



## Annaly 2024 Investor Day November 21, 2024

### Annaly Advantages

#### David Finkelstein

*Chief Executive Officer & Chief Investment Officer*

#### David Finkelstein:

Afternoon, everybody. Thank you all for being here. I do recognize many of you. But for those of you who I have not met, my name is David Finkelstein. I'm the CEO and CIO of Annaly Capital, and it is a pleasure to be here today. We have a crowded room, we also have countless more people on our webcast. And so we expect this to be a very substantial event for everybody. So thank you again. We're going to do something a little bit different than what you're accustomed to hearing from Annaly today. We're going to talk about the portfolio strategy and the businesses, but we do want to go broader and give the audience a real lens into how we manage the overall company and things like liquidity and financing management, as well as risk oversight, and also talk about policy.

And we have special guests at the end of the day. Jim Parrott and Mark Zandi, who are two of the foremost authorities on housing finance policy in the U.S., will speak with us through the moderation of our head of government relations Tanya Rakpraja, who has quite a policy background herself. And we have a diverse group of speakers for you today from the management team, people you'll get to meet for the first time. We also have today two of our senior board members with us, Mike Haylon, who's our board chair, and Tom Hamilton, who's the chair of our risk committee. And without whose support, we wouldn't have been able to do many of the things that we've been able to accomplish over the last number of years. So we very much appreciate it.

Now, if you look at the screen, I have four concepts up here and I'd like you to focus on those for a moment because these we believe are the key differentiators for Annaly. First of all, scale. Capital is everything. It opens doors to opportunities and partnerships, and most importantly, it ensures liquidity, and it's the key to our company. People. We have the top talent in the industry in my view. And it's not just the people that you're going to hear from today, but it's the people around them and underneath them that make Annaly what it is and certainly inform our success. Adaptability. Look, markets move at the speed of sound in today's environment and things can change very quickly, and a company like Annaly has to be incredibly agile. And I think as we talk about what we've done over the past number of years, you'll become of the mindset that we've exemplified adaptability over the last number of years.

And lastly, efficiency. We need to be as lean and as efficient as we possibly can because returns are a game of inches. And when we're thinking about investing a dollar, whether it's on the balance sheet or in people or technology or operations, everything is looked at on a return on investment standpoint. And what you'll find is we are the most efficient model in the industry and we're very proud of it. So my role today, to introduce today, will be to talk about both the history of the company, who we are, what we've done, how we've done, and then where we're going. Okay, so with that, let's get going.

All right. I think most of you know Annaly well, but for those who don't, we've been a public company now for 27 years. We came to market at a time of considerable volatility, right during the Russian debt crisis. And then we experienced 9/11 and the financial crisis and COVID and many events of volatility in between. And the point being is that this company has developed a pretty considerable muscle memory for managing through volatile times, and it's in the DNA of the company. And we have a lot of past experiences that we fall on when it comes to managing our portfolio.

Performance. 869% total shareholder returns since inception, roughly 9% average annual returns, something we're very happy with. We have 200 people in the company, which sounds like a lot of people for a mortgage REIT, but when you consider the diversity of the three businesses and the complexity of each of those businesses, we're actually rather lean. We have \$26 billion in dividends paid over the history of the company, on average about a billion a year. This is our mission, is to create income for our shareholders. And one of the proudest things about the company is that we've consistently maintained a strong dividend yield and provided income to our shareholders.

And lastly, here we have \$12 billion in capital, which is obviously evident, but what I think is most important about our capital base is the quality of the capital. It's 88% common equity, 12% preferred. And we've talked in the past about how we look at the different types of leverage. And capital structure leverage, or the amount of leverage in your capital structure, is evaluated in the context of other forms of leverage, whether it be balance sheet leverage or structural leverage in the assets. And we don't layer leverage, we're responsible about our leverage. And right now we have what we believe to be the cleanest capital structure of any scaled operator in the platform. So we like where we sit from that standpoint.

Now, I wanted to give you a little bit of history of the company, and I know there is a lot going on on this page and I really want to focus on the past five years. But first off, just a little bit of history. When Annaly started in the late '90s, it was a pure play Agency REIT. And the company existed in that form through the financial crisis, and it was a very beneficial time to be invested in Agency MBS, certainly. Now in the aftermath of the financial crisis, credit assets were still extraordinarily cheap, and so the company began to diversify both through organic expansion as well as acquisition. And we added onto the balance sheet, residential credit, commercial real estate, and even corporate middle market lending. And so if you fast-forward to 2020, and the beginning of 2020 is when this management team took over, we had four verticals.

We had Agency MBS, which is the hub and the liquidity engine, Resi-Credit, CRE, and Middle Market Lending. What we wanted to do strategically was bring Annaly back to exclusively housing finance in the residential space. And the reason being is that's our core competency, that's our brand. That's what we knew and we felt like the market would embrace that. And then COVID hit literally the week after we took over. Now, COVID was a material setback for everybody on the planet, including our sector, but what it did for us is it forced us to rethink how we looked at everything in our business, not just market shocks and volatility, but how Americans would use real estate. And in terms of the objective to get back to housing finance, it only sharpened the focus. So at the outset of COVID into the depths of COVID, we very quietly but very deliberately began to engage in three strategic priorities.

First was to package up our commercial real estate business such that when markets healed, spreads rebounded, and the economy began to correct, we could go to market and actually move that off balance sheet. The second thing we did was begin an MSR business on our balance sheet. Now, by way of background, prior to COVID, we did own a servicer, Pingora Loan Servicing. So we had exposure to MSR and we did operate a business that engaged in subservicing oversight. So we had the playbook to do that, but we wanted to do it on balance sheet. So in early 2020, we brought Ken Adler on board to help us build that out. Now the third strategic initiative we engaged in in early 2020 was in residential credit.

One of the things we experienced in 2017, 18, and 19 was the sector was exhibiting somewhat of a scarcity of assets and we needed to make sure we had a way to source assets in an efficient way to make sure we had quality assets coming on the balance sheet. So Mike Fania and his team began the planning stages to launch a residential correspondent channel. So those three things, we started in 2020. In 2021, first half of 2021, as a matter of fact, we sold commercial real estate to Slate without experiencing a loss, which we thought was an accomplishment. We bought our first MSR package in the spring of 2020, and our correspondent channel started acquiring loans also in the spring of 2020. So we were on our way. And growth was relatively slow at the outset, but we were making progress.

Now, fast-forward to 2022 and the Fed starts normalizing policy, rates are selling off, QT is beginning, and there's a lot of volatility in rates markets, and assets in our sector were cheapening. At the same time, corporate credit was doing extraordinarily well. There was such a bid for corporate credit that it just created such a tailwind for our middle market lending portfolio that we said, "Wait a minute, okay, rates are volatile, originators are somewhat disrupted from capital markets activities. They need liquidity. They have all this MSR on their balance sheet that they need to monetize because the origination complex is slowing down."

So we sold our middle market lending business to Ares at a profit, and we redeployed that capital largely into MSR. So that left us with three verticals, Agency MBS, Resi-Credit, and MSR.

Now also in that year, the market understood who we were and what our strategy was, and as a consequence, rewarded us with the ability to raise capital in that year. And also in 2022, S&P added us to their index, the S&P 400. Which coincidence or causality, I do think that understanding our business model enabled them to be comfortable with adding us to the index, and that enabled us to grow further. So that leaves us where we are today, which is three fully scaled strategies exclusive to housing finance, but diversity and synergies across the businesses. \$80+ billion dollar balance sheet. We're as liquid as we've been in many years. \$7.4 billion of unencumbered assets on the balance sheet, \$4.7 billion of which is cash and Agency MBS, which gives us a considerable amount of optionality.

And it's that type of liquidity that had enabled us to do the things rapidly in 2022 and beyond, and that will continue to let us do things rapidly as we move forward, but responsibly. We've financed nearly a million homes in the country, something we're very proud about. We're 10 times the size of the average mortgage REIT, and that scale gives us huge advantages, not just as it relates to costs, which we'll get into momentarily. And most notably, as I said, the core mission is to deliver a stable dividend for our shareholders and we yield 13% currently, which is very consistent with our historical average, and we've been very comfortable with the ability to deliver that through strong earnings available for distribution.

All right, let's get a little bit deeper into what we built and how it all fits together. Look, we operate in a world with considerable uncertainty and that uncertainty has only increased over the last number of years as we all know. And it requires diversity in your portfolio. You can't have every asset correlated. Now, I love Agency MBS as much as anybody. I spent the vast majority of my career in Agency MBS. But one thing I will tell you is that negative convexity can be painful when it materializes. That's why you get paid the spread you get paid in Agency. Now, our objective is to minimize the consequences of negative convexity.

Now, anybody who's ever participated in the mortgage market as seasoned veterans and the like, whether you're levered, unlevered, sell side, buy side, there's nobody who's ever spent any length of time in the mortgage market who hasn't been compelled to sell an Agency bond at the wrong price. And we're no exception. What we're trying to do is take advantage of the spread that Agency offers and the liquidity and the guarantee but minimize the consequences of negative convexity. And we think we've achieved that. And that's the biggest benefit to combining these three strategies obviously is the lack of perfect correlation in the returns. But there's many other synergies that we've come to realize over the last couple of years.

Obviously, MSR is a natural rate hedge for Agency, but in addition in this world with a lot of locked-in mortgages, MSR hedges turnover on your discount Agency MBS, which is something we've benefited from over the past couple of years. And also in a period of high policy rates, MSR through float income hedges your front-end exposure on your Agency portfolio. So the synergies are pretty considerable and they've only increased in the current environment. Also, modeling. Now, Srini who you'll speak with next, he will get into some of the modeling aspects of our Agency strategy. But understand that when we're bidding an MSR package, that Agency modeling effort goes hand-in-hand with that, and the synergies between Agency and MSR from an analytical standpoint are as considerable as you can imagine, and it's underappreciated.

Strategic relationships, particularly between resi and MSR and our partnerships. Now, it is no secret, or should be no secret that our largest partners on the residential credit side are also our largest partners on the MSR side in the origination and servicing community. These relationships are institutionalized. We are thought of as a liquidity provider and a capital partner to these institutions. And the relationships run very deep and it's effectively one-stop shopping with Annaly. And you combine that with our large capital base and it gives the origination community a lot of confidence to come to us and rely on us. And that's been a great benefit for having both of those businesses on balance sheet.

Operational synergies. Subservicing oversight on Agency is combined with the oversight of residential credit. Asset management and delinquencies are all harmonized such that we can minimize the costs and make sure we have the best expertise performing each function. And most importantly, financing synergies. We can look at our financing holistically and manage the cost and our liquidity at the top of the house to ensure that A, we're always very liquid, and B, we're overall minimizing the cost of financing by being able to look at these three businesses holistically. So that's just a little bit on the synergies and you're going to hear a lot more about that from the teams.

And just a quick summary on capital allocation over the last five years almost. Again 2020, four businesses, 78% of the capital was in Agency MBS with 22% spread between three credit businesses. Fast-forward to today and we're roughly 60-40 Agency to credit and MSR, which is close to where we want to be. We think the optimal range from a risk-adjusted return standpoint between Agency and the Resi and MSR businesses is 40% Resi/MSR to 50%, with Agency not falling below 50%. Because of the strong liquidity and the levered nature of the business, we want to maintain 50% Agency. But right now we're a little bit overweight Agency at 60% and we're perfectly fine with that. Now what that leads to is a model that has lower leverage, lower volatility, as you'll see when we talk about returns, and less interest rate exposure. And so we think we're in the right wheelhouse for where we want to be long-term but we do have room to increase Resi and MSR. All right. Again, the point about efficiency. So the model is truly built for efficiency. Three fully scaled businesses with all of the benefits of having operating platforms, when you're talking about asset aggregation as well as recapture and other benefits that we derive from the servicing community. But by plugging in to our origination and servicing partners, we avoid the operating leverage that those businesses entail and it's hugely beneficial to us. And it most shows up in our OpEx to equity ratio, which you can see at the bottom. That little sliver down there on the left is our OpEx to equity ratio, which is considerably below that of the monoline Agency REIT sector.

Now admittedly, a lot of those folks are very sub-scale, but we're only a little bit above the largest of the monoline Agency REITs in terms of OpEx to equity. So we do it very efficiently and very lean and considerably below hybrid REITs and MSR REITs for obvious reasons. And we put the mortgage originators in there, not because it's a good comparison but just to show what type of expenses those entities entail and that we're not looking to acquire those types of operations at this point because we think we can do it much more efficiently as we're currently constructed.

All right. Now, quick lens into each of the verticals. So again, Agency is the hub. We methodically invest in specified pools, which you'll learn about next. And for those of you who don't know V.S. Srinivasan, he's been in the Agency market for decades. He's one of the foremost experts of prepayment modeling. And his ability to select collateral and his team's ability to trade and also inform the collateral selection, I think is second to none. And as a consequence, we've developed a very high-quality Agency portfolio. And you see it in the speed environment of the collateral we own, quarter in and quarter out. When you look at our speeds on our premiums and our discounts that generally pay pretty quick. And in addition, he's equipped with a very high-quality rates team with decades of experience. And so we're constantly in the market navigating our duration and making sure we're making smart decisions. And the team does it quite effectively, many of whom you'll meet later on today in the cocktail reception actually. Again, best in class modeling you'll hear about.

Residential Credit. Largest non-bank issuer of prime and expanded prime, second-largest overall. We've securitized \$30 billion since 2018 and the pace of that securitization effort has only grown. And we've been very encouraged by what we've seen with the redevelopment of residential credit securitization over the past number of years and we feel like it's a very viable financing arrow in the quiver and will be for the foreseeable future. So we feel very good about it. What we, I think, are most proud about that business and keeps us sleeping well at night is the credit quality of what we've acquired. We have the lowest delinquencies amongst the top 10 issuers in the resi-credit sector. By controlling the product that comes through our channel, Mike and his team has done a very good job of making sure the portfolio remains healthy.

And then lastly, as it relates to Residential Credit, and this isn't something we talk about often, but we do have a large JV with one of the biggest sovereign wealth funds in the world and we are arms locked in this market providing liquidity and capital to the origination community. And we have a very durable platform of capital. Not just Annaly's capital, but we have outside capital as well. And to the extent, there's ever a technical dislocation in the market, we will be there to take advantage of it. Again, arms locked with one of the largest sovereign wealth funds in the world.

All right, MSR. So look, in a little over three years since purchasing our first package, we've become one of the top 10 servicers in the country. Portfolio of critical mass, nearly \$3 billion in market value, a couple of hundred billion in principal balance, the highest quality portfolio in the market, hands down. Just a touch over a 3% note rate, so the convexity is incredibly good and the credit quality is impeccable. And so that portfolio allows us to sleep easy at night, both with respect to prepayments but also as it relates to credit. And we've also developed best-in-class recapture capabilities. And it's not consequential now given the note

rate of our portfolio, but as we are going higher in coupon, as origination ultimately picks up, these recapture partnerships like the one we just announced with Rocket are going to be hugely valuable for us.

Now the last point I want to note on this page is that none of this works. None of these three businesses work without the best financing in the market. And you're going to hear more about that from Serena, our CFO who you know. But you're also going to meet our treasurer today, Pete Koukouras, who's been with the company for 20 years. So through the financial crisis, financed the company through then, through all the moments of volatility. And he has a tentacle on every part of the financing market. And he has developed a portfolio of financing options for this company that I think makes us more durable than anybody else. From obviously, 50-plus bilateral relationships, we have our own broker-dealer and we have \$5+ billion in warehouse financing across both MSR and Resi. And again, he's dialed into every aspect of the financing market. He is one of the most known guys in the sector and we're very proud to have him on our team. So you'll meet him later. But you can't do this without confidence in your financing, I promise you that.

All right, let's get into quickly how it all has worked. So what we have here on the top is just a year-to-date performance chart. And this is through the third quarter. 10.5% economic return, which we think compares quite favorably relative to both the Agency REITs, hybrid REITs, and even the MSR REITs which have led the sector. So overall it's been a good year for us thus far. We've delivered the dividend and generated a touch of book value appreciation. If we look back a slightly longer period of time, we used the last two years here. And the reason being is because Middle Market Lending went off balance sheet in the third quarter of 2022, and that's when MSR really got to scale at that point. So for the last two years, we've had each of these three businesses, we think fully scaled, and we have two years of data through what were quite volatile markets over the past couple of years.

And if you look at the returns, a little over 25%, compares obviously quite favorably to Agency and hybrids and certainly relative to MSR. But one point to note is that the MSR market has had a very good past couple of years and we were fortunate to get into the sector when we did. Now obviously, some of that's luck, but we had a plan and we knew what we wanted to do and we feel like we benefited quite a bit from venturing into or rather establishing ourselves in MSR. And from a Sharpe ratio standpoint, our Sharpe ratio is hands down much better than Agency and hybrids and comparable to the MSR sector. MSR has done well and we certainly acknowledge that and we're very glad to be a large participant in the market. And overall, we think we've had a pretty good beginning of a track record for the past couple of years.

Okay. Where are we going? And I don't want to steal a lot of the thunder of my colleagues, but I did just want to give you a little preview as to how we're looking at the world right now. As everybody knows in the Agency market, monetary policy is becoming more accommodative, but the Fed will continue to unwind its Agency balance sheet even as QT ends, which does present a little bit of a technical overhang on the market. And actually, you combine both those factors and it's pretty encouraging. More accommodative policies should ultimately lower volatility, but spreads are not going to tighten considerably with this backdrop of supply in the market.

Now, the positive technicals from money managers and banks even being involved is good. But nevertheless, we think spreads should tighten modestly or somewhat, but they're not going back to their ten-year historical average at all, which is just fine for us because it enables us to invest at relatively lofty spreads. And we're going to continue to maintain Agency as the hub of the company, and we're going to continue to invest in the technology and modeling capabilities to make sure that as borrower behavior changes, we're always ahead of the curve and we're always going to make that investment.

All right, Residential Credit. So there are structural tailwinds in resi-credit and particularly with this new administration coming on. I think what we saw in Trump 1.0 was that there was a desire to withdraw the footprint of the GSEs, not just recap and release but also reduce the products that they guaranteed. And what that does is create options for our correspondent channel to acquire different types of loans that might have otherwise fit the Agency model. So for example, Agency-eligible investor loans or second homes. We were big in those sectors when the caps were put in place by Calabria. And you'll probably see that type of policy move as well again in this administration, even in the absence of something more significant.

And then second liens and HELOCs, we do acquire through our correspondent channel with higher rates that are likely to remain persistent. That'll continue as folks look to tap equity out of their homes, and we're prepared and already acquiring those loans. We feel like there's room for growth there. And then in MSR... So the sector has changed with banks withdrawing and non-banks coming in because the need for liquidity

and capital and partners like us is much more considerable. They're great operating entities, we're the capital partner. And we marry the two and we have a sector that can actually trade and that's not going away. No matter how regulation changes, there will be a need for our liquidity and we'll continue to be able to grow that business on a go-forward basis.

So in short, we're very encouraged by the outlook. And there's a lot of uncertainty heading into 2025. We get it. We'll see how the administration takes shape, but we're encouraged overall. So key takeaways, proven history and management. You can invest in all aspects of the mortgage loan with Annaly and we allocate capital across the cheapest part of the loan. We're afforded opportunities based on our size and scale, and we also have very strong corporate governance and corporate responsibility practices. The synergies we spoke about, you see it come through the returns. And our partnerships are considerable and they're only growing. We do have favorable industry tailwinds that we think are ahead of us. And lastly, and most importantly, we have achieved the purpose of the model, which is providing a stable dividend yield for our investors, and that will always be our obligation in conjunction with preserving capital. So now with that, I'm going to pass it off to our macro strategist Andreas Strzodka, who is going to lead a discussion with our Agency and MSR Heads Srinii and Ken Adler.

## Agency MBS & Mortgage Servicing Rights

*Moderator*

**Andreas Strzodka**, *Head of Macro Strategy*

*Panelists*

**V.S. Srinivasan**, *Head of Agency*

**Ken Adler**, *Head of MSR & Head of Portfolio Analytics*

[Andreas Strzodka:](#)

Well, thank you. Thank you, David. My name is Andreas Strzodka. I'm the Head of Macro Strategy and I'm very excited to be moderating this panel today with my two colleagues, V.S. Srinivasan, the Head of our Agency business and Ken Adler, the Head of our Mortgage Servicing Rights business. Now we want to do three things today. The first third we'll spend a little bit about a market overview to see how everything is going right now. We will then speak about what makes Annaly's Agency and MSR businesses unique. And finally we'll talk about some of the synergies between the business. Now to get into the market overview, everybody in this room is aware the US economy remains exceptionally strong. That we expect the growth to come in at 2.75% this year. The labor market has slowed, hiring has slowed somewhat. The unemployment rate has risen off very low levels, but nonetheless, the labor market is in a very good place.

It's roughly in balance between supply and demand, and that should be a tailwind going forward. Inflation has slowed from very high levels. Yes, it remains above the Fed's 2% target because service sector inflation is fairly high. But if I had told anybody two years ago at the peak of inflation that we will get to this point today without seeing a meaningful economic downturn, you would've all laughed me out of the room. So I think things are pretty good on this, and I would just make the other point about inflation is that wages so far have moderated at a slower pace than inflation, and that has really led to positive real income growth for consumers which has fed this economic cycle. Now, I'll talk about housing real quick. So in the housing market, we're basically seeing a market at an equilibrium of very low levels of activity.

Anybody who already owns a home and got a mortgage way back when, has generally very low interest rates and they're locked into their homes right now, unable to move because it would be prohibitively expensive. At the same time, people that want to buy a home, they're facing high housing prices as well as high mortgage rates, which makes it difficult to move. Now we have seen an improvement in the level of inventories are coming off very low levels, but the rise in inventory has been driven by new homes, and it's been predominantly in areas of the south of the United States as well as the West, where it's much easier to build than call it in New York City. And now ultimately I think the outlook for the housing market will be very closely tied to the level of interest rates.

If you look at current market pricing, expectations are for mortgage rates to remain roughly here, which would suggest that the housing market remains roughly stuck. But again, the two will be highly correlated. Now on fixed income markets, I'll just make three quick points. The first one is real interest rates are very high, it's 2.1% 10-year real Treasury rates. So that's closer or more corresponding with the period that we saw before the financial crisis than the area of very low interest rates and very low spreads that we saw between the great financial crisis and the pandemic. I think the second thing is that volatility has been very high.

David talked about this briefly, interest rate volatility has moderated, but it's clearly not yet back to the level where it was in, call it between 2015 and 2019 when interest rate volatility was very low and very good, very kind to mortgage investors such as ours. And finally, I would just make the point that this year we have been encouraged by the stronger fixed income flows. The demand for fixed income has certainly improved, probably driven by the Federal Reserve. Flows this year, they're running at twice the rate of last year, and they're probably the second-best year in the past 20. So I'll leave it at that. Not to take too much of Mark Zandi's thunder from later on, but let me ask you Srinu, what's going on in the Agency market?

[V.S. Srinivasan:](#)

Thanks, Andreas. So Agency MBS spreads are attractive both on an absolute basis and relative to other fixed income assets. Over the last two years, there have been two significant headwinds for the sector,

elevated interest rate volatility and a supply demand imbalance. And over the last few months, we have made some progress on both fronts. Like Andreas said, the US economy is normalizing. Labor markets are more in balance, inflation pressures are easing, and this has led to a decline in volatility, with fits and spurts. But overall volatility has declined significantly from the peak in say the third quarter of 2023. But vol levels are still pretty high and we expect that without any unpleasant surprises that volatility will continue to decline in 2025, and that should be supportive for spreads. Though, supply-demand imbalance is also easing. In 2023, banks shed about \$160 billion in Agency MBS, and so far this year they have added about \$75 billion.

So that itself is a \$250 billion shift in the supply-demand equation. Andreas mentioned that fixed income flows have been pretty strong and typically a percentage of fixed income flows materialize as demand in the Agency MBS sector. And finally, historically, at least when the Fed embarks on an easing cycle, we have seen increased demand for Agency MBS from both foreign accounts and banks. So overall, we are very constructive on Agency MBS and we think spreads will tighten, particularly if interest rate volatility continues to decline. But what we don't expect is that spreads will go back to the levels you saw pre-COVID. That's the blue line in that chart. And the main reason for that is that the Fed is going to continue to let the Agency MBS portfolio run off even after they stop shrinking the balance sheet.

So that is an additional \$180 billion in supply that has to be absorbed by other market participants over and beyond the almost \$200 billion in organic growth that we expect in the Agency MBS sector. And this supply from the Fed is going to persist for many years. So we think that puts a floor on how tight Agency MBS spreads are going to get. So let's put some numbers around it. Over the last few months, current coupon spreads to the blended Treasury curve have traded in 115 to 140 basis point range. We think over the next few months this range could tighten to something like 110 to 125 basis point range. This is actually, as David mentioned, a pretty good outcome for us. The potential tightening in market spreads is generally supportive of book value and even at those tighter levels, spreads are wide enough that we can comfortably earn our dividend.

[Andreas Strzodka:](#)

Yes, thank you Srin. Ken, how's the MSR market treating you?

[Ken Adler:](#)

Well, you heard from Dave, it's been great. MSR investment has created great returns post-COVID, and the reason for those returns are in place today and go forward in our view and big picture, what those reasons are, I think they're pretty straightforward. They're slow prepayments industry-wide, they're low delinquencies and an ample supply of investment. Just to take a step back as to why the opportunity got created. During COVID, interest rates went down, mortgage interest rates in particular, to a point where virtually every homeowner or most homeowners in the United States could benefit from a refinance. As a result of that, mortgage lenders were able to do record volumes at record profit margins, that created the capital for them to retain MSR at a level that historically they've never been able to do before.

David talked about it being a little bit of luck. The rate at which things changed in 2022 certainly was not forecast, but we did foresee, and the reason I joined was seeing this buildup of MSR on non-bank balance sheets and the potential opportunity. So as the environment changed in 2022 and rates went higher, the profitability of these entities declined, they were left with very high fixed cost infrastructures. So in addition to scaling back their operations, MSR was sold to create liquidity. Very straightforward. So why do I say it's still in place today? That's because where interest rates are and where the stock of outstanding mortgages are struck, the likelihood of volumes and margins going to a level where the mortgage industry can economically retain the MSR that's created is just highly unlikely.

And that's really why we're so excited. Annaly is especially well situated because we've created a business where we're a friendly buyer. And what I mean by that is we do not directly compete with sellers. We don't touch consumers, we don't service our own loans, we don't do our own recapture activities, we outsource all of those activities. So all things being equal, people would like to work with us. The other thing that makes us a great buyer is the reliable source of capital. The amount of capital we have allocated to MSR, even at the targets that we've published, is still just a fraction of our capital. So our ability to have a reliable bid in the market and execution is needed because these sellers are relying on us for liquidity. It's there and it counts and yeah.



[Andreas Strzodka:](#)

Thanks Ken. So I think that describes generally a constructive market backdrop. I mean, as in any market environment risks remain, but we do think we're getting fairly compensated to take them. So now let's shift a little bit to our second topic, Annaly's secret sauce. So Srin, let me ask you, how do we manage our Agency portfolio different from other mortgage REITs or similar competitors?

[V.S. Srinivasan:](#)

Sure. Compared to our peer group, we have a lot more flexibility in rotating in and out of Agency MBS because we do invest in other asset classes. If you think about the Agency MBS sector, it is very competitive and there are a lot of smart people doing relative value or trades within the sector. And at Annaly we pride ourselves as being able to come up with the best relative value trades. But typically these trades add tens of basis points of alpha.

If you think of relative value trade across sectors, it's a lot less competitive and can often add hundreds of basis points of alpha. So our ability to rotate in and out of Agency MBS to MSR and Resi gives us the ability to capture some of this outsized alpha that can be generated. Now, what gives us that ability? Well, in the base case, we think of Agency MBS at 7.5x our debt-to-equity leverage, our MSR business at 1x and our Residential Credit business at 2x, but we don't always finance it that way. Ken maybe you can elaborate to everybody why the MSR business is always a debt to the Agency business.

[Ken Adler:](#)

And we thank you for that. Most participants looking to generate teen sorts of returns in the asset class are applying leverage to the asset, and we are no different, we do that as well. And what differentiates us is our cost of leverage, and Dave mentioned how we manage it at the top of the house, and you're going to hear later from our Treasurer more about the specifics of how that works. The big picture, MSR leverage is SOFR plus hundreds. Agency leverage is SOFR plus single digits. Because we run the Agency business with prudence, there's excess borrowing capacity available there that we can tap and thanks Srin for on the MSR side. Now we're not compromising firm-wide liquidity because we maintain financing lines against our MSR that are committed lines so they can be drawn on very short notice and that borrowing if it was ever needed for another investment opportunity or for whatever corporate purpose. So the blended cost of the leverage allocated to the business is just lower than our peers and provides us substantial competitive advantage.

[V.S. Srinivasan:](#)

So as Ken explained, at any given time, we can tap this MSR warehouse and increase our capital allocation to Agency MBS allowing us to grow our Agency MBS book. That's what gives us the ability to rotate in and out of Agency MBS very seamlessly. The diversified model also helps us handle spread volatility much better. So we have about 60% of our capital invested in Agency MBS, and thankfully over the last few years, the episodes of spread volatility in Agency MBS have not been correlated with common commensurate spread volatility in MSR and residential credit. So when spreads widen in an Agency MBS, the losses we take is spread across our entire capital base.

So in effect, we only lose 60% of what we would have lost if we were a mono line Agency MBS portfolio. Now you could argue that Agency MBS spreads go up and down, but locally they generally tend to mean revert. So these are just paper losses, who cares? But it's important to note that these spread widening episodes can be quite significant and prudent risk management demands that at some point you de-lever. It's just that with 60% of our capital and Agency MBS, we have a much longer runway before we hit the threshold where we have to do something. I think this is a very important distinction between us and how we manage our portfolio and how our peers have to manage their portfolio.

[Andreas Strzodka:](#)

Thank you guys. So we wouldn't be Annaly if we wouldn't be talking about our scale as the largest mortgage REIT. So Ken, let me ask you, how has our scale helped us build the MSR business?

[Ken Adler:](#)

Well, we spent a lot of time on the financing advantages and David referred to it and I did already. We are the desired partner for the mortgage industry when it comes to MSR investment and it's because of these partnerships we've put together. And what's really noteworthy is when people get this scale, you hear they

frequently internalize operations to create efficiency and save costs. What we've found is that scale can create more than those savings through these partnerships. In today's world, there's excess capacity in the mortgage industry both on the origination side and on the servicing side. So when you're negotiating contracts for mortgage services, you are priced out at the marginal costs of those services plus a reasonable profit margin as opposed to the average cost that these entities are paying themselves.

We have no overhead, so we are primarily a variable cost model, but we have a cost structure that's arguably as good and at times better than people that have their own platforms. And again, it's due to the excess capacity as a result of the downturn. The other opportunity that's created through that is when people that own MSR want to sell that MSR, if it's being subserviced or it's owned by somebody who services their own loans, they have a huge preference to sell it to somebody who will retain them as subservicer. So we are seeing opportunities that other people can't take advantage of and those partnerships are very strong. So when people talk about franchise value, the scale has allowed us to create these partnerships that have created real franchise value.

[Andreas Strzodka:](#)

Thanks. And Srin, how does scale help the Agency business?

[V.S. Srinivasan:](#)

Sure. I mean, as Andreas mentioned, we are the largest mortgage REIT out there and we are probably among the most active in trading specified pools. What this means is that we get a lot more color both on pricing and flows in the market. We are probably involved in the vast majority of flows that happen in the market. This leads to better execution. So when we execute trades, we can get better levels because we have more color. But even away from that, our scale and the nature of our business model gives us multiple points of connectivity with our dealers and financing partners.

We obviously trade Agency MBS with them, which allows them to earn some bid-ask spread, they securitize our non-Agency deals, the OBX shelf, which allows them to earn some fees. They're involved in the lucrative business of financing our warehouse lines for loans and MSR. So when it comes time to ration repo, fortunately financing has been plentiful for the last few years, but there will come a time when repo is being rationed. We feel like we have a much bigger competitive advantage because we have a much deeper relationship with our financial partners.

[Ken Adler:](#)

Yeah, look, the synergies are real in both directions. I mean, there's really one team at the firm that manages hedges, prices, models, all interest rate and prepayment exposure. So you're not going to find an MSR business that has access to the sort of portfolio analytics, performance attribution, prepayment modeling that goes on at an Annaly. And that's because of the magnitude of the Agency MBS effort.

[Andreas Strzodka:](#)

Thanks you. Thanks Ken. Yeah, that I think gets us to our last topic that we wanted to discuss today, which is the synergies between the business. So for everybody's edification, I sit close to them not only on the stage but also in our office and they frequently talk to each other for whatever reason. So let me ask you guys, what are you guys actually talking about?

[V.S. Srinivasan:](#)

So if you think about an Agency MBS book or an MSR book, the unique risk that we take is prepayment risk. And to manage these books well, what you need is a good understanding of prepays, the ability to spot emerging prepayment trends, take all of this information and put it into models, generate cash flows, and come up with good estimates of duration and convexity. So if you can do these five things right, everything else falls in place and we have an excellent team which does our analytics for us, which takes inputs from all of us and comes up with the analytics that gives us very reasonable duration and convexity on our portfolio. Now to answer your question, Ken and I are nerds, we spend most of our time talking about what we see in our markets and what that means for prepayments. I'll give you an example.

Earlier this year there was considerable debate on how fast newly originated collateral would prepay if mortgage rates rallied to say 6%. On the one hand, the newly originated collateral had very high loan balance, and historically higher loan balance pools tend to respond very aggressively to any rally in rates. On the other hand, they had very high loan to value ratios. What I mean by that is the loan size was typically

over 80% or 80% of the home value, and that can sometimes be a constraint to refinance. While we were having this debate on our desk, Ken chimed in and said that servicers have very attractive bids for current coupon MSR. So my first reaction was if servicers love current coupon MSR, they must not be expecting very fast speeds. Servicers are much closer to borrowers than any bond trader sitting up in New York trading bonds.

And if they thought that speeds are going to be slow because MSR is after all an IO cash flow and faster speeds hurt their valuation. But Ken did his due diligence, he went and talked to our subservicers, he talked to other MSR participants and he came and told us that they're actually expecting really fast speeds. They think they can refinance these borrowers really quickly and they're embedding into the value of MSR the value of the gain on sale on the new loan. So this sort of informed how we positioned ourselves in the Agency MBS book. If you look at our portfolio in higher coupons, particularly Fannie 6s and 6.5s, we were mostly in high quality specified pools.

Basically we paid up for call protection. And lo and behold, when rates did rally to around 6% in September speeds on generic Fannie 6s and 6.5s were much faster than anyone expected. For example, the cheapest Fannie 6.5s paid north of 50 CPR, almost 10 CPR faster than what the market was expecting just two, three months ago. But our portfolio specified pools, which we had paid up for call protection, our Fannie 6s paid at 17 CPR. So this is just one example, but we are constantly talking to each other, trying to understand what the servicer population is thinking about how prepayments are going to evolve. And we take that into account when we construct our Agency MBS portfolio.

[Ken Adler:](#)

Yeah. And I just want to add how we use it on the MSR side of synergy. Specified pools are a very granular pricing. You're pricing, the prepayment sensitivity of all sorts of loan attributes, whether it's loan size, geography, who the originator was, FICO, there's several others. MSR is not priced as granularly, it just isn't. And that's because the participants in that market are really not prepayment experts and they're not managing specified pools. So our MSR pricing infrastructure is able to capture those attributes where we believe our peers are absolutely not. And that's allowed us to absolutely construct a portfolio with higher performance qualities than generically and it's just not observed by the market. And that's thanks to the Agency book.

[Andreas Strzodka:](#)

Well, thank you very much guys. So unbeknownst to you, I'm getting the red light, which means we're unfortunately out of time. So I hope we were able to demonstrate that our scale and our flexibility helps us to try to achieve the most attractive relative and absolute returns and that we're doing all of this in a collaborative fashion. I'm now happy to announce Mike Fania, our Deputy Chief Investment Officer and Head of Residential Credit. He will give you an overview of the Onslow Bay conduit. With that, thank you very much for your attention. Over to you, Mike.

## Onslow Bay Correspondent Channel & Securitization Platform

**Mike Fania**, *Deputy Chief Investment Officer & Head of Residential Credit*

*[Mike Fania:](#)*

My name's Mike Fania, I'm Deputy CIO and Head of Residential Credit at Annaly. Over the next 25 minutes, we're going to talk about the current state of the Residential Credit portfolio. We're going to talk about the Onslow Bay Correspondent channel. It was launched in April of 2021, so a little over 3.5 years since implementation. We're going to talk about our securitization program. We're one of the largest securitizers across residential credit since 2018. We're going to talk about some key business initiatives that we have that we think can further entrench ourselves as a leader within the correspondent channel. And then lastly, we'll talk about some key differentiated advantages. So advantages that we think are unique to Annaly.

So first in terms of the state of the residential credit portfolio. So we ended Q3 with \$6.5 billion market value of assets, \$2.3 billion of capital, which represents 18% of the firm's capital. Of that \$6.5 billion, \$3.9 billion is coming directly from OBX and residential whole loans. So about 60% of the portfolio is proprietary assets organically created. We think that's something that is pretty significant, difficult to replicate. When you think about the GAAP consolidated whole loan portfolio, it's \$23.5 billion. So that doesn't show up in the economic market value of the portfolio.

But I think it's important to note because Onslow Bay is the sponsor of all those securitizations and ultimately we have the ability to call and re-lever those deals to the extent that that optionality exists. So very large residential whole loan portfolio that has been securitized. When you think about how this portfolio is actually financed, of that \$2.3 billion in terms of your debt outstanding, we're using bilateral repo on the credit security side. Usually the tenor of the repo is called four to six months. So it is not necessarily short-term, but we'll call it something in the intermediate term.

*[Speaker 1:](#)*

[Building fire safety announcement].

*[Mike Fania:](#)*

Hopefully they add some time back for me. So we got a lot to go through. So in terms of the residential whole loan portfolio, we have a number of slides, we'll detail that, but that is financed through warehouse facilities and we have a very broad and diversified set of facilities. I think what you don't see within this slide, but that does show up in terms of a competitive advantage. Ken did a very good job in terms of talking about it, but it's also similar with the residential credit portfolio.

*[Speaker 1:](#)*

[Building fire safety announcement].

*[Mike Fania:](#)*

So when you think about this portfolio, it's levered 1.8x. So that's the debt-to-equity on this portfolio. If this was a standalone company, if it's a standalone hybrid REIT, you're probably maintaining, call it 2 to 2.5 turns of balance sheet leverage. So in the same example that Ken gave where we have the implicit advantage of using Agency financing, we also have that same advantage on the residential credit portfolio as well. The difference in cost of financing Agency, which we'll call SOFR plus 10 to 20 basis points versus funding residential credit securities probably 100 basis points.

It's pretty significant. So significant advantage. And the reason we're able to do that is because of our liquidity. As Dave mentioned, we have \$4.7 billion of cash and unencumbered Agency MBS at the end of the quarter. So that's a key differentiator in terms of the three businesses and the diversified housing finance model. So then let's talk about what is Onslow Bay Financial. So Onslow Bay Financial is a taxable REIT subsidiary. So this is where all our mortgage activities occur. This is where we have 50 first lien and...

*[Speaker 1:](#)*

[Building fire safety announcement].

[Mike Fania:](#)

I'll keep going, 50 first and second lien licenses. This is where all our mortgage activities occur. This is where we buy MSR, it sits in Onslow Bay Financial. When we buy residential whole loans before we securitize, it sits in Onslow Bay Financial. What I think is very important about this is that there's full alignment between Onslow Bay Financial and Annaly. It is wholly owned. If you think about a number of asset management companies that have bought originators, there's some inherent conflicts of interest unless they own that entire origination platform. If you only own a minority share, there's potentially conflicts between senior management of that originator relative to the asset manager. But I think what's important is that we have that full alignment.

In terms of the correspondent channel, we've put over \$27 billion of locks through the correspondent, we funded close to \$17 billion of loans, and we currently have 240 approved correspondents. Just as important as the volume is our ability to distribute the risk. So in terms of our securitizations, David mentioned this, we've done \$30 billion in securitization since 2018. We've generated \$3.8 billion of assets. That's a 13-14% retention ratio on our securitizations. I think the most important part about the correspondent is that we control every facet of it. We control who our origination partners are, our servicing partners, we control loss mitigation, the diligence firms. We control all aspects of the acquisition of these assets. But I think also what's very important is that we control the pricing. We're the ones setting the gain on sale margin. We're the ones that are setting those ROE targets. So from soup to nuts, you have the entire chain of asset acquisition, mortgage loan acquisition from the entirety.

[Speaker 1:](#)

[Building fire safety announcement].

[Mike Fania:](#)

Why is the correspondent important? If you look at the graphs here, effectively what you're seeing is, capital deployment over the last 3.5 years, it's been significant. So we've gone from \$3.2 billion market value since the launch of the correspondent to \$6.5 billion today. So over \$3 billion of assets on our balance sheet. And it also represents 58% of the dedicated capital. So 60% of assets, 58% of dedicated capital.

But I think what's important is since the launch of the correspondent, we've gone through what I'll say is many cycles in terms of interest rates, in terms of credit spreads. So since the launch of this channel, we've had Fed Funds go from zero to 5.30%, to now, I think 4.58%, 4.59%. We've seen the 10-year trade in the range of 1.20% to 5%, and we've seen CDX, which is a reflection of high-yield spreads, corporate credit spreads, been anywhere from 270 to 625. Throughout all of that, we've had the ability to generate these assets, and we think without this channel it would have been very challenging to do so given how volatile the environment has been.

So very, very excited about where we stand today, but we have a number of key business initiatives. On the correspondent channel, everything that we do is fully delegated. So what that means is that we publish underwriting guidelines, we publish pricing, and it's up to the originator to underwrite that loan in accordance with our guidelines and deliver us that loan back best efforts. What we're effectively going to launch in the first half of this year is non-delegated platform.

Effectively what we are going to do, there's a number of small originators out there, they don't staff themselves with non-QM and DSCR underwriters. They may only get three or four leads per month. Right now, they may be brokering those loans. They'll broker them to a non-QM originator. We are going to help them underwrite the credit file. So that is a relationship that is very sticky because they need us from an operational perspective. So we're very bullish on the number of originators that are out there that need these non-delegated underwriting services.

That also coincides with the growth of the correspondent. Right now at 240 we think that there's 50 to 100 originators that are out there that are either doing non-del or they're fully delegated and they're not partners of ours. We have five full-time business development people, and they're very hard at work in terms of this.

The next one is just incremental originator tools. Anything that you can put out there to further ingratiate yourself with the origination community is very important. One is bank statements. We don't need to go through what it is, but effectively you're providing them a bank statement calculation. You're providing them a level of service that they're not able to get from our peers that puts them in our sphere and continues to do business with us.

The last is improved in terms of originator experience, so technology. A lot of these originators, they want to recycle their capital. They do not want to have loans on warehouse facilities. They don't want them on gestation facilities. It's very important the turn times and how quickly you can buy those loans. We've had a number of initiatives, whether it's enhancing our custody product, e-docs, electronic docs of the mortgage, and the title policy to help speed the gestation and the cycle time of those.

So from a balance sheet perspective, we're already positioned for growth. So you could look at the bottom part of this graph. Nine different warehouse providers. That's a pretty healthy number of providers, operationally that's very intensive, but there's a reason that we do that. We do it because we don't feel any of our providers have any leverage over us. We know where the market is. We can drive where the market is in terms of advanced rates, in terms of financing costs, if you had two to three warehouse providers, you would not have that position. So at the end of the quarter, we had \$3.5 billion of warehouse capacity, \$1.3 billion in terms of what's funded against it. So over \$2 billion of excess capacity. We're running 36%, 37% utilization. So we have significant balance sheet to be able to grow this business. What also is important, we have closed-end seconds. David mentioned this. HELOCs, we have over \$700 million of capacity. Non-mark to market, limited mark to market, \$750 million of capacity as well. So very well positioned.

Where do we stand today? We can walk through some of these graphs. You can see the volumes. They're pretty significant in terms of how much correspondent locks and funded we've put through. I think what's important for everyone here to understand is that we are not gaining market share through price. We are gaining market share through what we think is best-in-class services, a white glove experience for our correspondents. One of the first things that we set out to do when we launched the correspondent is that we want to be flexible, we want to be commercial, we want to be easy to work with. And I think that has reaped dividends in terms of the origination experience.

Now, our pricing is competitive, but one thing that these originators get in the originator community, they also get certainty of execution. So they get Annaly, they get \$12.4 billion of capital at the end of Q3. They feel very good when they lock a loan that ultimately what stands behind that. And there's been a lot of cycles, whether it was COVID, whether it was 2022 and rates rose pretty quickly, where aggregators and private equity entities that we compete with didn't necessarily behave in the same way. So when you look at these graphs, it's not price and we feel very, very confident about that.

But in terms of just the actual lock volumes. We did \$4.4 billion in Q3, that's up over \$2 billion year-over-year. It's up 83%. When we do fundings, we did \$2.9 billion in Q3. That's up 140% year over year. If you look at the bottom left, in terms of the month of October, this was record volumes. We did \$1.8 billion of locks, \$1.4 billion of fundings. And normally October isn't the month at which you're setting records. So really what this shows you is that the maturation of the correspondent is still not necessarily at that final stage. We still think we're in growth mode. The month of November, we've already done \$1 billion dollars of locks. So we've now had 12 consecutive months of \$1 billion dollars plus in locks, expanded credit locks. The last chart, I think, to the right is also important because this shows the correspondents, 240 correspondents. If you look at some of the large Agency correspondents, they may have 600 to 800 correspondents. We're not necessarily looking to achieve that, but I think what this graph shows is that we've only added 70 correspondents over the last year. So there's a rigorous onboarding, there's a rigorous renewal process associated with being an approved Onslow Bay seller. We're not just out there casting this wide net and anyone who wants to do business with us can. So the growth in terms of the correspondent, our partners, it's been measured.

We have one more chart in terms of just the production and we'll look at Onslow Bay standing as a correspondent lender. This is through the first six months of the year. And I think what really jumps out on the page here is we are a top 10 correspondent lender. Over the first six months we did north of \$5 billion. And when we talk about correspondent, these are true loan level locks. We're not talking about bulk and we put it through correspondent. It's true best efforts locks. I think what's important about this is that we're only focusing on 4% to 5% of the market. So if you think of the total mortgage market, it's \$1.5 trillion to \$1.75 trillion, non-QM and DSCR is 4% to 5% of that. So it's a \$75-\$85 billion market. Even with that context, you're still one of the largest platforms. What does that mean? It means that we have optionality to the extent that we wanted to go into different areas of the market, we feel that we have the capabilities and the infrastructure to do that.

David made mention of securitization. If you look at the top, I think this is noteworthy in that, we are the largest issuer of expanded credit. We are the second largest issuer of expanded credit and prime jumbo,

but we are the seventh largest issuer worldwide. So if you look at ABS and MBS combined, and this was a year to date, we are the seventh largest issuer. And of the six that are ahead of us, three really focus on auto loan securitization, which is a commoditized product. There's a lot of volume, standardized structures.

The last, I'll just talk about in terms of the growth of securitization. This is a little outdated. We've actually done 20 deals this year. We just priced our latest NQM17 yesterday. We've done 20 deals, \$10.5 billion. We've been very prudent in terms of distributing this risk.

This shows how do we stack up relative to the peer set. We're telling you we're so large, we're doing all this volume. Over \$11 billion of loans in the last 12 months. 85% of those loans are expanded credit loans. I think that's noteworthy, because again, there's a scarcity value to these assets. It's 4% to 5% of origination. If you think of a sector like prime jumbo, traditionally that's been 15% to 20% of the market. So not only are you doing more volume than the entire peer set, you're doing it in a product that is actually difficult to scale.

The chart to the right shows our actual securitization volume. This is important because we're not running a mortgage banking business. We're not buying these loans with the intent to sell them and get some onetime gain on sale. That is not in the scope of the business. When you think of what we're securitizing, non-QM and DSCR, you're generating assets that are three to four year weighted average life assets. They are on your balance sheet for three to four years, you're going to earn mid-teen returns. If you were to buy prime jumbo loans and express and wanted a 15% return, the amount of capital that you're deploying, it's 2% to 3%. So within non-QM and DSCR, the same return per each \$100 of loans, you're deploying three to four times more capital than you would if you expressed this through a prime jumbo strategy.

The other one is residential transition loans. This is an area of the market that we haven't necessarily been active in. We've done a lot of work in it, but I'll say the same thing in terms of, those assets are six to 12 month weighted average life assets. So they pay off very quickly. The amount of recycling of that capital, trying to build that on your balance sheet is challenging. We'd much rather have assets that we have for the next three to four years. So sustainability of non-QM and DSCR, we think, is very important and very, very powerful.

So what are some of the key differentiated advantages that we have? The first slide here, we don't need to walk through it in too much of granular detail, but when anyone tells you they're earning 15%, you should make sure that you understand how you're getting to 15%. Very high level, we're buying loans call it 315 to 320 over SOFR swaps. That's an unleveraged spread. We're going to the securitization market, we're getting 88% advance. So that's seven turns of structural leverage that you're getting against your whole loan portfolio. The cost of funds is 155 to 160 basis points. So we're earning 160 basis points of NIM and seven turns of structural leverage at the inception of the securitization when we come to market. So that gives you an unleveraged spread of 900 over. From there, we use a modest amount of recourse leverage, less than one turn of balance sheet leverage, in this example it's 0.7x, and you're deploying 8 cents of capital per each dollar. So \$13, \$14 of asset generation and then \$8 of capital deployment. And that gets you to those mid-teens.

Why is that important? You look at the next slide. This is really the investible market across residential credit. One of the first things I'll say is that if you think of where corporate credit spreads are. Everyone knows that corporate credit spread, it's easy to source, it's easy to track. Corporate credit spreads are at the tightest levels they've been in the past 25 years. You'd have to go back to 1997, 1998, to an environment to where corporate credit spreads have sit post-election. They've widened out a little bit, but very tight. That has bled into structured finance. That has also bled into residential credit.

So when you look across the menu of options, what can we actually invest in as a levered credit investor? The market itself does not look that appealing. The majority of assets are 10% area or inside. Every asset that's listed here uses more recourse and balance sheet leverage than what we're producing. I'd also make mention of if you look at the gross issuance. That's total issuance, so that includes senior bonds. The actual amount of sub bonds that you'd be able to invest, it's 5-20% of the UPB that's here. So if you're a levered credit investor, high cost of capital, very challenging without an asset generation platform to be able to compete within this market.

Another key differentiated advantage, and David mentioned this as well, is our performance. Volume in and of itself is not a goal. There's not a single person within our firm that's paid on volume. It's a little challenging when you have salespeople to try to incentivize them when you can't pay them on volume, but we deal with that I guess. However, when you look at what we're ultimately producing, we're buying the right



loans as well. We're not just out there buying everything and leading with price. You're buying a pretty tight credit box.

But when you look across our performance, we think it's industry leading. In terms of the top 10 non-QM / DSCR providers, you have the lowest delinquencies. If you look across all issuers that have \$1 billion dollars of outstanding issuance, non-QM and DSCR, there's only two issuers that have lower delinquencies than us. When you look at what actual they've issued, it's a very nominal amount, but I think it's pretty powerful in terms of you're controlling all the asset acquisition. You have asset management sitting on top of this. We have a satellite office in Dallas, 35, 40 people, a number of them are focused on loss mitigation. So it's not just the credit strategy on the front end, it's also the back end as well. With that \$30 billion that we've securitized, we've only taken \$1 million dollars of realized losses. Of that \$1 million, about \$750,000 is actually deferrals. Deferrals is where there was a forbearance. You're actually giving somebody a deferral, you add it to the end of the loan, the borrower still owes that. So we actually think that that number could come down. Now these losses will go higher, but ultimately we've outperformed our initial model expectations, and I think that's what's important and that's what this is trying to show.

What does it mean in terms of how the market actually values us? What is the brand recognition that we get as OBX, as Onslow Bay Financial? And I think this slide really tries to show that. We've had 175 investors participate in our deals. Haven't seen many other people publish the number of investors that they have so I have nothing to compare it to, but I will say that there's a number of insurance companies, there's a number of asset managers who participate in our deals who do not participate in other shelves. They'll tell us that. Or if they're opening up non-QM for the first time, we are one of the first issuers that they're doing it with. Don't know where we stand, but I think we feel pretty good that we have a very deep sponsorship of our securitization.

To show you the brand recognition, we actually picked a time. The third week of October there was four non-QM deals out in the market. There was three deals plus our deal. When all was said and done and we priced those transactions, our deal priced 6 to 26 basis points tighter from a spread perspective relative to our peers. So if you took the midpoint of that and say on average we transact 15 basis points tighter, two year spread duration, that's 30 basis points in price. We are executing better than the company that's right across the street from us. Buying that same loan, going through the Onslow Bay name, our brand recognition, we're executing better.

What does that mean? You could do two different things. One, you could push that volume through, you can increase our pricing. So I can give a better price to our origination community than the guy next to me and still get the same ROEs, or you're creating value for shareholders. So of the \$8.2 billion of non-QM that we did this year, that 30 basis points is \$25 million in actual value that we think we've created with the brand itself.

What are the takeaways? In terms of the portfolio, we think it's very well positioned. Hard to replicate. You need an asset generation tool. We feel very good in terms of what we've put forth. Correspondent channel, unique advantages. So not only are we doing this volume, we control every aspect of loan acquisition to asset management and all our associated partners as well. Capital markets presence, we just walked through the example. So we are executing better than our peers for that same loan. So inherently strong competitive advantage there.

And then lastly is just we think we're maybe 75-80% of the way there in terms of the full maturation of the correspondent. So that's why you continue to see those growth in even non-seasonal months. We feel there's a lot of bandwidth, we feel very well positioned. David's mandate of increasing our Resi Credit to 30%, we have a lot of resources, and we think we're as well positioned as you could be heading into 2025.

With that, we're going to take a short five to 10 minute break and the next panel will be risk and liquidity management.



## Risk & Liquidity Management

Moderator

**Steve Campbell**, *President & Chief Operating Officer*

Panelists

**Serena Wolfe**, *Chief Financial Officer*

**Johanna Griffin**, *Chief Risk Officer*

**Pete Koukouras**, *Treasurer*

[Steve Campbell:](#)

Okay, great. Well thank you all for coming back. My name is Steve Campbell, I'm the President and Chief Operating Officer here at Annaly. I just want to reiterate David's comments earlier. We really appreciate you all being here. We know it takes a lot to take time out of your day and to hear our story, and we really like to tell our story, so really appreciate you all being here.

With this session, we're going to go a little different direction. Earlier you've heard from our investment leaders about our investment strategies, you've heard about capital allocation, you've heard about our macro policies or our macro outlook, excuse me. And I think the common thread that you've heard through a lot of these is how important financing is to our business and our financing advantages, and just given our business model, we just want to shift our attention in this session to the right hand side of the balance sheet. Talk about our financing strategy, and also talk about how we think about and manage risk. And we'll take a particular focus on liquidity risk.

So with that, excited to have this conversation with our panel. Most of you probably know from analyst calls and investor meetings and earnings calls, Serena Wolfe, our Chief Financial Officer, who's been in the seat for about five years now, so very interested to hear her perspectives and what she brings to the topic. In the middle, we have Johanna Griffin. Johanna is our Chief Risk Officer. She's been at the firm for about nine years now, has experience with other major Wall Street firms, so has brought a lot of best practices from across the street from a risk perspective to further institutionalize our risk function of Annaly. Again, very happy and welcome Johanna. And then we also have Pete Koukouras, our Treasurer. David introduced him earlier, I don't think I'm going to be able to do justice compared to his introduction, so I won't. But again, 20 years of experience at Annaly, managed the financing through multiple market environments, so brings a wealth of experience to the discussion. Again, very happy to have these three and excited for the conversation.

With that, we'll jump right in. Serena, I'll start with you. Maybe just to set the table, can you just talk at a very high level about our financing in general, the different options we have and maybe even starting basically with our capital structure and how we think about that?

[Serena Wolfe:](#)

Sure, absolutely. One of the themes I think you would've heard from the previous sessions is the importance of collaboration across the businesses. And I would say that the collaboration between treasury and the businesses, which is also something David highlighted in his presentation earlier, is very important, almost critical. Because we need to make sure that we are considering all of our available financing options in comparison to what the investment opportunities are, and therefore what's the best solution or product for us based on the risk-adjusted returns.

Now, typically, top of the house facilities don't make sense for our business model. And so what that means is we generally end up or predominantly have asset level financing. That would be repurchase agreements, warehouse facilities, and with regards to our Residential Credit business, term financing through the securitization shelf. However you do see on this slide, and we have used capital with structural leverage within our capital stack historically. And at this point in time, that really consists mostly or consists entirely, actually, of preferred equity. But we do continually measure the relationship between corporate unsecured debt and our warehouse facilities. And we would only look to diversify our capital structure leverage in periods where the relationship between warehouse and corporate unsecured debt is historically tight,

because at those point in times, that's where we believe that it's worth paying the premium for the non-mark to market more flexible corporate unsecured.

[Steve Campbell:](#)

Great. So you mentioned asset level financing. Maybe you can dive a little deeper into that, talk about some of the options we have on the asset level financing side.

[Serena Wolfe:](#)

I'm going to do a bit of a call back to, again to something David said earlier, which is one of Annaly's advantages, which is our size and scale. As the largest mortgage REIT in the US, our size and scale provides us access to a large number of counterparties. Really what that does is it gives us the ability to maximize our flexibility of our funding sources and solutions, I would say.

What does that mean? That means we can fund our securities business through our wholly-owned broker dealer Arcola, or we can do it through bilateral repo, agreements with the top financial institutions globally. And then on the credit side of the business, we've had significant success in expanding our warehouse capacity, which Mike and David also mentioned. And we've also added sub limits for new products and non-mark to market and committed capacity, which for our credit business, our Resi business specifically, that's critical, because we hold assets on our warehouse prior to obtaining that term financing in the securitization market.

[Steve Campbell:](#)

Great, great. And you mentioned Arcola, our wholly-owned broker dealer, and I know it's been mentioned a couple of times today. Can you expand upon why Arcola is important to our financing strategy?

[Serena Wolfe:](#)

We actually get this question quite a bit from investors and others, and really the origin of Arcola is back with the market volatility of the GFC. At that point in time, management determined that we needed to access funding in a way that would be more resilient during times of turmoil in the funding markets. The liquidity that's provided by FICC was really the natural choice. So in 2008 we established Arcola, and in 2009 we got approvals from FINRA and the SEC, and that marks the 15 year journey of having our wholly-owned broker dealer.

Now, what Arcola does and access through FICC really gives us ability to obtain liquidity through a different source or a different pool as an FICC member. And that's complementary to Annaly's bilateral repurchase agreements. That has a number of benefits, the largest of which, or the most obvious of which is liquidity, which I mentioned before, and with that liquidity, you generally get a lower cost of financing through tighter spreads, and you generally get tighter haircuts than comparison to our bilateral repurchase agreements.

We have historically operated funding anywhere between 15-30% of our overall book with Arcola. What we believe is that having these multiple funding options for our repurchase agreements or our securities really enables us to choose the best mix of funding sources for repo. And that's given any market, considering rate, haircut, availability of term, and other factors that we may consider. Additionally access to FICC provides us with a unique perspective on the financial markets and comprehensive insights into markets that we wouldn't otherwise get, because we see the flows of funds through FICC and what other market participants are doing. I believe that's unique and a benefit not to be left out.

Finally, I would say it gives us greater flexibility in times of portfolio shifts, so we can bring leverage up and we can bring leverage down and we can achieve that type of significant portfolio shift reasonably seamlessly and efficiently through the use of Arcola, through the FICC markets. And I would say while other REITs have established their own broker dealers since we established Arcola, I firmly believe it is a competitive advantage of ours for many of the reasons that I talked about. Meaning, it maximizes our funding options, it reduces our costs, and as mentioned earlier, it provides stickier funding during times of volatility.

[Steve Campbell:](#)

Great. Great. Thank you, Serena. Shifting I think to Pete now, we talk about the overall financing options and strategy. You as the Treasurer are in charge of executing on that strategy. Can you talk to us a little bit about how that strategy has evolved over the last few years? Obviously everyone's known of the, as David

called it, the hub on the securities repo for the Agency book, but maybe you can go into some more detail around the overall business and how that's evolved.

[Pete Koukouras:](#)

Sure. The evolution of our funding has shifted from predominantly securities financing for the Agency and non-Agency portfolio, to focus more on non-securities asset-backed financing as the firm has diversified capital to whole loans and to MSRs. Creating a financing framework provided us with a cerebral approach to right sizing the funding capacity for each of these respective businesses, while maintaining a diversified counterparty base and really providing us financing optionality.

[Steve Campbell:](#)

And you talk about a framework, maybe you can expand on that a little bit?

[Pete Koukouras:](#)

We'll just talk about how we're funding leading up to securitizations. As Mike mentioned earlier, the securitization market is roughly 90% of our GAAP financing for our loan business. But what I'm going to touch on is how do we fund those loans leading up to securitization? And what we wanted to ensure was our whole loan warehouse financing is going to be able to provide our loan book with interim financing at attractive market levels. We also want to make sure that we had committed and non mark-to-market capacity with all of our counterparties. And as Mike mentioned earlier, we have nine different counterparties that we're funding through and that we believe drives better economics for us, and also carve outs on sub limits for additional loan products that we may purchase or we currently own in a much smaller scale. So think about second liens and HELOCs as well. And I think lastly, putting excess overall capacity in place to provide runway for growth of these portfolios.

[Steve Campbell:](#)

Great, great. I think we have a slide that shows some of that growth of the portfolio. Obviously, Mike had touched earlier on the securitization activity. You mentioned 90% of the financing being on the securitization side. You see that number of \$10 billion or so this year alone on the Onslow Bay shelf. So that obviously demonstrates the activity on the securitization side. And we gave a graphical representation of some of the things that Pete's mentioned here as well regarding counterparties and size of our financing on the warehouse side. So thanks Pete. And maybe, I know that Ken talked about it and David talked about it a little bit as well, that holistic approach to financing and how we think about it from a top of the house, but are able to utilize the advantages of the Agency funding for some of the credit assets. Maybe you can talk a little bit about that.

[Pete Koukouras:](#)

I'll touch about that on the MSR portion of it. Financing for this portfolio is a bit more conservative in nature because of the WAC on the collateral, which is slightly north of 3.1%. And it also has a higher cost of financing relative to our other funding options. The traditional financing that we put in place have all been pre-pledged two-year minimum committed facilities with a broader set of counterparts. And by having this capacity to fund these businesses is essential, but we do use the Agency portfolio strategically to help bridge fund some of the purchases on the loan side and the MSR side. And striking a balance between firm-wide liquidity and our ability to maximize our total cost of financing. And the last point that I want to make as we continue to talk about how we utilize the Agency portfolio to achieve better economics for these other ancillary businesses, we do so while maintaining maximum bans on our Agency leverage. And I think that's a key point that I wanted to get across.

[Steve Campbell:](#)

Right. Great. Thanks, Pete. So we talked about financing, we talked about the strategy overall, you heard about the investment side earlier. I'd like to shift now to the risk side and how we think about and manage risk. So Johanna, can you just describe the risk function at a high level, and specifically how that interacts with both the financing and the investment functions?

[Johanna Griffin:](#)

Sure. And hello everyone. The risk team is an independent function at Annaly. So we have a completely separate reporting line away from the investment teams. As Serena alluded to, there's a lot of collaboration.

So while we're separate and independent, we do work side by side with all of the investment colleagues and of course Pete's team. The three main things I would say that the risk function provides are controls, analytics, and I think equally important probably is transparency. You've heard from a lot of the panelists earlier today, there's a lot going on. There's a lot of different risks that touch each part of the portfolio.

So just to give a flavor as to the type of things that the risk team is responsible for, we're involved in the formulation and the monitoring of limits, looking at counterparty exposures and the onboarding of that in addition to surveillance. We do stress testing, we do Value-at-Risk runs. We're looking at the funding levels and haircuts. And we also do liquidity reporting.

*[Steve Campbell:](#)*

Great. And can you dive down a little bit deeper? You mentioned that various categories of risk. Just go through what those categories are at a broad level and how you think about those.

*[Johanna Griffin:](#)*

Sure. Just one thing I'll also touch on with the framework is there's three lines of defense in the framework, which is something that's often talked about because it's widely used across different industries and organizations. And I think it's widely adopted because it's simple and clear and it crystallizes roles and responsibilities. So while everyone's responsible really for managing the risk, the first line of defense is going to be the investment teams because they're actually executing and understanding and putting on the risk and hedging it appropriately. The second line of defense is kind of where the risk function falls in. And so we're in charge of monitoring it, providing guidance on risk appetite, and also that would be a compliance function would fall in that second stream. And lastly, it would be operational risk, which also feeds up to the risk function, and that's business continuity, cyber risk, and just ensuring that there's proper operational controls across the firm.

But Steve, to answer specifically your question, the type of risks, and these have been spoken about earlier today, but I think we would put them into kind of these six broad categories. So on the market side we would have the interest rate risk, convexity, curve risk. We would also have spread, basis risks or anything inherent with a securitized product portfolio. We're always looking at hedges as well. On the credit side, we would have delinquencies, losses. We're looking at tail risk and layered risk and also geographical dispersion of our portfolio. Then we have of course liquidity and funding and counterparty. And then on the operational side, and lastly, regulatory.

*[Steve Campbell:](#)*

Great. And quickly before we move on to the next topic, you mentioned reporting, and reporting is a big part of what you do. It's a big part of what the management team and the investment leaders rely on that come from the risk side. So can you comment briefly on some of the reporting and the more relevant reporting that you do?

*[Johanna Griffin:](#)*

Sure. I think an example would probably help crystallize, because as I said before, you have a lot of activity. You have Mike Fania's team doing the loan acquisition, securitizations, and trading, and you have the Agency and MSR teams and Pete's funding desk. So there's a myriad of portfolio changes happening due to transaction activity, but also to the market every day. So how do we make sense out of it? First thing in the morning, I have a fantastic risk team, very strong skillset in that team, they're great. At 7:30 a comprehensive risk report will go out to a wide variety of people on the trading floor. It will have all the products, it will have products and the hedges. We can see what our interest rate risk is, our duration, our curve exposure, our spread exposure. But importantly, it also will highlight the changes to our risk profile due to trading and also explaining what components change due to market moves and different variables.

In addition to that, we have liquidity reporting. We do a lot of stress testing, Value-at-Risk runs, counterparty reports. And then we also report on a regular basis into the Board Risk Committee as well as our Asset and Liability Committee every quarter.

*[Steve Campbell:](#)*

Great. Great. Thank you. Johanna. So one of the areas you mentioned is liquidity risk. So just diving a little deeper into liquidity risk specifically. Pete, I want to bounce it back to you. In managing the financing portfolio, how do you think about managing it with an eye towards liquidity?

[Pete Koukouras:](#)

Yeah, Steve, I think high level the evolution of how we've managed the firm's liquidity is really done through a few different things. One, the diversity of our financing. Secondly, coming up with a leverage framework to provide size and scale for the Resi loan and MSR businesses. And lastly, it's really the art of reducing our cost of financing while maximizing our liquidity through our Agency portfolio, as we mentioned various times today.

[Steve Campbell:](#)

And maybe honing in on just the Resi and the MSR side, anything specific you mentioned about how those are managed with, again, and eye towards liquidity?

[Pete Koukouras:](#)

So quickly to touch on loans and MSRs and how we think about achieving liquidity through funding these businesses. I mentioned earlier about implementing a leverage framework, and really that consists of targeting minimum debt-to-equity ratios for each respective businesses, for the Resi business and the MSR business, because that's going to provide parameters and guardrails to ensure that they're self-funded at minimum levels. So if everybody can kind of think about having a minimum amount of skin in the game for these businesses.

We've also negotiated financing facilities with key components such as committed and non-mark to market features of these facilities, which are key to our overall liquidity as a firm. And I think lastly, it's procuring financing capacity, which really helps us maintain dry powder in times of market stress, and also provides us the funding capacity for future loans and MSRs in our pipelines. And just a note, I think Mike mentioned this number a bit earlier, we're currently only utilizing about a third of our overall financing capacity for these businesses, which is roughly \$5 billion.

[Steve Campbell:](#)

And how about the security side? How do you think about liquidity on the security side?

[Pete Koukouras:](#)

Yeah, so I'm going to break this up into two different components. We'll talk about Arcola Securities and then we'll kind of hop into Annaly bilateral funding. Serena's earlier remarks she gave outlined the history and the purpose of Arcola. So I'm just going to kind of hit on a couple of high-level points as well. It provides us with access to FICC and other direct cash participants outside of who Annaly deals with. It provides us with a lower cost of financing and a reduced haircut. It also helps us with liability management and flexibility. Flexibility meaning if we wanted to take Agency leverage up or Agency leverage down, we could do it very seamlessly through our broker dealer.

And I think the last point I wanted to bring up, which is very important for the firm, it's its operational efficiencies by actually having our in-house self-clearance settlements team under the Arcola umbrella. And not only do they handle the settlements and operations of the firm, but they also handle the firm's exposure and margining as well.

Now, kind of flipping over to the Annaly bilateral funding, here, we tend to take a top-down approach by utilizing the Agency portfolio as a funding placeholder. That really gives us that optionality again, and we believe a competitive advantage. And then we have a hierarchy of financing our non-Agency collateral because this is going to increase liquidity while reducing costs. And I guess lastly would be our ability to kind of flex the duration profile on our Agency securities portfolio depending on market liquidity and other dynamics as well as kind of where we are in a Fed hiking or cutting cycle.

[Steve Campbell:](#)

Okay, great. And a lot has been said about managing the portfolio through times of stress, and whether it be great stress like the financial crisis or taper tantrum or even what we saw in September of 2019 or some of the blips we see around quarter end. Can you talk a little bit about how you think about managing the book through times of stress?

[Pete Koukouras:](#)

Yeah, I think each one of those events have had a slightly different impact on funding markets. And obviously I think more people now are concerned with funding markets kind of reverting back to September 2019. But without me kind of going through all the causation and the minutiae of current funding markets around quarter ends and month ends and period dates and settlements and things of that nature, I think what I can say that has helped us manage liquidity through times of episodic events have really been our in-house experience, both on the Arcola side and in the Annaly side. We have decades of experience. A gentleman by the name of Jon Hunt runs our Arcola funding portfolio. He's been in the business for over 25 years. As you folks know, I've been at Annaly for 20 years. So I think that along with working closely with risk and other key business stakeholders and coming up with a proper funding framework and liquidity management goes a long way as well.

And lastly, and probably most importantly are our longstanding counterparty relationships. We deal with over 50 counterparties. I've known a lot of these folks for many years. So that, along with our partnerships, I think really pays off for the firm in spades during any event of market stress.

[Steve Campbell:](#)

Yeah, no, that's a great point. Well good. Well, so Pete, you talked about how you manage liquidity, how you manage financing with an eye towards liquidity. Johanna, you talked before about overall risk framework. You mentioned liquidity as well. Can you talk a little bit more about how you monitor liquidity specifically? And maybe even just start with how do you define liquidity for our purposes?

[Johanna Griffin:](#)

Yeah, so just to start, what is the goal? What are we trying to solve for? We want to have adequate amounts of liquidity to meet our operational needs, business obligations, and importantly to manage through a stressed market environment for a reasonable amount of time. Now, in terms of how we define our liquidity, we use readily available cash and highly liquid unencumbered assets where in our case, our Agency RMBS. And we try to operate above a minimum threshold of liquidity at the firm.

[Steve Campbell:](#)

And how do you think about sizing that minimum threshold?

[Johanna Griffin:](#)

So in order to size it, our portfolio is changing from day to day, but we go back in history and we look at various Value-at-Risk runs, and we have many of them that go over different time horizons and day counts, whether it's one month, two months, six months and what have you. And it has all of the data for an adverse market reaction. And we apply those to our portfolio. We look at what would be a minimum level of stress that we would like to manage through, and that's how we establish it. So it's really a stress measure that we look at to size liquidity of our portfolio.

[Steve Campbell:](#)

Okay, great. And you talk about measuring liquidity at a spot point in time, but you also project liquidity. Can you talk about some of the things that go into that projection as you look to project it?

[Johanna Griffin:](#)

Yes. So every day we actually produce, as we mentioned, Pete manages it and we report it and project it. So we look at our current or spot liquidity, and then we want to see how that profile is going to look over a 30- or 45-day period. And there's two main components to that projection. The first one are the known ones, and that's fairly straightforward to model. It's all our trading obligations, our buys, our sells, our settlements as we look out the horizon. And it's also because we're a mortgage portfolio, it's the monthly paydowns, P&I payments, the quarterly dividend when that comes up. So the second part are the unknowns, and that's the part that's more difficult to model, which is what about the market moves? What is the adverse market move that could happen over this period? What could happen to haircuts or funding levels? And that's the other piece that we try to overlay so that we can see on a daily basis what that looks like over a 30- or 45-day range.



[Steve Campbell:](#)

Great. Great. Thank you. Well, great. Well, I know we only have a few minutes left. I thought that Serena, maybe we'll bring it back to you to wrap up our thinking on some of these topics. Can you give us your final thoughts on this interplay between financing and risk and the investment function? And maybe circling back to some of your comments at the beginning about capital structure, how you think about our current capital structure and where we stand today.

[Serena Wolfe:](#)

Sure. I think David mentioned it today and I think we've been pretty consistent about our desire to maintain a conservative leverage profile and capital structure. And we feel really good about where we are from a leverage perspective today. At Q3 was 5.7x. And we believe that our current capital structure is well-positioned for the current environment. Taking on any additional structural leverage, as I mentioned before, whether it's incremental preferred or a new issue unsecured or convertible debt would really need to be done at a highly cost-efficient manner.

And as you can see on this slide, I think it really highlights and illustrates our conservative nature of our capital structure. You can see that the amount of our preferred and corporate debt as a percentage of our long-term capital is roughly 12%, which is about 15 percentage points below the average mortgage rate and squarely between our ten-year and five-year average of 11 and 12%, respectively. And we're also down from 13% to 12% pre-COVID. We were at 13% pre-COVID, so we're down to 12%. Whereas other mortgage REITs have seen their capital structure increase from 18% pre-COVID to 27% today. So I think that really shows that we've maintained our conservative profile despite these bouts of volatility that we've experienced.

[Steve Campbell:](#)

Okay, great. And what are your views on some of the points made earlier by Pete and Johanna just on our funding strategy in general and liquidity?

[Serena Wolfe:](#)

Yeah, for sure. Look, Steve, as you know, leverage and liquidity is something that is discussed frequently at the executive level. It's also discussed at the operating committee level and our ALCO. We regularly update our Board and its committees, particularly the Risk Committee, about our leverage and liquidity and our strategy with regards to it and how things are operating in the funding markets. Market risk and liquidity are considerations in our performance scorecards in determining both the firm and the executives' incentive compensation. So why do I say that? I say that to highlight to everybody that it's something we take very seriously and it's a significant focus of both the firm and executives.

Some of you sometimes ask us what keeps us up at night, and I would say it's the funding markets. But I do sleep well, I'm a very good sleeper, and that's mostly because of our strategy around diversification, our deep and long-term relationships with our counterparties, much of which Pete and Johanna have talked about, and also our highly effective controls around liquidity and risk management. I think we have a unique competitive advantage that Pete and some of our other business leaders have talked about with regards to our flexibility to move liquidity between our different businesses and to maintain a competitive cost of funds given our diversification strategy and our robust funding sources. We believe firmly that our funding portfolio is well-positioned to benefit from the Fed cutting cycle. And as we've discussed previously on earnings calls, we expect to see an improvement in NIM as we close out 2024. And the blended cost of our preferred reached its high water market the earlier part of this year. And so therefore we will continue to gradually see a decline in that cost as the rate cutting cycle continues.

[Steve Campbell:](#)

Great. Well, unfortunately or fortunately, that concludes our time. I think we could talk about this for hours, but we'll spare this group today on that. So thank you again to our panelists and thank you for this. Appreciate, appreciate your time.

## Political Landscape | Implications for Markets & Economic Policy

Moderator

**Tanya Rakpraja**, *Head of Corporate Responsibility & Government Relations*

Panelists

**Mark Zandi**, *Chief Economist, Moody's Analytics*

**Jim Parrott**, *Nonresident Fellow, Urban Institute Co-Owner, Parrott Ryan Advisors*

[Tanya Rakpraja:](#)

I'm Tanya Rakpraja, Head of Corporate Responsibility and Government Relations. So we have spent some time today hearing about Annaly's numerous advantages. One thing that sets Annaly apart that is very unique about Annaly is our relationships with policymakers. It is about the level of engagement that we have on topics that impact financial markets, our business, and you as investors. We've spent years building relationships across parties and across administrations, and we will continue to do that because it is important that we are at that table.

So to that end, we have with us today two significant voices on the economy and on housing. We have Mark Zandi, which many of you all know is the chief economist at Moody's and a prolific writer and speaker on the economy and economic policy. And we have Jim Parrott. Jim is a fellow at the Urban Institute. He served in the Obama Administration at the National Economic Council and is a trusted advisor working across the aisle on housing policy. Thank you both for joining us. We're thrilled that you're here.

[Mark Zandi:](#)

Thanks, Tanya.

[Tanya Rakpraja:](#)

Today we're going to cover the economy, politics – what we know and what we don't know – and housing. So let's set the stage. Mark, start us off on the state of the economy.

[Mark Zandi:](#)

Sure. And thanks Tanya and David and Annaly for the opportunity. And I'll have to say this seat is so comfortable. I could fall asleep.

[Jim Parrott:](#)

No, don't do that.

[Mark Zandi:](#)

But it's good to be with you. Just for sake of disclosure, I'm on the board of NGIC, a mortgage insurer, and PolicyMap, which is a software data visualization company. So I'm the chief lead director on that organization. You said the economy.

[Tanya Rakpraja:](#)

The economy.

[Mark Zandi:](#)

The economy, okay.

[Jim Parrott:](#)

Not foreign policy.



[Mark Zandi](#)

Yeah, right. Economy. I don't think this is hyperbole when I say in aggregate, the economy is about as good as I've ever seen it as a professional economist. I've been a professional economist for 35 years, and the economy is performing exceptionally, creating a lot of jobs across every industry.

Unemployment is low, it's 4%-ish, it's low across every demographic, age, ethnicity, educational attainment. It's low from coast to coast. The one blemish was inflation, and we can talk about that, but inflation is now back in the bottle. The only difference between where underlying inflation is currently and the Fed's 2% target is the cost of home ownership, owner's equivalent rent. And that's just related to measurement issues with lags between rents and how you measure it in prices. So I think we're effectively where the Fed wants inflation to be.

Stock market's at a record high. If you're one of the two-thirds of Americans that own their own home, you're happy because house prices are at record highs. If you look at household debt service, the percent of income going to servicing debt, household debt in aggregate, it's low and stable despite the run-up in interest rates. Households did a wonderful job locking in the previously record low interest rates. I do think we need to make a distinction between the aggregate and the parts. I think of the economy, the metaphor I have in my mind is it's this big elephant. If I look at the elephant in its entirety, as I described it, it looks very good. But depending on where you touch the elephant, you can get a different picture. And I do think there are differences in terms of how the economy is performing across the distribution of income. So folks, everyone in this room, top third of the distribution, fabulously well, things are going great. Folks in the middle part of the distribution, the middle third of the distribution, it's okay, it's not bad, it's not great, it's kind of typical.

Folks in the bottom third of the distribution, struggling. They don't have any savings, they don't own stock, they don't own their own home, they are paying higher rent. The high inflation of a couple three years ago, particularly because it was rent and groceries and to a lesser degree gasoline, things that people need to buy and are a large share of folks' budget, particularly in the lower part of the income distribution, they're paying a lot more for those things. And it seems like everybody's got a food item that they buy on a regular basis that they use as a litmus test for how well things are going.

So I teach a class at Wharton. I'm from Philly, it's my hometown. And I was talking to one of the kids and said, "How are you doing?" And he said, "Not so well." And I go, "What's going on?" And he goes, "Well, I'm paying a lot more for ramen noodles." So my niece, she's 22 years old, she lives in Philly, she's a social worker, same kind of conversation, took a little longer to get around to the bottom line with her than the Wharton student. But finally she said she's not happy. And I said, "Why?" And kombucha tea? Moldy tea, apparently. I've never had it, but she's paying a lot more for it.

And I think that this goes a long way to explaining the election results. I do think incumbents around the world had a pretty serious inflation headwind, and everyone's losing. And that explains to a large degree what... There's many other explanations I'm sure, but I'm an economist and everything that looks like the economy, to me, it feels like that was the biggest headwind for Vice President Harrison on her reelection bid.

But one more factoid, and then I'll stop. The folks in the top third of the distribution account for 55% of consumer spending on average through the business cycle. Right now it's higher than that, but on average. Folks in the middle third account for a pro rata share, a third. And the folks in the bottom third account for 15% of the spending.

So I don't think that's a good thing. I think this goes a long way to explaining our fractured politics and our social unease, and it's a real problem, but the economy can move forward if the top two

thirds of the distribution are doing their thing. And they are doing their thing. The American consumer writ large is driving the train, not only here in the United States but globally, because we are consuming a lot, everything we produce here and then a lot of stuff where everyone produces around the world. So unlike in the financial crisis or in the teeth of the pandemic, when China was leading the way, it's the American economy that's leading the way. This is an exceptional economy.

[Tanya Rakpraja:](#)

Is your baseline expectation that we have a soft landing?

[Mark Zandi:](#)

Yeah, we've soft landed, mission accomplished. Come on, let's end that conversation. We have soft landed. The Federal Reserve has engineered an economy that... And actually not only did we not have a recession, the economy has performed much better than anyone would've anticipated. By the way, I was one of the few folks that said no recession. I just want you to stick that in. And the reason is because I think economists misdiagnosed the inflation.

The inflation is demand and supply. But most economists thought it was mostly demand. And if you have too much demand, the way you get that back in is you have to raise interest rates a lot, crush demand to get inflation back in. But it was mostly supply. And now it feels like duh. But a year or two ago was not obvious to people that it was the pandemic and the Russian War, the impact on supply chains, labor markets. The price of a gallon of regular unleaded was going for five bucks, a record high in June of 2022, because of the Russian invasion and the sanctions on Russian oil. And as those shocks have faded and moved into the background, at least in terms of their economic fallout, we've been able to get inflation back in without the Fed having to jack up interest rates even more and pushing the economy in the recession.

And then we got a bit of luck. Two things, one is immigration. Immigration has created a great deal of cost to many communities across the country, but the one benefit is it added to labor supply at the same time, the Fed was working to cool things off in the labor market, and they got it without having to jack up rates more because the immigration that came in took a lot of pressure off labor markets and key sectors of the economy, construction trades, manufacturing, transportation, distribution, retailing, hospitality, elder care and child care.

And the other fortunate thing that happened was, and this goes to my optimism about the economy fundamentally, no matter what else is going on, is the productivity growth is picked up. Underlying productivity growth feels a lot higher today than it did a few years ago. Some of which may be temporary. There's a lot of debate in the economics community about this. So all the quitting that went on a couple three years ago, people shuffled into jobs that are better suited to their skills. That'll give you a one-time pop to productivity growth, and I think we're enjoying some of that. But take a look at business formation. It's just incredible the number of businesses that have been forming since the pandemic hit for lots of different reasons. And it's the new businesses that incorporate the new technologies.

At the end of the day, artificial intelligence is only going to have real impacts on the economy once we have businesses form and incorporate that technology and optimize around that new technology. When existing companies like a Moody's tries to adopt AI, it's painful. It's very difficult. It takes time to realize the benefits of it. In fact, initially it could hurt productivity for lots of different reasons, but it's when new businesses form. And new businesses are forming across every industry, across every corner of the country. And that gives me great confidence in our economic future despite all the storms that are headed our way.

[Tanya Rakpraja:](#)

I have to ask, what's the biggest risk to your baseline that we've reached a soft landing and we're in a good place?

[Mark Zandi:](#)

Well, there are many risks. I think the biggest storm headed our way is change in economic policy that's coming. This is President Trump and his policies. Let me preface this by saying three things. Am I taking too much time? Is this okay?

[Tanya Rakpraja:](#)

No, this is, yeah, the conversation.

[Mark Zandi:](#)

Because I can speak for three days. Jim's raring to go.

[Jim Parrott:](#)

No.

[Mark Zandi:](#)

All right, I won't be too long.

[Mark Zandi:](#)

Let me preface this by saying I think President Trump is going to do what he said he was going to do on the campaign trail. He's not going to do it to the degree he said it, but he's going to do it. That's the lesson from Trump term number one. You got to give him credit, he did exactly what he said he was going to do. Again, not to the degree, but he did it.

Second thing I'd say is he's going to do it fast. Unlike in his first term when he didn't expect to win, he didn't have any personnel in place, he didn't really know what was... I think it took him a year to get going. TCJA, Tax Cut and Job Act, was almost a year after he was inaugurated.

And third, I'm not surprised he won with Republican sweep actually. I mean, I put the same probability on that as Harris winning with a split Congress. I come from Philly. I live in the suburbs of Philly, which was ground zero. And when I did my run, I live on Laurel Circle, a mile circle, half Republican, half Democrat. And I count the lawn signs when I'm running and it was 50/50. So by my barometer, it should have been close. Although, I didn't account for the size of the signs. So it was kind of a missing variable, Trump signs were definitely much larger than the Harris signs by orders of magnitude. That was not a variable in my model, but I expected it to be close. I was surprised by how easily he won. He won. He won. He won every swing state and he won with a plurality of the vote. And he's off and running because he has a mandate. And we're going to get tariffs. I strongly recommend you go listen to the Economic Club of Chicago interview he did three, four weeks ago.

[Tanya Rakpraja:](#)

But Mark, in term one, he did successfully increase tariffs to an effective... What? ... 3% rate on tariffs, versus 1% prior, which is a lot lower than what he had initially proposed, what's been currently proposed.

[Mark Zandi:](#)

Right.

[Tanya Rakpraja:](#)

So I mean, right now, he's talking about a 10 or 20% across the board increase tariffs. What is actually, do you think, plausible and why is that?

[Mark Zandi:](#)

Well, we went from one to three. That's the effective tariff rate. If you told me we go from three to six or three to seven at the peak, I'd say that it's about right. That sounds about right to me.

China, for sure, he's going to double. The effective tariff rate on China is 20%, if you told, mid-40, I'd say that sounds about right. And then, he wants to scare the heebie-jeebies out of everybody, and hopefully, he doesn't have to raise tariffs as much on everybody else and gets what he wants, whatever that is. But I would say just double it at the peak. And the peak is probably going to be by the end of 2025 because he's going to get going here very early.

Second policy, and then, I'll wrap it all up. We are going to get deportations in my view, not 12 million undocumented people, that's just not happening. But directionally, if you told me half a million people are deported, that sounds about right to me. I think he was reporting 350,000 people per annum in his first term.

Three, we are going to get tax cuts. Now, some of that's going to be unfunded. He's going to pay for some of that with higher tariff revenue, but it's going to add to deficits and debt.

And three, there is going to be some fed capture, in my view, not through firing Jay Powell, that's not happening, especially in a declining rate environment, they're all on the same page, but by appointments, the people he is going to appoint are going to be people that are more compliant with his perspective on things.

You add all of that up, that leads to some combination of higher inflation, higher interest rates and diminished growth. And I'm not the only one thinking this, this is exactly what the markets are saying. Go take a look at the ten-year Treasury yield, it was 3.6% two months ago when Harris was at the peak of her popularity and leading in the polls in the betting markets. As she started to lose and Trump started to win, that's when interest rates started to rise, we're now at 4.4. That 80 basis points, half of that is inflation expectations. Just go look at five-year break-evens, are up by 40 basis points, last I look.

The rest of it is the term premier, and that goes to deficits, debt and inflation uncertainty. So the stock market has gone up, but not a lot. And that goes to, I'm giving you a tax cut, that's the check to a shareholder. I mean, same PA, multiply a higher tax earnings, I get a higher share price. It goes to last regulation, deregulation. So financial stocks are up, utility stocks are up, technology stocks are up. And it goes to more M&A, we're going to get more M&A. So cap one, discover that's happened.

*[Tanya Rakpraja:](#)*

Right. So the stock markets and credit markets have had an undecidedly or a decidedly positive reaction to a Trump administration and Republican Congress. Jim, how do you think the Trump administration in their second term is going to be different from the first?

*[Jim Parrott:](#)*

Mark alluded this a little bit. I think there were three or four lessons they learned from the last go-round that they will change their course this time around on the process side. So last time around, as Mark said, it took the better part of a year for them to get their folks, their senior teams in place in the key agencies. Took them a while to figure out who they wanted to put in place, took them a while to get them through vetting, took them a while to then get confirmed. So they lost the better part of a year before they actually had much policy momentum.

Second, once those political folks got into place, the career folks around them sort of ran circles around them more or less, and tended to slow walk or push back a lot of the more extreme policy prescriptions that the political folks wanted to implement. So that stymied him a bit over the first really two years of that term.

And then lastly, and most frustratingly for Trump, his own political people pushed back on some of the more extreme policies that he wanted to implement when they had misgivings about them. So there was this inefficiency between what Trump wanted to happen and what he could make happen through the key agencies. I think he'll try to solve that this time around. So first, he'll try to

push through a much bigger slate really quickly, which may or may not work given the folks that he's trying to make a swing at so far.

But second, you'll see a purge of some kind, of senior level career folks at a lot of the key agencies, especially the State Department, but also, some other buildings.

And then third, we'll see many more loyalists this time around as political appointees, especially heading the agencies than we saw last time. Last time you had a mix, some institutionalists, some pragmatists, some traditional Republican types that had a lot of knowledge about the space in which they were being asked to lead. That often created a headwind for what Trump himself wanted to get done. I think this time around, you're much more likely to see the kind of folks you've seen nominated so far, people that are much more inclined to just push on whatever agenda Trump wants to see.

I think if you translate or you take that, and then, you shift to policy, it's worth remembering that there's a tension in Trump's general rhetoric, historically, with a lot of more traditional Republican takes on things. If you go back historically, a lot of them, but two of them are worth pointing out in particular. There's a tension between Trump's sort of economic populism, which you hear him sort lean into a fair amount on the campaign trail. There's also a tension and the sort of traditional Republican economic policy that we've seen up until Trump.

There's also a tension between a kind of dogmatism that Trump is inclined towards the sort of, "Damn the torpedoes, I'm going ahead with whatever X is," that, and a more market-sensitive, pragmatic sort of take on things that we would've gotten from the Bushes and Romney and folks like that.

The way that those tensions played out in the first Trump administration was really by different sort of competing factions in the Trump administration that really represented those different extremes. So for every Stephen Mnuchin, you'd have a Peter Navarro, for every Mark Calabria in Housing Finance, you'd have a Brian Montgomery, he's a more pragmatic, market-friendly kind of guy with FHA.

And so as those differing worldviews came up against each other when they with play through a policy, you'd wind up with outcomes that were kind of somewhere between the two extremes. I think this time around you're much less likely to get as strong a mix of institutionalists, pragmatists traditional Republicans, at least in some spaces. And as a result, you're going to see policy land much more towards the economic populace into the spectrum, much more towards the dogmatic end of the spectrum. And I think you'll see, how far towards that end of the spectrum they land will depend on the remaining sort of key personnel spots, especially Treasury and the NEC.

We can get into Congress in a second, but over the next six months when they get into trade policy debates, when they get into the tax policy, tax negotiations with the expiration of Trump's tax cuts, you'll really begin to see the tension between Trump's drive towards the sort of populist instincts and the natural pushback that you would've historically gotten from Republican concern about tariffs, concern about deficit spending.

Like in another era, the kinds of deficit spending that's going to be on the table next year would've seemed absolutely bananas to Republican-controlled Congress. It'll be interesting to see who in the Congress would stand up against Trump's interest in pushing heavy deficit spending to pay for tax cuts this time around. I'm guessing won't be nearly as strong as what we would have seen, say 10, 15 years ago.

And then the last piece of this, which is a bit of a caveat to all this is even though I'm skeptical that Congress provides a big check against some of Trump's instincts, I do think the markets are going to provide a bit of a check. I think he is more concerned about market impacts than he is about other versions of social responses to his more extreme positions.

The opening bid that he makes for extending the tax cuts and expanding them and all the rest freaks the bond market out. I think that'll matter. I think it's the sort of thing that will act as a bit of a check against what he'd like to do, whoever's in the Treasury job, whoever's in the NEC job. So I'm a little more hopeful in the economic sphere about moderation in other non-economic spheres because there isn't a similar sort of check there like we have in the market.

*[Tanya Rakpraja:](#)*

Yeah. I mean, President-elect Trump, during his first term, did pivot on policies that people thought could impact the economy, impact, damage investor sentiment. And so, I would expect that he would also have that willingness to pivot if there is a market reaction or if business leader or company feedback on policies that it could be damaging. And what about Congress? What do you expect from Congress?

*[Jim Parrott:](#)*

Yeah. As we suggested, I think it'll be, initially, a huge focus on tariffs and taxes I think will be the first two big items these guys take up. The Trump tax cuts expire at the end of next year and the sheer magnitude of what's set to expire, both on the corporate side and on the individual side, is going to bring Democrats to the table. There's a lot of stuff on the individual side in particular that's set to expire that Democrats wouldn't want to see expire, the child tax credit, for instance. So I think you're going to be forced into a negotiation that sort of has to succeed to most of the parties around the table.

It'll be a gigantically challenging math problem. Trump's already said he wants to see all of the tax cuts extended, that would cost about \$4.5 trillion. He's also added to that, eliminating taxes for tips, eliminating taxes for overtime, eliminating taxes for social security, decreasing the corporate tax rate from 21%, where it is now, which is already lower under the Trump tax cuts, to 15%. That is just enormous in its expense.

And then, he's also said, over the last three or four years, but also during the campaign, that messing with social security's off the table, messing with Medicare and Medicaid's off the table. So the things that you're supposed to have to mess with to make any of this math work is all off the table. And so, when you actually look at the charts of where expense comes from and you take all the things that Trump said off the table like defense, there's not much left in the pie to cut from. And so, if you're really looking at a \$6 trillion price tag or whatever the number would be, there's not nearly enough money left on the table to cover that.

So the tax debate will be interesting and I think, all-consuming, but if we're going to segue into housing, may be a hopeful opening for housing policy because I think a lot of that may be tax side in its focus. So there may be a silver lining in the big tax debate, I think.

And then, tariffs, as Mark said, I think, it's inevitable, that's something they're going to focus on. Whether Congress wants to focus on it or not, Trump will make them focus on it. I think for it to have any sort of permanence, he's going to want it to be a legislative move, not just an administrative move. So it feels like that's something that's going to consume a ton of their time next year too.

*[Tanya Rakpraja:](#)*

And what do you think is achievable on the tariff side?

*[Jim Parrott:](#)*

Me? Oh, God! I think Mark's right. We were talking about this yesterday. I think Trump will be trying to achieve as much signaling benefit as he can without blowing the economy up. And I think he'll, especially if he's got a pragmatic Treasury secretary, if it's Warsh or Bessent or one of these guys whose name is being kicked around, who's not all that excited about tariffs, just philosophically. I

think you're likely to see a big bazooka aimed at China initially, and then, some other players caught in the crossfire, Vietnam, some others that he's mentioned already.

My guess is he goes big on a couple of opening bids and tariffs just to scare the bejesus out of everybody and make it clear that he's not fooling around. And then, there'll be a pause and you wait to see what the effect of those moves is. And then, assuming that he can claim some sort of victory, maybe there isn't a phase two or a phase three.

But if you listen to his key economic validator types like Bessent who are out there talking on his behalf, they all talk in terms of targeted tariffs, they all talk in terms of phased-in tariffs, and I think that's what they mean. I think they mean aim a big bazooka at one player, maybe two, maybe three early, wait and see how that plays. Pray to God you can claim victory over something. Trump's happy, and then, hit pause, I think is probably the base case.

[Tanya Rakpraja:](#)

Great. So let's turn to the housing market. What is the housing outlook, Mark?

[Mark Zandi:](#)

Well, it depends on which part of the housing market you're looking at. I'll start with what's good and then go to what's not so good. What's good is house prices and mortgage credit quality. I mean, house prices have been steadily rising despite the run-up in interest rates, especially if I look at the FHFA House Price series for Fannie and Freddie, house prices related to Fannie and Freddie loans. It just barely paused when the Fed started jacking up rates and continues to rise. It's up 50% since the pandemic four years ago. It's up 100%, I think on the nose, 10 years ago.

And that just goes to the lack of supply. There's just no supply, both in the existing market because of interest rate lock and in the new home market, we've got very low vacancy rates for home ownership and for the affordable part of the rental market. And so, got high house prices, continue to rise very strongly. There's a boatload of equity out there. Mortgage credit quality... And now, I'm the head of the risk committee at MGI, I don't see any issues at all. It's like just shockingly good, how good it is. So that's the good.

Kind of the okay is the home building. The home building, that's the supply side of the market. It is, in terms of completions, at a very high level, that goes in part to the fact that during the pandemic builders couldn't build because of the supply chain issues and the labor market issues. And so, you saw a lot of building get bottled up under construction. The number of units under construction hit a record high about a year ago, they're starting to come in now, but still at a very high level.

And I think builders, they're showing more willingness to be flexible on effective price through buy-down. So they are new home sales have held up much better than existing. They're selling units because they're willing to cut price effectively. And so, we're seeing continued good construction. And they're the fundamental tailwinds, are very positive because we have a very severe shortage. And Jim and I have been doing a lot of work in this area and we've got a study coming out shortly on this.

[Jim Parrott:](#)

We've said that for two months.

[Mark Zandi:](#)

I know, I'm sorry. I'm sorry. It's complicated.

[Jim Parrott:](#)

It's going to be true eventually.



[Mark Zandi:](#)

Because we're looking at the supply shortfall by Census Tract, so that gets really pretty difficult, but that's a tailwind to building going forward for the foreseeable future.

Obviously, the bad is transactions and origination volume. I mean, because of the interest rate lock, people aren't moving. And now, we got mortgage rates back up to 7%, that's a killer. When rates were down closer to 6% a couple months ago, it almost felt like we were going to get a 5% handle. And I go, "Oh, this is..." Because I think once we get a 5% handle plus all the pent-up life that's out there, we're going to get more supply, more transactions. But no, we went right back. And by the way, there's no going back here for a while, going back to policy, and you know what that means for inflation and real interest rates for term premium.

And also, now we're talking about GSE reform, and there may be some evidence that GSE reform is getting into people's thinking, and that, certainly, will have an impact on mortgage spreads and mortgage rates.

So it feels like we're going to be stuck in a 7% world for a while, and that's just a no-go, particularly because house prices continue to move up. Life is building, people are in homes that aren't suited to their needs, children, job change, death, divorce. So it's building and you can feel the pent-up demand sitting there, but it won't be unleashed until we get mortgage rates back in. And I think that's going to be for a while. And then, if you don't get transactions, because existing home sales are as low as they've been in the teeth of the pandemic or in the height of the financial crisis, it's amazing how low they are. You're not going to get origination volume either. So that's, I want to say the good, not the bad, the good, the okay and the ugly, the good, the okay and the ugly. That's how I think about the housing market.

[Tanya Rakpraja:](#)

So how does that weigh on the economy if we're stuck in this environment for a while? Because mortgage rates aren't going to decline materially and interest rates are pricing current levels into the future. How does that weigh on the economy? What does that mean for the economy?

[Mark Zandi:](#)

Well, when you think about prices and you think about building and you think about transactions, the thing that matters most for the economy is building, because that's jobs. That's a lot of jobs. It's not just the building, it's everything that goes into the home, manufacturing, transportation, distribution, whole shoot in that. So that's a positive for the economy, a reasonably good positive.

Second is prices, that goes to wealth effects. I was alluding to that earlier, I am a homeowner, my home is worth a lot more. I feel more confident and I save less than otherwise would be the case. In fact, we're the only country on the planet where our saving rates are actually down, everywhere on the planet, they're up because people are scared to death. And you don't see these kinds of positive wealth effects. Here in the United States, wealth effects are real and people are out spending. Your home equity borrowing still very low by any standard, it's picking up. That's the only area of consumer credit that's seeing any kind of growth whatsoever because people are tapping into that equity.

Transactions, that's the least important thing because if you just look at it in terms of jobs or in terms of GDP, it's what the real estate brokers are doing. And I don't want to minimize it, but in the grand economic scheme of things, that's a small potato. It's really the home building and the wealth effects that matter most. So right now, housing has been an add, it might become less of an add because you're starting to see home building, particularly on the rental side, at the high end of the rental market, because that's where you are seeing some overbuilding and rents are weak. We are starting to see that roll over. And credit's getting a little bit more difficult if you want to build a multifamily tower. Where are we? In New York? Sorry, I've been traveling a lot. So in New York or Philly or Chicago or San Francisco, but other than that, that's where the juice is.



[Jim Parrott:](#)

Wait till we deport half the labor force and we'll see how the supply chain works out.

[Mark Zandi:](#)

What's that?

[Jim Parrott:](#)

So wait till we deport half the labor force-

[Mark Zandi:](#)

Yeah, make that point. That's a great point. That's a great point.

[Tanya Rakpraja:](#)

So what do you expect the Trump administration's focus on housing will be, Jim?

[Jim Parrott:](#)

Yeah, they didn't lean into this much in the campaign. They were forced to talk about it a little bit. And he would mention it only indirectly by talking about other stuff that he was going to do and how it would help the housing market. And he, somewhat laughably, most frequently, leaned into how deporting 10, 15, 20 million people, depending on the speech, was going to soften demand and thus bring down home prices, but as I was just sort of applying a second ago, that roughly, depending which state you're in, somewhere between 20 and 50% of the labor force in the construction industry comes from non-native born folks, i.e., immigrants. So if you begin deporting hundreds of thousands, much less seven figures of folks, you're going to create a pretty significant dislocation in the supply chain, which will lead to even more of a supply shortfall that we've had historically, which is going to lead even higher home prices and more of an affordability challenge. So that's going to be a mess.

But as far as intentional housing policy, I think GSE reform is where they're going to. I don't think they're going to focus much on the supply stuff that we've been talking about, Congress I think probably will, I think once we get into the tax debate, I think because much of the supply side support that Congress could usefully provide is tax side support, increased li tech, maybe some sort of tax benefit for building entry level homes, opportunity zones, that kind of thing.

I do think you'll see those sorts of things, make it into the mix, make it into the tax debate. So I'm mildly optimistic that we see Congress take this up, but I think as far as the Trump administration goes, on housing, it'll be Fannie and Freddie and driven mainly out of FHFA over the next year. I can't imagine the focus on it outside of FHFA much this year because in 2025, there's so much else to deal with. I think it'll be a 2026, 2027 sort of thing where Treasury finally gets engaged, you begin to see discussion about their exit the way that people should begin to pay attention to.

[Tanya Rakpraja:](#)

Yeah. So FHFA and the GSEs-

[Mark Zandi:](#)

I thought we lost you actually-

[Jim Parrott:](#)

Like, "That's it." She dropped the mic.

[Mark Zandi:](#)

"I'm done."

[Tanya Rakpraja:](#)

There has been a lot of coverage on FHFA and the GSEs. What do you see them being able to accomplish there?

[Jim Parrott:](#)

Yeah, I think it's going to be an interesting mess. So they are absolutely dead set on at least attempting to get them out. And they went pretty far down the field, as it were, last time in the Trump administration. And Calabria was running the FHFA, the regulator for Fannie and Freddie, was pretty anxious to close the deal. Mnuchin was uncomfortable with this sort of risk of disruption that the path out Calabria had in mind, or at least the pace at which he had the path in mind made Mnuchin uncomfortable so they couldn't get over the finish line. I think they'll pick up, roughly, where they left off.

I do think there are two sets of challenges that make me skeptical they're going to be able to pull it off. One is just the practical, legal economic challenges that go into getting them out. I mean, right now, the taxpayers got a quarter of a trillion dollar interest in the GSEs, depending on how you sort of count their various positions. You're going to have to write that down, more or less, in order to get them out. And writing down a quarter of a trillion dollar interest in the taxpayers, like not a politically insignificant thing. There's even some sort of legal impediment to that. So they've got issues like that they're going to have to work through, getting them in position for a capital raise, getting investors interested in a model that may be somewhat constrained for ideological reasons. So there are all kinds of logistical, legal issues in the thick... It will be hard.

But I think the biggest issue by a long shot is what they say and do about the government support beyond the PSPAs. So the way to think about the layers of support, now you got capital, let's just assume, theoretically, they get capital up to whatever the regulatory levels are supposed to be. You've got the PSPAs, which are the explicit backstop that Treasury provides for the GSEs, which is a quarter of a trillion dollars, a big number. And then, you've got, possibly, the implicit government guarantee beyond that.

And by that, I mean, if you blow through the first two, is the government going to bail them out or not? And the market-wide view before conservatorship last time around was, of course, they're going to bail them out. And so, that market assumption that the GSEs are going to be bailed out as what we all call the implicit guarantee, and that's what gave them a relatively high rating, it's what allowed the Fed to buy their MBS. The Fed can only buy the MBS of a, quote-unquote, "government Agency." They were able to rationalize the GSEs as a government Agency because of this implicit guarantee. So a whole lot of the GSE model worked well because of this assumption about an implicit guarantee.

So I mention all this because if you fast-forward into, say 2026, let's say they're on the five yard line, they're going to push it in or whatnot, we'll hear a lot of talk about whether the government would bail them out if they were to blow through all these layers of capital. And I think a lot of folks in this town just assume, "Well, of course, they bailed them out last time, why would it be any different this time?" I think there'll be a lot of ideological pressure in the administration and from conservatives outside of the administration to say, "Oh, no, no, no, no, no, if these jokers blow up again, it's not on the taxpayer, it's going to be on the shareholders." And there'll be a lot of pressure for them to say that, "We're not going down the moral hazard path again, yada, yada, yada."

So if we do hear that coming from these guys and there is a reason to actually believe them when they say this, that there is a meaningful doubt, the government wouldn't bail them out, the ripple effects of that are significant, they get downgraded by rating agencies, the Fed probably can't buy their MBS anymore. The whole model doesn't work quite as well as it would before. So I think that's going to be a pretty binding constraint for them.

And so, the question is, do they give in to market reality and sort of give a wink and a nod of your implicit guarantee? Or do they listen to the more ideologically charged folks in and out of the administration and either try to blow them out without the implicit guarantee, which I think is pretty unlikely, or just frankly, stop and blame Congress for not doing what they're supposed to be doing? If I had to guess, that's probably what they'll do.

[Tanya Rakpraja:](#)

Yeah.

[Jim Parrott:](#)

I say that with all this confidence, but you'll hear a lot of rhetoric from these guys over the next couple of years that, "We've got a mandate to bring them out. It's crazy to have them in government this long. It's irresponsible," all that. All I'm saying is it's really hard to get them out. And while getting from your 20 yard line to your opponent's five yard line takes a lot of yardage, it's going to be that last five yards that's going to be really tough.

[Tanya Rakpraja:](#)

Yep. And politicians of every stripe understand the importance of a liquid and a stable housing market and mortgage market in the end, right? So it'll be really hard to bring them out for all the reasons you've mentioned. What they'll likely be very successful at is reducing the GSE footprint, right?

[Jim Parrott:](#)

Yeah.

[Tanya Rakpraja:](#)

We saw FHFA director, Calabria, do this by tightening the credit box, raising pricing to juice up ROE's and bring in private capital, putting caps on second homes and investor properties, for example. So that we do expect to see.

[Jim Parrott:](#)

And I'm mildly optimistic. I hate the idea of bringing them out, for all kinds of reasons, at least in the way they would bring them out. So I'm mildly optimistic that's not going to happen, partly because I think the markets could provide a check on all this. And so, when you get to the five yard line and the market begins to pay attention to, not just the fact they're coming out, but the terms on which they're going to come out, and begins to say, "Whoa, whoa, whoa, we didn't sign up for that." And you've got all these big, foreign investors that are not willing to buy the MBS unless they've got a clear government backstop, blah, blah, blah. I think, at that point, Trump, who couldn't care less about any of this, will begin to pay attention and say, "Whoa, wait a minute. I didn't sign up for that." So I think in the Trump administration we get, even if it's just the most bananas version that we might be at risk of having, I think the market reality and his sensitivity to market reality may ultimately be the sort of grown up in the room that keeps us from going down that path.

[Tanya Rakpraja:](#)

Yeah, right. So ending on that note, let's do a quick lightning round. What are you keeping an eye on?

[Mark Zandi:](#)

That to me?

[Tanya Rakpraja:](#)

Yes.

[Mark Zandi:](#)

I'm really looking at the Eagles and wondering whether they're going to make it to the Super-

[Mark Zandi:](#)

I'll just mention two things that I'm watching very carefully. One is unemployment insurance claims because that's a window into layoffs and ultimately whether consumers continue to spend. I mean, nothing will cause consumers to pull back more than if layoffs start to pick up. So that's a very real-time barometer of the health of the labor market, and ultimately I think the broader economy.

The second thing I'm watching is the mortgage rate, because that matters to a lot of Americans and that's key to the housing market. And that's a window into how President Trump's policies-

[Tanya Rakpraja:](#)

This is supposed to be a quick lightning round.

[Mark Zandi:](#)

President Trump's policies are affecting the economy via all those other policies, including GSE reform. Because once it becomes clear, the GSE reform is more likely, it's going to show up in that mortgage rate very quickly.

[Tanya Rakpraja:](#)

Jim?

[Jim Parrott:](#)

Personnel, personnel, personnel. It'll define whether we have a slightly disruptive Trump administration or really disruptive Trump administration, and especially on economic stuff. So who's at Treasury? Who's at NEC? Has he gotten this sort of populist zaniness out of a system with all the non-economic stuff? God, I hope so. Are we're going to go back to something a little more normal on the economic side? So personnel for me for sure.

[Tanya Rakpraja:](#)

I'll have to say inflation because of the impact on consumer spending and balance sheet, and the labor market. So what's top of mind as it comes to opportunities the next year?

[Mark Zandi:](#)

Opportunities...

[Tanya Rakpraja:](#)

Quick.

[Mark Zandi:](#)

Jim, you try that first. I'm the economist. I'm always looking on the dark side of things.

[Jim Parrott:](#)

I think in areas where deregulation can help, you'll have a very open audience. I think with this Congress, this coming Congress, I think tax side help on housing will be there if you could frame it right. And I think the giant sums of money we're talking about on the tax side will open the door for a pretty meaningful supply side help and housing, I think, as an opportunity.

[Mark Zandi:](#)

I'm going to pass. Look at valuations in the stock market, look at crypto, look at corporate credit spreads, look at valuations across the market. Look at the fragility of the bond market generally. I don't know, it feels, when you say opportunity, I'm thinking of it from the prism of an investor. All I

know is my 93-year-old grandmother-in-law continues to ask me, her CDs roll over, "What do I do with that money?" And the answer I give her is, "I don't know. I don't know." So I don't know about opportunity in that context. I think we need to see some general leveling of valuations across markets.

[Tanya Rakpraja:](#)

For me, not from the investor's perspective, but as an American, I'd love to see less political division in this country.

[Mark Zandi:](#)

Oh, good luck with that.

[Tanya Rakpraja:](#)

And my last question, so your most outlandish prediction does not have to do with your job or your work.

[Jim Parrott:](#)

Oh wow.

[Mark Zandi:](#)

Most outlandish prediction?

[Jim Parrott:](#)

Do we have to believe in it?

[Mark Zandi:](#)

I know what mine is. I got a good one. My son who's getting married in April, says his new wife is pregnant. That would be good.

[Jim Parrott:](#)

Is this being videoed?

[Mark Zandi:](#)

It's all about me. It's all about me.

[Jim Parrott:](#)

Yeah, man, I don't know. Carolina makes a final four. Nothing to do with my job. What do you say?

[Tanya Rakpraja:](#)

I say LSU loses their next two games. Brian Kelly gets fired by LSU and they pay the 60 million contract to get them out.

[Jim Parrott:](#)

Whoa, you thought about this.

[Tanya Rakpraja:](#)

All right, so we will end on that note. There is a lot of themes throughout this conversation. I'd say one of the takeaways I had is that it's important to be nimble, it's important to be adaptive, it's important to be engaged. And these are all hallmarks of Annaly. So give us a few minutes. We are going to set up the stage for the Q&A that follows and we'll be back.

## Q&A

**David Finkelstein**, *Chief Executive Officer & Chief Investment Officer*

**Steve Campbell**, *President & Chief Operating Officer*

**Serena Wolfe**, *Chief Financial Officer*

**Mike Fania**, *Deputy Chief Investment Officer & Head of Residential Credit*

**V.S. Srinivasan**, *Head of Agency*

**Ken Adler**, *Head of MSR*

[David Finkelstein:](#)

All right everybody, hopefully you all found the afternoon enlightening and now we're going to open it up to a little bit of Q&A and we have Sean and Danielle with microphones. And then for those who are on the video feed, you can type questions in and we'll try and get to them as well. So let's get started. Who's up?

[Crispin Love:](#)

Thank you Crispin Love from Piper Sandler for David or anyone that the last segment kind of focused a lot on, GSE reform, so just curious on your views there, privatization of Ginnie/Fannie and kind of probability and then how you think kind of broader kind impacts to Agency and the Agency market as a whole.

[David Finkelstein:](#)

Yeah, great question. So to Mark's point about mortgage spreads, as we've looked over the last couple of weeks with Trump's election win, one of the barometers we look at is Ginnie/Fannie swaps to see if there's anything specific to Fannie and Freddie. And we haven't seen much movement in Ginnie/Fannie swaps. So we're reasonably comforted by the market's calmness associated with GSE reform. And look, ultimately we get it, the Trump 1.0 ended with an attempt to release the GSEs. They had bankers and they were ultimately going to raise capital and our expectation is that they will get back on that path. It is, to Jim's point, it's not an easy process. You have the \$350 billion that's owed to Treasury and you have a really precarious political environment to release the GSEs. And our hope is that they will do it, or attempt to do it, in a very methodical fashion.

Now there's a couple of points to note. Number one is you will have a significant amount of capital in the GSEs when they are released. You're going to have an regulatory oversight that's going to necessitate that they maintain healthy balance sheets. And you have this process or this distribution of credit risk called credit risk transfer, which is a fully developed market. And our expectation is that it will certainly continue. And so ultimately when you do have the GSEs released, and we don't think it's necessarily a bad thing at all, if they do it responsibly, you're going to have pretty healthy institutions that we think will maintain the support of global investors, number one.

And number two, if you look back to pre-financial crisis, you did have this notion of an implicit guarantee, but certainly wasn't explicit and the market operated very well, spreads were tighter than they are today. And the global sponsorship was more significant candidly than it was today with Japanese banks and China and others. And the GSEs were obviously big supporters. We don't expect retained portfolios to grow, but nevertheless that end state if it materializes is not necessarily a bad thing. And if it suggests spreads are a little bit wider that's okay.

And another point to note is they will much be much more profit focused, which means that we in our residential credit business are much more competitive with the GSEs and it'll provide more opportunities to expand that platform further. So long story short, nothing's going to happen for quite some time. We'll hear a lot about it there. There's good things and there's some things to be concerned about and we will manage it responsibly. A good question, Crispin.

[Doug Harter:](#)

So Mike, you showed that about 60% of the residential credit book is OBX created. Kind of where does that number go over the next one, three years? Does that ultimately get to a hundred percent? How does that play out?

[Mike Fania:](#)

Yeah, I think a lot of it depends on market opportunity and where spreads are, but Dave mentioned CRT. So if you look at the CRT market right now, they're not issuing below investment grade bonds. They're only issuing IG bonds. At one point, CRT was \$1 billion dollars plus, it was 25% of our portfolio. We've actually reduced that position post quarter end it's like \$725 million. So I think being diversified within Resi is something that we think makes sense. So we have the ability to buy third-party CUSIPs, we have the ability to buy third-party sponsored deals. But I think when you look at the current landscape, if spreads do not change, that number should go materially higher. It should be 75-80% over the next number of years because at this point there's nothing really comparable to the assets that were created.

[Doug Harter:](#)

And you talked about that you now you have the ability to do HELOCs or closed-end seconds. How do those returns compare to the 15% you talked about on non-QM?

[Mike Fania:](#)

Sure. So closed-end seconds, a lot of commentary about it. But in terms of who's actually producing closed-end seconds, it's large originators. It's mostly non-bank originators that have large servicing portfolios and there's probably three or four very large originators. It's Penny Mac, it's Mr. Cooper, it's Rocket, it's New Res. And they sell those out in the open market. So they're just in the bulk market and for a long period of time the market was paying 107 to 108 for a 9.5-10% closed-end second lien. So when we look at that when we're talking with our Agency team, I think our view on long-term speeds on closed-end seconds is a little bit different than the market participants who are currently buying and leveraging those assets.

So that kind of needs to bear out in terms of if rates rally, is there a consolidation of that closed-end second and you have cash-outs. But when you listen to the mortgage originators, when you listen to the non-banks and they talk about the opportunity, why they're doing closed-end seconds, they're doing it so they can ultimately cash out. So I think our view of long-term prepayment speeds is a little bit different than the market. So to pay a seven to eight point premium on a 20-year amortization is what we think relatively high risk.

[David Finkelstein:](#)

That highlights a good point about synergies between even Residential Credit and Agency. So the prepayment modeling that Srini's doing is even informing how Mike thinks about prepayments on seconds and HELOCs. And your typical credit investor isn't as focused on that as we are, but that's just another example of how the left side always knows what the right side is doing.

[Ken Adler:](#)

And just to expand, so on our book that's subserviced we have the opportunity to buy those seconds that come out from there. Mike just shared with you, we're not happy with the prepayment and the valuation, but here's the thing. We have the recapture agreement, so the blended note rate, the CLTV, eventually that loan ends up refinancing through that borrower going to another home or doing a cash-out refinance on the first. If the mortgage rate goes down just a little bit, we get that recaptured MSR. So we kind of benefit there.

[David Finkelstein:](#)

And they do show us on loans, seconds and HELOCs that are done off of our MSR, we get the look on those before they go to market or contextual with market like a last look, and candidly they're just a little bit rich right now.

[Mike Fania:](#)

Yeah, and I'll say just the HELOCs, it's a little bit different. We are pretty active. We have about \$175 million portfolio that's drawn. If you include the undrawn, it's probably closer to \$200 million. I think we would like to do a securitization in Q1 of this year of 2025. The key difference there is that the number of market



participants that are buying HELOCs is materially less than close end seconds. HELOCs is active management in terms of the draw. You have to hold capital against that HELOC. There's a lot of our peers that can't figure that out or they're buying loans and funds that they don't have that capital that they could hold against it. So I think we feel as we have a competitive advantage within the HELOC market, so have been a little bit more bullish there relative to just closed end seconds.

[Ken Lee:](#)

Hey, thanks Ken Lee, RBC Capital Markets. One question on capital allocation. You mentioned that capital allocation for agencies could go as low as 50%. What are the key factors that could drive potential changes over the near term in terms of capital allocation between MSRs, Resi Credit and agencies?

[David Finkelstein:](#)

It's valuation primarily and to a lesser extent, availability of MSR and Resi. Those two sectors do tend to be somewhat more episodic and MSR trades can be relatively chunky. So for example, as we approach year-end, if there's a need for liquidity and we think the valuation is right, you will see a shift from Agency to MSR. But generally speaking, we're nimble enough to where valuation can drive those differences in capital allocation.

[Ken Lee:](#)

And actually just one quick follow-up on that. Just from a broad perspective, how should we think about potential implications to ROE given potential changes in the capital allocation? Thanks.

[David Finkelstein:](#)

To ROE? So we've, we obviously have put out levered returns across the businesses and look Agency's in the mid-teens. Securitized Residential Credit through OBX is contextual with that, MSR is a little bit lower. So you would think that an allocation more towards MSR might adjust that down a little bit. But we're talking about a very marginal difference on an \$82 billion balance sheet. So we wouldn't expect much change through capital allocation specifically on ROEs over the near term.

[Bose George:](#)

Hi Bose George from KBW. Actually I wanted to ask about the repo markets just in terms of the stress into quarter end, year-end. Do you think that persists, is there scenarios where that could potentially impact your net interest margin? And at Arcola, does it impact the funding at FICC at all in terms of the cost of funds there? And then just lastly, does the fed have to do something with the standing repo facility to help stabilize the situation?

[David Finkelstein:](#)

So I'll start and then Serena, you can jump in.

Just with respect to quarter end financing volatility, we did see a little bit of a spike in cleared DVP repo at the end of the quarter. And it's important when you look at that elevated level of rates, to put it in the context of how rates have typically traded in a pre-COVID environment where reserves weren't as abundant as they were in the post-COVID environment. And if you compare it to those periods, it actually looks relatively normal. So at quarter end, month end even, tax dates, large coupon settlements, you do get elevated repo rates. And so what we saw at the end of the third quarter was what we think a little bit of friction in the plumbing of the repo market, but really a normalization in terms of a little bit less liquidity at quarter end and it's isolated enough to those types of dates to where it doesn't have a meaningful impact on the overall cost of financing. And if you looked at the days subsequent to quarter end, rates normalized relatively quickly to get back to contextual or within the corridor, Fed Funds corridor.

As far as the standing repo facility, it did see \$2.6 billion in demand at quarter end, which was very low relative to the need for financing. Not a lot traded at very high levels, but you would think when there's prints in the mid-fives in the repo facility, is it 5% more money would be channeled into there. However, there is a problem with the plumbing on the SFR. It's primarily that it's a triparty channel. So that means that you



commit your collateral in the morning and you don't get your cash until the afternoon. And as a consequence on quarter end, you have banks that intermediate that they end up with daylight overdraft charges and also a regulatory hit on their CLR test. So there is an issue with respect to the SFR being a liquidity providing mechanism to all at those types of dates. They could put some common sense fixes in it or potentially use the cleared market to help things. But nevertheless, there's a little bit of friction with the plumbing.

As far as year-end, look, a lot of times when we have these events, everybody gets a little bit concerned and they shore up their balance sheets sooner rather than later. And everybody is often very well-prepared for year-end. We're not taking it for granted, we're going to make sure that our financing is buttoned up and we have a responsible approach to it at a year-end. But I do think it's a normalization. We're watching reserves in the system and liquidity and making sure that we're prudently managing our financing though.

[Serena Wolfe:](#)

Despite the volatility that David has referenced and we're all aware of going back to normal pre-COVID levels, there's been no concern or no issues with us getting the availability of repo, Bose. We've been able to obtain all the necessary funding that we need both on the bilateral side of things and through Arcola. So it's not an availability issue, it's just a pricing issue. And like David mentioned, it's for a short period of time. And so we take that into consideration when Pete sets his strategy around weighted average days and things like that to make sure that we can minimize the potential impact of that disruption. And it is both in the bilateral side of things and the FICC markets that we've seen those spikes at period ends.

[Bose George:](#)

Great. And actually just one more on the dividend. Any reason the dividend should not be at least in line with what you're doing this year in 2025?

[David Finkelstein:](#)

Serena can answer that. No, I'll just say look, we have given guidance that we feel good about the earnings power of the portfolio and even said publicly, the dividend's safe through year-end. Look, there's a lot of fluidity to markets and particularly monetary policy. We are optimistic about the direction of the portfolio and we feel like earnings are well supporting the dividend and will continue to be. But look, we got to see how policy shakes out and whether the dividend has the potential go higher, or lower, we'll have to wait and see. But we feel really good about our earnings power currently both.

[Bose George:](#)

Thank you.

[Serena Wolfe:](#)

But nice try. We appreciate the effort.

[Harsh Hemnani:](#)

Thanks. Harsh Hemnani from Green Street. So you mentioned the non-delegated underwriting on residential credit in that correspondent channel. How much does that expand the opportunity set in the near to medium term in the context of that \$1 billion dollars run rate that you mentioned and then doing the underwriting in-house, does that have some incremental efficiency costs in your mind and how are you weighing those against the delegated piece, which seems to be performing well given the delinquencies to date?

[Mike Fania:](#)

Yeah, so that's a good question. Thanks, Harsh. In terms of the actual lock volume that we have been doing, I'll say it's averaging closer to a \$1.5 billion to \$1.6 billion in terms of what we would consider success for non-delegated maybe to start the first couple months, it's something in the context of \$25 to \$75 million. So initially we don't think it's going to be a very large contributor to the overall lock volume. I think what's important is the sustainability of non-del relative to the fully delegated channel. We think it's a much more

sticky relationship. So if you go back to 2022, you go back two, three years ago, only I'll say 35%, 40% of the loans that we were purchasing were through our correspondent channel. And a lot of that was because the bulk market originators were able to take down loans on balance sheet and then earn, call it two to three points above rate sheets, right?

So during 2022, a lot of originators took a lot of losses. They didn't know how to hedge their risk. They were still trying to bulk that risk. So now all the leverage has been on providers like ourselves where virtually the entire market is locking through correspondent channels. So I think what it does is it sets us up longer term that you're going to have a sustainable source of production that is not going to go away because they can't sell that asset two to three points higher in the bulk market. They need us to underwrite the risk. So I think in terms of how we think about the actual cost as well, it's probably, when we initially set it up, it'll be variable cost based. And to the extent that it is successful, we would bring it in-house, we would hire our own underwriting team. But I think the expectations that we have initially are modest, but we do think that there's market share out there that over the long term we'd be able to achieve.

[David Finkelstein:](#)

One more.

[Alan Rochard:](#)

First of all, thank you David. Given the record kind of opportunity, the MBS market, when you look at where OAS spreads are, I'm curious what your perspective is on the biggest governor in terms of your willingness to issue equity and if you had the opportunity, if the market afforded you opportunity, you could double your equity today and grow your portfolio, would that be something you'd look to do? I'm just curious anything about the size?

[David Finkelstein:](#)

Well, double is pretty ambitious, but folks probably saw we did issue a fair amount of equity in the third quarter and into the fourth quarter, roughly \$1.2 billion. And as we've said, there's two primary conditions that need to be met for us to raise equity. Number one, it has to be accretive to book. And number two, assets have to be attractive such that there's accretion to earnings. And if those two conditions aren't met, we're not going to raise equity. One of the points I brought up on the earnings call is that we have the additional benefit of additional equity by gaining greater scale. Now you can look at us and say, that's relatively greedy. You're a \$12 billion company, you're the biggest in the space, why do you need more scale? Well, we always need to make investments in technology and innovation and we'd like not to charge the shareholder to do it.

And so by issuing more equity, we can smooth that cost over a larger shareholder base. And so that is an additional benefit in a time where technology is moving rapidly and we can make some pretty solid investments and that helps as well. But in terms of our appetite to raise equity, we are well capitalized. We have all the liquidity we need, but if the market is telling us to go out and raise equity and it works for the shareholder, we'll certainly consider it. In terms of doubling the size of the company. Look, never say never, but we're focused on managing the portfolio in the most effective and efficient way possible and delivering the returns that we are capable of delivering to shareholders, not necessarily being a behemoth. Our primary focus is preservation of capital and delivering the dividend and making sure that our shareholders are happy. And that's a good-

[Serena Wolfe:](#)

What a perfect way to end

[David Finkelstein:](#)

Yeah, that is a good way to end it. And look, one point I'd like to note is I really do want to thank our communications folks for putting this all together. They did a tremendous job and it was a great effort on the part of everybody here today to get here in the rain. And I recognize that. And something to note is that we have gift bags for folks, and in those gift bags is actually umbrellas and-

[Steve Campbell:](#)

Annaly umbrellas.

[David Finkelstein:](#)

Annaly umbrellas. So you can see that our risk management culture extends all the way to investor relations. So nice work guys and thank you everybody. And we're going to have cocktails. Cocktails?

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