



*Michael Farrell, Chairman of Annaly, delivered opening remarks on the Company's fourth quarter 2006 earnings call. While this satirical essay is a tongue-in-cheek look at the excesses of the American debt bubble, readers should consider the facts about the sub-prime mortgage market, which is anything but a joke. Homes are at all-time lows in affordability, housing prices are declining in many parts of the country, and credit performance on the most recent vintages of mortgages has been horrendous, thanks in part to the loose underwriting standards of the mortgage industry, the complicity of the appraisal process and the proclivity of average Americans to borrow to finance homes and lifestyles they cannot afford. These things end badly.*

*We reprint those remarks below:*

***BOND, Mortgage Bond, 2007  
License to Mutilate Credit or The Secret Life of Walter Lender  
(Apologies to James Thurber)***

As he pulled into the driveway in his leased high performance German sports car, its 350 horsepower engine spewing out premium gasoline emissions, Walter smiled as he observed his expansive lawn, newly trimmed by guest workers to a crew cut, putting green length and his wife's luxury Japanese sports utility vehicle resting up against the foundation of his circa 2004, six thousand square foot McMansion. "Enough dawdling," Walter said to himself, "and onto the BlackBerry." He sat in the driveway in his BMW and moved on to his next mission: how to generate a mortgage payment equal to twelve times his borrower's net monthly income so that he can generate enough fee income to make the minimum monthly payment on his platinum, no late fee, cash is trash credit card. He pushed back his leather trimmed seat into the recline position and pulled out his Hewlett Packard no-documentation, no income verification, low FICO score, single amortization scoring calculator and began to crunch the numbers. His mind drifted....

Suddenly, the seductive thoughts of a solution formed in his head. If he could only get the borrower to project the next decade's earnings into the proper line on the loan document, then convince the loan underwriter that the sales price is actually five percent below the true last sale in the area, and sell the borrower on taking out a silent second home equity loan to generate the four percent minimum down payment, then this plan could work. But, much depended on the underwriter, the appraiser and the title insurance company being 'cooperative' so that the paperwork could slide easily into the Wall Street mortgage conduit's pipeline and fed through to some pension fund, seduced by the promise of high yield and high ratings, packaged in the form of a tranced, private label, S&P, Moody's and Fitch-rated mortgage-backed security collateralized debt obligation bond. "Yes, he decided, "it can be done!" He ran the numbers one more time, distracted by the kids who rushed past the car on their Trek off-road bikes on their way to Starbucks to pick up their daily double chocolate chip Frappuchino Grandes (oh, but for the simpler days, when



Talls were enough to satisfy their afternoon energy needs) but this was before the days of SAT prep courses followed by soccer and lacrosse practices, Mandarin lessons and then dinner, piano lessons, and off to bed. Yes, the life of a seven year old certainly was filled up with things these days.

Rain began to drip on the windshield, and Walter was startled awake by the moisture sensitive sensor on his windshield wipers. Whoosh, whoosh and reality came back to him. Tomorrow, in the deposition, he could plausibly deny that he knew anything about the chain of capital markets activities that surrounded that loan. But, he know that this Attorney General was determined to run for higher office one day, and that this focus on mortgage lending abuses was just a pathway to the Governor's mansion for him. And that pathway was lit up with downgrades from the ratings agencies, littered with accusations of predatory lending, falsified appraisals and paved with the headstones of borrowers (voters) who were coerced into buying more house for more money than ever before in the history of humankind.

Looking to his left, he was startled to see two men standing in the driveway, one with a clipboard, the other with a locksmith kit. He knew right away who they were: The Repo men from the auto leasing company. He opened the door, shook the keys from the ring and handed them over without remorse. As they pulled the two cars out of the driveway and drove away down the cul-de-sac, carefully avoiding the "Slow—Children At Play" plastic road reminders, Walter found his feet leading him into the yard, toward his pool and slowly, ever so slowly, he stepped, fully clothed in his Lancaster Shoppe tailor-made suit, into the Jacuzzi, where his wife was relaxing next to Herman, the pool boy, sharing a pitcher of imported frozen margueritas, finely mixed to automated perfection in their mail order catalog MaxiBlender. As he watched the sun set over his \$5000 Huntington Stainless Steel rotisserie BBQ grill, one thought filled his mind.....At least he still had his frequent flyer miles.

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