L.P. ("Angelo Gordon"), a privately-held, SEC-registered investment adviser, pursuant to a management agreement. The Manager, pursuant to a delegation agreement dated as of June 29, 2011, has delegated to Angelo Gordon the overall responsibility of its day-to-day duties and obligations arising under the management agreement.

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The Company conducts its operations to qualify and be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code").

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

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AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
March 31, 2019

2. Summary of significant accounting policies

The accompanying unaudited consolidated financial statements and related notes have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial reporting and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Certain prior period amounts have been reclassified to conform to the current period's presentation. In the opinion of management, all adjustments considered necessary for a fair statement of the Company's financial position, results of operations and cash flows have been included for the interim period and are of a normal and recurring nature. The operating results presented for interim periods are not necessarily indicative of the results that may be expected for any other interim period or for the entire year.

Cash and cash equivalents

Cash is comprised of cash on deposit with financial institutions. The Company classifies highly liquid investments with original maturities of three months or less from the date of purchase as cash equivalents. Cash equivalents includes cash invested in money market funds. As of March 31, 2019 and December 31, 2018, the Company held \$35.9 million and \$0.6 million, respectively, of cash equivalents. The Company places its cash with high credit quality institutions to minimize credit risk exposure. Cash pledged to the Company as collateral is unrestricted in use and, accordingly, is included as a component of "Cash and cash equivalents" on the consolidated balance sheets. Any cash held by the Company as collateral is included in the "Other liabilities" line item on the consolidated balance sheets and in cash flows from financing activities on the consolidated statement of cash flows. Due to broker, which is included in the "Other liabilities" line item on the consolidated balance sheets, does not include variation margin received on centrally cleared derivatives. See Note 9 for more detail. Any cash due to the Company in the form of principal payments is included in the "Other assets" line item on the consolidated balance sheets and in cash flows from operating activities on the consolidated statement of cash flows.

Restricted cash

Restricted cash includes cash pledged as collateral for clearing and executing trades, derivatives, financing arrangements and security deposits. Restricted cash also includes cash deposited into accounts related to rent deposits and collections, security deposits, property taxes, insurance premiums, interest expenses, property management fees and capital expenditures. Restricted cash is not available to the Company for general corporate purposes. As of March 31, 2019 and December 31, 2018, the Company held \$1.5 million and \$1.3 million, respectively, of restricted cash related to security deposits. Restricted cash may be returned to the Company when the related collateral requirements are exceeded or at the maturity of the derivative or financing arrangement. Restricted cash is carried at cost, which approximates fair value. Restricted cash does not include variation margin pledged on centrally cleared derivatives. See Note 9 for more detail.

Offering costs

The Company has incurred offering costs in connection with common stock offerings and registration statements. Where applicable, the offering costs were paid out of the proceeds of the respective offerings. Offering costs in connection with common stock offerings and costs in connection with registration statements have been accounted for as a reduction of additional paid-in capital.

Use of estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results may differ from those estimates.

Earnings/(Loss) per share

In accordance with the provisions of Accounting Standards Codification ("ASC") 260, "Earnings per Share," the Company calculates basic income/(loss) per share by dividing net income/(loss) available to common stockholders for the period by weighted-average shares of the Company's common stock outstanding for that period. Diluted income per share takes into account the effect of dilutive instruments, such as stock options, warrants, unvested restricted stock and unvested restricted stock units but uses the average share price for the period in determining the number of incremental shares that are to be added to the weighted-average number of shares outstanding. In periods in which the Company records a loss, potentially dilutive securities are excluded from the diluted loss per share calculation, as their effect on loss per share is anti-dilutive.

AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
March 31, 2019

Valuation of financial instruments

The fair value of the financial instruments that the Company records at fair value will be determined by the Manager, subject to oversight of the Company's Board of Directors, and in accordance with ASC 820, "Fair Value Measurements and Disclosures." When possible, the Company determines fair value using independent data sources. ASC 820 establishes a hierarchy that prioritizes the inputs to valuation techniques giving the highest priority to readily available unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements) when market prices are not readily available or reliable.

The three levels of the hierarchy under ASC 820 are described below:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Prices determined using other significant observable inputs. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.

Level 3 – Prices determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used. Unobservable inputs reflect the Company's assumptions about the factors that market participants would use in pricing an asset or liability, and would be based on the best information available.

Transfers between levels are assumed to occur at the beginning of the reporting period.

Accounting for real estate securities

Investments in real estate securities are recorded in accordance with ASC 320-10, "Investments – Debt and Equity Securities," ASC 325-40, "Beneficial Interests in Securitized Financial Assets," or ASC 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality." The Company has chosen to make a fair value election pursuant to ASC 825, "Financial Instruments" for its real estate securities portfolio. Real estate securities are recorded at fair market value on the consolidated balance sheets and the periodic change in fair market value is recorded in current period earnings on the consolidated statement of operations as a component of "Unrealized gain/(loss) on real estate securities and loans, net." Real estate securities acquired through securitizations are shown in the line item "Purchase of real estate securities" on the consolidated statement of cash flows.

These investments meet the requirements to be classified as available for sale under ASC 320-10-25 which requires the securities to be carried at fair value on the consolidated balance sheets with changes in fair value recorded to other comprehensive income, a component of stockholders' equity. Electing the fair value option allows the Company to record changes in fair value in the consolidated statement of operations, which, in management's view, more appropriately reflects the results of operations for a particular reporting period as all securities activities will be recorded in a similar manner.

When the Company purchases securities with evidence of credit deterioration since origination, it will analyze the securities to determine if the guidance found in ASC 310-30 is applicable.

The Company accounts for its securities under ASC 310 and ASC 325 and evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis. The determination of whether a security is other-than-temporarily impaired involves judgments and assumptions based on subjective and objective factors. When the fair value of a real estate security is less than its amortized cost at the balance sheet date, the security is considered impaired, and the impairment is designated as either "temporary" or "other-than-temporary."

When a real estate security is impaired, an OTTI is considered to have occurred if (i) the Company intends to sell the security (i.e., a decision has been made as of the reporting date) or (ii) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis. If the Company intends to sell the security or if it is more likely than not that the Company will be required to sell the real estate security before recovery of its amortized cost basis, the entire amount of the impairment loss, if any, is recognized in earnings as a realized loss and the cost basis of the security is adjusted to its fair value. Additionally, for securities accounted for under ASC 325-40, an OTTI is deemed to have occurred when there is an adverse change in the expected cash flows to be received and the fair value of the security is less than its carrying amount. In determining whether an adverse change in cash flows occurred, the present value of the remaining cash flows, as estimated at the initial transaction date (or the last date previously revised), is compared to the present value of the expected cash flows at the current reporting date. The estimated cash flows reflect those a "market participant" would use and include observations of current information and events, and assumptions related to fluctuations in interest rates, prepayment speeds and the timing and amount of potential credit losses.

AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
March 31, 2019

Cash flows are discounted at a rate equal to the current yield used to accrete interest income. Any resulting OTTI adjustments are reflected in the "Net realized gain/(loss)" line item on the consolidated statement of operations.

The determination as to whether an OTTI exists is subjective, given that such determination is based on information available at the time of assessment as well as the Company's estimate of the future performance and cash flow projections for the individual security. As a result, the timing and amount of an OTTI constitutes an accounting estimate that may change materially over time.

Increases in interest income may be recognized on a security on which the Company previously recorded an OTTI charge if the performance of such security subsequently improves.

Any remaining unrealized losses on securities at March 31, 2019 do not represent other than temporary impairment as the Company has the ability and intent to hold the securities to maturity or for a period of time sufficient for a forecasted market price recovery up to or above the amortized cost of the investment, and the Company is not required to sell the security for regulatory or other reasons. In addition, any unrealized losses on the Company's Agency RMBS accounted for under ASC 320 are not due to credit losses given their explicit guarantee of principal and interest by the GSEs, but rather are due to changes in interest rates and prepayment expectations. See Note 3 for a summary of OTTI charges recorded.

Sales of securities are driven by the Manager's portfolio management process. The Manager seeks to mitigate risks including those associated with prepayments, defaults, severities, amongst others and will opportunistically rotate the portfolio into securities with more favorable attributes. Strategies may also be employed to manage net capital gains, which need to be distributed for tax purposes.

Realized gains or losses on sales of securities, loans and derivatives are included in the "Net realized gain/(loss)" line item on the consolidated statement of operations. The cost of positions sold is calculated using a first in, first out, or FIFO, basis. Realized gains and losses are recorded in earnings at the time of disposition.

Accounting for residential and commercial mortgage loans

Investments in mortgage loans are recorded in accordance with ASC 310-10, "Receivables." At purchase, the Company may aggregate its mortgage loans into pools based on common risk characteristics. Once a pool of loans is assembled, its composition is maintained. The Company has chosen to make a fair value election pursuant to ASC 825 for its mortgage loan portfolio. Loans are recorded at fair market value on the consolidated balance sheets and any periodic change in fair market value will be recorded in current period earnings on the consolidated statement of operations as a component of "Unrealized gain/(loss) on real estate securities and loans, net."

The Company amortizes or accretes any premium or discount over the life of the loans utilizing the effective interest method. On at least a quarterly basis, the Company evaluates the collectability of both interest and principal on its loans to determine whether they are impaired. A loan or pool of loans is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the existing contractual terms. Income recognition is suspended for loans at the earlier of the date at which payments become 90-days past due or when, in the opinion of management, a full recovery of income and principal becomes doubtful. When the ultimate collectability of the principal of an impaired loan or pool of loans is in doubt, all payments are applied to principal under the cost recovery method. When the ultimate collectability of the principal of an impaired loan is not in doubt, contractual interest is recorded as interest income when received, under the cash basis method until an accrual is resumed when the loan becomes contractually current and performance is demonstrated to be

resumed. A loan is written off when it is no longer realizable and/or legally discharged.

When the Company purchases mortgage loans with evidence of credit deterioration since origination and it determines that it is probable it will not collect all contractual cash flows on those loans, it will apply the guidance found in ASC 310-30. Mortgage loans that are delinquent 60 or more days are considered non-performing.

The Company updates its estimate of the cash flows expected to be collected on at least a quarterly basis for loans accounted for under ASC 310-30. In estimating these cash flows, there are a number of assumptions that will be subject to uncertainties and contingencies including both the rate and timing of principal and interest receipts, and assumptions of prepayments, repurchases, defaults and liquidations. If based on the most current information and events it is probable that there is a significant increase in cash flows previously expected to be collected or if actual cash flows are significantly greater than cash flows previously expected, the Company will recognize these changes prospectively through an adjustment of the loan's yield over its remaining life. The Company will adjust the amount of accretable yield by reclassification from the nonaccretable difference. The adjustment is

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accounted for as a change in estimate in conformity with ASC 250, "Accounting Changes and Error Corrections" with the amount of periodic accretion adjusted over the remaining life of the loan. Decreases in cash flows expected to be collected from previously projected cash flows, which includes all cash flows originally expected to be collected by the investor plus any additional cash flows expected to be collected arising from changes in estimate after acquisition, may be recognized as impairment. Increases in interest income may be recognized on a loan on which the Company previously recorded an OTTI charge if the performance of such loan subsequently improves.

Investments in debt and equity of affiliates

The Company's unconsolidated ownership interests in affiliates are accounted for using the equity method. A majority of the Company's investments held through affiliated entities are comprised of real estate securities, Excess MSR, and loans. These types of investments may also be held directly by the Company. These entities have chosen to make a fair value election on their financial instruments pursuant to ASC 825; as such, the Company will treat these investments consistently with this election.

On December 9, 2015, the Company, alongside private funds under the management of Angelo Gordon, through AG Arc LLC, one of the Company's indirect subsidiaries ("AG Arc"), formed Arc Home LLC ("Arc Home"). The Company has chosen to make a fair value election with respect to its investment in AG Arc pursuant to ASC 825.

On August 29, 2017, the Company, alongside private funds under the management of Angelo Gordon, formed Mortgage Acquisition Holding I LLC ("MATH") to conduct a residential mortgage investment strategy. MATH in turn sponsored the formation of an entity called Mortgage Acquisition Trust I LLC ("MATT") to purchase predominantly "Non-QMs," which are residential mortgage loans that are not deemed "qualified mortgage," or "QM," loans under the rules of the CFPB. Non-QMs are not eligible for delivery to Fannie Mae, Freddie Mac, or Ginnie Mae. MATT is expected to make an election to be treated as a real estate investment trust beginning with the 2018 tax year.

During Q3 2018, the Company transferred certain of its CMBS from certain of its non-wholly owned subsidiaries to a consolidated entity. The Company executed this transfer in order to obtain financing on these real estate securities. As a result, there was a reclassification of these assets from the "Investments in debt and equity of affiliates" line item to the "CMBS" line item on the Company's consolidated balance sheets. In addition, the Company has also shown this reclassification as a non-cash transfer from the "Investments in debt and equity of affiliates" line item to the "CMBS" line item on its consolidated statements of cash flows.

The below table reconciles the fair market value of investments to the "Investments in debt and equity of affiliates" line item on the Company's consolidated balance sheet (in thousands).

	March 31, 2019		December 31, 2018			
	Assets	Liabilities	Equity	Assets	Liabilities	Equity
Real Estate Securities, Excess MSR and Loans, at fair value (1)(2)	\$244,867	\$(176,950)	\$67,917			