

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

FORM 10-K

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

For the fiscal year ended December 31, 2016

OR

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

For the transition period from _____ to _____

Commission File Number: 001-36099

**CHERRY HILL MORTGAGE INVESTMENT
CORPORATION**

(Exact name of registrant as specified in its charter)

Maryland

46-1315605

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

301 Harper Drive, Suite 110

Moorestown, New Jersey

(Address of principal executive offices)

08057

(Zip Code)

(877) 870 – 7005

(Registrant’s telephone number, including area code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$0.01 par value	New York Stock Exchange

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

None

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant’s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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

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

The aggregate market value of the registrant’s common stock, \$0.01 par value per share, at June 30, 2016, held by those persons deemed by the registrant to be non-affiliates (based upon the closing sale price of the common stock on the New York Stock Exchange on June 30, 2016) was approximately \$100.4 million. Shares of the registrant’s common stock held by each executive officer and director and by each entity or person that, to the registrant’s knowledge, owned 10% or more of the registrant’s outstanding common stock as of June 30, 2016, have been excluded from this number in that these persons may be deemed affiliates of the registrant. The determination of affiliate status for this purpose is not necessarily a conclusive determination for other purposes.

On March 14, 2017, the registrant had a total of 7,525,348 shares of common stock, \$0.01 par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant’s Definitive Proxy Statement on Schedule 14A relating to its 2017 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission by no later than May 1, 2017, are incorporated by reference into Part III, Items 10 through 14, inclusive, of this Annual Report on Form 10-K as indicated herein.

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GLOSSARY

This glossary defines some of the terms that we use elsewhere in this Annual Report and is not a complete list of all of the defined terms used herein. In this Annual Report on Form 10-K, unless specifically stated otherwise or the context otherwise indicates, references to “we,” “us,” “our,” the “Company” or “CHMI” refer to Cherry Hill Mortgage Investment Corporation, a Maryland corporation, together with its consolidated subsidiaries; references to the “Manager” or to “CHMM” refer to Cherry Hill Mortgage Management, LLC, a Delaware limited liability company; and references to the “Operating Partnership” refer to Cherry Hill Operating Partnership, LP, a Delaware limited partnership.

“**Agency**” means a U.S. Government agency, such as Ginnie Mae, or a GSE.

“**Agency RMBS**” means RMBS issued by an Agency or for which an Agency guarantees payments of principal and interest on the securities.

“**ASC**” means an Accounting Standards Codification.

“**ARM**” means an adjustable-rate residential mortgage loan.

“**CFTC**” means the U.S. Commodity Futures Trading Commission.

“**CMO**” means a collateralized mortgage obligation. CMOs are structured debt instruments representing interests in specified pool of mortgage loans into multiple classes, or tranches, of securities, with each tranche having different maturities or risk profiles.

“**credit enhancement**” means techniques to improve the credit ratings of securities, including overcollateralization, creating retained spread, creating subordinated tranches and insurance.

“**Excess MSR**” means an interest in an MSR, representing a portion of the interest payment collected from a pool of mortgage loans, net of a basic servicing fee paid to the mortgage servicer.

“**Fannie Mae**” means the Federal National Mortgage Association.

“**FHA**” means the Federal Housing Administration.

“**FHFA**” means the U.S. Federal Housing Finance Agency.

“**FHA mortgage loan**” means a mortgage loan that is insured by FHA.

“**Freddie Mac**” means the Federal Home Loan Mortgage Corporation.

“**FRM**” means a fixed-rate residential mortgage loan.

“**Ginnie Mae**” means the Government National Mortgage Association, a wholly-owned corporate instrumentality of the United States of America within HUD.

“**GSE**” means a government-sponsored enterprise. When we refer to GSEs, we mean Fannie Mae or Freddie Mac.

“**HUD**” means the U.S. Department of Housing and Urban Development.

“**hybrid ARM**” means a residential mortgage loan that has an interest rate that is fixed for a specified period of time (typically three, five, seven or ten years) and thereafter adjusts to an increment over a specified interest rate index.

“**inverse IO**” means an inverse interest-only security, which is a type of stripped security. These debt securities receive no principal payments and have a coupon rate which has an inverse relationship to its reference index.

“**IO**” means an interest-only security, which is a type of stripped security. IO strips receive a specified portion of the interest on the underlying assets.

“**MBS**” means mortgage-backed securities.

“**MSR**” means a mortgage servicing right. An MSR provides a mortgage servicer with the right to service a mortgage loan or a pool of mortgages in exchange for a portion of the interest payments made on the mortgage or the underlying mortgages. An MSR is made up of two components: a basic servicing fee and an Excess MSR. The basic servicing fee is the amount of compensation for the performance of servicing duties.

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“mortgage loan” means a loan secured by real estate with a right to receive the payment of principal and interest on the loan (including the servicing fee).

“non-Agency RMBS” means RMBS that are not issued or guaranteed by an Agency, including investment grade (AAA through BBB rated) and non-investment grade (BB rated through unrated) classes.

“non-conforming loan” means a residential mortgage loan that does not conform to the Agency underwriting guidelines and does not meet the funding criteria of Fannie Mae and Freddie Mac.

“non-QM loan” means a mortgage loan that does not satisfy the requirements for a qualified mortgage.

“prime mortgage loan” means a mortgage loan that generally conforms to GSE underwriting guidelines or is a non-QM loan with a FICO score generally above 700.

“qualified mortgage” means a mortgage that complies with the ability to repay rule and related requirements in Regulation Z.

“REIT” means a real estate investment trust.

“residential mortgage pass-through certificate” is a MBS that represents an interest in a “pool” of mortgage loans secured by residential real property where payments of both interest and principal (including principal prepayments) on the underlying residential mortgage loans are made monthly to holders of the security, in effect “passing through” monthly payments made by the individual borrowers on the mortgage loans that underlie the security, net of fees paid to the issuer/guarantor and servicer.

“RMBS” means a residential MBS.

“Servicing Related Assets” means Excess MSRs and MSRs.

“SIFMA” means the Securities Industry and Financial Markets Association.

“stripped security” is an RMBS structured with two or more classes that receives different distributions of principal or interest on a pool of RMBS. Stripped securities include IOs and inverse IOs.

“TBA” means a forward-settling Agency RMBS where the pool is “to-be-announced.” In a TBA, a buyer will agree to purchase, for future delivery, Agency RMBS with certain principal and interest terms and certain types of underlying collateral, but the particular Agency RMBS to be delivered is not identified until shortly before the TBA settlement date.

“TRS” means a taxable REIT subsidiary.

“UPB” means unpaid principal balance.

“U.S. Treasury” means the U.S. Department of Treasury.

“VA” means the Department of Veterans Affairs.

“VA mortgage loan” means a mortgage loan that is partially guaranteed by the VA in accordance with its regulations.

FORWARD-LOOKING INFORMATION

We make forward-looking statements in this Annual Report on Form 10-K within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). For these statements, we claim the protections of the safe harbor for forward-looking statements contained in such Sections. Forward-looking statements are subject to substantial risks and uncertainties, many of which are difficult to predict and are generally beyond our control. These forward-looking statements include information about possible or assumed future results of our business, financial condition, liquidity, results of operations, plans and objectives. When we use the words “believe,” “expect,” “anticipate,” “estimate,” “plan,” “continue,” “intend,” “should,” “could,” “would,” “may,” “potential” or the negative of these terms or other comparable terminology, we intend to identify forward-looking statements. Statements regarding the following subjects, among others, may be forward-looking:

- the Company’s investment objectives and business strategy;
- the Company’s ability to raise capital through the sale of its equity and debt securities;
- the Company’s ability to obtain future financing arrangements and refinance existing financing arrangements as they mature;
- the Company’s expected leverage;
- the Company’s expected investments;
- the Company’s ability to acquire Servicing Related Assets;
- estimates or statements relating to, and the Company’s ability to make, future distributions;
- the Company’s ability to compete in the marketplace;
- market, industry and economic trends;
- recent market developments and actions taken and to be taken by the U.S. Government, the U.S. Treasury and the Board of Governors of the Federal Reserve System, Fannie Mae, Freddie Mac, Ginnie Mae and the U.S. Securities and Exchange Commission (“SEC”);
- mortgage loan modification programs and future legislative actions;
- the Company’s ability to maintain its qualification as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”);
- the Company’s ability to maintain its exclusion from registration as an investment company under the Investment Company Act of 1940, as amended (the “Investment Company Act”); projected capital and operating expenditures;
- availability of investment opportunities in mortgage-related, real estate-related and other securities;
- availability of qualified personnel;
- prepayment rates; and
- projected default rates.

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

- the factors referenced in this Annual Report on Form 10-K, including those set forth under "Item 1. Business" and "Item 1A. Risk Factors";
- general volatility of the capital markets;
- changes in the Company's investment objectives and business strategy;
- availability, terms and deployment of capital;
- availability of suitable investment opportunities;
- the Company's dependence on its external manager, Cherry Hill Mortgage Management, LLC ("the Manager"), and the Company's ability to find a suitable replacement if the Company or the Manager were to terminate the management agreement the Company has entered into with the Manager;
- changes in the Company's assets, interest rates or the general economy;
- increased rates of default and/or decreased recovery rates on the Company's investments;
- changes in interest rates, interest rate spreads, the yield curve, prepayment rates or recapture rates;
- limitations on the Company's business due to compliance with requirements for maintaining its qualification as a REIT under the Code and its exclusion from registration as an investment company under the Investment Company Act; and
- the degree and nature of the Company's competition, including competition for its targeted assets.

Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, it cannot guarantee future results, levels of activity, performance or achievements. These forward-looking statements apply only as of the date of this Annual Report on Form 10-K. The Company is not obligated, and does not intend, to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. See "Item 1A. Risk Factors" of this Annual Report on Form 10-K.

PART I

Item 1. Business

Cherry Hill Mortgage Investment Corporation is a publicly traded residential real estate finance company focused on acquiring, investing in and managing residential mortgage assets in the United States. We were incorporated in Maryland on October 31, 2012, and we commenced operations on October 9, 2013 following the completion of our initial public offering (“IPO”) and a concurrent private placement. Our common stock is listed and traded on the New York Stock Exchange under the symbol “CHMI.” We are externally managed by Cherry Hill Mortgage Management, LLC, an SEC-registered investment adviser established by Stanley Middleman. Our Manager is a party to a services agreement with Freedom Mortgage Corporation (“Freedom Mortgage”), which is owned and controlled by Mr. Middleman.

We operate so as to continue to qualify to be taxed as a REIT under the Code. To qualify as a REIT, we must distribute annually to our stockholders an amount at least equal to 90% of our REIT taxable income, determined without regard to the deduction for dividends paid and excluding any net capital gain. We currently expect to distribute substantially all of our REIT taxable income to our stockholders. We will be subject to income tax on our taxable income that is not distributed and to an excise tax to the extent that certain percentages of our taxable income are not distributed by specified dates. CHMI Solutions, Inc. (“Solutions”), our TRS, and its wholly owned subsidiary, Aurora Financial Group, Inc. (“Aurora”), are subject to regular corporate U.S. federal, state and local income taxes on their taxable income.

Our principal objective is to generate attractive current yields and risk-adjusted total returns for our stockholders over the long term, primarily through dividend distributions and secondarily through capital appreciation. We intend to attain this objective, subject to market conditions and availability and terms of financing, by selectively constructing and actively managing a targeted portfolio of Servicing Related Assets, RMBS, prime mortgage loans and other cashflowing residential mortgage assets.

We operate our business through the following segments: (i) investments in Servicing Related Assets; and (ii) RMBS. For information regarding the segments in which we operate, see “Item 8. Consolidated Financial Statements and Supplementary Data—Note 3—Segment Reporting.”

Our Targeted Asset Classes

Our primary targeted asset classes currently include:

- Servicing Related Assets consisting of MSRs and Excess MSRs; and
- RMBS, including Agency RMBS, residential mortgage pass-through certificates, CMOs (IOs and inverse IOs) and TBAs.

Our Strategy

Our strategy, which may change due to the availability and terms of capital and as market conditions warrant, involves:

- allocating a substantial portion of our equity capital to the acquisition of Servicing Related Assets through bulk or possibly flow purchases;
- the creation of Excess MSRs from MSRs acquired by our mortgage servicing subsidiary, Aurora;
- acquiring RMBS on a leveraged basis; and
- opportunistically mitigating our prepayment, interest rate and, to a lesser extent, credit risk by using a variety of hedging instruments and where applicable and available, recapture agreements.

Servicing Related Asset Strategy. We currently expect that the primary method by which we will invest in Excess MSRs will be through the creation of Excess MSRs from MSRs acquired by Aurora. We plan to acquire MSRs from servicers, which may include Freedom Mortgage, primarily on a bulk purchase basis but may also enter into flow arrangements on terms to be negotiated in the future.

Our ability to acquire MSRs is subject to the applicable REIT qualification tests. We have to hold our MSRs through Aurora, which is subject to corporate income tax. In certain cases, we will create Excess MSRs from

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those MSR which will be transferred to one of our subsidiaries which function as qualified REIT subsidiaries. These intercompany transfers are eliminated in consolidation for financial statement purposes. The portion of the interest payments represented by the Excess MSR will not be subject to an entity level tax as long as we comply with the REIT qualification tests. The tax liability of Aurora negatively impacts our returns from the MSR that it holds. In addition, our investments in MSR will expose us to default risk and the potential for credit losses.

We do not directly service the mortgage loans underlying the MSR we acquire; rather, we contract with a third-party servicer, currently Freedom Mortgage, to handle servicing functions for the loans underlying the MSR.

RMBS Strategy. Our RMBS strategy focuses primarily on the acquisition and ownership of Agency RMBS that are whole-pool, residential mortgage pass-through certificates. However, from time to time we invest in CMOs, including IOs and inverse IOs, primarily to take advantage of particularly attractive prepayment-related or structural opportunities in the RMBS markets. In addition to investing in specific pools of Agency RMBS, we utilize forward-settling purchases and sales of Agency RMBS where the underlying pools of mortgage loans are "to-be-announced" ("TBA"s). Pursuant to these TBA transactions, we agree to purchase or sell, for future delivery, Agency RMBS with certain principal and interest terms and certain types of underlying collateral, but the particular Agency RMBS to be delivered is not identified until shortly before the TBA settlement date. Generally, we do not take delivery of the specified pool but instead enter into an offsetting transaction before the date when we would be required to take delivery. Our ability to engage in TBA transactions is limited by the gross income and asset tests applicable to REITs.

Our RMBS strategy includes selective investments in non-Agency RMBS, including GSE risk-sharing securities. GSE risk-sharing securities are general obligations of Fannie Mae and Freddie Mac that provide credit protection with respect to defaults on reference pools of loans. We currently expect to expand our participation in that market. However, the extent of our investments in GSE risk-sharing securities is limited by the gross income and asset tests applicable to REITs. We also intend to invest opportunistically in legacy non-Agency RMBS issued during or after 2010. To date, the GSE risk-sharing securities are the only non-Agency RMBS in which we have invested. If and when market conditions permit us to execute our prime mortgage loan acquisition and financing strategy, we expect that we will retain certain bonds collateralized by the prime mortgage loans we securitize. We also may selectively invest across the entire capital structure of non-Agency RMBS that are newly issued by third parties. Non-Agency RMBS are subject to risk of default, among other risks, and could result in greater losses.

Prime Mortgage Loans. We believe that the market for non-conforming loans including, in particular, prime non-conforming mortgage loans, will grow. While our interest in this asset class is undiminished, we do not currently anticipate that either market conditions or available long-term financing will result in our execution of this strategy in 2017. The prime mortgage loans may be ARMs, hybrid ARMs or FRMs with original terms to maturity of not more than 30 years and will be either fully amortizing or interest-only for up to ten years, and fully amortizing thereafter. We expect that these loans may include both qualified mortgages and, if and when market conditions permit, non-QM loans.

Our overall strategy, and each category of that strategy, is adaptable to changing market environments, subject to compliance with the income and other tests that we must satisfy to maintain our qualification as a REIT and maintain our exclusion from regulation as an investment company under the Investment Company Act. As a result, our acquisition and management decisions will depend on prevailing market conditions, and our targeted asset classes and strategy may vary over time in response to market conditions.

Our Manager

We are externally managed by our Manager and, with the exception of Aurora which employs a nominal amount of employees, we have no employees. We have entered into a management agreement with our Manager, pursuant to which our Manager is responsible for our investment strategies and decisions and our day-to-day operations, subject to the supervision and oversight of our board of directors. Our Manager is a Delaware limited liability company originally established by Mr. Middleman. The Manager is party to a services agreement with Freedom Mortgage which is owned and controlled by Mr. Middleman. The sole member of the Manager is a blind trust for the benefit of Mr. Middleman. We rely on our Manager to provide or obtain on our behalf the personnel and services necessary for us to conduct our business.

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The executive offices of our Manager are located at 907 Pleasant Valley Ave., Mount Laurel, New Jersey 08054, and the telephone number of our Manager's executive offices is (877) 870-7005.

We have an Investment Committee to monitor our investment policies, portfolio holdings, financing and hedging strategies and compliance with our investment guidelines. The members of our Investment Committee are Mr. Lown, our President; Mr. Evans, our Chief Investment Officer; Mr. Levine, our Chief Financial Officer, Treasurer and Secretary; and the MSR portfolio manager and head of risk/operations.

Our Manager is registered as an investment adviser under the Investment Advisers Act of 1940, as amended, or the Advisers Act, and is subject to the regulatory oversight of the Investment Management Division of the SEC.

Our Investment Guidelines; Transactions with Freedom Mortgage

The investment guidelines for our assets and borrowings are as follows:

- No investment will be made if it causes us to fail to qualify as a REIT under the Code.
- No investment will be made if it causes us to be regulated as an investment company under the Investment Company Act.
- We will not enter into principal transactions or split price executions with Freedom Mortgage or any of its affiliates unless such transaction is otherwise in accordance with our investment guidelines and the management agreement between us and our Manager and the terms of such transaction are at least as favorable to us as to Freedom Mortgage or its affiliate.
- Any proposed material investment that is outside our targeted asset classes must be approved by at least a majority of our independent directors.

Our Manager makes the determinations as to the percentage of assets that are invested in each of our targeted asset classes, consistent with our investment guidelines. Our Manager's acquisition decisions depend on prevailing market conditions and may change over time in response to opportunities available in different interest rate, economic and credit environments. In addition, our investment guidelines may be changed from time to time by our board of directors without the approval of our stockholders. Changes to our investment guidelines may include, without limitation, modification or expansion of the types of assets which we may acquire.

Our board of directors receives a report of our investments each quarter in conjunction with its review of our quarterly results. The Nominating and Corporate Governance Committee, which is comprised solely of our independent directors, reviews the material terms of any transaction between us and Freedom Mortgage, including the pricing terms, to determine if the terms of those transactions are fair and reasonable. We also retain two independent valuation services to assist our management and our independent directors in making pricing determinations on any Servicing Related Assets we may purchase from Freedom Mortgage.

On November 15, 2016, we completed the sale of approximately half of our Excess MSRs to Freedom Mortgage. At the closing, we received cash proceeds of approximately \$38.0 million, repaid \$12.0 million of outstanding borrowings drawn on our \$25 million term loan facility with NexBank SSB, or the NexBank term loan, with a portion of the cash proceeds and released our security interests on the related MSRs. We invested the remaining cash proceeds in Agency RMBS and expect to redeploy those proceeds into future MSR acquisitions. See "Item 8. Consolidated Financial Statements and Supplementary Data – Note 19 – Subsequent Events" for information regarding the sale of the balance of our Excess MSRs.

Our Financing Strategies and Use of Leverage

We finance our RMBS with what we believe to be a prudent amount of leverage, which will vary from time to time based upon the particular characteristics of our portfolio, availability of financing and market conditions. Our borrowings for RMBS consist of repurchase transactions under master repurchase agreements. These agreements represent uncommitted financing provided by the counterparties. Our repurchase transactions are collateralized by our RMBS. In a repurchase transaction, we sell an asset to a counterparty at a discounted value, or the loan amount, and simultaneously agree to repurchase the same asset from such counterparty at a price equal to the loan amount plus an interest factor. Despite being legally structured as sales and subsequent repurchases, repurchase transactions are generally accounted for as debt secured by the underlying assets. During

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the term of a repurchase transaction, we generally receive the income and other payments distributed with respect to the underlying assets. While the proceeds of our repurchase financings often will be used to purchase additional RMBS subject to the same master repurchase agreement, our repurchase financing arrangements do not restrict our ability to use proceeds from these arrangements to support our other liquidity needs. Our master repurchase agreements are documented under the standard form master repurchase agreement published by SIFMA.

We have entered into repurchase agreements with 23 counterparties as of December 31, 2016. From time to time we expect to negotiate and enter into additional master repurchase agreements with other counterparties that could produce opportunities to acquire certain RMBS that may not be available from our existing counterparties. See “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources” in this Annual Report on Form 10-K.

During the second half of 2015, we also obtained financing for our RMBS from the Federal Home Loan Bank of Indianapolis, or the FHLBI. However, as a result of the implementation of a regulatory change, our membership in the FHLBI was terminated in December 2016. See “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources.”

Although our Excess MSRs from Freedom Mortgage had been pledged to secure a term loan, that loan was repaid in full in February 2017. In September 2016, Aurora and Cherry Hill QRS III, LLC (“QRS III”) entered into a loan and security agreement (the “MSR Financing Facility”), pursuant to which Aurora and QRS III pledged their respective rights in all existing and future MSRs for loans owned or securitized by Fannie Mae to secure borrowings up to a maximum of \$25 million outstanding at any one time. See “Item 8. Consolidated Financial Statements and Supplementary Data—Note 13—Notes Payable”. We may utilize other types of borrowings in the future, including term facilities, securitization, or other more complex financing structures. Additionally, we may take advantage of available borrowings, if any, under new programs established by the U.S. Government to finance our assets. We also may raise capital by issuing unsecured debt or preferred or common stock.

Interest Risk Hedging

We opportunistically manage our interest rate related risks by using various hedging strategies. Subject to maintaining our qualification as a REIT and maintaining our exclusion from regulation as an investment company under the Investment Company Act, we use certain derivative financial instruments and other hedging instruments to mitigate interest rate risk we expect to arise from our repurchase agreement financings associated with our RMBS. We also attempt to mitigate duration and basis risk arising from our investment portfolio. The interest rate hedging instruments that we currently use include: interest rate swaps, TBAs and swaptions. Our overall hedging strategy takes into account the natural hedging effect of our Servicing Related Assets, which tend to increase in value as interest rates rise. See “Item 8. Consolidated Financial Statements and Supplementary Data—Note 2—Basis of Presentation and Significant Accounting Policies—Derivatives and Hedging Activities.”

Policies with Respect to Certain Other Activities

If our board of directors determines that additional funding is required, we may raise such funds through additional offerings of equity or debt securities, the retention of cash flow and other funds from debt financing, or a combination of these methods. In the event that our board of directors determines to raise additional equity capital, it has the authority, without stockholder approval, to issue additional shares of common stock or preferred stock in any manner and on such terms and for such consideration as it deems appropriate, at any time. We may, in the future, offer equity or debt securities in exchange for assets. We have not in the past and will not in the future underwrite the securities of other companies. Our board of directors may change any of these policies without prior notice to you or a vote of our stockholders.

Competition

We compete with other mortgage REITs, specialty finance companies, savings and loan associations, banks, mortgage bankers, insurance companies, mutual funds, institutional investors, investment banking firms, financial institutions, governmental bodies and other entities for investment opportunities in general. See “Item 1A, Risk Factors—We operate in a highly competitive market.”

Employees

We do not have any employees of our own other than Aurora, which has four employees.

Our Tax Status

We have elected to be taxed as a REIT under the Code. Provided that we maintain our qualification as a REIT, we generally will not be subject to U.S. federal income tax on our REIT taxable income that is currently distributed to our stockholders. REITs are subject to a number of organizational and operational requirements, including a requirement that they currently distribute at least 90% of their annual REIT taxable income excluding net capital gains. We cannot assure you that we will be able to comply with such requirements in the future. Failure to qualify as a REIT in any taxable year would cause us to be subject to U.S. federal income tax on our taxable income at regular corporate rates (and any applicable state and local taxes). Even if we qualify for taxation as a REIT, we may be subject to certain federal, state, local and non-U.S. taxes on our income. For example, the income generated by our TRSs, including Aurora, is subject to U.S. federal, state and local income tax.

See “Item 1A. Risk Factors—U.S. Federal Income Tax Risks” for additional tax status information.

Our Exclusion from Regulation as an Investment Company

We are organized as a holding company and conduct business primarily through our subsidiaries. We believe we have conducted and intend to conduct our operations so that neither we nor any of our subsidiaries are required to register as an investment company under the Investment Company Act.

Section 3(a)(1)(A) of the Investment Company Act defines an investment company as any issuer that is or holds itself out as being engaged primarily in the business of investing, reinvesting or trading in securities. Section 3(a)(1)(C) of the Investment Company Act defines an investment company as any issuer that is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of the issuer’s total assets (exclusive of U.S. Government securities and cash items) on an unconsolidated basis, which we refer to as the 40% test. Excluded from the term “investment securities,” among other things, are U.S. Government securities and securities issued by majority-owned subsidiaries that are not themselves investment companies and are not relying on the exclusion from the definition of investment company set forth in Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

We believe neither we nor our Operating Partnership is considered an investment company under Section 3(a)(1)(A) of the Investment Company Act because neither we nor our Operating Partnership engage primarily or hold ourselves out as being engaged primarily in the business of investing, reinvesting or trading in securities. Rather, through our Operating Partnership’s wholly-owned or majority-owned subsidiaries, we and our Operating Partnership are primarily engaged in the non-investment company businesses of these subsidiaries, namely the business of purchasing or otherwise acquiring mortgages and other interests in real estate.

We rely upon certain exemptions from registration as an investment company under the Investment Company Act including, in the case of our subsidiary, Cherry Hill QRS I, LLC, Section 3(c)(5)(C) of the Investment Company Act. Section 3(c)(5)(C), as interpreted by the staff of the SEC, requires an entity to invest at least 55% of its assets in “mortgages and other liens on and interests in real estate,” which we refer to as “qualifying real estate interests,” and at least 80% of its assets in qualifying real estate interests plus “real estate-related assets.” In satisfying the 55% requirement, the entity may treat securities issued with respect to an underlying pool of mortgage loans in which it holds all of the certificates issued by the pool as qualifying real estate interests. We treat the Agency whole-pool pass-through securities in which we have invested as qualifying real estate interests for purposes of the 55% requirement. The Excess MSRs and Agency CMOs we have acquired are not treated as qualifying real estate interests for purposes of the 55% requirement, but are treated as real estate-related assets that qualify for the 80% test. In addition, Cherry Hill QRS I, LLC will treat its investments in Cherry Hill QRS II, LLC and Cherry Hill QRS III, LLC as real estate-related assets because substantially all of the assets held by those subsidiaries will be real estate-related assets.

We monitor our compliance with the 40% Test and the holdings of our subsidiaries to ensure that each of our subsidiaries is in compliance with an applicable exemption or exclusion from registration as an investment company under the Investment Company Act. In the event that we or our Operating Partnership were to acquire

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assets that could make either entity fall within the definition of an investment company under Section 3(a)(1)(A) or Section 3(a)(1)(C) of the Investment Company Act, we believe that we would still qualify for an exclusion from registration pursuant to Section 3(c)(5)(C).

Qualification for exclusion from registration under the Investment Company Act limits our ability to make certain investments. In addition, complying with the tests for exclusion from registration could restrict the time at which we can acquire and sell assets. To the extent that the SEC or its staff provides more specific guidance regarding any of the matters bearing upon such exclusions, we may be required to adjust our strategy accordingly. Any additional guidance from the SEC or its staff could further inhibit our ability to pursue the strategies we have chosen.

Website Access to Reports

We maintain a website at www.chmireit.com. We are providing the address to our website solely for the information of investors. The information on our website is not a part of, nor is it incorporated by reference, into this report. Through our website, we make available, free of charge, our annual proxy statement, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. The SEC maintains a website that contains these reports at www.sec.gov.

Corporate Information

Our principal executive offices are located at 301 Harper Drive, Suite 110, Moorestown, New Jersey, 08057. Our telephone number is (877) 870-7005. The offices of our Manager are located at 907 Pleasant Valley Ave., Mount Laurel, New Jersey, 08054.

Item 1A. Risk Factors

The Company's business and operations are subject to a number of risks and uncertainties, the occurrence of which could adversely affect its business, financial condition, results of operations and ability to make distributions to stockholders and could cause the value of the Company's capital stock to decline. Please refer to the section entitled "Forward-Looking Information."

Risks Related To Our Business

We may not be able to continue to operate our business successfully or generate sufficient revenue to make or sustain distributions to our stockholders.

We commenced operations on October 9, 2013. We cannot assure you that we will be able to continue to operate our business successfully or implement our strategies. There can be no assurance that we will be able to continue to generate sufficient returns to pay our operating expenses and make satisfactory distributions to our stockholders. The results of our operations depend on several factors, including the availability of opportunities for the acquisition of target assets, the level and volatility of interest rates, the availability of adequate short and long-term financing, conditions in the financial markets and general economic conditions.

Difficult conditions in the mortgage and residential real estate markets as well as general market concerns may adversely affect the value of the assets in which we invest, and these conditions may persist for the foreseeable future.

Our business is materially affected by conditions in the residential mortgage market, the residential real estate market, the financial markets and the economy in general. In particular, the residential mortgage market in the United States has experienced a variety of difficulties and changed economic conditions, including defaults, credit losses and liquidity concerns. Over the past several years, certain commercial banks, investment banks and insurance companies have announced extensive losses from exposure to the residential mortgage market. These factors have impacted investor perception of the risk associated with RMBS, other real estate-related securities and various other asset classes in which we may invest. As a result, values of our target assets have experienced volatility. Deterioration of the mortgage market and investor perception of the risks associated with RMBS and other residential mortgage assets that we acquire could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders.

We are dependent on mortgage servicers and subservicers to service the mortgage loans relating to our Servicing Related Assets.

Our investments in Servicing Related Assets are dependent on the entity performing the actual servicing of the mortgage loans, called the mortgage servicer, to perform its servicing obligations. As a result, we could be materially and adversely affected if the mortgage servicer is terminated by the applicable Agency. The duties and obligations of mortgage servicers are defined through contractual agreements, which generally provide for the possibility for termination of the mortgage servicer in the absolute discretion of the applicable Agency. In addition, the termination of a mortgage servicer could take effect across all mortgages being serviced by that mortgage servicer. Freedom Mortgage acts as the mortgage servicer for the MSR's held by Aurora.

We could also be materially and adversely affected if the mortgage servicer is unable to adequately service the underlying mortgage loans due to the following reasons, among others:

- its failure to comply with applicable laws and regulation;
- its failure to perform its loss mitigation obligations;
- a downgrade in its servicer rating;
- its failure to perform adequately in its external audits;
- a failure in or poor performance of its operational systems or infrastructure;
- regulatory or legal scrutiny, enforcement proceedings, consent orders or similar actions regarding any aspect of its operations, including, but not limited to, servicing practices and foreclosure processes lengthening foreclosure timelines, or
- the transfer of servicing to another party.

MSR's are subject to numerous federal, state and local laws and regulations and may be subject to various judicial and administrative decisions imposing various requirements and restrictions on the servicer's business. If Freedom Mortgage or any other mortgage servicer that we may use actually or allegedly failed to comply with applicable laws, rules or regulations, the mortgage servicer could be exposed to fines, penalties or other costs, or the mortgage servicer could be terminated as the servicer and the MSR's would be eliminated and lose all value, which could have a material adverse effect on our business, financial condition, results of operations or cash flows. If these laws, regulations and decisions change, we could be exposed to similar fines, penalties or costs. In addition, if a mortgage servicer that we use experiences any of the failures or regulatory scrutiny described above, then we could become subject to heightened regulatory or legal scrutiny by virtue of being a counterparty of these entities. Such scrutiny could result in our incurring meaningful additional costs or fines or being subject to material operational requirements or restrictions, each of which could adversely affect our business and results of operations.

In addition, a bankruptcy by any mortgage servicer that services the mortgage loans for us could result in:

- payments made by such mortgage servicer to us, or obligations incurred by it, being voided by a court under federal or state preference laws or federal or state fraudulent conveyance laws; or
- any agreement between us and the mortgage servicer being rejected in a bankruptcy proceeding.

Because we do not and in the future may not have the employees, servicing platforms, or technical resources necessary to service mortgage loans, upon a discontinuance or bankruptcy of any mortgage servicer that we use, we would need to engage an alternate mortgage servicer, which may not be readily available on acceptable terms or at all.

Any of the foregoing events could have a material and adverse effect on us.

The performance of loans underlying our MSR's may be adversely affected by the performance of parties who service these mortgage loans.

The performance of the loans underlying our MSR's is subject to risks associated with inadequate or untimely servicing. If our mortgage servicers commit a material breach of their obligations as a servicer, we may be subject to damages if the breach is not cured within a specified period of time following notice. Poor performance by a mortgage servicer may result in greater than expected delinquencies and foreclosures and

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losses on the mortgage loans underlying our MSRs. A substantial increase in our delinquency or foreclosure rate or the inability to process claims could adversely affect our ability to access the capital and secondary markets for our financing needs.

Governmental investigations or examinations, or private lawsuits, including purported class action lawsuits, involving Freedom Mortgage could have a material adverse effect on Freedom Mortgage.

Freedom Mortgage is routinely involved in legal proceedings concerning matters that arise in the ordinary course of its business. These legal proceedings can range from private actions involving a single plaintiff to class action lawsuits with potentially thousands of class members. Participants in the mortgage industry, including Freedom Mortgage, are also routinely subject to government investigations and inquiries. An adverse result in governmental investigations or examinations, or private lawsuits, including purported class action lawsuits, could have a material adverse effect on Freedom Mortgage's financial results. Litigation and other proceedings may require that Freedom Mortgage pay settlement costs, legal fees, damages, penalties or other charges, which could adversely affect its financial results. In particular, ongoing and other legal proceedings brought under state consumer protection statutes may result in a separate fine for each violation of the statute, which, particularly in the case of class action lawsuits, could result in damages substantially in excess of the amounts earned from the underlying activities and that could have a material adverse effect on Freedom Mortgage's liquidity and financial position.

On April 15, 2016, it was announced that Freedom Mortgage had agreed to pay \$113 million to settle allegations that it did not comply with originations, underwriting and quality control requirements of the Federal Housing Authority of the U.S. Department of Housing and Urban Development ("HUD") that resulted in claims submitted to HUD. Freedom Mortgage neither admitted nor denied liability. The settlement provides for a down payment and thirty-six monthly payments thereafter with the unpaid balance accruing interest at 1%. Freedom Mortgage has informed us that it does not expect the settlement to materially and adversely affect either its financial condition or its results of operations.

Our ability to invest in, and dispose of, our investments in Servicing Related Assets may be subject to the receipt of third-party consents.

The Agencies may require that we submit ourselves to costly or burdensome conditions as a prerequisite to their consent to our investments in Servicing Related Assets. These conditions may diminish or eliminate the investment potential of certain of those assets by making such investments too expensive for us or by severely limiting the potential returns available or otherwise imposing unacceptable conditions. The potential costs, issues or restrictions associated with receiving any such Agency's consent for any such acquisitions or dispositions by us cannot be determined with any certainty. To the extent we are unable to acquire or dispose of Servicing Related Assets when we determine it would be beneficial to do so, our results of operations may be adversely impacted.

The value of our Servicing Related Assets may vary substantially with changes in interest rates.

The values of Servicing Related Assets are highly sensitive to changes in interest rates. The value of Servicing Related Assets typically increases when interest rates rise and decreases when interest rates decline due to the effect those changes in interest rates have on prepayment estimates. Subject to qualifying and maintaining our qualification as a REIT, we may pursue various hedging strategies to seek to reduce our exposure to adverse changes in interest rates. Our hedging activity will vary in scope based on the level and volatility of interest rates, the type of assets held and other changing market conditions. Interest rate hedging may fail to protect or could adversely affect us. To the extent we do not utilize derivatives to hedge against changes in the fair value of our Servicing Related Assets, our balance sheet, results of operations and cash flows would be susceptible to significant volatility due to changes in the fair value of, or cash flows from, those assets as interest rates change.

If delinquencies increase, the value of our Servicing Related Assets may decline significantly.

Delinquency rates have a significant impact on the value of our Servicing Related Assets. An increase in delinquencies will generally result in lower revenue because, typically, servicers will only collect servicing fees from GSEs or mortgage owners for performing loans. Our expectation of delinquencies is a significant assumption underlying the cash flow projections on the related pools of mortgage loans. If delinquencies are significantly greater than expected, the estimated fair value of the Servicing Related Assets could be diminished. As a result, we could suffer a loss.

Prepayment rates can change, adversely affecting the performance of our assets.

The frequency at which prepayments (including voluntary prepayments by borrowers, loan buyouts and liquidations due to defaults and foreclosures) occur on mortgage loans is affected by a variety of factors, including the prevailing level of interest rates as well as economic, demographic, tax, social, legal, and other factors. Generally, borrowers tend to prepay their mortgages when prevailing mortgage rates fall below the interest rates on their mortgage loans. If borrowers prepay their mortgage loans at rates that are faster or slower than expected, it may adversely affect our results.

We record our Servicing Related Assets on our balance sheet at fair value, and changes in their fair value is reflected in our consolidated results of operations. The determination of the fair value of Servicing Related Assets requires our management to make numerous estimates and assumptions that could materially differ from actual results. Such estimates and assumptions include, among other things, prepayment rates, as well as estimates of the future cash flows from the Servicing Related Assets, interest rates, delinquencies and foreclosure rates of the underlying mortgage loans. The ultimate realization of the value of the Servicing Related Assets, which are measured at fair value on a recurring basis, may be materially different than the fair values of such assets as may be reflected in our consolidated financial statements as of any particular date. The use of different estimates or assumptions in connection with the valuation of these assets could produce materially different fair values for such assets. Our failure to make accurate assumptions regarding prepayment rates or the other factors examined in determining fair value could cause the fair value of our Servicing Related Assets to materially vary, which could have a material adverse effect on our financial position, results of operations and cash flows. If the fair value of our Servicing Related Assets decreases, we would be required to record a non-cash charge, which would have a negative impact on our financial results. Furthermore, a significant increase in prepayment speeds could materially reduce the ultimate cash flows we receive from the Servicing Related Assets, and we could ultimately receive substantially less than what we paid for such assets.

Voluntary prepayment rates generally increase when interest rates fall and decrease when interest rates rise, but changes in prepayment rates are difficult to predict. Prepayments can also occur when borrowers sell the property and use the sale proceeds to prepay the mortgage as part of a physical relocation or when borrowers default on their mortgages and the mortgages are prepaid from the proceeds of a foreclosure sale of the property. Fannie Mae and Freddie Mac will generally, among other conditions, purchase mortgages that are 120 days or more delinquent from mortgage-backed securities trusts when the cost of guaranteed payments to security holders, including advances of interest at the security coupon rate, exceeds the cost of holding the nonperforming loans in their portfolios. Ginnie Mae provides the issuer the option to buy 90 days or more delinquent loans out of the mortgage-backed securities that it services, which may also contribute to an increase in prepayment rates. Consequently, prepayment rates also may be affected by conditions in the housing and financial markets, which may result in increased delinquencies on mortgage loans. Additionally, changes in the government-sponsored entities' decisions as to when to repurchase delinquent loans can materially impact prepayment rates.

Interest rate mismatches between our assets and any borrowings used to fund purchases of our assets may reduce our income during periods of changing interest rates.

Some of our assets will be fixed-rate securities or have a fixed rate component (such as RMBS backed by hybrid ARMs). This means that the interest we earn on these assets will not vary over time based upon changes in a short-term interest rate index. Although the interest we would earn on any RMBS backed by ARMs generally will adjust for changing interest rates, such interest rate adjustments may not occur as quickly as the interest rate adjustments to any related borrowings, and such interest rate adjustments will generally be subject to interest rate caps, which potentially could cause such RMBS to acquire many of the characteristics of fixed-rate securities if interest rates were to rise above the cap levels. We generally fund our fixed-rate target assets with short-term borrowings. Therefore, there will be an interest rate mismatch between our assets and liabilities. Although we hedge to minimize interest rate exposure, the use of interest rate hedges also introduces the risk of other interest rate mismatches and exposures. During periods of changing interest rates, these mismatches could cause our business, financial condition and results of operations and ability to make distributions to our stockholders to be materially adversely affected.

Ordinarily, short-term interest rates are lower than long-term interest rates. If short-term interest rates rise disproportionately relative to long-term interest rates (a flattening of the yield curve), our borrowing costs may increase more rapidly than the interest income earned on our assets. Because we expect that our investments in RMBS, on average, will bear interest based on longer-term rates than our borrowings, a flattening of the yield

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curve would tend to decrease our net income and the market value of our assets. Additionally, to the extent cash flows from RMBS are reinvested in new RMBS, the spread between the yields of the new RMBS and available borrowing rates may decline, which could reduce our net interest margin or result in losses. Any one of the foregoing risks could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders. It is also possible that short-term interest rates may exceed long-term interest rates, in which event our borrowing costs may exceed our interest income and we could incur operating losses.

We cannot predict the impact future actions by regulators or U.S. government bodies, including the U.S. Federal Reserve, will have on our business, and any such actions may negatively impact us.

Regulators and U.S. government bodies have a major impact on our business. The U.S. Federal Reserve is a major participant in, and its actions significantly impact, the residential mortgage market. For example, quantitative easing, a program implemented by the U.S. Federal Reserve to keep long-term interest rates low and stimulate the U.S. economy, has had the effect of reducing the difference between short-term and long-term interest rates. As a result of the reduction in long-term interest rates, prepayment speeds increased. The U.S. Federal Reserve's purchases of Agency RMBS have resulted in a narrowing of the spread earned by Agency RMBS investors. While the U.S. Federal Reserve has discontinued quantitative easing, the effects on the Agency RMBS market have not completely dissipated as the U.S. Federal Reserve continues to re-invest paydowns of its holdings in Agency RMBS. We cannot predict or control the impact future actions by regulators or U.S. government bodies such as the U.S. Federal Reserve will have on our business. Accordingly, future actions by regulators or U.S. government bodies, including the U.S. Federal Reserve, could have a material and adverse effect on our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Interest rate caps on the ARMs and hybrid ARMs that may back our RMBS may reduce our net interest margin during periods of rising interest rates.

ARMs and hybrid ARMs are typically subject to periodic and lifetime interest rate caps. Periodic interest rate caps limit the amount an interest rate can increase during any given period. Lifetime interest rate caps limit the amount an interest rate can increase through the maturity of the loan. We generally fund our RMBS with borrowings that typically are not subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, our financing costs could increase without limitation while caps could limit the interest we earn on the ARMs and hybrid ARMs that will back our RMBS. This problem is magnified for ARMs and hybrid ARMs that are not fully indexed because such periodic interest rate caps prevent the coupon on the security from fully reaching the specified rate in one reset. Further, some ARMs and hybrid ARMs may be subject to periodic payment caps that result in a portion of the interest being deferred and added to the principal outstanding. As a result, we may receive less cash income on RMBS backed by ARMs and hybrid ARMs than necessary to pay interest on our related borrowings. Interest rate caps on RMBS backed by ARMs and hybrid ARMs could reduce our net interest margin if interest rates were to increase beyond the level of the caps, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Our Manager relies on analytical models and other data to analyze potential asset acquisition and disposition opportunities and to manage our portfolio. These models are based on assumptions and the results may differ significantly from actual experience.

Our Manager relies on analytical models and information and data supplied by third parties. These models and data may be used to value assets or potential asset acquisitions and dispositions and also in connection with our asset management activities. If these models and data prove to be incorrect, misleading or incomplete, any decisions made in reliance thereon could expose us to potential risks. In addition, models are only as accurate as the assumptions that go into building the models. Our Manager's use of models and data may induce it to purchase certain assets at prices that are too high, sell certain other assets at prices that are too low or miss favorable opportunities altogether. Similarly, any hedging activities that are based on faulty models and data may prove to be unsuccessful.

Some models, such as prepayment models or mortgage default models, may be predictive in nature. The use of predictive models has inherent risks. For example, such models may incorrectly forecast future behavior,

leading to potential losses. In addition, the predictive models used by our Manager may differ substantially from those models used by other market participants, with the result that valuations based on these predictive models may be substantially higher or lower for certain assets than actual market prices. Furthermore, because predictive models are usually constructed based on historical data supplied by third parties, the success of relying on such models may depend heavily on the accuracy and reliability of the supplied historical data, and, in the case of predicting performance in scenarios with little or no historical precedent (such as extreme broad-based declines in home prices, or deep economic recessions or depressions), such models must employ greater degrees of extrapolation, and are therefore more speculative and of more limited reliability.

All valuation models rely on correct market data inputs. If incorrect market data is entered into even a well-founded valuation model, the resulting valuations will be incorrect. However, even if market data is input correctly, “model prices” will often differ substantially from market prices, especially for securities with complex characteristics or whose values are particularly sensitive to various factors. If our market data inputs are incorrect or our model prices differ substantially from market prices, our business, financial condition and results of operations and our ability to make distributions to our stockholders could be materially adversely affected.

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

While in many cases our determination of the fair value of our assets is based on valuations provided by third-party dealers and pricing services, we value assets based upon our judgment, and such valuations may differ from those provided by third-party dealers and pricing services. Valuations of certain assets are often difficult to obtain or unreliable. Depending on the complexity and illiquidity of an asset, valuations of the same asset can vary substantially from one dealer or pricing service to another. The valuation process has been particularly difficult recently because market events have made valuations of certain assets unpredictable, and the disparity of valuations provided by third-party dealers has widened. Our business, financial condition and results of operations and our ability to make distributions to our stockholders could be materially adversely affected if our fair value determinations of these assets are materially higher than actual market values.

An increase in interest rates may cause a decrease in the volume of certain of our target assets, which could adversely affect our ability to acquire target assets that satisfy our investment objectives and to make distributions to our stockholders.

Rising interest rates generally reduce the demand for mortgage loans due to the higher cost of borrowing. A reduction in the volume of mortgage loans originated may affect the volume of target assets available to us, which could adversely affect our ability to acquire assets that satisfy our investment objectives. Rising interest rates may also cause our target assets that were issued prior to an interest rate increase to provide yields that are below prevailing market interest rates. If rising interest rates cause us to be unable to acquire a sufficient volume of our target assets with a yield that is above our borrowing cost, our ability to satisfy our investment objectives and to make distributions to our stockholders could be materially adversely affected.

The lack of liquidity of our assets may adversely affect our business, including our ability to sell our assets.

Mortgage-related assets generally experience periods of illiquidity, including the period of delinquencies and defaults with respect to residential and commercial mortgage loans during the financial crisis. In addition, validating third-party pricing for illiquid assets may be more subjective than with respect to more liquid assets. Any illiquidity of our assets makes it difficult for us to sell such assets if the need or desire arises. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we previously recorded our assets. Assets that are illiquid are more difficult to finance, and to the extent that we use leverage to finance assets that become illiquid we may lose that leverage or have it reduced. Assets tend to become less liquid during times of financial stress, which is often the time that liquidity is most needed. As a result, our ability to sell assets or vary our portfolio in response to changes in economic and other conditions may be limited by liquidity constraints, which could adversely affect our results of operations and financial condition.

We use leverage in executing our business strategy, which may adversely affect the return on our assets and may reduce cash available for distribution to our stockholders, as well as increase losses when economic conditions are unfavorable.

We use leverage to finance our investments in certain of our target assets and to enhance our financial returns. Our primary source of leverage is short-term borrowings under master repurchase agreements collateralized by our RMBS assets. Other sources of leverage include the MSR Financing Facility and, in the future, may include other credit facilities.

Through the use of leverage, we acquire positions with market exposure significantly greater than the amount of capital committed to the transaction. Although we are not required to maintain any particular minimum or maximum target debt-to-equity leverage ratio with respect to our RMBS assets, the amount of leverage we may employ for this asset class will depend upon the availability of particular types of financing and our Manager's assessment of the credit, liquidity, price volatility, financing counterparty risk and other factors. Our Manager has discretion, without the need for further approval by our board of directors, to change the amount of leverage we utilize for our RMBS. We do not have a targeted debt-to-equity ratio for our RMBS. We use leverage for the primary purpose of financing our RMBS portfolio and not for the purpose of speculating on changes in interest rates. We may, however, be limited or restricted in the amount of leverage we may employ by the terms and provisions of any financing or other agreements that we may enter into in the future, and we are subject to margin calls as a result of our financing activity.

Our ability to achieve our investment and leverage objectives depends on our ability to borrow money in sufficient amounts and on favorable terms. In particular, our ability to execute on our prime mortgage loan strategy and our ability to build a significant servicing portfolio is dependent on obtaining sufficient financing on attractive terms. In addition, we must be able to renew or replace our maturing borrowings on a continuous basis. In recent years, investors and financial institutions that lend in the securities repurchase market have tightened lending standards in response to the difficulties and changed economic conditions that have materially adversely affected the RMBS market. These market disruptions have been most pronounced in the non-Agency RMBS market, and the impact has also extended to Agency RMBS, which has made the value of these assets unstable and relatively illiquid compared to prior periods. This could potentially increase our financing costs and reduce our liquidity. In addition, because we rely on short-term financing, we are exposed to changes in the availability of financing which may make it more difficult for us to secure continued financing.

Leverage magnifies both the gains and the losses of our positions. Leverage increases our returns as long as we earn a greater return on investments purchased with borrowed funds than our cost of borrowing such funds. However, if we use leverage to acquire an asset and the value of the asset decreases, the leverage may increase our loss. Even if the asset increases in value, if the asset fails to earn a return that equals or exceeds our cost of borrowing, the leverage will decrease our returns.

We are required to post large amounts of cash as collateral or margin to secure our leveraged RMBS positions. In the event of a sudden, precipitous drop in value of our financed assets, we might not be able to liquidate assets quickly enough to repay our borrowings, further magnifying losses. Even a small decrease in the value of a leveraged asset may require us to post additional margin or cash collateral. Our debt service payments and posting of margin or cash collateral will reduce cash flow available for distribution to stockholders. We may not be able to meet our debt service obligations. To the extent that we cannot meet our debt service obligations, we risk the loss of some or all of our assets to sale to satisfy our debt obligations.

To the extent we might be compelled to liquidate qualifying real estate assets to repay debts, our compliance with the REIT rules regarding our assets and our sources of income could be negatively affected, which could jeopardize our qualification as a REIT. Failing to qualify as a REIT would cause us to be subject to U.S. federal income tax (and any applicable state and local taxes) on all of our income and decrease profitability and cash available for distributions to stockholders.

Adverse market developments generally will cause our lenders to require us to pledge cash as additional collateral. If our assets were insufficient to meet these collateral requirements, we might be compelled to liquidate particular assets at inopportune times and at unfavorable prices.

Adverse market developments, including a sharp or prolonged rise in interest rates, a change in prepayment rates or increasing market concern about the value or liquidity of one or more types of our target assets, might reduce the market value of our portfolio, which generally will cause our lenders to initiate margin calls. A margin

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call means that the lender requires us to pledge cash as additional collateral to re-establish the ratio of the value of the collateral to the amount of the borrowing. If we are unable to satisfy margin calls, our lenders may foreclose on our collateral. The liquidation of collateral may jeopardize our ability to qualify as a REIT. Our failure to qualify as a REIT would cause us to be subject to U.S. federal income tax (and any applicable state and local taxes) on all of our income and decrease profitability and cash available for distribution to our stockholders.

Our use of repurchase transactions gives our lenders greater rights in the event that we file for bankruptcy, which may make it difficult for us to recover our collateral in the event of a bankruptcy filing.

Our borrowings under master repurchase agreements are intended to qualify for special treatment under the bankruptcy code, giving our lenders the ability to void the automatic stay provisions of the bankruptcy code and take possession of and liquidate collateral pledged in our repurchase transactions without delay if we file for bankruptcy. Furthermore, the special treatment of repurchase agreements under the bankruptcy code may make it difficult for us to recover our pledged assets in the event that any of our lenders files for bankruptcy. Thus, the use of repurchase transactions exposes our pledged assets to risk in the event of a bankruptcy filing by either our lenders or us.

If our lenders default on their obligations to resell the RMBS back to us at the end of the repurchase transaction term, the value of the RMBS has declined by the end of the repurchase transaction term or we default on our obligations under the repurchase transaction, we will lose money on these transactions, which, in turn, may materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

When we engage in a repurchase transaction, we initially sell securities to the financial institution in exchange for cash and our counterparty is obligated to resell the securities to us at the end of the term of the transaction, which is typically from 30 to 180 days, but which may be up to 364 days or more. The cash we receive when we initially sell the securities is less than the value of those securities. This difference is referred to as the haircut. If these haircuts are increased we will be required to post additional cash collateral for our RMBS. If our counterparty defaults on its obligation to resell the securities to us, we would incur a loss on the transaction equal to the amount of the haircut (assuming there was no change in the value of the securities). See “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources” for information regarding borrowings under the Company’s repurchase agreements.

If we default on one of our obligations under a repurchase transaction, the counterparty can terminate the transaction and cease entering into any other repurchase transactions with us. Such a default also would constitute a default under many of our financing agreements with other counterparties. In that case, there is no assurance we would be able to establish a suitable replacement facility on acceptable terms or at all.

Hedging against interest rate changes and other risks may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders.

Subject to maintaining our qualification as a REIT and exemption from registration under the Investment Company Act, we pursue various hedging strategies to seek to reduce our exposure to adverse changes in interest rates. Our hedging activity varies in scope based on the level and volatility of interest rates, the types of liabilities and assets held and other changing market conditions. Interest rate hedging may fail to protect or could adversely affect us because, among other things:

- interest rate hedging can be expensive, particularly during periods of rising and volatile interest rates;
- available interest rate hedges may not correspond directly with the interest rate risk for which protection is sought;
- the duration of the hedge may not match the duration of the related assets or liabilities being hedged;
- to the extent hedging transactions do not satisfy certain provisions of the Code, and are not made through a TRS, the amount of income that a REIT may earn from hedging transactions to offset interest rate losses is limited by U.S. federal tax provisions governing REITs;
- the value of derivatives used for hedging may be adjusted from time to time in accordance with accounting rules to reflect changes in fair value. Downward adjustments or “mark-to-market losses,” would reduce our total stockholders’ equity;

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- the credit quality of the hedging counterparty owing money on the hedge may be downgraded to such an extent that it impairs our ability to sell or assign our side of the hedging transaction; and
- the hedging counterparty owing money in the hedging transaction may default on its obligation to pay.

Our hedging transactions, which are intended to limit losses, may actually adversely affect our earnings, which could reduce our cash available for distribution to our stockholders.

Changes in regulations relating to swaps activities may cause us to limit our swaps activity or subject us and our Manager to additional disclosure, recordkeeping, and other regulatory requirements.

The enforceability of agreements underlying hedging transactions may depend on compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. Recently, new regulations have been promulgated by U.S. and foreign regulators attempting to strengthen oversight of derivative contracts. Any actions taken by regulators could constrain our strategy and could increase our costs, either of which could materially and adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders. In particular, the Dodd-Frank Act requires most derivatives to be executed on a regulated market and cleared through a central counterparty, which has resulted in increased margin requirements and costs. On December 7, 2012, the CFTC issued a no-action letter that provides mortgage REITs relief from such registration, or the MREIT No-Action Letter, if they meet certain conditions and submit a claim for such no-action relief. We believe we meet the conditions set forth in the MREIT No-Action Letter and we have filed our claim with the CFTC to perfect the use of the no-action relief from registration. However, if in the future we do not meet the conditions set forth in the MREIT No-Action Letter or the relief provided by the MREIT No-Action Letter becomes unavailable for any other reason, we may need to seek to obtain another exemption from registration or we may be required to register as a “commodity pool operator” with the CFTC. If we are required to register with the CFTC as a commodity pool operator, we would become subject to additional disclosure, recordkeeping and reporting requirements, which may increase our expenses or otherwise limit our ability to conduct our business as contemplated.

We may change our investment strategy, investment guidelines and asset allocation without notice or stockholder consent, which may result in riskier investments. In addition, our charter provides that our board of directors may authorize us to revoke or otherwise terminate our REIT election, without the approval of our stockholders.

Our board of directors has the authority to change our investment strategy or asset allocation at any time without notice to or consent from our stockholders. To the extent that our investment strategy changes in the future, we may make investments that are different from, and possibly riskier than, the investments described in this Annual Report and the other documents we file with the SEC from time to time. A change in our investment or leverage strategy may increase our exposure to interest rate and real estate market fluctuations or require us to sell a portion of our existing investments, which could result in gains or losses and therefore increase our earnings volatility. Decisions to employ additional leverage in executing our investment strategies could increase the risk inherent in our asset acquisition strategy. Furthermore, a change in our asset allocation could result in our allocating assets in a different manner than as described in this Annual Report.

In addition, our charter provides that our board of directors may authorize us to revoke or otherwise terminate our REIT election, without the approval of our stockholders, if it determines that it is no longer in our best interests to qualify as a REIT. These changes could adversely affect our financial condition, results of operations, the market value of our common stock, and our ability to make distributions to our stockholders.

We operate in a highly competitive market.

Our profitability depends, in large part, on our ability to acquire targeted assets at favorable prices. We compete with a number of entities when acquiring our targeted assets, including other mortgage REITs, financial companies, public and private funds, commercial and investment banks and residential and commercial finance companies. We may also compete with the U.S. Federal Reserve and the U.S. Treasury to the extent they purchase assets in our targeted asset classes. Many of our competitors are substantially larger and have considerably greater access to capital and other resources than we do. Furthermore, new companies with significant amounts of capital have recently been formed or have raised additional capital, and may continue to

be formed and raise additional capital in the future, and these companies may have objectives that overlap with ours, which may create competition for assets we wish to acquire. Some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of assets to acquire and establish more relationships than us. We also may have different operating constraints from those of our competitors including, among others, (i) tax-driven constraints such as those arising from our qualification as a REIT, (ii) restraints imposed on us by our efforts to comply with certain exclusions or exemptions from the definition of an “investment company” and (iii) restraints and additional costs arising from our status as a public company. Furthermore, competition for assets in our targeted asset classes may lead to the price of such assets increasing, which may further limit our ability to generate desired returns. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations.

Our ability to make distributions to our stockholders depends on our operating results, our financial condition and other factors, and we may not be able to make regular cash distributions at a fixed rate or at all under certain circumstances.

We intend to continue to make distributions to our stockholders in amounts such that we distribute all or substantially all of our REIT taxable income in each year (subject to certain adjustments). This distribution policy will enable us to avoid being subject to U.S. federal income tax on our taxable income that we distribute to our stockholders. However, our ability to make distributions will depend on our earnings, applicable law, our financial condition and such other factors as our board of directors may deem relevant from time to time. We will declare and make distributions to our stockholders only to the extent approved by our board of directors.

Residential whole mortgage loans are subject to increased risks.

We may acquire and manage pools of residential whole mortgage loans. Residential whole mortgage loans are subject to increased risks of loss. Unlike Agency RMBS, whole mortgage loans generally are not guaranteed by the U.S. Government or any GSE, though in some cases they may benefit from private mortgage insurance. Additionally, by directly acquiring whole mortgage loans, we do not receive the structural credit enhancements that benefit senior tranches of CMOs. A whole mortgage loan is directly exposed to losses resulting from default. Therefore, the value of the underlying property, the creditworthiness and financial position of the borrower and the priority and enforceability of the lien will significantly impact the value of such mortgage. In the event of a foreclosure, we may assume direct ownership of the underlying real estate. The liquidation proceeds upon sale of such real estate may not be sufficient to recover our cost basis in the loan, and any costs or delays involved in the foreclosure or liquidation process may increase losses.

Whole mortgage loans are also subject to “special hazard” risk (property damage caused by hazards, such as earthquakes or environmental hazards, not covered by standard property insurance policies), and to bankruptcy risk (reduction in a borrower’s mortgage debt by a bankruptcy court). In addition, claims may be assessed against us on account of our position as a mortgage holder or property owner, including assignee liability, responsibility for tax payments, environmental hazards and other liabilities. In some cases, these liabilities may be “recourse liabilities” or may otherwise lead to losses in excess of the purchase price of the related mortgage or property.

Risks Related to our Relationship with our Manager and Freedom Mortgage

Our Manager has limited experience operating a REIT and we cannot assure you that our Manager’s past experience will be sufficient to successfully manage our business as a REIT.

Our Manager has limited experience operating a REIT. The REIT provisions of the Code are complex, and any failure to comply with those provisions in a timely manner could prevent us from qualifying as a REIT or force us to pay unexpected taxes and penalties. In such event, our net income would be reduced and we could incur a loss.

Our Manager has limited experience operating a public company or complying with regulatory requirements, including the Sarbanes-Oxley Act, which may hinder its ability to achieve our objectives.

Prior to our commencement of operations in October 2013, our Manager had no experience operating a public company or complying with regulatory requirements, including the Sarbanes-Oxley Act. Our Manager’s

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inexperience may hinder our Manager's ability to achieve our objectives and we cannot assure you that we will be able to successfully execute our business strategies as a public company, or comply with regulatory requirements applicable to public companies.

We are dependent on our Manager and certain key personnel that are or will be provided to us through our Manager and may not find a suitable replacement if our Manager terminates the management agreement or such key personnel are no longer available to us.

We do not have any employees of our own other than four employees of Aurora. We are completely reliant on our Manager, which has significant discretion as to the implementation of our operating policies and execution of our business strategies and risk management practices. We also depend on our Manager's access to the professionals and services provided by Freedom Mortgage to our Manager. The departure of Messrs. Lown or Levine or other senior officers could have a material adverse effect on our ability to achieve our objectives.

We can offer no assurance that our Manager will remain our manager or that we will continue to have access to our Manager's senior management. We are subject to the risk that our Manager will terminate the management agreement or that we may deem it necessary to terminate the management agreement or prevent certain individuals from performing services for us and that no suitable replacement will be found to manage us.

If our management agreement is terminated and no suitable replacement is found to manage us or we are unable to find a suitable replacement on a timely basis, we may not be able to continue to execute our business strategy. No assurances can be given that our Manager will act in our best interests with respect to the allocation of personnel, services and resources to our business. The failure of any of the key personnel of our Manager to service our business with the requisite time and dedication could materially and adversely affect our ability to execute our business plan.

The management fee payable to our Manager is payable regardless of the performance of our portfolio, which may reduce our Manager's incentive to devote the time and effort to seeking profitable opportunities for our portfolio.

We pay our Manager a management fee, which may be substantial, based on our stockholders' equity (as defined in the management agreement) regardless of the performance of our portfolio. The management fee takes into account the net issuance proceeds of both common and preferred stock offerings, as well as issuances of equity securities by our Operating Partnership. Our Manager's entitlement to non-performance-based compensation might reduce its incentive to devote the time and effort of its professionals to seeking profitable opportunities for our portfolio, which could result in a lower performance of our portfolio and materially adversely affect our business, financial condition and results of operations.

Our investment guidelines are very broad, and our board of directors will not approve each decision made by our Manager to acquire, dispose of, or otherwise manage an asset.

Our Manager is authorized to follow very broad guidelines in pursuing our strategy. Our board of directors will periodically review our portfolio and asset-management decisions. However, it generally will not review all of our proposed acquisitions, dispositions and other management decisions. In addition, in conducting periodic reviews, our board of directors will rely primarily on information provided to it by our Manager. Furthermore, our Manager may arrange for us to use complex strategies or to enter into complex transactions that may be difficult or impossible to unwind by the time they are reviewed by our board of directors. Our Manager has great latitude within the broad guidelines in determining the types of assets it may decide are proper for us to acquire and other decisions with respect to the management of those assets subject to our maintaining our qualification as a REIT. Poor decisions could have a material adverse effect on our business, financial condition and results of operations and our ability to make distributions to our stockholders.

There will be conflicts of interest in our relationships with our Manager and Freedom Mortgage, which could result in decisions that are not in the best interests of our stockholders.

Our Manager is a Delaware limited liability company established by Mr. Middleman. The Manager is a party to a services agreement with Freedom Mortgage which is wholly owned and controlled by Mr. Middleman. The Manager is owned by a "blind trust" for the benefit of Mr. Middleman.

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We are dependent on our Manager for our day-to-day management and operations. In turn, the Manager is dependent on the performance of Freedom Mortgage under the services agreement. Various potential and actual conflicts of interest may arise from the activities of Freedom Mortgage and its affiliates by virtue of this relationship. The ability of our Manager's officers and personnel, with the exception of those officers that are dedicated to us, to engage in other business activities, including the management of Freedom Mortgage, may reduce the time our Manager and certain of its officers and personnel spend managing us.

Our management agreement with our Manager and our other agreements with Freedom Mortgage that were executed in connection with our initial public offering were negotiated between related parties, and their respective terms may not be as favorable to us as if they were negotiated on an arm's-length basis with unaffiliated third parties. Furthermore, we may choose not to enforce, or to enforce less vigorously, our rights under such agreements because of our desire to maintain our ongoing relationships with Freedom Mortgage and our Manager. In the future, Freedom Mortgage may sponsor other vehicles that invest in Excess MSRs or prime loans or other investments, and there may be situations where we compete with Freedom Mortgage or its affiliates for opportunities to acquire MSRs or prime mortgage loans or other assets. Freedom Mortgage is a separate and distinct company with its own business interests and will be under no obligation to maintain its current business strategy. Freedom Mortgage will be under no obligation to offer MSRs or other assets to us, and Freedom Mortgage may offer those assets to third parties without offering such assets to us.

In addition, there may be conflicts of interest inherent in our relationship with Freedom Mortgage through our Manager to the extent Freedom Mortgage or our Manager invests in or creates new vehicles to invest in assets in which we may invest or whose investment objectives overlap with our investment objectives. Certain investments appropriate for us may also be appropriate for one or more of these other investment vehicles. Members of our board of directors may serve as officers and/or directors of these other entities. In addition, in the future our Manager or its affiliates may have investments in and/or earn fees from such other investment vehicles that are higher than their economic interests in us and which may therefore create an incentive to allocate investments to such other investment vehicles.

Our management agreement with our Manager generally does not limit or restrict our Manager or its affiliates from engaging in any business or managing other pooled investment vehicles that invest in investments that meet our investment objectives, except that under our management agreement neither our Manager nor any entity controlled by or under common control with our Manager is permitted to raise or sponsor any new pooled investment vehicle whose investment policies, guidelines or plans target as its primary investment category investments in Excess MSRs.

The ability of our Manager and its officers and employees to engage in other business activities, subject to the terms of our management agreement with our Manager, may reduce the amount of time our Manager, its officers or other employees spend managing us. In addition, we may engage (subject to our investment guidelines) in material transactions with Freedom Mortgage or our Manager, including, but not limited to, certain financing arrangements, co-investments in, or purchases of, MSRs or other assets, that present an actual, potential or perceived conflict of interest. It is possible that actual, potential or perceived conflicts could give rise to investor dissatisfaction, litigation or regulatory enforcement actions. Appropriately dealing with conflicts of interest is complex and difficult, and our reputation could be damaged if we fail, or appear to fail, to deal appropriately with one or more potential, actual or perceived conflicts of interest. Regulatory scrutiny of, or litigation in connection with, conflicts of interest could have a material adverse effect on our reputation, which could materially adversely affect our business in a number of ways, including causing an inability to raise additional funds, a reluctance of counterparties to do business with us, a decrease in the prices of our common and preferred securities and a resulting increased risk of litigation and regulatory enforcement actions.

The management agreement with our Manager was not negotiated on an arm's-length basis and may not be as favorable to us as if it had been negotiated with an unaffiliated third party and may be costly and difficult to terminate.

The management agreement that we have entered into with our Manager was negotiated between related parties, and its terms, including fees payable, may not be as favorable to us as if it had been negotiated with an unaffiliated third party. Various potential and actual conflicts of interest may arise from the activities of Freedom Mortgage and its affiliates.

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Termination of our management agreement without cause is subject to several conditions which may make such a termination difficult and a significant termination fee could be payable by us. That fee will increase the effective cost to us of terminating the management agreement, thereby adversely affecting our ability to terminate our Manager without cause.

Pursuant to the management agreement, our Manager will not assume any responsibility other than to render the services called for thereunder and will not be responsible for any action of our board of directors in following or declining to follow the Manager's advice or recommendations. Our Manager will maintain a contractual as opposed to a fiduciary relationship with us. Under the terms of the management agreement, our Manager, Freedom Mortgage, and their affiliates and each of their officers, directors, trustees, members, stockholders, partners, managers, Investment Committee members, employees, agents, successors and assigns, will not be liable to us for acts or omissions performed in accordance with and pursuant to the management agreement, except because of acts constituting bad faith, willful misconduct, gross negligence, fraud or reckless disregard of their duties under the management agreement. In addition, we will indemnify our Manager, Freedom Mortgage, and their affiliates and each of their officers, directors, trustees, members, stockholders, partners, managers, Investment Committee members, employees, agents, successors and assigns, with respect to all expenses, losses, damages, liabilities, demands, charges and claims arising from acts of our Manager not constituting bad faith, willful misconduct, gross negligence, fraud or reckless disregard of duties, performed in good faith in accordance with and pursuant to the management agreement.

If our Manager ceases to be our Manager pursuant to the management agreement, our lenders and our derivative counterparties may cease doing business with us.

If our Manager ceases to be our Manager, it would constitute an event of default or early termination event under many of our financing and hedging agreements, upon which our counterparties would have the right to terminate their agreements with us. If our Manager ceases to be our Manager for any reason, including upon the non-renewal of our management agreement, and we are unable to obtain financing or enter into or maintain derivative transactions, our business, financial condition and results of operations and our ability to make distributions to our stockholders may be materially adversely affected.

Risks Related to Our Organizational Structure

Maintenance of our exclusion from regulation as an investment company under the Investment Company Act imposes significant limitations on our operations.

We intend to continue to conduct our operations so that neither we nor any of our subsidiaries is required to register as an investment company under the Investment Company Act. We conduct our business primarily through our Operating Partnership and its wholly-owned subsidiaries. The securities issued by our subsidiaries that are excluded from the definition of "investment company" under Section 3(c)(7) of the Investment Company Act, together with other investment securities we may own, cannot exceed 40% of the value of all our assets (excluding U.S. Government securities and cash) on an unconsolidated basis. This requirement limits the types of businesses in which we may engage and the assets we may hold. Certain of our subsidiaries rely on the exclusion provided by Section 3(c)(5)(C) under the Investment Company Act which is designed for entities primarily engaged in the business of "purchasing or otherwise acquiring mortgages and other liens on and interests in real estate." This exclusion generally requires that at least 55% of the entity's assets on an unconsolidated basis consist of qualifying real estate assets and at least 80% of the entity's assets consist of qualifying real estate assets or real estate-related assets. These requirements limit the assets those subsidiaries can own and the timing of sales and purchases of those assets.

To classify the assets held by our subsidiaries as qualifying real estate assets or real estate-related assets, we rely on no-action letters and other guidance published by the SEC staff regarding those kinds of assets, as well as upon our analyses (in consultation with outside counsel) of guidance published with respect to other types of assets. There can be no assurance that the laws and regulations governing the Investment Company Act status of companies similar to ours, or the guidance from the SEC or its staff regarding the treatment of assets as qualifying real estate assets or real estate-related assets, will not change in a manner that adversely affects our operations. To the extent that the SEC staff provides more specific guidance regarding any of the matters bearing upon our exemption from the need to register under the Investment Company Act, we may be required to adjust our strategy accordingly. Any additional guidance from the SEC staff could further inhibit our ability to pursue

the strategies that we have chosen. Furthermore, although we intend to monitor the assets of our subsidiaries regularly, there can be no assurance that our subsidiaries will be able to maintain their exclusion from registration. Any of the foregoing could require us to adjust our strategy, which could limit our ability to make certain investments or require us to sell assets in a manner, at a price or at a time that we otherwise would not have chosen. This could negatively affect the value of our common stock, the sustainability of our business model and our ability to make distributions.

The ownership limits in our charter may discourage a takeover or business combination that may have benefited our stockholders.

To assist us in qualifying as a REIT, among other purposes, our charter generally limits the beneficial or constructive ownership of our stock by any person, other than Mr. Middleman, to no more than 9.0% in value or the number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our stock. This and other restrictions on ownership and transfer of our shares of stock contained in our charter may discourage a change of control of us and may deter individuals or entities from making tender offers for our common stock on terms that might be financially attractive to you or which may cause a change in our management. In addition to deterring potential transactions that may be favorable to our stockholders, these provisions may also decrease your ability to sell our common stock.

Our stockholders' ability to control our operations is severely limited.

Our board of directors approves our major strategies, including our strategies regarding investments, financing, growth, debt capitalization, REIT qualification and distributions. Our board of directors may amend or revise these and other strategies without a vote of our stockholders.

Certain provisions of Maryland law could inhibit a change in our control.

Certain provisions of the Maryland General Corporation Law, or the MGCL, may have the effect of inhibiting a third party from making a proposal to acquire us or impeding a change of control under circumstances that otherwise could provide our stockholders with the opportunity to realize a premium over the then-prevailing market price of our common stock, including:

- “business combination” provisions that, subject to limitations, prohibit certain business combinations between us and an “interested stockholder” (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding voting stock or an affiliate or associate of ours who, at any time within the two-year period immediately prior to the date in question, was the beneficial owner of 10% or more of the voting power of our then-outstanding stock) or an affiliate of an interested stockholder for five years after the most recent date on which the stockholder became an interested stockholder, and thereafter require two supermajority stockholder votes to approve any such combination; and
- “control share” provisions that provide that a holder of “control shares” of the Company (defined as voting shares of stock which, when aggregated with all other shares of stock owned by the acquiror or in respect of which the acquiror is able to exercise or direct the exercise of voting power (except solely by virtue of a revocable proxy), entitle the acquiror to exercise one of three increasing ranges of voting power in electing directors) acquired in a “control share acquisition” (defined as the direct or indirect acquisition of ownership or control of issued and outstanding “control shares,” subject to certain exceptions) generally has no voting rights with respect to the control shares except to the extent approved by our stockholders by the affirmative vote of two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares.

We have elected to opt-out of these provisions of the MGCL, in the case of the business combination provisions, by resolution of our board of directors exempting any business combination between us and any other person (provided that such business combination is first approved by our board of directors, including a majority of our directors who are not affiliates or associates of such person), and, in the case of the control share provisions, pursuant to a provision in our bylaws. However, our board of directors may by resolution elect to repeal the foregoing opt-out from the business combination provisions of the MGCL, and we may, by amendment to our bylaws, opt in to the control share provisions of the MGCL in the future.

Our authorized but unissued common and preferred stock may prevent a change in our control.

Our charter authorizes us to issue additional authorized but unissued common stock and preferred stock without stockholder approval. In addition, our board of directors may, without stockholder approval, (i) amend our charter to increase or decrease the aggregate number of our shares of stock or the number of shares of any class or series of stock that we have authority to issue, (ii) classify or reclassify any unissued common stock or preferred stock and set the preferences, rights and other terms of the classified or reclassified shares. As a result, among other things, our board may establish a class or series of common stock or preferred stock that could delay or prevent a transaction or a change in our control that might involve a premium price for our common stock or otherwise be in the best interests of our stockholders.

Our rights and the rights of our stockholders to take action against our directors and officers are limited, which could limit your recourse in the event of actions not in your best interest.

Our charter limits the liability of our present and former directors and officers to us and our stockholders for money damages to the maximum extent permitted under Maryland law. Under current Maryland law, our present and former directors and officers will not have any liability to us or our stockholders for money damages other than liability resulting from:

- actual receipt of an improper benefit or profit in money, property or services; or
- active and deliberate dishonesty by the director or officer that was established by a final judgment and is material to the cause of action.

In addition, our charter authorizes us to indemnify our present and former directors and officers for actions taken by them in those and other capacities to the maximum extent permitted by Maryland law and our bylaws require us to indemnify our present and former directors and officers, to the maximum extent permitted by Maryland law, in the defense of any proceeding to which he or she is made, or threatened to be made, a party by reason of his or her service to us as a director or officer in these and other capacities. In addition, we may be obligated to pay or reimburse the expenses incurred by our present and former directors and officers without requiring a preliminary determination of their ultimate entitlement to indemnification. As a result, we and our stockholders may have more limited rights against our present and former directors and officers than might otherwise exist absent the current provisions in our charter and bylaws or that might exist with other companies, which could limit your recourse in the event of actions not in your best interests.

Our charter contains provisions that make removal of our directors difficult, which could make it difficult for our stockholders to effect changes to our management.

Our charter provides that, subject to the rights of holders of one or more classes or series of preferred stock to elect or remove one or more directors, a director may be removed only for “cause” (as defined in our charter), and then only by the affirmative vote of at least two-thirds of the votes entitled to be cast generally in the election of directors. Vacancies may be filled only by a majority of the remaining directors in office, even if less than a quorum, for the full term of the directorship in which the vacancy occurred (other than vacancies among any directors elected by the holder or holders of any class or series of preferred stock, if such right exists). These requirements make it more difficult to change our management by removing and replacing directors and may prevent a change in our control that is in the best interests of our stockholders.

Risks Related to Our Common Stock

The market price and trading volume of our common stock may be volatile.

The market price of our common stock may be highly volatile and subject to wide fluctuations. In addition, the trading volume in our common stock may fluctuate and cause significant price variations to occur. The stock market has experienced price and volume fluctuations that have affected the market price of many companies in industries similar or related to ours and that have been unrelated to these companies’ operating performances. If the market price of our common stock declines significantly, you may be unable to resell your shares at a gain. Further, fluctuations in the trading price of our common stock may adversely affect the liquidity of the trading market for our common stock and, in the event that we seek to raise capital through future equity financings, our ability to raise such equity capital.

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We cannot assure you that the market price of our common stock will not fluctuate or decline significantly in the future. Some of the factors that could negatively affect our share price or result in fluctuations in the price or trading volume of our common stock include:

- actual or anticipated variations in our quarterly operating results;
- increases in market interest rates that lead purchasers of our common stock to demand a higher yield or to seek alternative investments;
- changes in market valuations of similar companies;
- adverse market reaction to any increased indebtedness we incur in the future;
- additions or departures of key personnel;
- actions by stockholders;
- speculation in the press or investment community;
- general market, economic and political conditions and the impact of these conditions on the global credit markets;
- the operating performance of other similar companies;
- changes in accounting principles; and
- passage of legislation or other regulatory developments that adversely affect us or our industry.

For as long as we are an emerging growth company, we will not be required to comply with certain reporting requirements, including those relating to accounting standards and disclosure about our executive compensation, that apply to other public companies.

We are an “emerging growth company,” as defined in Section 2(a) of the Securities Act, as modified by the JOBS Act. As such, we are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies,” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding a non-binding advisory vote on executive compensation and of stockholder approval of any golden parachute payments not previously approved. To the extent we continue to take advantage of any of these exemptions, we do not know if some investors will find our common stock less attractive as a result. The result may be a less active trading market for our common stock and our stock price may be more volatile.

We could remain an “emerging growth company” until the last day of the fiscal year following the fifth anniversary of the IPO or until the earliest of (a) the last day of the first fiscal year in which our annual gross revenues exceed \$1 billion, (b) the date that we become a “large accelerated filer” as defined in Rule 12b-2 under the Exchange Act, which would occur if the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the last business day of our most recently completed second fiscal quarter, or (c) the date on which we have issued more than \$1 billion in non-convertible debt securities during the preceding three-year period.

In addition, pursuant to Section 107 of the JOBS Act, as an “emerging growth company,” we are permitted to take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards, which would allow us to delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have elected to take advantage of the benefits of this extended transition period. This election is irrevocable. As a result of our election to utilize the extended transition period, our financial statements may not be comparable to those of other public companies that comply with such new or revised accounting standards. Please refer to “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates—Emerging Growth Company Status” for further discussion of our election to utilize the extended transition period for complying with new or revised accounting standards.

Future sales of our common stock or other securities convertible into our common stock could cause the market value of our common stock to decline and could result in dilution of your shares.

Sales of substantial amounts of shares of our common stock could cause the market price of our common stock to decrease significantly. We cannot predict the effect, if any, of future sales of our common stock, or the availability of shares of our common stock for future sales, on the value of our common stock. Sales of substantial amounts of shares of our common stock, or the perception that such sales could occur, may adversely affect prevailing market values for our common stock.

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

In the future, we may attempt to increase our capital resources by making offerings of debt or additional offerings of equity securities, including commercial paper, medium-term notes, senior or subordinated notes and classes of preferred stock or common stock. Upon liquidation, holders of our debt securities and shares of preferred stock and lenders with respect to other borrowings will receive a distribution of our available assets prior to the holders of our common stock. Additional equity offerings may dilute the holdings of our existing stockholders or reduce the market price of our common stock, or both. Our preferred stock, if issued, could have a preference on liquidating distributions or a preference on dividend payments that could limit our ability to make a dividend distribution to the holders of our common stock. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, holders of our common stock bear the risk of our future offerings reducing the market price of our common stock and diluting their stock holdings in us.

Broad market fluctuations could negatively impact the market price of our common stock.

The stock market has experienced extreme price and volume fluctuations that have affected the market price of many companies in industries similar or related to ours and that have been unrelated to these companies' operating performances. These broad market fluctuations could reduce the market price of our common stock. Furthermore, our operating results and prospects may be below the expectations of public market analysts and investors or may be lower than those of companies with comparable market capitalizations, which could lead to a material decline in the market price of our common stock.

We have not established a minimum distribution payment level, and we cannot assure you of our ability to make distributions in the future.

We expect to make regular distributions to holders of our common stock in amounts such that we distribute all or substantially all of our REIT taxable income in each year. We have not established a minimum distribution payment level, and our ability to make distributions may be adversely affected by a number of factors, including the risk factors described in this report. All distributions will be made at the discretion of our board of directors and will depend on our earnings, our financial condition, debt covenants, maintenance of our REIT qualification, applicable law and other factors as our board of directors may deem relevant from time to time.

No assurance can be given that the level of any distributions we make to our stockholders will achieve a market yield or increase or even be maintained over time, any of which could materially and adversely affect the market price of our common stock. In addition, some of our distributions may include a return of capital, which would reduce the amount of capital available to operate our business.

In addition, we cannot assure you that we will be able to invest in MSRs and other residential mortgage-related assets with a yield equal to or greater than the yield of the Excess MSRs that we have sold or have agreed to sell to Freedom Mortgage, or that the \$3.0 million in yield maintenance payments that Freedom Mortgage has agreed to make to us in 2017 will be sufficient to permit us to maintain the level of distributions that we have made to our stockholders in the past.

Furthermore, distributions that we make to our stockholders will generally be taxable to our stockholders as ordinary income. However, a portion of our distributions may be designated by us as long-term capital gains to the extent that they are attributable to capital gain income recognized by us or may constitute a return of capital

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to the extent that they exceed our earnings and profits as determined for U.S. federal income tax purposes. A return of capital is not taxable, but has the effect of reducing the tax basis of a stockholder's investment in our common stock.

Common stock eligible for future sales may depress the market price of our common stock.

We cannot predict the effect, if any, of future sales of shares of our common stock or securities that are convertible into or exchangeable or exercisable for shares of our common stock, or the availability of such securities for future sales, on the value of our common stock. Sales of substantial amounts of our common stock or securities that are convertible into or exchangeable or exercisable for shares of our common stock, or the perception that such sales could occur, may adversely affect prevailing market prices for our common stock.

We have registered for public resale 1,000,000 shares of our common stock held by Mr. Middleman. Mr. Middleman could sell, or indicate an intention to sell, any or all of these shares in the public market. As a result, the trading price of our common stock could decline. In addition, the perception in the market that these sales may occur could also cause the trading price of our common stock to decline.

U.S. Federal Income Tax Risks

Our failure to qualify as a REIT would subject us to U.S. federal, state and local income taxes, which could adversely affect the value of our common stock and would substantially reduce the cash available for distribution to our stockholders.

We operate in a manner that is intended to cause us to qualify as a REIT for U.S. federal income tax purposes. However, the U.S. federal income tax laws governing REITs are complex, and interpretations of the U.S. federal income tax laws governing qualification as a REIT are limited. Moreover, our qualification and taxation as a REIT depend upon our ability to meet on a continuing basis, through actual annual operating results, certain qualification tests set forth in the U.S. federal income tax laws. Although we intend to operate so that we continue to qualify as a REIT, given the complex nature of the rules governing REITs, the ongoing importance of factual determinations, including the potential tax treatment of the investments we make, and the possibility of future changes in our circumstances, no assurance can be given that our actual results of operations for any particular taxable year will satisfy such requirements.

If we fail to qualify as a REIT in any calendar year, and do not qualify for certain statutory relief provisions, we would be required to pay U.S. federal income tax (and any applicable state and local taxes), including any applicable alternative minimum tax, on our taxable income at regular corporate rates, and dividends paid to our stockholders would not be deductible by us in computing our taxable income. Further, if we fail to qualify as a REIT, we might need to borrow money or sell assets in order to pay any resulting tax. Our payment of income tax would decrease the amount of our income available for distribution to our stockholders. Furthermore, if we fail to qualify or maintain our qualification as a REIT, we no longer would be required under U.S. federal tax laws to distribute substantially all of our REIT taxable income to our stockholders. Unless our failure to qualify as a REIT was subject to relief under U.S. federal tax laws, we could not re-elect to qualify as a REIT until the fifth calendar year following the year in which we failed to qualify.

Complying with REIT requirements may cause us to forego or liquidate otherwise attractive investments.

To qualify as a REIT, we must continually satisfy various tests regarding the sources of our income, the nature and diversification of our assets, the amounts we distribute to our stockholders and the ownership of our common stock. In order to meet these tests, we may be required to forego investments we might otherwise make. We may be required to make distributions to stockholders at disadvantageous times or when we do not have funds readily available for distribution, and may be unable to pursue investments that would be otherwise advantageous to us in order to satisfy the source of income or asset diversification requirements for qualifying as a REIT. Thus, compliance with the REIT requirements may hinder our investment performance.

Failure to make required distributions would subject us to tax, which would reduce the cash available for distribution to our stockholders.

To qualify as a REIT, we must distribute to our stockholders each calendar year at least 90% of our REIT taxable income (including certain items of non-cash income), determined without regard to the deduction for dividends paid and excluding net capital gain. To the extent that we satisfy the 90% distribution requirement, but

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distribute less than 100% of our taxable income, we will be subject to U.S. federal corporate income tax on our undistributed income. In addition, we will incur a 4% nondeductible excise tax on the amount, if any, by which our distributions in any calendar year are less than the sum of:

- 85% of our REIT ordinary income for that year;
- 95% of our REIT capital gain net income for that year; and
- any undistributed taxable income from prior years.

We intend to distribute our taxable income to our stockholders in a manner intended to satisfy the 90% distribution requirement and to avoid both corporate income tax and the 4% nondeductible excise tax. However, there is no requirement that TRSs distribute their after tax net income to their parent REIT or its stockholders.

Our taxable income may substantially exceed our net income as determined based on generally accepted accounting principles (“GAAP”), because, for example, realized capital losses will be deducted in determining our GAAP net income, but may not be deductible in computing our taxable income. In addition, we may invest in assets that generate taxable income in excess of economic income or in advance of the corresponding cash flow from the assets. As a result of the foregoing, we may generate less cash flow than taxable income in a particular year. To the extent that we generate such non-cash taxable income in a taxable year, we may incur corporate income tax and the 4% nondeductible excise tax on that income if we do not distribute such income to stockholders in that year. In that event, we may be required to use cash reserves, incur debt, sell assets, make taxable distributions of our shares or debt securities or liquidate non-cash assets at rates or at times that we regard as unfavorable to satisfy the distribution requirement and to avoid corporate income tax and the 4% nondeductible excise tax in that year.

Despite qualification as a REIT, we may face other tax liabilities that reduce our cash flows.

Despite qualification as a REIT, we may be subject to certain U.S. federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, and state or local income, property and transfer taxes. In addition, Solutions, Aurora and any other TRSs we form will be subject to regular corporate U.S. federal, state and local taxes. Any of these taxes would decrease cash available for distributions to our stockholders.

We may lose our REIT qualification or be subject to a penalty tax if the U.S. Internal Revenue Service, or IRS, successfully challenges our characterization of our investments in Excess MSR.

We create Excess MSRs from the MSRs held by Aurora. The IRS has issued two private letter rulings to other REITs holding that Excess MSRs are qualifying assets for purposes of the 75% asset test and produce qualifying income for purposes of the 75% gross income test. Any income that is qualifying income for the 75% gross income test is also qualifying income for the 95% gross income test. A private letter ruling may be relied upon only by the taxpayer to whom it is issued, and the IRS may revoke a private letter ruling. Based on these private letter rulings and other IRS guidance regarding excess mortgage servicing fees, we generally intend to treat our investments in Excess MSRs as qualifying assets for purposes of the 75% asset test and as producing qualifying income for purposes of the 95% and 75% gross income tests. However, we have not sought, and we do not intend to seek, our own private letter ruling. Thus, it is possible that the IRS could successfully take the position that our Excess MSRs are not qualifying assets or do not produce qualifying income, presumably by recharacterizing Excess MSRs as an interest in servicing compensation, in which case we may fail one or more of the income and asset requirements for REIT qualification. If we failed one of those tests, we would either be required to pay a penalty tax, which could be material, to maintain REIT status or we would fail to qualify as a REIT.

The failure of RMBS subject to a repurchase agreement to qualify as real estate assets would adversely affect our ability to qualify as a REIT.

We have entered into repurchase agreements under which we nominally sell certain of our RMBS to a counterparty and simultaneously agree to repurchase the sold assets. We believe that, for U.S. federal income tax purposes, these transactions will be treated as secured debt and we will be treated as the owner of the RMBS that are the subject of any such repurchase agreement notwithstanding that such agreements may transfer record

ownership of such assets to the counterparty during the term of the agreement. It is possible, however, that the IRS could successfully assert that we do not own the RMBS during the term of the repurchase agreement, in which case we could fail to qualify as a REIT.

Our ability to engage in TBA transactions could be limited by the requirements necessary to qualify as a REIT, and we could fail to qualify as a REIT as a result of these investments.

We purchase and sell TBAs for purposes of managing interest related risks associated with our liabilities under repurchase agreements, including duration and basis risks. We generally treat such TBA purchases and sales as hedging transactions that hedge indebtedness incurred to acquire or carry real estate assets, or “qualifying liability hedges” for REIT purposes. From time to time, we also opportunistically engage in TBA transactions because we find them attractive on their own. The law is unclear regarding whether income and gains from TBAs that are not qualifying liability hedges are qualifying income for the 75% gross income test and whether TBAs are qualifying assets for the 75% asset test.

To the extent that we engage in TBA transactions that are not qualifying liability hedges for REIT purposes, unless we receive a favorable private letter ruling from the IRS or we are advised by counsel that income and gains from such TBAs should be treated as qualifying income for purposes of the 75% gross income test, we will limit our income and gains from dispositions of such TBAs and any non-qualifying income to no more than 25% of our gross income for each calendar year. Further, unless we receive a favorable private letter ruling from the IRS or we are advised by counsel that TBAs should be treated as qualifying assets for purposes of the 75% asset test, we will limit our investment in such TBAs and any non-qualifying assets to no more than 25% of our total assets at the end of any calendar quarter and will limit the TBAs held by us that are issued by any one issuer to no more than 5% of our total assets at the end of any calendar quarter. Accordingly, our ability to purchase and sell Agency RMBS through TBAs and to hold or dispose of TBAs, through dollar roll transactions or otherwise, could be limited.

Even if we are advised by counsel that such TBAs should be treated as qualifying assets or that income and gains from such TBAs should be treated as qualifying income, it is possible that the IRS could successfully take the position that such assets are not qualifying assets and such income is not qualifying income. In that event, we could be subject to a penalty tax or we could fail to qualify as a REIT if (i) the value of our TBAs, together with our other non-qualifying assets for the 75% asset test, exceeded 25% of our total assets at the end of any calendar quarter, (ii) the value of our TBAs issued by any one issuer exceeded 5% of our total assets at the end of any calendar quarter, or (iii) our income and gains from our TBAs that are not qualifying liability hedges, together with our non-qualifying income for the 75% gross income test, exceeded 25% of our gross income for any taxable year.

Complying with REIT requirements may limit our ability to hedge effectively.

The REIT provisions of the Code substantially limit our ability to hedge. Our aggregate gross income from non-qualifying hedges, fees, and certain other non-qualifying sources cannot exceed 5% of our annual gross income. As a result, we might have to limit our use of advantageous hedging techniques or implement those hedges through a TRS. Any hedging income earned by a TRS would be subject to U.S. federal, state and local income tax at regular corporate rates. This could increase the cost of our hedging activities or expose us to greater risks associated with interest rate changes or other changes than we would otherwise want to bear.

Our ownership of and relationship with Solutions, Aurora and any future TRSs that we form will be limited and a failure to comply with the limits would jeopardize our REIT status and may result in the application of a 100% excise tax.

A REIT may own up to 100% of the stock of one or more TRSs. A TRS may earn income that would not be qualifying income if earned directly by the parent REIT. Both the subsidiary and the REIT must jointly elect to treat the subsidiary as a TRS. A corporation (other than a REIT) of which a TRS directly or indirectly owns more than 35% of the voting power or value of the stock will automatically be treated as a TRS. Overall, no more than 25% (20% for taxable years beginning after December 31, 2017) of the value of a REIT’s total assets may consist of stock or securities of one or more TRSs. A domestic TRS will pay U.S. federal, state and local income tax at regular corporate rates on any income that it earns. In addition, the TRS rules limit the deductibility of interest paid or accrued by a TRS to its parent REIT to assure that the TRS is subject to an

appropriate level of corporate taxation. The rules also impose a 100% excise tax on certain transactions between a TRS and its parent REIT that are not conducted on an arm's-length basis. Solutions, Aurora and any future domestic TRS that we may form will pay U.S. federal, state and local income tax on its taxable income, and its after-tax net income will be available for distribution to us but is not required to be distributed to us unless necessary to maintain our REIT qualification.

Our ownership limitation may restrict change of control or business combination opportunities in which our stockholders might receive a premium for their common stock.

In order for us to qualify as a REIT for each taxable year after 2013, no more than 50% in value of our outstanding shares of stock may be owned, directly or indirectly, by five or fewer individuals during the last half of any calendar year. "Individuals" for this purpose include natural persons, private foundations, some employee benefit plans and trusts, and some charitable trusts. In order to help us qualify as a REIT, among other purposes, our charter generally prohibits any person, other than Mr. Middleman, from beneficially or constructively owning more than 9.0% in value or in number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our stock.

The ownership limitation and other restrictions could have the effect of discouraging a takeover or other transaction in which holders of shares of our common stock might receive a premium for their common stock over the then-prevailing market price or which holders might believe to be otherwise in their best interests.

Dividends payable by REITs do not qualify for the reduced tax rates available for some dividends.

The maximum tax rate applicable to "qualified dividend income" payable to U.S. stockholders that are taxed at individual rates is 20%. Dividends payable by REITs, however, are generally not eligible for the reduced rates on qualified dividend income. The more favorable rates applicable to regular corporate qualified dividends could cause investors who are taxed at individual rates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends treated as qualified dividend income, which could adversely affect the value of the shares of REITs, including our common stock.

We may be subject to adverse legislative or regulatory tax changes that could reduce the market price of our common stock.

At any time, the U.S. federal income tax laws or regulations governing REITs or the administrative interpretations of those laws or regulations may be amended. We cannot predict when or if any new U.S. federal income tax law, regulation or administrative interpretation, or any amendment to any existing U.S. federal income tax law, regulation or administrative interpretation, will be adopted, promulgated or become effective and any such law, regulation or interpretation may take effect retroactively. We and our stockholders could be adversely affected by any such change in, or any new, U.S. federal income tax law, regulation or administrative interpretation.

Our recognition of "phantom" income may reduce a stockholder's after-tax return on an investment in our common stock.

We may recognize taxable income in excess of our economic income, known as phantom income, in the first years that we hold certain investments, and experience an offsetting excess of economic income over our taxable income in later years. As a result, stockholders at times may be required to pay U.S. federal income tax on distributions that economically represent a return of capital rather than a dividend. These distributions would be offset in later years by distributions representing economic income that would be treated as returns of capital for U.S. federal income tax purposes. Taking into account the time value of money, this acceleration of U.S. federal income tax liabilities may reduce a stockholder's after-tax return on his or her investment to an amount less than the after-tax return on an investment with an identical before-tax rate of return that did not generate phantom income.

Liquidation of our assets may jeopardize our REIT qualification.

To maintain our qualification as a REIT, we must comply with requirements regarding our assets and our sources of income. If we are compelled to liquidate our assets to repay obligations to our lenders or for other reasons, we may be unable to comply with these requirements, thereby jeopardizing our qualification as a REIT, or we may be subject to a 100% tax on any resultant gain if we sell assets that are treated as inventory or property held primarily for sale to customers in the ordinary course of business.

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Our qualification as a REIT and exemption from U.S. federal income tax with respect to certain assets may be dependent on the accuracy of legal opinions or advice rendered or given or statements by the issuers of assets that we acquire, and the inaccuracy of any such opinions, advice or statements may adversely affect our REIT qualification and result in significant corporate-level tax.

When purchasing securities, we may rely on opinions or advice of counsel for the issuer of such securities, or statements made in related offering documents, for purposes of determining whether such securities represent debt or equity securities for U.S. federal income tax purposes, the value of such securities, and also to what extent those securities constitute qualified real estate assets for purposes of the REIT asset tests and produce income that qualifies under the 75% gross income test. The inaccuracy of any such opinions, advice or statements may adversely affect our ability to qualify as a REIT and result in significant corporate-level tax.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

Our business is operated from space provided through our Manager located at 301 Harper Drive, Suite 110, Moorestown, New Jersey 08057, telephone (877) 870-7005, 315 Route 34, Suite 121, Colts Neck, New Jersey 07722, telephone (856) 380-9960 and 623 Fifth Avenue, 24th Floor, New York, New York 10022, telephone (877) 870-7005.

Item 3. Legal Proceedings

From time to time, the Company may be involved in various claims and legal actions in the ordinary course of business. As of December 31, 2016, the Company is not aware of any material legal or regulatory claims.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

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

Market Information

Our common stock has been listed and traded on the New York Stock Exchange (“NYSE”) under the symbol “CHMI” since October 4, 2013. Prior to October 4, 2013, our common stock was not listed on any exchange or over-the-counter market. On March 13, 2017, the closing sale price for our common stock on the NYSE was \$18.12 per share. The following table presents the quarterly high and low closing sale prices per share of our common stock on the NYSE for the periods indicated below:

	Common Stock	
	High	Low
2016		
Fourth Quarter	\$ 18.85	\$ 16.04
Third Quarter	\$ 17.94	\$ 14.99
Second Quarter	\$ 16.04	\$ 14.07
First Quarter	\$ 14.55	\$ 12.65
2015		
Fourth Quarter	\$ 15.59	\$ 12.95
Third Quarter	\$ 16.86	\$ 15.13
Second Quarter	\$ 17.87	\$ 16.19
First Quarter	\$ 18.44	\$ 16.74

Holders

As of March 14, 2017, we had five holders of record of our common stock. The five holders of record include Cede & Co., which holds shares as nominee for The Depository Trust Company, which itself holds shares on behalf of the beneficial owners of our common stock. Such information was obtained from our registrar and transfer agent.

Dividends

The Company has elected to be taxed as a REIT under the Code. To qualify as a REIT, the Company must distribute at least 90% of its annual REIT taxable income to stockholders within the time frame set forth in the Code, and the Company must also meet certain other requirements. Although we may borrow funds to make distributions, cash for such distributions is expected to be largely generated from our results of operations. Dividends are declared and paid at the discretion of our board of directors and depend on our taxable net income, cash available for distribution, financial condition, ability to maintain our qualification as a REIT, and such other factors that our board of directors may deem relevant. From time to time, a portion of our dividends on our capital stock may be characterized as capital gains or return of capital. For 2016 and 2015, all of our common stock dividends were characterized as ordinary income to stockholders. (See “Item 1A, Risk Factors,” and “Item 7, Management’s Discussion and Analysis of Financial Conditions and Results of Operations,” of this Annual Report on Form 10-K, for information regarding the sources of funds used for dividends and for a discussion of factors which may adversely affect our ability to pay dividends.)

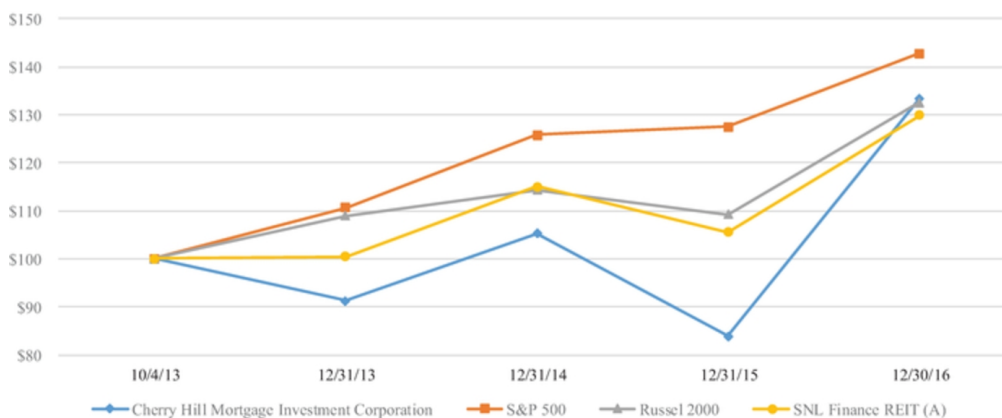
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We declared the following quarterly cash dividends on our common stock for the quarterly periods indicated below:

	Declaration Date	Record Date	Payment Date	Amount per Share
2016				
Fourth Quarter	12/8/2016	12/31/2016	1/31/2017	\$ 0.64
Third Quarter	9/8/2016	9/30/2016	10/25/2016	\$ 0.49
Second Quarter	6/16/2016	6/30/2016	7/26/2016	\$ 0.49
First Quarter	3/8/2016	3/31/2016	4/26/2016	\$ 0.49
2015				
Fourth Quarter	12/10/2015	12/31/2015	1/26/2016	\$ 0.49
Third Quarter	9/10/2015	9/30/2015	10/27/2015	\$ 0.49
Second Quarter	6/18/2015	6/30/2015	7/28/2015	\$ 0.49
First Quarter	3/5/2015	3/31/2015	4/28/2015	\$ 0.51

Stockholder Return Performance

The following graph is a comparison of the cumulative total stockholder return on our common stock, the S&P 500 Index, the Russell 2000 Index (the “Russell 2000”) and the SNL Finance REIT Index, a peer group index, from October 4, 2013 (commencement of trading of our common stock on the New York Stock Exchange) to December 31, 2016. The graph assumes that \$100 was invested on October 4, 2013 in our common stock, the S&P 500, the Russell 2000 and the SNL Finance REIT Index and that all dividends were reinvested without the payment of any commissions. There can be no assurance that the performance of our common stock will continue in line with the same or similar trends depicted in the graph below:



	Period Ended				
	October 4, 2013	December 31, 2013	December 31, 2014	December 31, 2015	December 30, 2016
Cherry Hill Mortgage Investment Corporation	\$ 100.00	\$ 91.22	\$ 105.32	\$ 83.92	\$ 133.39
Russel 2000	\$ 100.00	\$ 109.00	\$ 114.34	\$ 109.29	\$ 132.58
SNL Finance REIT (A)	\$ 100.00	\$ 100.47	\$ 115.06	\$ 105.51	\$ 129.97
S&P 500	\$ 100.00	\$ 110.67	\$ 125.82	\$ 127.56	\$ 142.82

Source: SNL Financial LC

(A) In addition to the Company, as of December 31, 2016, the SNL Finance REIT Index comprised the following companies: AG Mortgage Investment Trust, American Capital Agency Corp., American Capital Mortgage Inv, American Church Mortgage Co., Annaly Capital Mgmt Inc., Anworth Mortgage Asset Corp., Apollo Commercial Real Estate, Apollo Residential Mortgage, Arbor Realty Trust Inc., Ares Commercial Real Estate, ARMOUR Residential REIT Inc., Bimini Capital Mgmt Inc., Blackstone Mortgage Trust, Capstead Mortgage Corp., Chimera Investment Corp., Colony Financial Inc., CV Holdings Inc, CYS Investments, Dynex Capital Inc., Ellington Residential Mortgage, Five Oaks Investment Corp, Hannon Armstrong Sustainable, Hatteras Financial Corp., Invesco Mortgage Capital Inc., iStar Financial Inc., JAVELIN Mortgage, JER Investors Trust Inc., Ladder Capital Corp, MFA Financial Inc., New Resdl Invt Corp, New York Mortgage Trust Inc., Newcastle Investment Corp., NorthStar Realty Finance Corp., Orchid Island Capital Inc., Origen Financial Inc., Owens Realty Mortgage Inc., PennyMac Mortgage Investment, RAIT Financial Trust, Redwood Trust Inc., Resource Capital Corp., Starwood Property Trust Inc., Two Harbors Investment Corp., United Development Funding IV, Western Asset Mrtg Cap Corp, and ZAIS Financial Corp.

Securities Authorized For Issuance Under Equity Compensation Plans

During 2013, the board of directors approved and the Company adopted the Cherry Hill Mortgage Investment Corporation 2013 Equity Incentive Plan (“2013 Plan”). The 2013 Plan provides for the grant of options to purchase shares of the Company’s common stock, stock awards, stock appreciation rights, performance units, incentive awards and other equity-based awards, including long term incentive plan units (“LTIP-OP Units”) of the Company’s operating partnership, Cherry Hill Operating Partnership, LP (the “Operating Partnership”). Each LTIP-OP Unit awarded is deemed equivalent to an award of one share of our common stock under the 2013 Plan and reduces the 2013 Plan’s share authorization for other awards on a one-for-one basis.

The following table presents information with respect to the Company’s equity compensation plans as of December 31, 2016:

Equity Incentive Plan Information

As of December 31, 2016

	<u>Number of Securities Issued or to be Issued Upon Exercise</u>	<u>Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans</u>
Equity compensation Plans Approved By Shareholders		1,335,218
LTIP-OP Units	140,350	
Forfeited LTIP-OP Units	(916)	
Shares of Common Stock	28,503	
Forfeited Shares of Common Stock	(3,155)	
Equity Compensation Plans Not Approved By Shareholders	—	—

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

Item 6. Selected Financial Data

All currency figures are presented in thousands, except per share amounts or as otherwise noted.

The selected financial data set forth below has been derived from our audited consolidated financial statements.

This information should be read in conjunction with “Item 1. Business,” “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the audited consolidated financial statements and notes thereto included under “Item 8. Consolidated Financial Statements and Supplementary Data” in this Annual Report on Form 10-K.

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Operating Data:	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014	Year Ended December 31, 2013
Income				
Interest income	\$ 30,722	\$ 27,712	\$ 26,497	\$ 6,228
Interest expense	7,808	5,983	4,307	867
Net interest income	22,914	21,729	22,190	5,361
Servicing fee income	7,579	1,719	—	—
Servicing costs	2,562	761	—	—
Net servicing income (loss)	5,017	958	—	—
Other income (loss)				
Realized gain (loss) on RMBS, net	1,399	854	(60)	(527)
Realized gain (loss) on investments in Excess MSRs, net	1,520	—	—	—
Realized gain (loss) on derivatives, net	(7,963)	(3,913)	(2,643)	59
Realized gain (loss) on acquired assets, net	—	449	—	—
Unrealized gain (loss) on derivatives, net	12,080	(59)	(6,564)	2,747
Unrealized gain (loss) on investments in Excess MSRs	249	(19)	(5,100)	14,894
Unrealized gain (loss) on investments in MSRs	(3,285)	(1,123)	—	—
Total Income	31,931	18,876	7,823	22,534
Expenses				
General and administrative expense	3,284	3,081	3,028	716
Management fee to affiliate	2,946	2,783	2,560	616
Total Expenses	6,230	5,864	5,588	1,332
Income (Loss) Before Income Taxes	25,701	13,012	2,235	21,202
Provision for corporate business taxes	458	(343)	(140)	—
Net Income (Loss)	25,243	13,355	2,375	21,202
Net (income) loss allocated to noncontrolling interests	(411)	(141)	(22)	(107)
Net Income (Loss) Applicable to Common Stockholders	\$ 24,832	\$ 13,214	\$ 2,353	\$ 21,095
Net income (Loss) Per Share of Common Stock				
Basic	\$ 3.31	\$ 1.76	\$ 0.31	\$ 12.50
Diluted	\$ 3.30	\$ 1.76	\$ 0.31	\$ 12.50
Weighted Average Number of Shares of Common Stock Outstanding				
Basic	7,512,444	7,509,543	7,505,546	1,688,275
Diluted	7,523,297	7,512,444	7,508,827	1,688,275
Dividends per share of Common Stock	\$ 2.11	\$ 1.98	\$ 2.03	\$ 0.45
Balance Sheet Data:				
RMBS, available-for-sale	\$ 671,904	\$ 508,242	\$ 416,003	\$ 286,979
Investments in Servicing Related Assets at fair value	61,263	97,803	91,322	110,306
Total Assets	792,878	636,340	531,926	427,398
Repurchase agreements	594,615	385,560	362,126	261,302
Federal Home Loan Bank advances	—	62,250	—	—
Derivative liabilities	694	4,595	4,088	592
Notes payable	22,886	24,313	—	—
Dividends payable	4,816	3,684	3,830	3,375
Total Liabilities	636,869	484,003	371,608	266,276
Total Stockholders' Equity	156,009	152,337	160,318	161,122

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

The following discussion and analysis should be read in conjunction with our audited consolidated financial statements and the accompanying notes included in “Item 8. Consolidated Financial Statements and Supplementary Data” of this Annual Report on Form 10-K.

All currency amounts are presented in thousands, except per share amounts or otherwise noted.

General

We are a public residential real estate finance company focused on acquiring, investing in and managing residential mortgage assets in the United States. We were incorporated in Maryland on October 31, 2012, and we commenced operations on or about October 9, 2013 following the completion of our IPO and a concurrent private placement. Our common stock is listed and traded on the New York Stock Exchange under the symbol “CHMI.” We are externally managed by our Manager, an SEC-registered investment adviser and a related party of Freedom Mortgage.

Our principal objective is to generate attractive current yields and risk-adjusted total returns for our stockholders over the long term, primarily through dividend distributions and secondarily through capital appreciation. We attempt to attain this objective by selectively constructing and actively managing a portfolio of Servicing Related Assets and RMBS, and subject to market conditions, other cash flowing residential mortgage assets.

We are subject to the risks involved with real estate and real estate-related debt instruments. These include, among others, the risks normally associated with changes in the general economic climate, changes in the mortgage market, changes in tax laws, interest rate levels, and the availability of financing.

We elected to be treated as a REIT under the Code commencing with our short taxable year ended December 31, 2013. We operate so as to continue to qualify to be taxed as a REIT. Our asset acquisition strategy focuses on acquiring a diversified portfolio of residential mortgage assets that balances the risk and reward opportunities our Manager observes in the marketplace. Since our IPO we have been, and we currently intend to continue as, a servicing-centric REIT with a substantial portion of our equity capital allocated to Servicing Related Assets.

Prior to our acquisition of Aurora in May 2015, these assets were limited to Excess MSRs. The acquisition of Aurora included a portfolio of Fannie Mae and Freddie Mac MSRs with an aggregate UPB of approximately \$718.4 million as of May 29, 2015. Aurora subsequently acquired three additional portfolios of Fannie Mae and Freddie Mac MSRs with an aggregate UPB of approximately \$3.1 billion as of their respective closing dates. In November 2016, we agreed to sell to Freedom Mortgage all of the Excess MSRs it had previously sold to us. As part of that transaction, Aurora acquired a portfolio of Ginnie Mae MSRs with an aggregate UPB of approximately \$4.5 billion. See “Item 8. Consolidated Financial Statements – Note 19 – Subsequent Events.”

Aurora has the licenses necessary to service mortgage loans on a nationwide basis and is approved to service loans for Fannie Mae, Freddie Mac and Ginnie Mae.

In addition to Servicing Related Assets, we invest in whole pool Agency RMBS, primarily those backed by 30-, 20- and 15-year fixed rate mortgages (“FRMs”) that offer what we believe to be favorable prepayment and duration characteristics. We finance our RMBS with leverage, the amount of which will vary from time to time depending on the particular characteristics of our portfolio, the availability of financing and market conditions. We do not have a targeted leverage ratio for our RMBS. Our borrowings for RMBS consist of short-term borrowings under master repurchase agreements. During the second half of 2015, we also used advances from the FHLBI to finance our Agency RMBS. We have also invested in Agency CMOs consisting of interest-only securities as well as risk-sharing securities issued by Fannie Mae and Freddie Mac.

In January 2016, the FHFA released a final rule that amends regulations governing membership in the Federal Home Loan Bank (“FHLB”) system. The final rule, which largely adopts the provisions included in the proposed rule issued by the FHFA in September 2014, prevents captive insurance companies from obtaining and maintaining membership in the FHLB system and, consequently, accessing low-cost funding through the FHLB system. The final rule became effective on February 19, 2016. As a result of this rule, CHMI Insurance, our captive insurance subsidiary, terminated its membership in the FHLBI in November and was dissolved in December 2016.

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Subject to maintaining our qualification as a REIT, we utilize derivative financial instruments (or hedging instruments) to hedge our exposure to potential interest rate mismatches between the interest we earn on our assets and our borrowing costs caused by fluctuations in short-term interest rates. In utilizing leverage and interest rate hedges, our objectives include, where desirable, locking in, on a long-term basis, a spread between the yield on our assets and the cost of our financing in an effort to improve returns to our stockholders.

We also operate our business in a manner that permits us to maintain our exclusion from registration as an investment company under the Investment Company Act.

Factors Impacting our Operating Results

Our income is generated primarily by the net spread between the income we earn on our assets and the cost of our financing and hedging activities as well as the amortization of any purchase premiums or the accretion of discounts. Our net income includes the actual interest payments we receive on our Excess MSR, if any, and RMBS, the net servicing fee we receive on our MSR and the accretion/amortization of any purchase discounts/premiums. Changes in various factors such as market interest rates, prepayment speeds, estimated future cash flows, servicing costs and credit quality could affect the amount of premium to be amortized or discount to be accreted into interest income for a given period. Market interest rates and prepayment rates vary according to the type of investment, conditions in the financial markets, competition and other factors, none of which can be predicted with any certainty. Our operating results may also be affected by credit losses in excess of initial anticipations or unanticipated credit events experienced by borrowers whose mortgage loans underlay the MSR held by Aurora.

Set forth below is the positive gross spread between the yield on RMBS and our costs of funding those assets at the end of each of the quarters indicated below:

Average Net Yield Spread at Period End

Quarter Ended	Average Asset Yield	Average Cost of Funds	Average Net Interest Rate Spread
December 31, 2016	3.43%	1.49%	1.94%
September 30, 2016	3.46%	1.44%	2.02%
June 30, 2016	3.39%	1.62%	1.77%
March 31, 2016	3.56%	1.70%	1.86%
December 31, 2015	3.60%	1.89%	1.71%
September 30, 2015	3.01%	1.93%	1.08%
June 30, 2015	3.63%	1.96%	1.67%
March 31, 2015	3.83%	1.92%	1.91%
December 31, 2014	3.70%	1.99%	1.71%
September 30, 2014	3.61%	2.00%	1.61%
June 30, 2014	3.62%	2.00%	1.62%
March 31, 2014	3.56%	2.10%	1.46%

The average net interest spread has fluctuated but risen over the past two years. During that time, we have strategically taken the opportunity to reduce our Average Cost of Funds by restructuring our swaps portfolio as interest rates declined. The new positioning helped to partially offset increased repurchase rates charged by our counterparties in anticipation of increases in the federal funds rate.

Changes in the Market Value of Our Assets

We hold our Servicing Related Assets as long-term investments. Our Excess MSR, and our MSR, are carried at their fair value with changes in their fair value recorded in other income or loss in our consolidated statements of operations. Those values may be affected by events or headlines that are outside of our control, such as Brexit, other events impacting the U.S. or global economy generally or the U.S. residential market specifically, and events or headlines impacting the parties with which we do business. See "Item 1A. Risk Factors – Risks Related to our Business."

Our RMBS are carried at their fair value, as available-for-sale in accordance with ASC 320, *Accounting for Certain Investments in Debt or Equity Securities*, with changes in fair value recorded through accumulated other

comprehensive income (loss), a component of stockholders' equity. As a result, we do not expect that changes in the market value of our RMBS will normally impact our operating results, but such changes will affect our book value. However, at least on a quarterly basis, we assess both our ability and intent to continue to hold our RMBS as long-term investments. As part of this process, we monitor our RMBS for other-than-temporary impairment. A change in our ability and/or intent to continue to hold any of our RMBS could result in our recognizing an impairment charge or realizing losses while holding these assets.

Impact of Changes in Market Interest Rates on Our Assets

The value of our assets may be affected by prepayment rates on mortgage loans. Prepayment speed is the measurement of how quickly borrowers pay down the UPB of their loans or how quickly loans are otherwise liquidated or charged off. Generally, in a declining interest rate environment, prepayment speeds tend to increase. Conversely, in an increasing interest rate environment, prepayment speeds tend to decrease. When we acquire Servicing Related Assets or RMBS, we anticipate that the underlying mortgage loans will prepay at a projected rate generating an expected cash flow (in the case of Servicing Related Assets) and yield. If we purchase assets at a premium to par value and borrowers prepay their mortgage loans faster than expected, the corresponding prepayments on our assets may reduce the expected yield on such assets because we will have to amortize the related premium on an accelerated basis. Similarly, if we purchase assets at a discount to par value, and borrowers prepay their mortgage loans slower than expected, the decrease in corresponding prepayments may reduce the expected yield on assets because we will not be able to accrete the related discount as quickly as originally anticipated.

If prepayment speeds are significantly greater than expected, the carrying value of the Servicing Related Assets could exceed their estimated fair value. If the fair value of the Servicing Related Assets decreases, we would be required to record a non-cash charge, which would have a negative impact on our financial results. Furthermore, a significant increase in prepayment speeds could materially reduce the ultimate cash flows we receive from the Servicing Related Assets, and we could ultimately receive substantially less than what we paid for such assets. We do not utilize derivatives to hedge against changes in the fair value of the Servicing Related Assets. Our balance sheet, results of operations and cash flows are susceptible to significant volatility due to changes in the fair value of, or cash flows from, the Servicing Related Assets as interest rates change.

A slower than anticipated rate of prepayment also will cause the life of the related RMBS to extend beyond that which was projected. As a result we would have a lower yielding asset for a longer period of time. In addition, if we have hedged our interest rate risk, extension may cause the security to be outstanding longer than the related hedge thereby reducing the protection intended to be provided by the hedge.

Voluntary and involuntary prepayment rates may be affected by a number of factors including, but not limited to, the availability of mortgage credit, the relative economic vitality of the area in which the related properties are located, the servicing of the mortgage loans, possible changes in tax laws, other opportunities for investment, homeowner mobility and other economic, social, geographic, demographic and legal factors, none of which can be predicted with any certainty.

We attempted to reduce the exposure of our Excess MSRs to voluntary prepayments through the structuring of our recapture agreements with Freedom Mortgage. With the sale of our Excess MSRs to Freedom Mortgage in November 2016 and February 2017, these arrangements were terminated. In June 2016, Aurora entered into a joint marketing recapture agreement with Freedom Mortgage. Pursuant to this agreement, Freedom Mortgage will attempt to refinance certain mortgage loans underlying Aurora's portfolio of Fannie Mae and Freddie Mac MSRs as directed by Aurora. If a loan is refinanced, Aurora will pay Freedom Mortgage a fee for its origination services. Freedom Mortgage will be entitled to sell the loan for its own benefit and will transfer the related MSR to Aurora. The agreement has an initial term of one year, subject to automatic renewals of one year each and subject to termination by either party upon 60 days prior notice. All new loans must qualify for sale to Fannie Mae or Freddie Mac and meet other conditions set forth in the agreement. As of December 31, 2016, Aurora received MSRs with an aggregate UPB of approximately \$9.8 million and paid fees of approximately \$21,000 to Freedom Mortgage under this program.

With respect to our business operations, increases in interest rates, in general, may over time cause:

- the interest expense associated with our borrowings to increase;
- the value of our assets to fluctuate;

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- the coupons on any adjustable-rate and hybrid RMBS we may own to reset, although on a delayed basis, to higher interest rates;
- prepayments on our RMBS to slow, thereby slowing the amortization of our purchase premiums and the accretion of our purchase discounts; and
- an increase in the value of any interest rate swap agreements we may enter into as part of our hedging strategy.

Conversely, decreases in interest rates, in general, may over time cause:

- prepayments on our RMBS to increase, thereby accelerating the amortization of our purchase premiums and the accretion of our purchase discounts;
- the interest expense associated with our borrowings to decrease;
- the value of our assets to fluctuate;
- to the extent we enter into interest rate swap agreements as part of our hedging strategy, the value of these agreements to decrease; and
- coupons on any adjustable-rate and hybrid RMBS assets we may own to reset, although on a delayed basis, to lower interest rates.

Effects of Spreads on our Assets

The spread between the yield on our assets and our funding costs affects the performance of our business. Wider spreads imply greater income on new asset purchases but may have a negative impact on our stated book value. Wider spreads may also negatively impact asset prices. In an environment where spreads are widening, counterparties may require additional collateral to secure borrowings which may require us to reduce leverage by selling assets. Conversely, tighter spreads imply lower income on new asset purchases but may have a positive impact on stated book value of our existing assets. In this case we may be able to reduce the amount of collateral required to secure borrowings.

Credit Risk

We are subject to varying degrees of credit risk in connection with our assets. Although we expect relatively low credit risk with respect to our portfolio of Agency RMBS, we are subject to the credit risk of the borrowers under the loans for which we hold MSR. Through loan level due diligence, we attempt to mitigate this risk by seeking to acquire high quality assets at appropriate prices given anticipated and unanticipated losses. We also conduct ongoing monitoring of acquired assets. Nevertheless, unanticipated credit losses could occur which could adversely impact our operating results.

Sale of Excess MSRs

In November 2016, we agreed to sell to Freedom Mortgage the Excess MSRs it had previously sold to us. The sale occurred in two steps: the first part of the sale was closed in November for cash. The second part of the sale closed in February 2017. In that part of the sale, we exchanged the remaining Excess MSRs for a portfolio of MSRs on loans backing securities guaranteed by Ginnie Mae. As previously disclosed, the total gain on the sale is approximately \$15 million. However, only approximately \$6.6 million of the gain was recognized in the fourth quarter of 2016 which, after adjustment for previous unrealized losses on Pool 1 and Pool 2014 of approximately \$2.6 million and an adjustment to interest income from the retrospective method of amortization of approximately \$2.4 million, netted a realized gain of approximately \$1.5 million. The balance of the gain on sale will be recognized in the first quarter of 2017. In addition, due to the increase in market interest rates subsequent to our identification of particular MSRs that were exchanged for the second part of the Excess MSRs, and assuming that those market interest rates remain at or above the levels on the date of filing of this report, we anticipate that the value of those MSRs will be significantly higher at March 31, 2017. As a result of the impact of these two factors on the calculation of book value, and assuming that the impact of all other factors affecting book value remains relatively similar to the impact at December 31, 2016, we anticipate that our book value per share at March 31, 2017, will be meaningfully higher than it was at December 31, 2016.

Critical Accounting Policies and Use of Estimates

Our financial statements are prepared in accordance with U.S. GAAP, which requires the use of estimates that involve the exercise of judgment and the use of assumptions as to future uncertainties. In accordance with SEC guidance, the following discussion addresses the accounting policies that we apply with respect to our operations. Our most critical accounting policies involve decisions and assessments that could affect our reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, as well as our reported amounts of revenues and expenses. We believe that all of the decisions and assessments upon which our financial statements are based were reasonable at the time made and based upon information available to us at that time. Our critical accounting policies and accounting estimates may be expanded over time as we diversify our portfolio. The material accounting policies and estimates that we expect to be most critical to an investor's understanding of our financial results and condition and require complex management judgment are discussed below.

Classification of Investment Securities and Impairment of Financial Instruments

ASC 320-10, Debt and Equity Securities, requires that at the time of purchase, we designate a security as either trading, available-for-sale, or held-to-maturity depending on our ability and intent to hold such security to maturity. Securities available-for-sale will be reported at fair value, while securities held-to-maturity will be reported at amortized cost. Although we may hold most of our securities until maturity, we may, from time to time, sell any of our securities as part of our overall management of our asset portfolio. Accordingly, we elect to classify substantially all of our securities as available-for-sale. All assets classified as available-for-sale will be reported at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity. See "—Valuation of Financial Instruments."

When the estimated fair value of a security is less than amortized cost, we consider whether there is an other-than-temporary impairment, or OTTI, in the value of the security. An impairment is deemed an OTTI if (i) we intend to sell the security, (ii) it is more likely than not that we will be required to sell the security before recovering our cost basis, or (iii) we do not expect to recover the entire amortized cost basis of the security even if we do not intend to sell the security or believe it is more likely than not that we will be required to sell the security before recovering our cost basis. If the impairment is deemed to be an OTTI, the resulting accounting treatment depends on the factors causing the OTTI. If the OTTI has resulted from (i) our intention to sell the security, or (ii) our judgment that it is more likely than not that we will be required to sell the security before recovering our cost basis, an impairment loss is recognized in current earnings equal to the difference between our amortized cost basis and fair value. Whereas, if the OTTI has resulted from our conclusion that we will not recover our cost basis even if we do not intend to sell the security, the credit loss portion of the impairment is recorded in current earnings and the portion of the loss related to other factors, such as changes in interest rates, continues to be recognized in accumulated other comprehensive income (loss). Determining whether there is an OTTI may require management to exercise significant judgment and make significant assumptions, including, but not limited to, estimated cash flows, estimated prepayments, loss assumptions, and assumptions regarding changes in interest rates. As a result, actual impairment losses could differ from reported amounts. Such judgments and assumptions are based upon a number of factors, including (i) credit of the issuer or the borrower, (ii) credit rating of the security, (iii) key terms of the security, (iv) performance of the loan or underlying loans, including debt service coverage and loan-to-value ratios, (v) the value of the collateral for the loan or underlying loans, (vi) the effect of local, industry, and broader economic factors, and (vii) the historical and anticipated trends in defaults and loss severities for similar securities.

Valuation of Financial Instruments

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

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

- Level 1 Inputs are quoted prices in active markets for identical assets or liabilities as of the measurement date under current market conditions. Additionally, the entity must have the ability to access the active market and the quoted prices cannot be adjusted by the entity.
- Level 2 Inputs include quoted prices in active markets for similar assets or liabilities; quoted prices in inactive markets for identical or similar assets or liabilities; or inputs that are observable or can be corroborated by observable market data by correlation or other means for substantially the full-term of the assets or liabilities.
- Level 3 Unobservable inputs are supported by little or no market activity. The unobservable inputs represent the assumptions that market participants would use to price the assets and liabilities, including risk. Generally, Level 3 assets and liabilities are valued using pricing models, discounted cash flow methodologies, or similar techniques that require significant judgment or estimation.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety. We have used Level 2 for our RMBS and for our derivative assets and liabilities and Level 3 for our Servicing Related Assets.

When available, we use quoted market prices to determine the fair value of an asset or liability. If quoted market prices are not available, we will consult independent pricing services or third party broker quotes, provided that there is no ongoing material event that affects the issuer of the securities being valued or the market. If there is such an ongoing event, or if quoted market prices are not available, we will determine the fair value of the securities using valuation techniques that use, when possible, current market-based or independently-sourced market parameters, such as interest rates.

Investments in Excess MSR

Upon acquisition, we elected to record our investments in Excess MSR at fair value. We made this election in order to provide the users of the financial statements with better information regarding the effects of prepayment risk and other market factors on the Excess MSR. Under this election, we record a valuation adjustment on our Excess MSR investments on a quarterly basis to recognize the changes in fair value in net income as described in “—Revenue Recognition on Investments in Excess MSR” below.

The fair values of Excess MSR are determined by projecting net servicing cash flows, which are then discounted to estimate the fair value. The fair values of Excess MSR are impacted by a variety of factors, including prepayment assumptions, discount rates, delinquency rates, contractually specified servicing fees, and underlying portfolio characteristics. The underlying assumptions and estimated values are corroborated by values received from independent third parties. Changes in fair value of our Excess MSR are reported in other income or loss in our consolidated statements of income. For additional information on our fair value methodology, see “Item 8. Consolidated Financial Statements and Supplementary Data—Note 9. Fair Value.”

Revenue Recognition on Investments in Excess MSR

Investments in Excess MSR are aggregated into pools as applicable and each pool of Excess MSR is accounted for in the aggregate. Income for Excess MSR is accreted into income on an effective yield or “interest” method, based upon the expected excess servicing amount through the expected life of the underlying mortgages. Changes to expected cash flows result in a cumulative retrospective adjustment, which will be recorded in the period in which the change in expected cash flows occurs. Under the retrospective method, the income recognized for a reporting period is measured as the difference between the amortized cost basis at the end of the period and the amortized cost basis at the beginning of the period, plus any cash received during the period. The amortized cost basis is calculated as the present value of estimated future cash flows using an effective yield, which is the yield that equates all past actual and current estimated future cash flows to the initial investment. The difference between the fair value of Excess MSR and their amortized cost basis are recorded as “Unrealized gain (loss) on investments in excess mortgage servicing rights.” Fair value is generally determined by discounting the expected future cash flows using discount rates that incorporate the market risks and liquidity premium specific to the Excess MSR, and therefore may differ from their effective yields.

Investments in MSRs

The Company has elected the fair value option to record its investments in MSRs in order to provide users of the consolidated financial statements with better information regarding the effects of prepayment risk and other market factors on the MSRs. Under this election, the Company records a valuation adjustment on its investments in MSRs on a quarterly basis to recognize the changes in fair value in net income as described below. The Company's MSRs represent the right to service mortgage loans. As an owner and manager of MSRs, the Company may be obligated to fund advances of principal and interest payments due to third-party owners of the loans, but not yet received from the individual borrowers. These advances are reported as servicing advances within the "Receivables and other assets" line item on the consolidated balance sheets. MSRs are reported at fair value on the consolidated balance sheets. Although transactions in MSRs are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels, costs to service and discount rates). Changes in the fair value of MSRs as well as servicing fee income and servicing expenses are reported on the consolidated statements of income. In determining the valuation of MSRs, management used internally developed models that are primarily based on observable market-based inputs but which also include unobservable market data inputs. See "Item 8. Consolidated Financial Statements - Note 9—Fair Value."

Revenue Recognition on Investments in MSRs

Mortgage servicing fee income represents revenue earned for servicing mortgage loans. The servicing fees are based on a contractual percentage of the outstanding principal balance and recognized as revenue as the related mortgage payments are collected. Corresponding costs to service are charged to expense as incurred. Approximately \$1.5 million and \$800,000 in reimbursable servicing advances were receivable at December 31, 2016 and 2015, respectively, and have been classified within "Receivables and other assets" on the consolidated balance sheets.

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

Revenue Recognition on Securities

Interest income from coupon payments is accrued based on the outstanding principal amount of the RMBS and their contractual terms. Premiums and discounts associated with the purchase of the RMBS are amortized into interest income over the projected lives of the securities using the interest method. Our policy for estimating prepayment speeds for calculating the effective yield is to evaluate historical performance, consensus prepayment speeds, and current market conditions. Adjustments are made for actual prepayment activity.

Repurchase Transactions

We finance the acquisition of our RMBS for our portfolio through repurchase transactions under master repurchase agreements. Repurchase transactions are treated as collateralized financing transactions and are carried at their contractual amounts as specified in the respective transactions. Accrued interest payable is included in "Accrued expense and other liabilities" on the consolidated balance sheets.

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Securities financed through repurchase transactions remain on our consolidated balance sheets as an asset and cash received from the purchaser is recorded on our consolidated balance sheets as a liability. Interest paid in accordance with repurchase transactions is recorded in interest expense.

Income Taxes

The Company elected to be taxed as a REIT under the Code commencing with its short taxable year ended December 31, 2013. The Company expects to continue to qualify to be treated as a REIT. As long as the Company qualifies as a REIT, the Company generally will not be subject to U.S. federal income taxes on its taxable income to the extent it annually distributes at least 90% of its REIT taxable income to stockholders and does not engage in prohibited transactions. The Company's taxable REIT subsidiaries ("TRSs"), Solutions and Aurora, are subject to U.S. federal income taxes on their taxable income.

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

Emerging Growth Company Status

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

Results of Operations

Presented below is a comparison of the Company's results of operations for the periods indicated (dollars in thousands):

Results of Operations

	Year Ended December 31,		
	2016	2015	2014
Income			
Interest income	\$ 30,722	\$ 27,712	\$ 26,497
Interest expense	7,808	5,983	4,307
Net Interest Income	22,914	21,729	22,190
Servicing fee income	7,579	1,719	—
Servicing costs	2,562	761	—
Net servicing income	5,017	958	—
Other Income (Loss)			
Realize gain (loss) on RMBS, net	1,399	854	(60)
Realized gain (loss) on investments in Excess MSRs, net	1,520	—	—
Realized gain (loss) on derivatives, net	(7,963)	(3,913)	(2,643)
Realized gain (loss) on acquired assets, net	—	449	—
Unrealized gain (loss) on derivatives, net	12,080	(59)	(6,564)
Unrealized gain (loss) on Excess MSRs	249	(19)	(5,100)
Unrealized gain (loss) on investments in MSRs	(3,285)	(1,123)	—
Total Income	31,931	18,876	7,823
Expenses			
General and administrative expense	3,284	3,081	3,028
Management fee to affiliate	2,946	2,783	2,560
Total Expenses	6,230	5,864	5,588
Income (Loss) Before Income Taxes	25,701	13,012	2,235
(Benefit from) provision for corporate business taxes	458	(343)	(140)
Net Income (Loss)	25,243	13,355	2,375
Net income allocated to LTIP - OP Units	(411)	(141)	(22)
Net income (loss) Applicable to Common Stockholders	\$ 24,832	\$ 13,214	\$ 2,353

Presented below is summary financial data on our segments together with a reconciliation to the same data for the Company as a whole, for the periods indicated (dollars in thousands):

Segment Summary Data

	For			
	Year Ended December 31, 2016			
	Servicing Related Assets	RMBS	All Other	Total
Interest income	\$ 14,129	\$ 16,593	\$ —	\$ 30,722
Interest expense	1,371	6,437	—	7,808
Net interest income	12,758	10,156	—	22,914
Servicing fee income	7,579	—	—	7,579
Servicing costs	2,562	—	—	2,562
Net servicing income	5,017	—	—	5,017
Other income	(1,516)	5,516	—	4,000
Other operating expenses	—	—	6,230	6,230
Corporate business taxes	458	—	—	458
Net income (loss)	\$ 15,801	\$ 15,672	\$ (6,230)	\$ 25,243

	Year Ended December 31, 2015			
	Servicing Related Assets	RMBS	All Other	Total
Interest income	\$ 14,313	\$ 13,399	\$ —	\$ 27,712
Interest expense	583	5,400	—	5,983
Net interest income	13,730	7,999	—	21,729
Servicing fee income	1,719	—	—	1,719
Servicing costs	761	—	—	761
Net servicing income	958	—	—	958
Other income	(693)	(3,118)	—	(3,811)
Other operating expenses	—	—	5,864	5,864
Corporate business taxes	(343)	—	—	(343)
Net income (loss)	\$ 14,338	\$ 4,881	\$ (5,864)	\$ 13,355

	Year Ended December 31, 2014			
	Servicing Related Assets	RMBS	All Other	Total
Interest income	\$ 15,854	\$ 10,643	\$ —	\$ 26,497
Interest expense	—	4,307	—	4,307
Net interest income	15,854	6,336	—	22,190
Servicing fee income	—	—	—	—
Servicing costs	—	—	—	—
Net servicing income	—	—	—	—
Other income	(5,100)	(9,267)	—	(14,367)
Other operating expenses	—	—	5,588	5,588
Corporate business taxes	(140)	—	—	(140)
Net income (loss)	\$ 10,894	\$ (2,931)	\$ (5,588)	\$ 2,375

Interest Income

Interest income for the year ended December 31, 2016, was \$30.7 million as compared to \$27.7 million for the year ended December 31, 2015, after giving effect for the estimated “catch up” premium amortization (benefit) cost of approximately \$2.4 million and approximately \$1.9 million, respectively. The \$3.0 million increase in interest income was comprised of a decrease of approximately \$200,000 in Servicing Related Assets and an increase of approximately \$3.2 million in RMBS.

Interest Expense

Interest expense for the year ended December 31, 2016, was \$7.8 million as compared to \$6.0 million for the year ended December 31, 2015. The \$1.8 million increase was comprised of approximately \$800,000 from Servicing Related Assets and approximately \$1.0 million from RMBS. The changes were primarily due to additional repurchase agreement borrowings and an overall increase in repurchase rates offset by a lower swap cost.

Change in Fair Value of Investments in Servicing Related Assets

The fair value of our investments in Servicing Related Assets for the year ended December 31, 2016, decreased by approximately \$3.0 million. The decrease was a function of (i) only a modest increase in the value of our investments in Excess MSR, which consisted of only Excess MSR Pool 2 at year end, of approximately \$249,000 for the year ended December 31, 2016 as compared to an increase of approximately \$2.3 million for the year ended December 31, 2015 and (ii) a larger decrease in the fair value of our investments in MSR of approximately \$3.3 million for the year ended December 31, 2016, as compared to a decrease of approximately \$1.1 million for the year ended December 31, 2015.

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Change in Fair Value of Derivatives

The fair value of derivatives at December 31, 2016 increased by approximately \$12.1 million from December 31, 2015, primarily due to changes in interest rates.

General and Administrative Expense

General and administrative expense for the year ended December 31, 2016 increased by approximately \$200,000 from the year ended December 31, 2015, primarily due to the addition of Aurora and associated costs.

Management Fees to Affiliate

Management fees for the year ended December 31, 2016 increased by approximately \$160,000 from the year ended December 31, 2015, primarily due to an increase in book value and additional pass through costs.

Net Income Allocated to LTIP - OP Units

Net income allocated to LTIP—OP Units which are owned by directors and officers of the Company and by certain employees of Freedom Mortgage who provide services to us through the Manager, represents approximately 1.9% of net income for the year ended December 31, 2016.

Accumulated Other Comprehensive Income (Loss)

Set forth below are the changes in our accumulated other comprehensive income (loss) for the periods indicated below (dollars in thousands):

	<u>Year Ended December 31, 2016</u>
Accumulated other comprehensive gain (loss), December 31, 2015	\$ (197)
Other comprehensive income (loss)	(6,196)
Accumulated other comprehensive gain (loss), December 31, 2016	\$ (6,393)
	<u>Year Ended December 31, 2015</u>
Accumulated other comprehensive gain (loss), December 31, 2014	\$ 6,641
Other comprehensive income (loss)	(6,838)
Accumulated other comprehensive gain (loss), December 31, 2015	\$ (197)
	<u>Year Ended December 31, 2014</u>
Accumulated other comprehensive gain (loss), December 31, 2013	\$ (5,033)
Other comprehensive income (loss)	11,674
Accumulated other comprehensive gain (loss), December 31, 2014	\$ 6,641

Our GAAP equity changes as the values of our RMBS are marked to market each quarter, among other factors. The primary causes of mark to market changes are changes in interest rates and credit spreads. During the year ended December 31, 2016, a 21 basis point increase in the 10 Year US Treasury rate caused a net unrealized loss on our RMBS of approximately \$6.2 million, recorded in accumulated other comprehensive income (loss).

Non-GAAP Financial Measures

This Management's Discussion and Analysis of Financial Condition and Results of Operations section contains analysis and discussion of non-GAAP measurements. The non-GAAP measurements include the following:

- core earnings

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- core earnings per average common share;

Core earnings is a non-GAAP financial measure and is defined by the Company as GAAP net income (loss) applicable to common stockholders, excluding realized gain (loss) on RMBS, realized and unrealized (gain) loss on investments in Excess MSRs and MSRs realized and unrealized gain (loss) on derivatives, realized (gain) loss on acquired assets, and changes in fair value of MSRs primarily due to realization of expected cashflows (runoff). MSRs are adjusted to exclude outstanding LTIP-OP units in our Operating Partnership. Additionally, core earnings excludes (i) any tax (benefit) expense on unrealized (gain) loss on MSRs and (ii) any estimated catch up premium authorization (benefit) cost due to the use of current rather than historical estimates of constant prepayment rates for amortization of Excess MSRs. Core earnings are provided for purposes of comparability to other issuers that invest in residential mortgage-related assets. The Company believes providing investors with core earnings, in addition to related GAAP financial measures, gives investors greater transparency into the Company's ongoing operational performance. The concept of core earnings does have significant limitations, including the exclusion of realized and unrealized gains (losses), and may not be comparable to similarly-titled measures of other peers, which may use different calculations. As a result, core earnings should not be considered a substitute for the Company's GAAP net income (loss) or as a measure of the Company's liquidity.

Core Earnings Summary

Core earnings for the year ended December 31, 2016, as compared to the year ended December 31, 2015, increased by approximately \$1.7 million, or \$0.23 per average common share due to short term strategic trades which we do not expect to continue.

The following table provides GAAP measures of net income (loss) and details with respect to reconciling the aforementioned line items to core earnings and related per average common share amounts, for the periods indicated (dollars in thousands):

	Year Ended December 31,		
	2016	2015	2014
Net income (loss)	\$ 25,243	\$ 13,355	\$ 2,375
Realized (gain) loss on RMBS, net	(1,399)	(854)	60
Realized (gain) loss on investments in Excess MSRs, net	(1,520)	—	—
Realized (gain) loss on derivatives, net	7,963	3,913	2,643
Realized (gain) loss on acquired assets, net	—	(449)	—
Unrealized (gain) loss on derivatives, net	(12,080)	59	6,564
Unrealized (gain) loss on investments in Excess MSRs	(249)	19	5,100
Unrealized (gain) loss on investments in MSRs	3,285	1,123	—
Tax (benefit) expense on unrealized (gain) loss on MSRs	862	—	—
Estimated "catch up" premium amortization (benefit) cost	(2,358)	(1,862)	(1,536)
Changes due to realization of expected cash flows	(3,512)	(430)	—
Reversal of (gain) loss on acquired assets, net	244	—	—
Yield maintenance income	250	—	—
Total core earnings:	\$ 16,729	\$ 14,874	\$ 15,206
Core earnings attributable to noncontrolling interests	(272)	(157)	(111)
Core Earnings Attributable to Common Stockholders	\$ 16,457	\$ 14,717	\$ 15,095
Core Earnings Attributable to Common Stockholders, per Share	\$ 2.19	\$ 1.96	\$ 2.01
GAAP Net income (Loss) Per Share of Common Stock	\$ 3.31	\$ 1.76	\$ 0.31

(A) Certain prior period amounts have been reclassified to conform to current period presentation.

Our Portfolio

Excess MSRs

As of December 31, 2016 and December 31, 2015, we had approximately \$29.4 million and \$78.0 million, respectively, of estimated carrying value of Excess MSRs. The remaining Excess MSRs were sold to Freedom

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Mortgage on February 1, 2017. See “Item 8. Consolidated Financial Statements—Note 7—Transactions with Affiliates and Affiliated Entities and Note 19 Subsequent Events.”

Our investments represent between a 50% and 85% interest in the Excess MSR on three pools (as of December 31, 2015) and one pool (as of December 31, 2016) of mortgage loans with an aggregate UPB at December 31, 2016 and December 31, 2015, of approximately \$6.0 billion and \$15.0 billion, respectively. Freedom Mortgage is the servicer of the loans underlying these Excess MSRs, and it earns a basic fee and all ancillary income associated with the portfolios in exchange for providing all servicing functions. In addition, Freedom Mortgage retains the remaining interest in the Excess MSRs. We do not have any servicing duties, liabilities or obligations associated with the servicing of the portfolios underlying these Excess MSRs. These investments in Excess MSRs were subject to recapture agreements with Freedom Mortgage which have been terminated in connection with the sales described above. Under the recapture agreements, we are generally entitled to our percentage interest in the Excess MSRs on any initial or subsequent refinancing by Freedom Mortgage of a loan in the original portfolio. In other words, we are generally entitled to our percentage interest in the Excess MSRs on both (i) a loan resulting from a refinancing by Freedom Mortgage of a loan in the original portfolio, and (ii) a loan resulting from a refinancing by Freedom Mortgage of a previously recaptured loan.

Upon completion of our IPO and the concurrent private placement, we entered into two separate Excess MSR acquisition and recapture agreements with Freedom Mortgage related to our investments in Excess MSRs. We also entered into a flow and bulk purchase agreement related to future purchases of Excess MSRs from Freedom Mortgage. In three separate transactions in 2014, we purchased from Freedom Mortgage Excess MSRs on mortgage loans with an aggregate UPB of approximately \$334.7 million. We acquired an interest between 71% and 85% in the Excess MSRs for an aggregate purchase price of approximately \$2.174 million. The terms of the purchase include recapture provisions that are the same as those in the Excess MSR acquisition agreements we entered into with Freedom Mortgage in October 2013.

The mortgage loans underlying the Excess MSRs purchased in 2014 are collectively referred to as “Pool 2014,” and the recapture provisions, which are identical, are collectively referred to as the “Pool 2014—Recapture Agreement.”

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The following tables summarize the collateral characteristics of the loans underlying our Excess MSR investments as of the dates indicated (dollars in thousands):

Excess MSR Collateral Characteristics

As of December 31, 2016

	Collateral Characteristics							Weighted Average Loan Age (months)	ARMs % ^(A)
	Current Carrying Amount	Original Principal Balance	Current Principal Balance	Number of Loans	WA Coupon	WA Maturity (months)			
Excess MSR Pool 2									
Original Pool	12,734	10,704,024	3,695,561	26,338	2.58%	304	54	100.0%	
Recaptured Loans	15,792	—	2,357,581	15,051	3.56%	333	12	0.0%	
Recapture Agreement	866	—	—	—	—	—	—	—	
Excess MSR Pool 2 Total/WA	29,392	10,704,024	6,053,142	41,389	2.96%	315	38	61.1%	

As of December 31, 2015

	Collateral Characteristics							Weighted Average Loan Age (months)	ARMs % ^(A)
	Current Carrying Amount	Original Principal Balance	Current Principal Balance	Number of Loans	WA Coupon	WA Maturity (months)			
Excess MSR Pool 1									
Original Pool	\$38,633	\$ 10,026,722	\$ 6,865,916	37,204	3.49%	311	36	0.9%	
Recaptured Loans	4,204	—	550,549	2,834	3.77%	331	7	0.5%	
Recapture Agreement	645	—	—	—	—	—	—	—	
Excess MSR Pool 1 Total/WA	43,482	10,026,722	7,416,465	40,038	3.51%	312	34	0.8%	
Excess MSR Pool 2									
Original Pool	17,967	10,704,024	5,041,239	34,109	2.35%	318	41	100.0%	
Recaptured Loans	14,371	—	2,238,467	13,832	3.74%	342	9	0.1%	
Recapture Agreement	716	—	—	—	—	—	—	—	
Excess MSR Pool 2 Total/WA	33,054	10,704,024	7,279,706	47,941	2.78%	325	31	69.3%	
Excess MSR Pool 2014									
Original Pool	947	334,672	197,900	1,242	3.65%	327	30	0.0%	
Recaptured Loans	559	—	67,990	321	3.65%	335	9	0.0	
Recapture Agreement	—	—	—	—	—	—	—	—	
Excess MSR Pool 2014 Total/WA	1,506	334,672	265,890	1,563	3.65%	329	25	0.0	
Total/Weighted Average	\$78,042	\$ 21,065,418	\$ 14,962,061	89,542	3.16%	319	32	34.1%	

(A) ARM % represents the percentage of the total principal balance of the pool that corresponds to ARMs and hybrid ARMs.

MSRs

By virtue of our acquisition of Aurora on May 29, 2015, we acquired its portfolio of Fannie Mae and Freddie Mac MSRs. On October 30, 2015, Aurora acquired a portfolio of Fannie Mae and Freddie Mac MSRs with an aggregate UPB of approximately \$1.4 billion. On January 29, 2016, Aurora acquired a portfolio of MSRs on mortgage loans owned or securitized by Fannie Mae with an aggregate unpaid principal balance of approximately \$463 million. In addition, on June 30, 2016, Aurora acquired a portfolio of MSRs on mortgage loans owned or securitized by Fannie Mae with an aggregate unpaid principal balance of approximately \$1.3 billion. The following tables set forth certain characteristics of the mortgage loans underlying those MSRs as of the dates indicated (dollars in thousands):

MSR Collateral Characteristics

As of December 31, 2016

	Collateral Characteristics						
	Current Carrying Amount	Current Principal Balance	WA Coupon	WA Servicing Fee	WA Maturity (months)	Weighted Average Loan Age (months)	ARMs % ^(A)
MSRs							
Conventional	\$ 31,871	\$ 3,262,181	3.81%	0.25%	284	31	0.2%
MSR Total/WA	31,871	3,262,181	3.81%	0.25%	284	31	0.2%

As of December 31, 2015

	Collateral Characteristics						
	Current Carrying Amount	Current Principal Balance	WA Coupon	WA Servicing Fee	WA Maturity (months)	Weighted Average Loan Age (months)	ARMs % ^(A)
MSRs							
Conventional	\$ 19,761	\$ 2,016,351	3.76%	0.25%	273	31	0.2%
MSR Total/WA	19,761	2,016,351	3.76%	0.25%	273	31	0.2%

(A) ARMs % represents the percentage of the total principal balance of the pool that corresponds to ARMs and hybrid ARMs.

RMBS

The following tables summarize the characteristics of our RMBS portfolio and certain characteristics of the collateral underlying our RMBS as of the dates indicated (dollars in thousands):

RMBS Characteristics

As of December 31, 2016

Asset Type	Original Face Value	Book Value	Gross Unrealized			Number of Securities	Weighted Average			Maturity (Years) (D)
			Gains	Losses	Carrying Value ^(A)		Rating	Coupon	Yield ^(C)	
RMBS										
Fannie Mae	\$493,645	\$454,012	\$1,517	\$(6,592)	\$448,937	68	(B)	3.74%	3.32%	24
Freddie Mac	222,469	200,207	587	(2,691)	198,103	27	(B)	3.62%	3.47%	26
CMOs	34,596	24,086	857	(79)	24,864	9	Unrated	4.78%	5.04%	12
Total/Weighted Average	\$750,710	\$678,305	\$2,961	\$(9,362)	\$671,904	104		3.74%	3.43%	24

As of December 31, 2015

Asset Type	Original Face Value	Book Value	Gross Unrealized		Carrying Value ^(A)	Number of Securities	Weighted Average			Maturity (Years) (D)
			Gains	Losses			Rating	Coupon	Yield ^(C)	
RMBS										
Fannie Mae	\$329,767	\$308,367	\$1,961	\$(1,556)	\$308,772	44	(B)	3.77%	3.59%	24
Freddie Mac	208,154	193,567	821	(977)	193,411	24	(B)	3.61%	3.48%	24
CMOs	16,646	6,493	—	(434)	6,059	4	Unrated	4.55%	7.39%	10
Total/Weighted Average	\$554,567	\$508,427	\$2,782	\$(2,967)	\$508,242	72		3.72%	3.60%	23

(A) See “Item 8. Consolidated Financial Statements and Supplementary Data—Note 9. Fair Value” regarding the estimation of fair value, which is equal to carrying value for all securities.

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

(C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the Book Value. Prior period amounts have been reclassified to conform to current period presentation.

(D) The weighted average maturity is based on the timing of expected principal reduction on the assets.

The following table summarizes the net interest spread of our RMBS portfolio as of the dates indicated:

Net Interest Spread

	December 31, 2016	December 31, 2015	December 31, 2014
Weighted Average Asset Yield	3.22%	2.61%	3.05%
Weighted Average Interest Expense	1.56%	1.15%	1.39%
Net Interest Spread	1.66%	1.46%	1.66%

Liquidity and Capital Resources

Liquidity is a measurement of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund and maintain investments and other general business needs. Additionally, to maintain our status as a REIT under the Code, we must distribute annually at least 90% of our REIT taxable income. In future years, a portion of this requirement may be able to be met through stock dividends, rather than cash, subject to limitations based on the value of our stock.

Our primary sources of funds for liquidity consist of cash provided by operating activities (primarily income from our investments in Excess MSRs and RMBS and net servicing income from our MSRs), sales or repayments of RMBS and borrowings under repurchase agreements and the MSR Financing Facility.

In the future, sources of funds for liquidity may include potential additional MSR financing, warehouse agreements, securitizations and the issuance of equity or debt securities, when feasible, but will not include advances from the FHLBI because our membership in the FHLBI has been terminated. Our primary uses of funds are the payment of interest, management fees, outstanding commitments, other operating expenses, investments in new or replacement assets and the repayment of borrowings, as well as dividends. We seek to maintain adequate cash reserves and other sources of available liquidity to meet any margin calls resulting from decreases in value related to a reasonably possible (in the opinion of management) change in interest rates.

As of the date of this filing, we have sufficient liquid assets to satisfy all of our short-term recourse liabilities. With respect to the next twelve months, we expect that our cash on hand combined with our cash flow provided by operations will be sufficient to satisfy our anticipated liquidity needs with respect to our current investment portfolio, including related financings, potential margin calls and operating expenses. While it is inherently more difficult to forecast beyond the next twelve months, we currently expect to meet our long-term liquidity requirements through our cash on hand and, if needed, additional borrowings, proceeds received from repurchase agreements and similar financings, proceeds from equity offerings and the liquidation or refinancing of our assets.

Our operating cash flow differs from our net income due primarily to: (i) accretion of discount or premium on our RMBS and Excess MSRs, (ii) unrealized gains or losses on our Servicing Related Assets, and (iii) other-than-temporary impairment on our securities, if any.

Repurchase Agreements

As of December 31, 2016, we had repurchase agreements with 23 counterparties and approximately \$594.6 million of outstanding repurchase agreement borrowings from 15 of those counterparties, which were used to finance RMBS. As of December 31, 2016, our exposure (defined as the amount of cash and securities pledged as collateral, less the borrowing under the repurchase agreement) to any of the counterparties under the repurchase agreements did not exceed five percent of our equity. Under these agreements, which are uncommitted facilities, we sell a security to a counterparty and concurrently agree to repurchase the same security at a later date for a higher specified price. The sale price represents financing proceeds and the difference between the sale and repurchase prices represents interest on the financing. The price at which the security is sold generally represents the market value of the security less a discount or “haircut”. The weighted average haircut on our repurchase debt at December 31, 2016, was approximately 5.4%. During the term of the repurchase agreement, which can be as short as 30 days, the counterparty holds the security and posted margin as collateral. The counterparty monitors and calculates what it estimates to be the value of the collateral during the term of the agreement. If this value declines by more than a de minimis threshold, the counterparty requires us to post additional collateral (or “margin”) in order to maintain the initial haircut on the collateral. This margin is typically required to be posted in the form of cash and cash equivalents. Furthermore, we are, from time to time, a party to derivative agreements or financing arrangements that may be subject to margin calls based on the value of such instruments.

Set forth below is the average aggregate balance of borrowings under the Company’s repurchase agreements for each of the periods shown and the aggregate balance as of the end of each such period (dollars in thousands):

Repurchase Agreement Average and Maximum Amounts

Quarter Ended	Average Monthly Amount	Maximum Month-End Amount	Ending Amount
December 31, 2016	\$ 636,880	\$ 688,628	\$ 594,615
September 30, 2016	\$ 511,475	\$ 537,139	\$ 466,209
June 30, 2016	\$ 485,476	\$ 544,862	\$ 456,075
March 31, 2016	\$ 406,360	\$ 414,153	\$ 398,374
December 31, 2015	\$ 408,227	\$ 443,446	\$ 385,560
September 30, 2015	\$ 396,013	\$ 440,727	\$ 440,727
June 30, 2015	\$ 382,333	\$ 384,386	\$ 384,386
March 31, 2015	\$ 376,083	\$ 377,361	\$ 373,868
December 31, 2014	\$ 354,878	\$ 363,493	\$ 362,126
September 30, 2014	\$ 315,830	\$ 329,239	\$ 329,239
June 30, 2014	\$ 288,881	\$ 293,747	\$ 293,747
March 31, 2014	\$ 263,505	\$ 269,982	\$ 269,982

The increases in the Company’s borrowings under its repurchase agreements were primarily due to the temporary investment of funds received from the following sources pending the redeployment of a portion of such funds into MSR investments: amounts borrowed under the MSR Finance Facility, the sale of approximately half of our Excess MSRs in November 2016 and principal payments on the Excess MSRs.

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These short-term borrowings were used to finance certain of our investments in RMBS. The RMBS repurchase agreements are guaranteed by the Company. The weighted average difference between the market value of the assets and the face amount of available financing for the RMBS repurchase agreements, or the haircut, was 5.4% and 5.0% as of December 31, 2016 and December 31, 2015, respectively indicated. The following tables provide additional information regarding our repurchase agreements (dollars in thousands):

Repurchase Agreement Characteristics

As of December 31, 2016

	<u>RMBS Market Value</u>	<u>Repurchase Agreements</u>	<u>Weighted Average Rate</u>
Less than one month	\$ 65,121	\$ 60,690	1.14%
One to three months	464,585	456,502	0.91%
Greater than three months	78,854	77,423	0.90%
Total/Weighted Average	\$ 608,560	\$ 594,615	0.93%

As of December 31, 2015

	<u>RMBS Market Value</u>	<u>Repurchase Agreements</u>	<u>Weighted Average Rate</u>
Less than one month	\$ 97,283	\$ 93,926	0.55%
One to three months	295,534	284,687	0.56%
Greater than three months	7,029	6,947	0.52%
Total/Weighted Average	\$ 399,846	\$ 385,560	0.56%

The amount of collateral as of December 31, 2016 and December 31, 2015, including cash, was \$632.1 million and \$404.1 million, respectively.

The weighted average term to maturity of our borrowings under repurchase agreements as of December 31, 2016 and December 31, 2015 was 65 days and 47 days, respectively.

FHLBI Advances

As of December 31, 2016, we had no FHLBI advances outstanding, and our captive insurance subsidiary had terminated its membership in the FHLBI and had been dissolved. At December 31, 2015, we had FHLBI advances of approximately \$62.3 million, which were used to finance RMBS. In addition, at December 31, 2015, CHMI Insurance held FHLBI Stock of approximately \$3.3 million as required by the FHLBI

These short-term borrowings were used to finance certain of our investments in RMBS. The FHLBI Advances were guaranteed by the Company. The weighted average difference between the market value of the assets and the face amount of available financing for the FHLBI Advances, or the haircut, was 4.9% as of December 31, 2015. The following table provides additional information regarding FHLBI Advances (dollars in thousands):

Federal Home Loan Bank Advance Characteristics

As of December 31, 2015

	<u>Federal Home Loan Bank advances</u>		<u>Weighted Average Rate</u>
Less than one month	\$	15,000	0.44%
One to three months		—	—
Greater than three months		47,250	0.57%
Total/Weighted Average	\$	62,250	0.54%

The amount of collateral as of December 31, 2015, including FHLBI stock and securities pledged but not being backed by any advances, was \$86.4 million.

The weighted average term to maturity of our borrowings under FHLBI advances as of December 31, 2015 was 94 days.

MSR Financing Facility

In September 2016, Aurora and QRS III entered into a loan and security agreement (the “MSR Financing Facility”), pursuant to which Aurora and QRS III pledged their respective rights in all existing and future MSRs for loans owned or securitized by Fannie Mae to secure borrowings up to a maximum of \$25 million outstanding at any one time. The facility has a two-year revolving period, subject to extension by agreement, during which only interest payments are due. Borrowings bear interest at a spread over one month LIBOR. At the end of the revolving period, the outstanding amount will be converted to a three-year term loan with monthly payments of interest (calculated as a spread over the rate for one-year interest rate swaps) and principal (calculated on a ten-year amortization schedule). At December 31, 2016, approximately \$14.0 million was outstanding under the MSR Financing Facility.

Cash Flows

Operating and Investing Activities

Our operating activities provided cash of approximately \$34.5 million and our investing activities used cash of approximately \$146.1 million for the year ended December 31, 2016. The cash provided by operating activities and the cash used in investing activities is a result of the execution of our ongoing investment strategy.

Dividends

We conduct our operations in a manner intended to satisfy the requirements for qualification as a REIT for U.S. federal income tax purposes. U.S. federal income tax law generally requires that a REIT distribute annually at least 90% of its REIT taxable income, without regard to the deduction for dividends paid and excluding net capital gains, and that it pay tax at regular corporate rates to the extent that it annually distributes less than 100% of its taxable income. We intend to make regular quarterly distributions of all or substantially all of our REIT taxable income to holders of our common stock out of assets legally available for this purpose, if and to the extent authorized by our board of directors. Before we pay any dividend, whether for U.S. federal income tax purposes or otherwise, we must first meet both our operating requirements and debt service on our repurchase agreements and other debt payable. If our cash available for distribution is less than our REIT taxable income, we could be required to sell assets or borrow funds to make cash distributions, or we may make a portion of the required distribution in the form of a taxable stock distribution or distribution of debt securities. We will make distributions only upon the authorization of our board of directors. The amount, timing and frequency of distributions will be authorized by our board of directors based upon a variety of factors, including:

- actual results of operations;
- our level of retained cash flows;
- our ability to make additional investments in our target assets;
- restrictions under Maryland law;
- any debt service requirements;
- our taxable income;
- the annual distribution requirements under the REIT provisions of the Code; and
- other factors that our board of directors may deem relevant

Our ability to make distributions to our stockholders will depend upon the performance of our investment portfolio, and, in turn, upon our Manager’s management of our business. Distributions will be made quarterly in cash to the extent that cash is available for distribution. We may not be able to generate sufficient cash available for distribution to pay distributions to our stockholders. In addition, our board of directors may change our distribution policy in the future.

We make distributions based on a number of factors, including an estimate of taxable earnings per common share. Dividends distributed and taxable and GAAP earnings will typically differ due to items such as fair value

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adjustments, differences in premium amortization and discount accretion, and nondeductible general and administrative expenses. Our dividend per share may be substantially different than our taxable earnings and GAAP earnings per share. Our GAAP earnings (loss) per share for the years ended December 31, 2016 and December 31, 2015 were \$3.31 and \$1.76, respectively.

Our long term view of the attractiveness of the investment opportunities in our target asset classes has not changed. However, the current levels of asset pricing have reduced the available returns. We intend to expand the scope of our investments in our target assets with the goal of creating a more diversified and stable revenue profile. We believe a more stable source of income should provide value to our stockholders over time. Our diversification strategy involves execution risks and requires capital. There is no assurance as to when we will be able to raise that capital, if at all.

Off-balance Sheet Arrangements

As of December 31, 2016, we did not have any off-balance sheet arrangements. We did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured investment vehicles, or special purpose or variable interest entities, established to facilitate off-balance sheet arrangements or other contractually narrow or limited purposes. Further, we have not guaranteed any obligations of unconsolidated entities or entered into any commitment or intend to provide additional funding to any such entities.

Contractual Obligations

Our contractual obligations as of December 31, 2016 and December 31, 2015 included repurchase agreements, FHLBI advances on certain RMBS (as of December 31, 2015 only), borrowings under the \$25 million Term Loan and the facility from FirstTrust (as of December 31, 2015 only), borrowings under the MSR Financing Facility (as of December 31, 2016 only), our subservicing agreement with Freedom Mortgage and our management agreement with our Manager. Pursuant to our management agreement, our Manager is entitled to receive a management fee and the reimbursement of certain expenses.

The following table summarizes our contractual obligations as of the dates indicated (dollars in thousands):

Contractual Obligations Characteristics

As of December 31, 2016

	<u>Less than 1 year</u>	<u>1 to 3 years</u>	<u>3 to 5 years</u>	<u>More than 5 years</u>	<u>Total</u>
Repurchase agreements					
Borrowings under repurchase agreements	\$ 594,615	\$ —	\$ —	\$ —	\$ 594,615
Interest on repurchase agreement borrowings ^(A)	\$ 877	\$ —	\$ —	\$ —	\$ 877
Term Loan					
Borrowings under Term Loan facility	\$ 2,841	\$ 6,045	\$ —	\$ —	\$ 8,886
Interest on Term Loan borrowings	\$ 424	\$ 350	\$ —	\$ —	\$ 774
MSR Financing Facility					
Borrowings under MSR Financing facility	\$ —	\$ 1,388	\$ 12,612	\$ —	\$ 14,000
Interest on MSR Financing borrowings	\$ 622	\$ 1,313	\$ 1,075	\$ —	\$ 3,010

As of December 31, 2015

	Less than 1 year	1 to 3 years	3 to 5 years	More than 5 years	Total
Repurchase agreements					
Borrowings under repurchase agreements	\$ 385,560	\$ —	\$ —	\$ —	\$ 385,560
Interest on repurchase agreement borrowings ^(A)	\$ 263	\$ —	\$ —	\$ —	\$ 263
Federal Home Loan Bank advances					
Borrowings under FHLBI advances	\$ 62,250	\$ —	\$ —	\$ —	\$ 62,250
Interest on FHLBI advance borrowings ^(A)	\$ 92	\$ —	\$ —	\$ —	\$ 92
Term Loan					
Borrowings under Term Loan facility	\$ 1,958	\$ 6,583	\$ 15,762	\$ —	\$ 24,303
Interest on Term Loan borrowings	\$ 1,308	\$ 3,215	\$ 493	\$ —	\$ 5,016

(A) Interest expense is calculated based on the interest rate in effect at December 31, 2016 and includes all interest expense incurred and expected to be incurred in the future through the contractual maturity of the associated repurchase agreement.

The table above does not include amounts due under the management agreement with our Manager. Those payments are discussed below.

Management Agreement

The management agreement with our Manager provides that our Manager is entitled to receive a management fee, the reimbursement of certain expenses and, in certain circumstances, a termination fee. The management fee is an amount equal to 1.5% per annum of our stockholders’ equity, adjusted as set forth in the management agreement, and calculated and payable quarterly in arrears. We will also be required to pay a termination fee equal to three times the average annual management fee earned by our Manager during the two four-quarter periods ending as of the end of the fiscal quarter preceding the date of termination. Such termination fee will be payable upon termination of the management agreement by us without cause or by our Manager if we materially breach the management agreement.

We pay all of our direct operating expenses, except those specifically required to be borne by our Manager under the management agreement. Our Manager is responsible for all costs incident to the performance of its duties under the management agreement. Our Manager uses the proceeds from its management fee in part to pay Freedom Mortgage for services provided under the Services Agreement between the Manager and Freedom Mortgage. Our chief financial officer receives a nominal portion of his overall compensation directly from Aurora for acting as its president. With that exception, our officers receive no cash compensation directly from us. Our Manager provides us with our officers. Our Manager is entitled to be reimbursed for an agreed upon portion of the costs of the wages, salary and other benefits with respect to our chief financial officer, controller and general counsel, originally based on the percentages of their working time and efforts spent on matters related to our company. The amount of the wages, salary and benefits reimbursed with respect to the officers our Manager provides to us is subject to the approval of the compensation committee of our board of directors.

The term of the management agreement will expire on October 22, 2020 and will be automatically renewed for a one-year term on such date and on each anniversary of such date thereafter unless terminated or not renewed as described below. Either we or our Manager may elect not to renew the management agreement upon expiration of its initial term or any renewal term by providing written notice of non-renewal at least 180 days, but not more than 270 days, before expiration. In the event we elect not to renew the term, we will be required to pay our Manager the termination fee described above. We may terminate the management agreement at any time for cause effective upon 30 days prior written notice of termination from us to our Manager, in which case no termination fee would be due. Our board of directors will review our Manager’s performance prior to the automatic renewal thereof and, as a result of such review, upon the affirmative vote of at least two-thirds of the members of our board of directors or of the holders of a majority of our outstanding common stock, we may terminate the management agreement based upon unsatisfactory performance by our Manager that is materially detrimental to us or a determination by our independent directors that the management fees payable to our Manager are not fair, subject to the right of our Manager to prevent such a termination by agreeing to a reduction of the management fees payable to our Manager. Upon any termination of the management agreement based on unsatisfactory performance or unfair management fees, we are required to pay our Manager the

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termination fee described above. Our Manager may terminate the management agreement, without payment of the termination fee, in the event we become regulated as an investment company under the Investment Company Act. Our Manager may also terminate the management agreement upon 60 days' written notice if we default in the performance of any material term of the management agreement and the default continues for a period of 30 days after written notice to us, whereupon we would be required to pay our Manager the termination fee described above.

Subservicing Agreement

Freedom Mortgage is directly servicing the Company's portfolio of Fannie Mae and Freddie Mac MSR, and beginning in February 2017, Ginnie Mae MSR, pursuant to a subservicing agreement entered into on June 10, 2015. The agreement has an initial term of three years, expiring on September 1, 2018, and is subject to automatic renewal for additional three year terms unless either party chooses not to renew. The agreement may be terminated without cause by either party by giving notice as specified in the agreement. If the agreement is not renewed by the Company or terminated by the Company without cause, market rate deboarding fees will be due to the sub-servicer. Under that agreement, Freedom Mortgage agrees to service the applicable mortgage loans in accordance with applicable law and the requirements of the applicable agency. The Company pays fees for specified services.

Joint Marketing Recapture Agreement

In June 2016, Aurora entered into a joint marketing recapture agreement with Freedom Mortgage. Pursuant to this agreement, Freedom Mortgage will attempt to refinance certain mortgage loans underlying Aurora's servicing MSR portfolio as directed by Aurora. If a loan is refinanced, Aurora will pay Freedom Mortgage a fee for its origination services. Freedom will be entitled to sell the loan for its own benefit and will transfer the related MSR to Aurora. The agreement has an initial term of one year, subject to automatic renewals of one year each and subject to termination by either party upon 60 days prior notice. All new loans must qualify for sale to Fannie Mae or Freddie Mac and meet other conditions set forth in the agreement. As of December 31, 2016, MSR on 36 loans with an aggregate unpaid principal balance of approximately \$9.8 million had been received from Freedom Mortgage which generated approximately \$20,500 in fees due to Freedom Mortgage.

Inflation

Virtually all of our assets and liabilities are financial in nature. As a result, interest rates and other factors affect our performance more so than inflation, although inflation rates can often have a meaningful influence over the direction of interest rates. Furthermore, our financial statements are prepared in accordance with GAAP and our distributions are determined by our board of directors primarily based on our REIT taxable income, and, in each case, our activities and balance sheet are measured with reference to historical cost and/or fair market value without considering inflation.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We seek to manage our risks related to the credit quality of our assets, interest rates, liquidity, prepayment speeds and market value while, at the same time, seeking to provide an opportunity to stockholders to realize attractive risk-adjusted returns through ownership of our capital stock. While we do not seek to avoid risk completely, we believe the risk can be quantified from historical experience and seek to actively manage that risk, to earn sufficient compensation to justify taking those risks and to maintain capital levels consistent with the risks we undertake.

Interest Rate Risk

Interest rates are highly sensitive to many factors, including fiscal and monetary policies and domestic and international economic and political considerations, as well as other factors beyond our control. We are subject to interest rate risk in connection with our assets and our related financing obligations. In general, we finance the acquisition of certain of our assets through financings in the form of repurchase agreements and bank facilities. We expect to make use of MSR financing, warehouse facilities, securitizations, re-securitizations, and public and private equity and debt issuances in addition to transaction or asset specific funding arrangements. In addition, the values of our Servicing Related Assets are highly sensitive to changes in interest rates, historically increasing

when rates rise and decreasing when rates decline. Subject to maintaining our qualification as a REIT, we attempt to mitigate interest rate risk through utilization of hedging instruments, primarily interest rate swap agreements. We may also use financial futures, options, interest rate cap agreements, and forward sales. These instruments are intended to serve as a hedge against future interest rate changes on our borrowings.

Interest Rate Effect on Net Interest Income

Our operating results depend in large part on differences between the income earned on our assets and our cost of borrowing and hedging activities. The costs of our borrowings are generally based on prevailing market interest rates. During a period of rising interest rates, our borrowing costs generally will increase (1) while the yields earned on our leveraged fixed-rate mortgage assets will remain static and (2) at a faster pace than the yields earned on our leveraged adjustable-rate and hybrid adjustable-rate RMBS, which could result in a decline in our net interest spread and net interest margin. The severity of any such decline would depend on our asset/liability composition at the time as well as the magnitude and duration of the interest rate increase. Further, an increase in short-term interest rates could also have a negative impact on the market value of our assets, other than our Servicing Related Assets. A decrease in interest rates could have a negative impact on the market value of our Servicing Related Assets. If any of these events happen, we could experience a decrease in net income or incur a net loss during these periods, which could adversely affect our liquidity and results of operations.

Hedging techniques are partly based on assumed levels of prepayments of our assets, specifically our RMBS. If prepayments are slower or faster than assumed, the life of the investment will be longer or shorter, which would reduce the effectiveness of any hedging strategies we may use and may cause losses on such transactions. Hedging strategies involving the use of derivatives are highly complex and may produce volatile returns.

Interest Rate Cap Risk

Any adjustable-rate RMBS that we acquire will generally be subject to interest rate caps, which potentially could cause such RMBS to acquire many of the characteristics of fixed-rate securities if interest rates were to rise above the cap levels. This issue will be magnified to the extent we acquire adjustable-rate and hybrid adjustable-rate RMBS that are not based on mortgages which are fully indexed. In addition, adjustable-rate and hybrid adjustable-rate RMBS may be subject to periodic payment caps that result in some portion of the interest being deferred and added to the principal outstanding. This could result in our receipt of less cash income on such assets than we would need to pay the interest cost on our related borrowings. To mitigate interest rate mismatches, we may utilize the hedging strategies discussed above under “—Interest Rate Risk.” Actual economic conditions or implementation of decisions by our Manager may produce results that differ significantly from the estimates and assumptions used in our models.

Prepayment Risk; Extension Risk

The following tables summarize the estimated change in fair value of our interests in the Excess MSR as of the dates indicated given several parallel changes in the discount rate and voluntary prepayment rate (dollars in thousands):

Excess MSR Fair Value Changes

As of December 31, 2016

	(20)%	(10)%	—%	10%	20%
Discount Rate Shift in %					
Estimated FV	\$ 32,595	\$ 30,911	\$ 29,392	\$ 28,016	\$ 26,763
Change in FV	\$ 3,203	\$ 1,519	\$ —	\$ (1,376)	\$ (2,629)
% Change in FV	11%	5%	—	(5)%	(9)%
Voluntary Prepayment Rate Shift in %					
Estimated FV	\$ 31,710	\$ 30,517	\$ 29,392	\$ 28,331	\$ 27,336
Change in FV	\$ 2,318	\$ 1,125	\$ —	\$ (1,062)	\$ (2,056)
% Change in FV	8%	4%	—	(4)%	(7)%
Recapture Rate Shift in %					
Estimated FV	\$ 29,219	\$ 29,306	\$ 29,392	\$ 29,479	\$ 29,565
Change in FV	\$ (173)	\$ (87)	\$ —	\$ 87	\$ 173
% Change in FV	(1)%	(0)%	—	0%	1%

As of December 31, 2015

	(20)%	(10)%	—%	10%	20%
Discount Rate Shift in %					
Estimated FV	\$ 86,063	\$ 81,859	\$ 78,042	\$ 74,577	\$ 71,406
Change in FV	\$ 8,016	\$ 3,812	\$ —	\$ (3,470)	\$ (6,642)
% Change in FV	10%	5%	—	(4)%	(9)%
Voluntary Prepayment Rate Shift in %					
Estimated FV	\$ 85,033	\$ 81,428	\$ 78,042	\$ 74,886	\$ 71,919
Change in FV	\$ 6,986	\$ 3,380	\$ —	\$ (3,162)	\$ (6,128)
% Change in FV	9%	4%	—	(4)%	(8)%
Recapture Rate Shift in %					
Estimated FV	\$ 77,775	\$ 77,911	\$ 78,042	\$ 78,184	\$ 78,320
Change in FV	\$ (272)	\$ (136)	\$ —	\$ 136	\$ 272
% Change in FV	(0)%	(0)%	—	0%	0%

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The following table summarizes the estimated change in fair value of our interests in the MSR as of the date indicated given several parallel shifts in the discount rate and voluntary prepayment rate (dollars in thousands):

MSR Fair Value Changes

As of December 31, 2016

	(20)%	(10)%	—%	10%	20%
Discount Rate Shift in %					
Estimated FV	\$ 34,443	\$ 33,110	\$ 31,871	\$ 30,716	\$ 29,638
Change in FV	\$ 2,573	\$ 1,239	\$ —	\$ (1,155)	\$ (2,232)
% Change in FV	8%	4%	—	(4)%	(7)%
Voluntary Prepayment Rate Shift in %					
Estimated FV	\$ 34,963	\$ 33,355	\$ 31,871	\$ 30,497	\$ 29,222
Change in FV	\$ 3,093	\$ 1,485	\$ —	\$ (1,374)	\$ (2,648)
% Change in FV	10%	5%	—	(4)%	(8)%
Servicing Cost Shift in %					
Estimated FV	\$ 32,915	\$ 32,393	\$ 31,871	\$ 31,348	\$ 30,826
Change in FV	\$ 1,044	\$ 522	\$ —	\$ (522)	\$ (1,044)
% Change in FV	3%	2%	—	(2)%	(3)%

As of December 31, 2015

	(20)%	(10)%	—%	10%	20%
Discount Rate Shift in %					
Estimated FV	\$ 21,261	\$ 20,486	\$ 19,761	\$ 19,084	\$ 18,450
Change in FV	\$ 1,500	\$ 724	\$ —	\$ (677)	\$ (1,312)
% Change in FV	8%	4%	—	(3)%	(7)%
Voluntary Prepayment Rate Shift in %					
Estimated FV	\$ 21,656	\$ 20,672	\$ 19,761	\$ 18,916	\$ 18,130
Change in FV	\$ 1,894	\$ 911	\$ —	\$ (845)	\$ (1,631)
% Change in FV	10%	5%	—	(4)%	(8)%
Servicing Cost Shift in %					
Estimated FV	\$ 20,490	\$ 20,126	\$ 19,761	\$ 19,397	\$ 19,033
Change in FV	\$ 728	\$ 364	\$ —	\$ (364)	\$ (728)
% Change in FV	4%	2%	—	(2)%	(4)%

The following tables summarize the estimated change in fair value of our RMBS as of the dates indicated given several parallel shifts in interest rates (dollars in thousands):

RMBS Fair Value Changes

As of December 31, 2016

	December 31, 2016	Fair Value Change				
		+25 Bps	+50 Bps	+75 Bps	+100 Bps	+150 Bps
RMBS Portfolio						
RMBS, available-for-sale, net of swaps	\$ 672,190					
RMBS Total Return (%)		(0.46)%	(1.02)%	(1.66)%	(2.37)%	(3.87)%
RMBS Dollar Return		\$(3,069)	\$(6,769)	\$(11,092)	\$(15,775)	\$(25,834)

As of December 31, 2015

	December 31, 2015	Fair Value Change				
		+25 Bps	+50 Bps	+75 Bps	+100 Bps	+150 Bps
RMBS Portfolio						
RMBS, available-for-sale, net of swaps	\$ 503,697					
RMBS Total Return (%)		(0.49)%	(1.07)%	(1.74)%	(2.47)%	(4.04)%
RMBS Dollar Return		\$(2,444)	\$(5,406)	\$(8,785)	\$(12,456)	\$(20,353)

The sensitivity analysis is hypothetical and is presented solely to assist an analysis of the possible effects on the fair value under various scenarios. It is not a prediction of the amount or likelihood of a change in any particular scenario. In particular, the results are calculated by stressing a particular economic assumption independent of changes in any other assumption. In practice, changes in one factor may result in changes in another, which might counteract or amplify the sensitivities. In addition, changes in the fair value based on a 10% variation in an assumption generally may not be extrapolated because the relationship of the change in the assumption to the change in fair value may not be linear.

Counterparty Risk

When we engage in repurchase transactions, we generally sell securities to lenders (i.e., repurchase agreement counterparties) and receive cash from the lenders. The lenders are obligated to resell the same securities back to us at the end of the term of the transaction. Because the cash we receive from the lender when we initially sell the securities to the lender is less than the value of those securities (this difference is the haircut), if the lender defaults on its obligation to resell the same securities back to us we would incur a loss on the transaction equal to the amount of the haircut (assuming there was no change in the value of the securities). As of December 31, 2016, the Company's exposure (defined as the amount of cash and securities pledged as collateral, less the borrowing under the repurchase agreement) to any of the counterparties under the repurchase agreements did not exceed five percent of the Company's equity.

Our interest rate swaps are required to be cleared on an exchange which greatly mitigates, but does not entirely eliminate, counterparty risk.

Our investments in Servicing Related Assets are dependent on the mortgage sub-servicer, Freedom Mortgage, to perform its sub-servicing obligations. If our sub-servicer fails to perform its obligations and is terminated by one or more Agencies as an approved servicer, the value of our MSR's may be adversely affected. In addition, when we purchase MSR's from third parties, we rely, to a certain extent, on the ability and willingness of the sellers to perform their contractual obligations to remedy breaches of representations and warranties or to repurchase the affected loan and indemnify us for any losses.

Funding Risk

To the extent available on desirable terms, we expect to continue to finance our RMBS with repurchase agreement financing. We also anticipate continuing to finance our MSR's with bank loans secured by a pledge of those MSR's. Over time, as market conditions change, in addition to these financings, we may use other forms of leverage. Weakness in the financial markets, the residential mortgage markets and the economy generally could adversely affect one or more of our potential lenders and could cause one or more of our potential lenders to be unwilling or unable to provide us with financing or to increase the costs of that financing.

Liquidity Risk

Our Servicing Related Assets, as well as some of the assets that may in the future comprise our portfolio, are not publicly traded. A portion of these assets may be subject to legal and other restrictions on resale or will otherwise be less liquid than publicly-traded securities. The illiquidity of these assets may make it difficult for us to sell such assets if the need or desire arises, including in response to changes in economic and other conditions.

Credit Risk

Although we expect relatively low credit risk with respect to our portfolios of our Agency RMBS, our investment in MSR's exposes us to the credit risk of borrowers. To the extent we invest in non-Agency RMBS and prime mortgage loans, we expect to encounter credit risk related to these asset classes.

To date, our only investments in non-Agency RMBS have been credit risk transfer securities issued by Fannie Mae and Freddie Mac.

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Item 8. Consolidated Financial Statements and Supplementary Data.

Consolidated Financial Statements

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders of Cherry Hill Mortgage Investment Corporation

We have audited the accompanying consolidated balance sheets of Cherry Hill Mortgage Investment Corporation and subsidiaries (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Cherry Hill Mortgage Investment Corporation and subsidiaries at December 31, 2016 and 2015, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP
New York, New York
March 14, 2017

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

	December 31, 2016	December 31, 2015
Assets		
RMBS, available-for-sale	\$ 671,904	\$ 508,242
Investments in Servicing Related Assets at fair value	61,263	97,803
Cash and cash equivalents	15,824	10,603
Restricted cash	22,469	9,942
Derivative assets	9,121	422
Receivables and other assets	12,297	9,328
Total Assets	\$ 792,878	\$ 636,340
Liabilities and Stockholders' Equity		
Liabilities		
Repurchase agreements	\$ 594,615	\$ 385,560
Federal Home Loan Bank advances	—	62,250
Derivative liabilities	694	4,595
Notes payable	22,886	24,313
Dividends payable	4,816	3,684
Due to affiliates	1,894	998
Payables for unsettled trades	6,202	—
Accrued expenses and other liabilities	5,762	2,603
Total Liabilities	\$ 636,869	\$ 484,003
Stockholders' Equity		
Preferred stock, \$0.01 par value, 100,000,000 shares authorized, none issued and outstanding as of December 31, 2016 and December, 31, 2015	\$ —	\$ —
Common stock, \$0.01 par value, 500,000,000 shares authorized and 7,525,348 shares issued and outstanding as of December 31, 2016 and 500,000,000 shares authorized and 7,519,038 shares issued and outstanding as of December, 31, 2015	75	75
Additional paid-in capital	148,457	148,332
Retained earnings (deficit)	12,093	3,133
Accumulated other comprehensive income (loss)	(6,393)	(197)
Total CHMI Stockholders' Equity	\$ 154,232	\$ 151,343
Non-controlling interests in operating partnership	1,777	994
Total Stockholders' Equity	\$ 156,009	\$ 152,337
Total Liabilities and Stockholders' Equity	\$ 792,878	\$ 636,340

See notes to consolidated financial statements.

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

	Year Ended December 31,		
	2016	2015	2014
Income			
Interest income	\$ 30,722	\$ 27,712	\$ 26,497
Interest expense	7,808	5,983	4,307
Net interest income	22,914	21,729	22,190
Servicing fee income	7,579	1,719	—
Servicing costs	2,562	761	—
Net servicing income (loss)	5,017	958	—
Other income (loss)			
Realized gain (loss) on RMBS, net	1,399	854	(60)
Realized gain (loss) on investments in Excess MSR's, net	1,520	—	—
Realized gain (loss) on derivatives, net	(7,963)	(3,913)	(2,643)
Realized gain (loss) on acquired assets, net	—	449	—
Unrealized gain (loss) on derivatives, net	12,080	(59)	(6,564)
Unrealized gain (loss) on investments in Excess MSR's	249	(19)	(5,100)
Unrealized gain (loss) on investments in MSR's	(3,285)	(1,123)	—
Total Income	31,931	18,876	7,823
Expenses			
General and administrative expense	3,284	3,081	3,028
Management fee to affiliate	2,946	2,783	2,560
Total Expenses	6,230	5,864	5,588
Income (Loss) Before Income Taxes	25,701	13,012	2,235
Provision for corporate business taxes	458	(343)	(140)
Net Income (Loss)	25,243	13,355	2,375
Net (income) loss allocated to noncontrolling interests	(411)	(141)	(22)
Net Income (Loss) Applicable to Common Stockholders	\$ 24,832	\$ 13,214	\$ 2,353
Net income (Loss) Per Share of Common Stock			
Basic	\$ 3.31	\$ 1.76	\$ 0.31
Diluted	\$ 3.30	\$ 1.76	\$ 0.31
Weighted Average Number of Shares of Common Stock Outstanding			
Basic	7,512,444	7,509,543	7,505,546
Diluted	7,523,297	7,512,444	7,508,827

See notes to consolidated financial statements.

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

	<u>Year Ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net income (loss)	\$ 25,243	\$ 13,355	\$ 2,375
Other comprehensive income (loss):			
Net unrealized gain (loss) on RMBS	(4,797)	(5,984)	11,614
Reclassification of net realized (gain) loss on RMBS in earnings	(1,399)	(854)	60
Other comprehensive income (loss)	(6,196)	(6,838)	11,674
Comprehensive income (loss)	\$ 19,047	\$ 6,517	\$ 14,049
Comprehensive income (loss) attributable to noncontrolling interests	310	69	129
Comprehensive income (loss) attributable to common stockholders	\$ 18,737	\$ 6,448	\$ 13,920

See notes to consolidated financial statements.

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

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Deficit)	Non-Controlling Interest in Operating Partnership	Total Stockholders' Equity
Balance, December 31, 2013	7,500,000	\$ 75	\$ 148,078	\$ (5,033)	\$ 17,695	\$ 307	\$ 161,122
Issuance of common stock	9,543	— ^(A)	180	—	—	—	180
Net Income	—	—	—	—	2,353	22	2,375
Other Comprehensive Income	—	—	—	11,674	—	—	11,674
LTIP-OP Unit awards	—	—	—	—	—	320	320
Distribution paid on LTIP-OP Units	—	—	—	—	—	(104)	(104)
Common dividends declared, \$2.03 per share	—	—	—	—	(15,249)	—	(15,249)
Balance, December 31, 2014	7,509,543	\$ 75	\$ 148,258	\$ 6,641	\$ 4,799	\$ 545	\$ 160,318
Issuance of common stock	9,495	— ^(B)	74	—	—	—	74
Net Income	—	—	—	—	13,214	141	13,355
Other Comprehensive Income	—	—	—	(6,838)	—	—	(6,838)
LTIP-OP Unit awards	—	—	—	—	—	463	463
Distribution paid on LTIP-OP Units	—	—	—	—	—	(155)	(155)
Common dividends declared, \$1.98 per share	—	—	—	—	(14,880)	—	(14,880)
Balance, December 31, 2015	7,519,038	\$ 75	\$ 148,332	\$ (197)	\$ 3,133	\$ 994	\$ 152,337
Issuance of common stock	6,310	— ^(C)	125	—	—	—	125
Net Income	—	—	—	—	24,832	411	25,243
Other Comprehensive Income	—	—	—	(6,196)	—	—	(6,196)
LTIP-OP Unit awards	—	—	—	—	—	618	618
Distribution paid on LTIP-OP Units	—	—	—	—	—	(246)	(246)
Common dividends declared, \$2.11 per share	—	—	—	—	(15,872)	—	(15,872)
Balance, December 31, 2016	7,525,348	\$ 75	\$ 148,457	\$ (6,393)	\$ 12,093	\$ 1,777	\$ 156,009

(A) de minimis (\$10.00 rounds to \$0.00).

(B) de minimis (\$95.00 rounds to \$0.00).

(C) de minimis (\$63.00 rounds to \$0.00).

See notes to consolidated financial statements.

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

	Year Ended December 31,		
	2016	2015	2014
Cash Flows From Operating Activities			
Net income (loss)	\$ 25,243	\$ 13,355	\$ 2,375
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Realized (gain) loss on RMBS, net	(1,399)	(854)	60
Realized gain (loss) on investments in Excess MSR's, net	(1,520)	—	—
Realized gain on bargain purchase	—	(449)	—
Accretion of premium and other amortization	4,115	3,811	2,058
Change in fair value of investments in Servicing Related Assets	3,036	1,142	5,100
Unrealized (gain) loss on derivatives, net	(12,080)	59	6,564
Realized (gain) loss on derivatives, net	7,963	3,913	2,643
LTIP-OP Unit awards	618	463	320
Changes in:			
Receivables from unsettled trades	—	309	6,930
Receivables and other assets	(2,908)	1,643	(414)
Due to affiliate	896	229	153
Payables for unsettled trades	6,202	—	—
Accrued expenses and other liabilities	4,291	(246)	718
Net cash provided by (used in) operating activities	\$ 34,457	\$ 23,375	\$ 26,507
Cash Flows From Investing Activities			
Purchase of RMBS	(312,095)	(303,278)	(202,679)
Principal paydown of RMBS	55,847	47,131	25,369
Proceeds from sale of RMBS	83,735	154,455	57,511
Acquisition of Excess MSR's	—	—	(2,181)
Principal paydown of Excess MSR's	7,804	13,261	16,065
Proceeds from sale of Excess MSR's	42,493	—	—
Aurora acquisition, net of cash received	—	(3,839)	—
Acquisition of MSR's	(15,395)	(13,861)	—
Purchase of derivatives	(8,616)	(4,046)	(1,585)
Sale of derivatives	133	291	157
Purchases of Federal Home Loan Bank stock	—	(3,261)	—
Net cash provided by (used in) investing activities	\$ (146,094)	\$ (113,147)	\$ (107,343)
Cash Flows From Financing Activities			
Changes in restricted cash	(12,527)	(2,995)	(3,203)
Borrowings under repurchase agreements	2,263,101	1,672,421	1,510,859
Repayments of repurchase agreements	(2,054,046)	(1,648,983)	(1,410,035)
Proceeds from Federal Home Loan Bank advances	7,000	109,550	—
Repayments of Federal Home Loan Bank advances	(69,250)	(47,300)	—
Proceeds from bank loans	14,000	25,000	—
Principal paydown of bank loans	(15,427)	(4,656)	—
Dividends paid	(15,872)	(15,028)	(14,789)
LTIP-OP Units distributions paid	(246)	(155)	(104)
Issuance of common stock, net of offering costs	125	74	180
Net cash provided by (used in) financing activities	\$ 116,858	\$ 87,928	\$ 82,908
Net Increase (Decrease) in Cash and Cash Equivalents	\$ 5,221	\$ (1,844)	\$ 2,072
Cash and Cash Equivalents, Beginning of Period	10,603	12,447	10,375
Cash and Cash Equivalents, End of Period	\$ 15,824	\$ 10,603	\$ 12,447
Supplemental Disclosure of Cash Flow Information			
Cash paid during the period for interest expense	\$ 6,981	\$ 5,606	\$ 3,867
Dividends declared but not paid	\$ 4,816	\$ 3,684	\$ 3,830

See notes to consolidated financial statements.

**Cherry Hill Mortgage Investment Corporation and Subsidiaries
Notes to Consolidated Financial Statements**

Note 1 — Organization and Operations

Cherry Hill Mortgage Investment Corporation (together with its consolidated subsidiaries, the “Company”) was organized in the state of Maryland on October 31, 2012 to invest in residential mortgage assets in the United States. Under the Company’s charter, as of December 31, 2012, the Company was authorized to issue 1,000 shares of common stock. On June 6, 2013, the Company amended and restated its charter and increased its authorized capitalization. Accordingly, at December 31, 2013, the Company was authorized to issue up to 500,000,000 shares of common stock and 100,000,000 shares of preferred stock, each with a par value of \$0.01 per share.

The accompanying consolidated financial statements include the accounts of the Company’s subsidiaries, Cherry Hill Operating Partnership LP, Cherry Hill QRS I, LLC, Cherry Hill QRS II, Cherry Hill QRS III, LLC, CHMI Insurance Company, LLC (“CHMI Insurance”), CHMI Solutions, Inc. (“CHMI Solutions”) (formerly CHMI Solutions, LLC) and Aurora Financial Group, Inc. (“Aurora”). See “Note 18 – CHMI Insurance Company” for information regarding the dissolution of CHMI Insurance.

On October 9, 2013, the Company completed an initial public offering (the “IPO”) of 6,500,000 shares of common stock and a concurrent private placement of 1,000,000 shares of common stock. The IPO and concurrent private placement resulted in the sale of 7,500,000 shares of common stock, at a price per share of \$20.00. The net proceeds to the Company from the IPO and the concurrent private placement were approximately \$148.1 million, after deducting offering-related expenses payable by the Company. The Company did not conduct any activity prior to the IPO and the concurrent private placement. Substantially all of the net proceeds from the IPO and the concurrent private placement were used to invest in excess mortgage servicing rights on residential mortgage loans (“Excess MSRs”) and residential mortgage-backed securities (“RMBS” or “securities”), the payment of principal and interest on which is guaranteed by a U.S. government agency or a U.S. government sponsored enterprise (“Agency RMBS”).

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

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

Note 2 — Basis of Presentation and Significant Accounting Policies

Basis of Accounting

The accompanying consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (“GAAP”). The consolidated financial statements include the accounts of the Company and its consolidated subsidiaries. All significant intercompany transactions and balances have been eliminated. The Company consolidates those entities in which it has an investment of 50% or more and has control over significant operating, financial and investing decisions of the entity.

Emerging Growth Company Status

On April 5, 2012, the Jumpstart Our Business Startups Act (the “JOBS Act”) was signed into law. The JOBS Act contains provisions that, among other things, reduce certain reporting requirements for qualifying public companies. Because the Company qualifies as an “emerging growth company,” it may, under Section 7(a)(2)(B) of the Securities Act of 1933, delay adoption of new or revised accounting standards

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applicable to public companies until such standards would otherwise apply to private companies. The Company has elected to take advantage of this extended transition period until the first to occur of the date that it (i) is no longer an “emerging growth company” or (ii) affirmatively and irrevocably opts out of this extended transition period. As a result, the consolidated financial statements may not be comparable to those of other public companies that comply with such new or revised accounting standards. Until the date that the Company is no longer an “emerging growth company” or affirmatively and irrevocably opts out of the extended transition period, upon issuance of a new or revised accounting standard that applies to the consolidated financial statements and that has a different effective date for public and private companies, the Company will disclose the date on which adoption is required for non-emerging growth companies and the date on which it will adopt the recently issued accounting standard.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make a number of significant estimates and assumptions. These include estimates of fair value of Excess MSRs and MSRs (collectively, “Servicing Related Assets”), RMBS, derivatives and credit losses including the period of time during which the Company anticipates an increase in the fair values of securities sufficient to recover unrealized losses on those securities, and other estimates that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amounts of certain revenues and expenses during the reporting period. It is likely that changes in these estimates (e.g., valuation changes due to supply and demand, credit performance, prepayments, interest rates, or other reasons) will occur in the near term. The Company’s estimates are inherently subjective in nature. Actual results could differ from the Company’s estimates and differences may be material.

Risks and Uncertainties

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

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

Investments in RMBS

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

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

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Investment securities transactions are recorded on the trade date. At disposition, the net realized gain or loss is determined on the basis of the cost of the specific investment and is included in earnings. All RMBS sold in the year ended December 31, 2016 were settled prior to period end.

Revenue Recognition – Interest income from coupon payments is accrued based on the outstanding principal amount of the RMBS and their contractual terms. Premiums and discounts associated with the purchase of the RMBS are accreted into interest income over the projected lives of the securities using the interest method. The Company's policy for estimating prepayment speeds for calculating the effective yield is to evaluate historical performance, consensus on prepayment speeds, and current market conditions. Adjustments are made for actual prepayment activity. Approximately \$2.0 million and \$1.5 million in interest income was receivable at December 31, 2016 and December 31, 2015 respectively, and has been classified within "Receivables and other assets" on the consolidated balance sheets. For further discussion on Receivables and other assets, see Note 14.

Impairment – The Company evaluates its RMBS, on a quarterly basis, to assess whether a decline in the fair value below the amortized cost basis is an other-than-temporary impairment ("OTTI"). The presence of OTTI is based upon a fair value decline below a security's amortized cost basis and a corresponding adverse change in expected cash flows due to credit related factors as well as non-credit factors, such as changes in interest rates and market spreads. Impairment is considered other-than-temporary if an entity (i) intends to sell the security, (ii) will more likely than not be required to sell the security before it recovers in value, or (iii) does not expect to recover the security's amortized cost basis, even if the entity does not intend to sell the security. Under these scenarios, the impairment is other-than-temporary and the full amount of impairment should be recognized currently in earnings and the cost basis of the security is adjusted. However, if an entity does not intend to sell the impaired security and it is more likely than not that it will not be required to sell before recovery, the OTTI should be separated into (i) the estimated amount relating to credit loss, or the credit component, and (ii) the amount relating to all other factors, or the non-credit component. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss recognized in accumulated other comprehensive income. The difference between the new amortized cost basis and the cash flows expected to be collected is accreted into interest income in accordance with the effective interest method. There were approximately \$173,000 of OTTI during the year ended December 31, 2016 and has been classified within "Realized gain (loss) on RMBS, net" on the consolidated statements of income. The Company did not record any OTTI charges during the year ended December 31, 2015.

Investments in Excess MSRs

Classification – The Company has elected the fair value option to record its investments in Excess MSRs in order to provide users of the consolidated financial statements with better information regarding the effects of prepayment risk and other market factors on the Excess MSRs. Under this election, the Company records a valuation adjustment on its investments in Excess MSRs on a quarterly basis to recognize the changes in fair value in net income as described below. In determining the valuation of Excess MSRs, management used internally developed models that are primarily based on observable market-based inputs but which also include unobservable market data inputs (see Note 9).

Revenue Recognition – Excess MSRs are aggregated into pools as applicable. Each pool of Excess MSRs is accounted for in the aggregate. Interest income for Excess MSRs is accreted into interest income on an effective yield or "interest" method, based upon the expected excess mortgage servicing amount over the expected life of the underlying mortgages. Changes to expected cash flows result in a cumulative retrospective adjustment, which will be recorded in the period in which the change in expected cash flows occurs. Under the retrospective method, the interest income recognized for a reporting period would be measured as the difference between the amortized cost basis at the end of the period and the amortized cost basis at the beginning of the period, plus any cash received during the period. The amortized cost basis is calculated as the present value of estimated future cash flows using an effective yield, which is the yield that equates all past actual and current estimated future cash flows to the initial investment. The difference between the fair value of Excess MSRs and their amortized cost basis is recorded on the consolidated statements income as "Unrealized gain (loss) on investments in Excess MSRs." Fair value is generally determined by discounting the expected future cash flows using discount rates that incorporate the market risks and liquidity premium specific to the Excess MSRs and, therefore, may differ

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from their effective yields. The sale of investments in Excess MSR are recognized upon settlement date. Approximately \$5.6 million and \$2.2 million in Excess MSR cashflow was receivable at December 31, 2016 and December 31, 2015 respectively, and has been classified within “Receivables and other assets” on the consolidated balance sheets.

Investments in MSRs

Classification – MSRs include rights associated with servicing contracts acquired in connection with the Aurora business combination and MSRs acquired through the bulk purchase of such rights from third parties. At initial recognition, the fair value of MSRs is established using assumptions consistent with those used to establish the fair value of existing MSRs. The Company has elected the fair value option to record its investments in MSRs in order to provide users of the consolidated financial statements with better information regarding the effects of prepayment risk and other market factors on the MSRs. Under this election, the Company records a valuation adjustment on its investments in MSRs on a quarterly basis to recognize the changes in fair value in net income as described below. The Company’s MSRs represent the right to service mortgage loans. As an owner and manager of MSRs, the Company may be obligated to fund advances of principal and interest payments due to third-party owners of the loans, but not yet received from the individual borrowers. These advances are reported as servicing advances within the “Receivables and other assets” line item on the consolidated balance sheets. MSRs are reported at fair value on the consolidated balance sheets. Although transactions in MSRs are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels, costs to service and discount rates). Changes in the fair value of MSRs as well as servicing fee income and servicing expenses are reported on the consolidated statements of income. In determining the valuation of MSRs, management used internally developed models that are primarily based on observable market-based inputs but which also include unobservable market data inputs (see Note 9). For reporting purposes, conventional conforming loans are aggregated into one category.

Revenue Recognition – Mortgage servicing fee income represents revenue earned for servicing mortgage loans. The servicing fees are based on a contractual percentage of the outstanding principal balance and recognized as revenue as the related mortgage payments are collected. Corresponding costs to service are charged to expense as incurred. Approximately \$1.4 million and \$787,000 in reimbursable servicing advances were receivable at December 31, 2016 and December 31, 2015, respectively, and have been classified within “Receivables and other assets” on the consolidated balance sheets. Advances on Fannie Mae and Freddie Mac MSRs made in accordance with the relevant guidelines are recoverable. As a result, the Company has determined that no reserves for unrecoverable advances are necessary at December 31, 2016 and 2015.

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

As a result of the Company’s investments in MSRs, it is obligated from time to time to repurchase an underlying loan from the GSE for which it is being serviced due to an alleged breach of a representation or warranty. Loans acquired in this manner are recorded at the purchase price less any principal recoveries and are then offered for sale in the scratch and dent market. In the year ended December 31, 2016 the Company purchased five loans, with an aggregate UPB of approximately \$1.64 million at the time of purchase, as required by the applicable agency. None of those loans have been sold.

Derivatives and Hedging Activities

Derivative transactions include swaps, swaptions, Treasury futures and “to-be-announced” securities (“TBAs”). Swaps and swaptions are entered into by the Company solely for interest rate risk management purposes. TBAs and treasury futures are used for duration risk and basis risk management purposes. The decision of whether or not a given transaction/position (or portion thereof) is economically hedged is made on a case-by-case basis, based on the risks involved and other factors as determined by management, including restrictions imposed by the Code on REITs. In determining whether to economically hedge a risk, the Company may consider whether other assets, liabilities, firm commitments and anticipated transactions already offset or

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reduce the risk. All transactions undertaken as economic hedges are entered into with a view towards minimizing the potential for economic losses that could be incurred by the Company. Generally, derivatives entered into are not intended to qualify as hedges under GAAP, unless specifically stated otherwise.

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

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

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

Cash and Cash Equivalents and Restricted Cash

The Company considers all highly liquid short-term investments with maturities of 90 days or less when purchased to be cash equivalents. Substantially all amounts on deposit with major financial institutions exceed insured limits. Restricted cash represents the Company's cash held by counterparties as collateral against the Company's derivatives in each case as of December 31, 2016 (approximately \$1.1 million), borrowings under its repurchase agreements (approximately \$20.4 million) as well as cash held that relates to the \$8.9 million of borrowings on a term loan (“Term Loan”) (approximately \$1.1 million). As of December 31, 2015, cash held by counterparties as collateral against the Company's derivatives (approximately \$4.6 million), borrowings under its repurchase agreements (approximately \$4.2 million) as well as cash held that relates to the \$24.3 million of borrowings on the Term Loan (approximately \$1.1 million). For further information on the restricted cash as it relates to the Term Loan, see Note 13.

Due to Affiliate

This represents amounts due to the Manager pursuant to the Management Agreement. For further information on the Management Agreement, see Note 7.

Income Taxes

The Company elected to be taxed as a REIT under the Code commencing with its short taxable year ended December 31, 2013. The Company expects to continue to qualify to be treated as a REIT. As long as the Company qualifies as a REIT, the Company generally will not be subject to U.S. federal income taxes on its taxable income to the extent it annually distributes at least 90% of its REIT taxable income to stockholders and does not engage in prohibited transactions. The Company's taxable REIT subsidiaries (“TRSs”), CHMI Solutions and Aurora, are subject to U.S. federal income taxes on their taxable income.

The Company accounts for income taxes in accordance with ASC 740, *Income Taxes*. ASC 740 requires the recording of deferred income taxes that reflect the net tax effect of temporary differences between the carrying amounts of the Company's assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, including operating loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is

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recognized in earnings in the period that includes the enactment date. The Company assesses its tax positions for all open tax years and determines if it has any material unrecognized liabilities in accordance with ASC 740. The Company records these liabilities to the extent it deems them more-likely-than-not to be incurred. The Company records interest and penalties related to income taxes within the provision for income taxes in the consolidated statements of income. The Company has not incurred any interest or penalties.

Realized Gain (Loss) on Investments, Net

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

	Year Ended December 31,		
	2016	2015	2014
Realized gain (loss) on RMBS, net			
Gain on RMBS	\$ 1,572	\$ 1,398	\$ 303
Loss on RMBS	(173)	(544)	(363)
Net realized gain (loss) on RMBS	1,399	854	(60)
Realized gain (loss) on derivatives, net	(7,963)	(3,913)	(2,643)
Unrealized gain (loss) on derivatives, net	12,080	(59)	(6,564)
Realized gain (loss) on Excess MSRs, net	1,520	—	—
Unrealized gain (loss) on Excess MSRs, net	249	(19)	(5,100)
Unrealized gain (loss) on MSRs, net	(3,285)	(1,123)	—
Realized gain (loss) on acquired assets, net	—	449	—
Total	\$ 4,000	\$ (3,811)	\$ (14,367)

The gain and loss on the specified categories of investments presented above represent the amounts reclassified from accumulated other comprehensive income (loss) in earnings.

Repurchase Agreements and Interest Expense

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

Federal Home Loan Bank of Indianapolis Advances

Advances from the Federal Home Loan Bank of Indianapolis (“FHLBI”) at December 31, 2015 were secured by the pledge of Agency RMBS, had bullet maturities and bore interest at rates based on specified margins over LIBOR. Advances were treated as collateralized financing transactions and were carried at their contractual amounts. Interest was recorded at the contractual amount on an accrual basis. See Note 12 for information regarding the regulatory change leading to the withdrawal of our captive insurance subsidiary from membership in the FHLBI.

Dividends Payable

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

Comprehensive Income

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

Business Combinations

Business combinations are accounted for under the acquisition method of accounting in accordance with ASC Topic 805, *Business Combinations* (“ASC 805”). Under the acquisition method the acquiring entity in a business combination recognizes 100 percent of the acquired assets and assumed liabilities, regardless of the percentage owned, at their estimated fair values as the date of acquisition. Any excess of the purchase price over the fair value of net assets and other identifiable intangible assets acquired is recorded as goodwill. To the extent the fair value of net assets acquired, including other identifiable assets, exceeds the purchase price, a bargain purchase gain is recognized. Assets acquired and liabilities assumed from contingencies must also be recognized at fair value, if the fair value can be determined during the measurement period. Results of operations of an acquired business are included in the consolidated statements of income from the date of acquisition. Acquisition-related costs, including conversion and restructuring charges, are expensed as incurred. We applied this guidance to the Aurora acquisition that occurred in 2015; see Note 17 for further information.

Recent Accounting Pronouncements

Revenue Recognition – In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, *Revenue from Contracts with Customers*, which supersedes the revenue recognition requirements in ASC 606, *Revenue Recognition*, and most industry-specific guidance throughout the Industry Topics of the Codification. Under the new revenue recognition guidance, entities are required to identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract and recognize revenue when the entity satisfies a performance obligation. In April 2015, the FASB voted for a one-year deferral of the effective date, resulting in this new guidance being effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017. Subsequent to the initial issuance, the FASB has continued to issue updates to this guidance to provide additional clarification and implementation instructions to issuers regarding (i) principal versus agent considerations, (ii) identifying performance obligations, (iii) licensing, and (iv) narrow-scope improvements and practical expedients relating to assessing collectability, presentation of sales taxes, non-cash consideration, and completed contracts and contract modifications at transition. The Company has reviewed the scope of the guidance and monitored the determinations of the FASB Transition Resource Group and concluded that a number of the Company's most significant revenue streams are not within the scope of the standard because the standard does not apply to revenue on contracts accounted for under the transfers and servicing of financial assets or financial instruments standards. Therefore, revenue recognition for these contracts will remain unchanged. Further, the FASB has issued, and may issue in the future, interpretive guidance that may cause the Company's evaluation to change. However, the Company continues to evaluate certain select revenue streams for the effect that this guidance will have on its consolidated financial statements. The Company is also still assessing the standard's new disclosure requirements. The Company has not yet selected a transition method.

Going Concern – In August 2014, the FASB issued ASU 2014-15, *Disclosures of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which amends ASC Subtopic 205-40, *Presentation of Financial Statements – Going Concern*. ASU 2014-15 intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. This standard was effective for the Company beginning December 31, 2016. The Company's disclosures reflect required elements of this standard as a result of management's evaluation.

Business Combinations – In September 2015, the FASB issued ASU 2015-16, *Simplifying the Accounting for Measurement-Period Adjustments*, which amends ASC 805, *Business Combinations*. ASU 2015-16 provides updated guidance regarding simplifying the accounting for recognizing adjustments to provisional amounts identified during the measurement period in a business combination. To simplify the accounting for these adjustments, the amendments in this update eliminate the requirement to retrospectively account for the adjustments and to recognize them in the period that they are identified. This guidance was effective for the Company beginning January 1, 2016. The adoption of this guidance did not have a significant impact on the Company's consolidated financial statements.

Leases – In February 2016, the FASB issued ASU 2016-02, *Leases*, an accounting standards update that requires the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. A lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for

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the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset to not recognize lease assets and lease liabilities. In transition, lessees are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach, which includes a number of optional practical expedients that entities may elect to apply. This guidance is effective for fiscal years beginning after December 15, 2018, with early application permitted. While the Company is currently evaluating the effect that this guidance will have on its consolidated financial statements, it will result in the recognition of certain operating leases as right-of-use assets and lease liabilities on the consolidated balance sheets. The Company currently has no commitments under noncancelable operating leases.

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

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

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

Restricted Cash – In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows*, an accounting standards update that amends the guidance on restricted cash within the statement of cash flows. The update amends the classification of restricted cash and cash equivalents to be included within cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts. This guidance is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. The adoption will impact the presentation of the cash flows, but will not otherwise have a material impact on the consolidated results of operations or financial condition.

Business Combinations – In January 2017, the FASB issued ASU 2017-01, *Business Combinations*, an accounting standards update that amends the guidance on business combinations. The update clarifies the definition of a business and provides a framework that gives entities a basis for making reasonable judgments about whether a transaction should be accounted for as an acquisition of assets or a business. This guidance is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017. The Company will apply this guidance to its assessment of applicable transactions, such as acquisitions and disposals of assets or business, consummated after the adoption date.

Changes in Presentation

Certain prior period amounts have been reclassified to conform to current period presentation.

Note 3 — Segment Reporting

The Company conducts its business through the following segments: (i) investments in RMBS; (ii) investments in Servicing Related Assets; and (iii) “All Other” which consists primarily of general and

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administrative expenses including fees to the directors and management fees pursuant to the Management Agreement (see Note 7). For segment reporting purposes, the Company does not allocate interest income on short-term investments or general and administrative expenses.

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

	Servicing Related Assets	RMBS	All Other	Total
Income Statement				
Year Ended December 31, 2016				
Interest income	\$ 14,129	\$ 16,593	\$ —	\$ 30,722
Interest expense	1,371	6,437	—	7,808
Net interest income	12,758	10,156	—	22,914
Servicing fee income	7,579	—	—	7,579
Servicing costs	2,562	—	—	2,562
Net servicing income	5,017	—	—	5,017
Other income	(1,516)	5,516	—	4,000
Other operating expenses	—	—	6,230	6,230
(Benefit from) provision for corporate business taxes	458	—	—	458
Net income (loss)	\$ 15,801	\$ 15,672	\$ (6,230)	\$ 25,243
Year Ended December 31, 2015				
Interest income	\$ 14,313	\$ 13,399	\$ —(A)	\$ 27,712
Interest expense	583	5,400	—	5,983
Net interest income	13,730	7,999	—	21,729
Servicing fee income	1,719	—	—	1,719
Servicing costs	761	—	—	761
Net servicing income	958	—	—	958
Other income	(693)	(3,118)	—	(3,811)
Other operating expenses	—	—	5,864	5,864
(Benefit from) provision for corporate business taxes	(343)	—	—	(343)
Net income (loss)	\$ 14,338	\$ 4,881	\$ (5,864)	\$ 13,355
Year Ended December 31, 2014				
Interest income	\$ 15,854	\$ 10,643	\$ —(A)	\$ 26,497
Interest expense	—	4,307	—	4,307
Net interest income	15,854	6,336	—	22,190
Servicing fee income	—	—	—	—
Servicing costs	—	—	—	—
Net servicing income	—	—	—	—
Other income	(5,100)	(9,267)	—	(14,367)
Other operating expenses	—	5,588	5,588	—
(Benefit from) provision for corporate business taxes	(140)	—	—	(140)
Net income (loss)	\$ 10,894	\$ (2,931)	\$ (5,588)	\$ 2,375
Balance Sheet				
December 31, 2016				
Investments	\$ 61,263	\$ 671,904	\$ —	\$ 733,167
Other assets	8,826	32,495	18,390	59,711
Total assets	70,089	704,399	18,390	792,878
Debt	22,886	594,615	—	617,501
Other liabilities	2,481	9,490	7,397	19,368
Total liabilities	25,367	604,105	7,397	636,869
GAAP book value	\$ 44,722	\$ 100,294	\$ 10,993	\$ 156,009
December 31, 2015				
Investments	\$ 97,803	\$ 508,242	\$ —	\$ 606,045
Other assets	3,562	13,984	12,749	30,295
Total assets	101,365	522,226	12,749	636,340
Debt	24,313	447,810	—	472,123
Other liabilities	1,883	4,903	5,094	11,880
Total liabilities	26,196	452,713	5,094	484,003
GAAP book value	\$ 75,169	\$ 69,513	\$ 7,655	\$ 152,337

(A) de minimus (\$192 rounds to \$0)

Note 4 — Investments in RMBS

All of the Company’s RMBS are classified as available for sale and are, therefore, reported at fair value with changes in fair value recorded in other comprehensive income except for securities that are OTTI. There were approximately \$173,000 of OTTI during the year ended December 31, 2016. The Company did not record any OTTI charges during the year ended December 31, 2015. The following is a summary of the Company’s RMBS investments as of the periods indicated, (dollars in thousands):

Summary of RMBS Assets

As of December 31, 2016

Asset Type	Original Face Value	Book Value	Gross Unrealized		Carrying Value ^(A)	Number of Securities	Weighted Average			Maturity (Years) ^(D)
			Gains	Losses			Rating	Coupon	Yield ^(C)	
RMBS										
Fannie Mae	\$493,645	\$454,012	\$ 1,517	\$ (6,592)	\$ 448,937	68	(B)	3.74%	3.32%	24
Freddie Mac	222,469	200,207	587	(2,691)	198,103	27	(B)	3.62%	3.47%	26
CMOs	34,596	24,086	857	(79)	24,864	9	Unrated	4.78%	5.04%	12
Total/Weighted Average	\$750,710	\$678,305	\$ 2,961	\$ (9,362)	\$ 671,904	104		3.74%	3.43%	24

As of December 31, 2015

Asset Type	Original Face Value	Book Value	Gross Unrealized		Carrying Value ^(A)	Number of Securities	Weighted Average			Maturity (Years) ^(D)
			Gains	Losses			Rating	Coupon	Yield ^(C)	
RMBS										
Fannie Mae	\$329,767	\$308,367	\$ 1,961	\$ (1,556)	\$ 308,772	44	(B)	3.77%	3.59%	24
Freddie Mac	208,154	193,567	821	(977)	193,411	24	(B)	3.61%	3.48%	24
CMOs	16,646	6,493	—	(434)	6,059	4	Unrated	4.55%	7.39%	10
Total/Weighted Average	\$554,567	\$508,427	\$ 2,782	\$ (2,967)	\$ 508,242	72		3.72%	3.60%	23

- (A) See Note 9 regarding the estimation of fair value, which approximates carrying value for all securities.
- (B) The Company used an implied AAA rating for the Fannie Mae and Freddie Mac securities.
- (C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the Book Value. Prior period amounts have been reclassified to conform to current period presentation.
- (D) The weighted average stated maturity.

Summary of RMBS Assets by Maturity

As of December 31, 2016

Years to Maturity	Original Face Value	Book Value	Gross Unrealized		Carrying Value ^(A)	Number of Securities	Weighted Average		Maturity (Years) ^(D)	
			Gains	Losses			Rating	Coupon		Yield ^(C)
Less than 1 Year	\$ —	\$ —	\$ —	\$ —	\$ —	—	—%	—%	—	
1-5 Years	—	—	—	—	—	—	—%	—%	—	
5-10 Years	16,069	17,110	185	(454)	16,841	3	(B)	4.18%	3.99%	8
Over 10 Years	734,641	661,195	2,776	(8,908)	655,063	101	(B)	3.73%	3.42%	24
Total/Weighted Average	\$750,710	\$678,305	\$ 2,961	\$ (9,362)	\$ 671,904	104		3.74%	3.43%	24

As of December 31, 2015

Years to Maturity	Original Face Value	Book Value	Gross Unrealized		Carrying Value ^(A)	Number of Securities	Weighted Average		Maturity (Years) ^(D)	
			Gains	Losses			Rating	Coupon		Yield ^(C)
Less than 1 Year	\$ —	\$ —	\$ —	\$ —	\$ —	—	—	—	—	
1-5 Years	—	—	—	—	—	—	—	—	—	
5-10 Years	5,500	5,553	—	(216)	5,337	3	(B)	4.76%	4.96%	9
Over 10 Years	549,067	502,874	2,782	(2,751)	502,905	69	(B)	3.71%	3.59%	24
Total/Weighted Average	\$554,567	\$508,427	\$ 2,782	\$ (2,967)	\$ 508,242	72		3.72%	3.60%	23

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

(B) The Company used an implied AAA rating for the Fannie Mae and Freddie Mac securities.

(C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the Book Value. Prior period amounts have been reclassified to conform to current period presentation.

(D) The weighted average stated maturity.

At December 31, 2016 and December 31, 2015, the Company pledged Agency RMBS investments with a carrying value of approximately \$608.6 million and \$399.8 million respectively, as collateral for repurchase agreements. At December 31, 2016, the Company had no pledged Agency RMBS investments as collateral for FHLBI advances. At December 31, 2015, the Company pledged Agency RMBS investments with a carrying value of approximately \$83.2 million, as collateral for FHLBI advances. At December 31, 2016 and December 31, 2015, the Company did not have any securities purchased from and financed with the same counterparty that did not meet the conditions of ASC 860, *Transfers and Servicing*, to be considered linked transactions and, therefore, classified as derivatives.

Unrealized losses that are considered other-than-temporary are recognized currently in earnings. Based on management's analysis of these securities, the performance of the underlying loans and changes in market factors, management determined that unrealized losses as of the balance sheet date on the Company's securities were primarily the result of changes in market factors, rather than issuer-specific credit impairment. The Company performed analyses in relation to such securities, using management's best estimate of their cash flows, which support its belief that the carrying values of such securities were fully recoverable over their expected holding period. Such market factors include changes in market interest rates and credit spreads, or certain macroeconomic events, which did not directly impact the Company's ability to collect amounts contractually due. Management continually evaluates the credit status of each of the Company's securities and the collateral supporting those securities. This evaluation includes a review of the credit of the issuer of the security (if applicable), the credit rating of the security (if applicable), the key terms of the security (including credit support), debt service coverage and loan to value ratios, the performance of the pool of underlying loans and the estimated value of the collateral supporting such loans, including the effect of local, industry and broader economic trends and factors. In connection with the above, the Company weighs the fact that all of its investments in Agency RMBS are guaranteed by U.S. government agencies or U.S. government sponsored entities.

These factors include underlying loan default expectations and loss severities, which are analyzed in connection with a particular security's credit support, as well as prepayment rates. The result of this evaluation is considered when determining management's estimate of cash flows and in relation to the amount of the unrealized loss and the period elapsed since it was incurred. Significant judgment is required in this analysis.

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During the years ended December 31, 2016, the Company recorded approximately \$173,000 charges for OTTI. For the year ended December 31, 2015, the Company did not record any OTTI charges.

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

RMBS Unrealized Loss Positions

As of December 31, 2016

Duration in Loss Position	Original Face Value	Book Value	Gross Unrealized Losses	Carrying Value ^(A)	Number of Securites	Weighted Average			Maturity (Years) ^(D)
						Rating	Coupon	Yield ^(C)	
Less than Twelve Months	\$ 494,847	\$ 476,129	\$ (9,362)	\$ 466,767	68	(B)	3.65%	3.40%	25
Twelve or More Months	—	—	—	—	—	(B)	—%	—%	—
Total/Weighted Average	\$ 494,847	\$ 476,129	\$ (9,362)	\$ 466,767	68		3.65%	3.40%	25

As of December 31, 2015

Duration in Loss Position	Original Face Value	Book Value	Gross Unrealized Losses	Carrying Value ^(A)	Number of Securites	Weighted Average			Maturity (Years) ^(D)
						Rating	Coupon	Yield ^(C)	
Less than Twelve Months	\$ 271,585	\$ 274,996	\$ (2,749)	\$ 272,247	39	(B)	3.65%	3.48%	24
Twelve or More Months	11,146	940	(218)	722	1	(B)	3.00%	25.37%	17
Total/Weighted Average	\$ 282,731	\$ 275,936	\$ (2,967)	\$ 272,969	40		3.65%	3.55%	24

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

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

(C) The weighted average yield is based on the most recent annualized monthly interest income, divided by the Book Value. Prior period amounts have been reclassified to conform to current period presentation.

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

Note 5 — Investments in Servicing Related Assets

Excess MSRs

In October 2013, the Company entered into an agreement (“Excess MSR Agreement 1”) with Freedom Mortgage Corporation (“Freedom Mortgage”) to invest in Excess MSRs with Freedom Mortgage. Freedom Mortgage originated the mortgage servicing rights on the related pool of residential fixed rate Ginnie Mae-eligible FHA and VA mortgage loans with an aggregate unpaid principal balance (“UPB”) of approximately \$10.0 billion (“Excess MSR Pool 1”). Freedom Mortgage was entitled to receive an initial weighted average total mortgage servicing amount of approximately 28 basis points (“bps”) on the performing UPB, as well as any ancillary income from Excess MSR Pool 1. Pursuant to Excess MSR Agreement 1, Freedom Mortgage performed all servicing functions and advancing functions related to Excess MSR Pool 1 for a basic fee (the amount representing reasonable compensation for performing the servicing duties) of 8 bps. The remainder, or “excess mortgage servicing amount,” was initially equal to a weighted average of 20 bps.

Pursuant to Excess MSR Agreement 1, the Company acquired the right to receive 85% of the excess mortgage servicing amount on Excess MSR Pool 1 and, subject to certain limitations and pursuant to a recapture agreement (the “Excess MSR Pool 1—Recapture Agreement”), 85% of the Excess MSRs on future mortgage loans originated by Freedom Mortgage that represented refinancings of loans in Excess MSR Pool 1 (which loans then become part of Excess MSR Pool 1) for approximately \$60.6 million. Freedom Mortgage co-invested, pari passu with the Company, in 15% of the Excess MSRs. Freedom Mortgage, as servicer, also retained the ancillary income and the servicing obligations and liabilities.

On November 15, 2016, the Company sold all of the Excess MSRs relating to Excess MSR Pool 1 to Freedom Mortgage, and Excess MSR Agreement 1 was terminated. See Note 7.

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In October 2013, the Company entered into an agreement (“Excess MSR Agreement 2”) with Freedom Mortgage to invest with Freedom Mortgage in another pool of Excess MSR. Freedom Mortgage acquired the mortgage servicing rights from a third-party seller on a pool of residential Ginnie Mae-eligible VA hybrid adjustable rate mortgage loans with an outstanding aggregate principal balance of approximately \$10.7 billion (“Excess MSR Pool 2”). Freedom Mortgage is entitled to receive an initial weighted average total mortgage servicing amount of 44 bps on the performing UPB, as well as any ancillary income from Excess MSR Pool 2. Pursuant to Excess MSR Agreement 2, Freedom Mortgage performs all servicing functions and advancing functions related to Excess MSR Pool 2 for a basic fee (the amount representing reasonable compensation for performing the servicing duties) of 10 bps. Therefore, the remainder, or “excess mortgage servicing amount” is initially equal to a weighted average of 34 bps.

Pursuant to Excess MSR Agreement 2, The Company acquired the right to receive 50% of the excess mortgage servicing amount on Excess MSR Pool 2 and, subject to certain limitations and pursuant to a recapture agreement (the “Excess MSR Pool 2—Recapture Agreement”), 50% of the Excess MSR on future mortgage loans originated by Freedom Mortgage that represent refinancings of loans in Excess MSR Pool 2 (which loans then become part of Excess MSR Pool 2) for approximately \$38.4 million. Freedom Mortgage has co-invested, *pari passu* with the Company, in 50% of the Excess MSR. Freedom Mortgage, as servicer, also retains the ancillary income and the servicing obligations and liabilities. If Freedom Mortgage is terminated as the servicer, the Company’s right to receive its portion of the excess mortgage servicing amount is also terminated. To the extent that Freedom Mortgage is terminated as the servicer and receives a termination payment, the Company is entitled to a pro rata share, or 50%, of such termination payment.

On February 1, 2017, the Company sold all of the Excess MSR relating to Excess MSR Pool 2 to Freedom Mortgage and Excess MSR Agreement 2 was terminated. See Notes 7 and 17.

In October 2013, the Company also entered into a flow and bulk Excess MSR purchase agreement related to future purchases of Excess MSR from Freedom Mortgage (the “Flow and Bulk Excess MSR Purchase Agreement”). Freedom Mortgage was entitled to receive an initial weighted average total mortgage servicing amount of 44 bps on the performing UPB, as well as any ancillary income from Excess MSR Pool 2014. On February 28, 2014, pursuant to the flow and bulk Excess MSR Purchase Agreement, the Company purchased from Freedom Mortgage Excess MSR on mortgage loans originated by Freedom Mortgage during the first quarter of 2014 with an UPB of approximately \$76.8 million. The Company acquired an approximate 85% interest in the Excess MSR for approximately \$567,000. The terms of the purchase include recapture provisions that are the same as those in the Excess MSR acquisition agreements the Company entered into with Freedom Mortgage in October 2013.

On March 31, 2014, pursuant to the flow and bulk Excess MSR Purchase Agreement, the Company purchased from Freedom Mortgage Excess MSR on mortgage loans originated by a third party originator with an aggregate UPB of approximately \$159.8 million. Freedom Mortgage purchased the MSR on these mortgage loans from a third party on January 31, 2014. The Company acquired an approximate 71% interest in the Excess MSR for approximately \$946,000. The terms of the purchase include recapture provisions that are the same as those in the Excess MSR acquisition agreements the Company entered into with Freedom Mortgage in October 2013.

On June 30, 2014, pursuant to the flow and bulk Excess MSR purchase agreement, the Company purchased from Freedom Mortgage Excess MSR on mortgage loans originated by Freedom Mortgage during the second quarter of 2014 with an aggregate UPB of approximately \$98.1 million. The Company acquired an approximate 85% interest in the Excess MSR for approximately \$661,000. The terms of the purchase include recapture provisions that are the same as those in the Excess MSR acquisition agreements the Company entered into with Freedom Mortgage in October 2013.

The mortgage loans underlying the Excess MSR purchased in 2014 are collectively referred to as “Pool 2014,” and the recapture provisions, which are identical, are collectively referred to as the “Pool 2014—Recapture Agreement.”

On November 15, 2016, the Company sold all of the Excess MSR relating to Excess MSR Pool 2014 to Freedom Mortgage, and the flow and bulk Excess MSR purchase agreement was terminated. See Note 7.

MSRs

On May 29, 2015, in conjunction with the acquisition of Aurora, the Company acquired MSRs on conventional mortgage loans with an aggregate UPB of approximately \$718.4 million.

On June 10, 2015, the Company agreed to transfer the direct servicing of the MSR portfolio to Freedom Mortgage pursuant to a subservicing agreement with Freedom Mortgage. The transfer occurred in September 2015. Pending the transfer, the former servicing employees of Aurora, now employees of Freedom Mortgage, directly serviced the portfolio for Aurora. The servicing was provided at cost pursuant to the Management Agreement with the Manager and the Services Agreement between the Manager and Freedom Mortgage. The cost for such services is included in servicing costs on the consolidated statements of income.

Aurora subsequently acquired from third parties three portfolios of MSRs on loans owned or securitized by Fannie Mae or Freddie Mac with an aggregate UPB of approximately \$3.1 billion as of their respective closing dates.

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

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

Servicing Related Assets Summary

As of December 31, 2016

	Unpaid Principal Balance	Amortized Cost Basis ^(A)	Carrying Value ^(B)	Weighted Average Coupon	Weighted Average Maturity (Years) ^(C)	Changes in Fair Value Recorded in Other Income (Loss) ^(D)
Excess MSR Pool 2	\$6,053,142	\$ 19,754	\$ 28,526	2.96%	26.3	\$ (493)
Excess MSR Pool 2 — Recapture Agreement	—	1,187	866			742
MSRs ^(E)	3,262,181	35,156	31,871	3.81	23.7	(3,285)
Total	\$9,315,323	\$ 56,097	\$ 61,263	3.26%	25.4	\$ (3,036)

As of December 31, 2015

	Unpaid Principal Balance	Amortized Cost Basis ^(A)	Carrying Value ^(B)	Weighted Average Coupon	Weighted Average Maturity (Years) ^(C)	Changes in Fair Value Recorded in Other Income (Loss) ^(D)
Excess MSR Pool 1	\$ 7,416,465	\$ 39,483	\$ 42,837	3.51%	26.0	\$ (2,822)
Excess MSR Pool 1 — Recapture Agreement	—	2,209	645	—	—	331
Excess MSR Pool 2	7,279,706	23,116	32,338	2.78%	27.1	2,626
Excess MSR Pool 2 — Recapture Agreement	—	1,780	716	—	—	(324)
Excess MSR Pool 2014	265,890	1,685	1,506	3.65%	27.4	170
Excess MSR Pool 2014 — Recapture Agreement	—	—	—	—	—	—
MSRs ^(E)	2,016,351	20,884	19,761	3.76%	22.7	(1,123)
Total	\$ 16,978,412	\$ 89,157	\$ 97,803	3.23%	26.1	\$ (1,142)

(A) The amortized cost basis of the recapture agreements is determined based on the relative fair values of the recapture agreements and related Excess MSRs at the time they were acquired.

(B) Carrying value represents the fair value of the pools or recapture agreements, as applicable (see Note 9).

(C) The weighted average maturity represents the weighted average expected timing of the receipt of cash flows of each investment.

(D) The portion of the change in fair value of the recapture agreement relating to loans recaptured as of December 31, 2016 and December 31, 2015 is reflected in the respective pool.

(E) MSR cost basis consists of the carrying value of the prior period, adjusted for any acquisitions made during the current period.

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

Geographic Concentration of Servicing Related Assets

As of December 31, 2016

	Percentage of Total Outstanding Unpaid Principal Balance
Texas	10.0%
California	8.9%
Florida	6.7%
Virginia	5.9%
North Carolina	5.8%
Georgia	5.8%
New Jersey	5.6%
Washington	5.5%
Colorado	5.2%
All other	40.6%
Total	100.0%

As of December 31, 2015

	Percentage of Total Outstanding Unpaid Principal Balance
California	12.3%
Texas	9.4%
Florida	6.5%
Virginia	6.0%
North Carolina	5.2%
Washington	5.1%
Georgia	5.0%
All other	50.5%
Total	100.0%

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

Note 6 — Equity and Earnings per Share

Equity Incentive Plan

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

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

Equity Incentive Plan Information

As of December 31, 2016

	Number of Securities Issued or to be Issued Upon Exercise	Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans
Equity compensation Plans Approved By Shareholders		1,335,218
LTIP-OP Units	140,350	
Forfeited LTIP-OP Units	(916)	
Shares of Common Stock	28,503	
Forfeited Shares of Common Stock	(3,155)	
Equity Compensation Plans Not Approved By Shareholders	—	—

As of December 31, 2015

	Number of Securities Issued or to be Issued Upon Exercise	Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans
Equity compensation Plans Approved By Shareholders		1,377,112
LTIP-OP Units	103,850	
Shares of Common Stock	19,038	
Equity Compensation Plans Not Approved By Shareholders	—	—

As of December 31, 2014

	Number of Securities Issued or to be Issued Upon Exercise	Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans
Equity compensation Plans Approved By Shareholders		1,421,607
LTIP-OP Units	68,850	
Shares of Common Stock	9,543	
Equity Compensation Plans Not Approved By Shareholders	—	—

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

An LTIP-OP Unit and a share of common stock of the Company have substantially the same economic characteristics in as much as they effectively share equally in the net income or loss of the Operating

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

The table below sets forth certain information regarding the LTIP-OP Units that have been granted by the board of directors (dollars in thousands, except per share data):

LTIP-OP Unit Grant Information

<u>Grant Date</u>	<u>Number of Grantees</u>	<u>Stock Price on Grant Date</u>	<u>Number of Units Granted</u>	<u>Aggregate Fair Market Value</u>
June 15, 2016	14	\$ 15.85	36,500	\$ 579
September 9, 2015	12	\$ 15.80	35,000	\$ 553
June 10, 2014	10	\$ 19.33	31,350	\$ 606

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

As of December 31, 2016, 69,789 LTIP-OP Units have vested. The Company recognized approximately \$618,000 and \$463,000 in share-based compensation expense in the years ended December 31, 2016 and 2015, respectively. There was approximately \$849,000 of total unrecognized share-based compensation expense as of December 31, 2016, related to the 69,645 non-vested LTIP-OP Units. This unrecognized share-based compensation expense is expected to be recognized ratably over the remaining vesting period of up to three years. The aggregate expense related to the LTIP-OP Unit grants is presented as "General and administrative expense" in the Company's consolidated income statement.

On January 27, 2014, the Company granted each of the independent directors pursuant to the 2013 Plan \$10,000 (based on the closing price on the grant date) of common stock (530 shares each for a total of 1,590 shares), which were fully vested on the date of grant, and \$50,000 (based on the closing price on the date of grant) of restricted shares of common stock (2,651 shares each for a total of 7,953 shares) which were subject to forfeiture in certain circumstances within one year from the grant date. They are no longer subject to forfeiture and are vested.

On September 9, 2015, the Company granted each of the independent directors pursuant to the 2013 Plan \$50,000 (based on the closing price on the date of grant) of restricted shares of common stock (3,165 each for a total of 9,495 shares) which were subject to forfeiture in certain circumstances within one year from the grant date. The shares are no longer subject to forfeiture and are vested. This unrecognized share-based compensation expense is expected to be recognized ratably over the remaining vesting period of up to three years.

On June 15, 2016, pursuant to the 2013 Plan, the Company granted each of the independent directors \$50,000 (based on the closing price on the date of grant) of restricted shares of common stock (3,155 shares each for a total of 9,465 shares) which were subject to forfeiture in certain circumstances within one year from the grant date. This unrecognized share-based compensation expense is expected to be recognized ratably over the vesting period. The 3,155 shares granted to Mr. Kislak were forfeited when he resigned as a director of the Company on September 19, 2016. The forfeited shares have been returned to the shares available for future issuance under the 2013 Plan.

As of December 31, 2016, 1,335,218 shares of common stock remain available for future issuance under the 2013 Plan.

Non-Controlling Interests in Operating Partnership

Non-controlling interests in the Operating Partnership in the accompanying consolidated financial statements relate to LTIP-OP Units in the Operating Partnership held by parties other than the Company.

As of December 31, 2016, the non-controlling interest holders in the Operating Partnership owned 139,434 LTIP-OP Units, or approximately 1.9% of the Operating Partnership. Pursuant to ASC 810, *Consolidation*,

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changes in a parent's ownership interest (and transactions with non-controlling interest unit holders in the Operating Partnership) while the parent retains its controlling interest in its subsidiary should be accounted for as equity transactions. The carrying amount of the non-controlling interest will be adjusted to reflect the change in its ownership interest in the subsidiary, with the offset to equity attributable to the Company.

Earnings per Share

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

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

	Year Ended December 31,		
	2016	2015	2014
Numerator:			
Net income attributable to common stockholders and participating securities	\$ 25,243	\$ 13,355	\$ 2,375
Net income allocable to common stockholders	\$ 24,832	\$ 13,214	\$ 2,353
Denominator:			
Weighted average common shares outstanding	7,512,444	7,509,543	7,505,546
Weighted average diluted shares outstanding	7,523,297	7,512,444	7,508,827
Basic and Dilutive:			
Basic earnings per share	\$ 3.31	\$ 1.76	\$ 0.31
Diluted earnings per share	\$ 3.30	\$ 1.76	\$ 0.31

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

Note 7 — Transactions with Affiliates and Affiliated Entities

Manager

The Company has entered into a management agreement with the Manager, pursuant to which the Manager provides for the day-to-day management of the Company's operations (the "Management Agreement"). The Management Agreement requires the Manager to manage the Company's business affairs in conformity with the policies that are approved and monitored by the Company's board of directors. The Management Agreement terminates on October 22, 2020, subject to automatic renewal for successive one-year terms and to certain termination rights. The Manager's performance is reviewed prior to any renewal and may be terminated by the Company for cause without payment of a termination fee, or may be terminated without cause with payment of a termination fee, as defined in the Management Agreement, equal to three times the average annual management fee amount earned by the Manager during the two four-quarter periods ending as of the end of the most recently completed fiscal quarter prior to the effective date of the termination, upon either the affirmative vote of at least two-thirds of the members of the board of directors or the affirmative vote of the holders of at least a majority of the outstanding common stock. Pursuant to the Management Agreement, the Manager, under the supervision of the Company's board of directors, formulates investment strategies, arranges for the acquisition of assets, arranges for financing, monitors the performance of the Company's assets and provides certain advisory, administrative and managerial services in connection with the operations of the Company. For performing these services, the Company pays the Manager the management fee which is payable in cash quarterly in arrears, in an amount equal to 1.5% per annum of the stockholders' equity (as defined in the Management Agreement).

The Manager is a party to a services agreement (the "Services Agreement") with Freedom Mortgage, pursuant to which Freedom Mortgage provides to the Manager the personnel, services and resources as needed

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

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

Management Fee to Affiliate

	Year Ended December 31,		
	2016	2015	2014
Management fees	\$ 2,303	\$ 2,263	\$ 2,150
Compensation reimbursement	643	520	410
Total	\$ 2,946	\$ 2,783	\$ 2,560

Subservicing Agreement

Freedom Mortgage is directly sub-servicing the Company's portfolio of MSR's pursuant to a subservicing agreement entered into on June 10, 2015. The agreement has an initial term of three (3) years, expiring on September 1, 2018, and is subject to automatic renewal for additional three year terms unless either party chooses not to renew. The agreement may be terminated without cause by either party by giving notice as specified in the agreement. Under that agreement, Freedom Mortgage agrees to service the applicable mortgage loans in accordance with applicable law and the requirements of the applicable agency. The Company pays fees for specified services which are included in "Servicing costs" on the consolidated statements of income.

Joint Marketing Recapture Agreement

In June 2016, Aurora entered into a joint marketing recapture agreement with Freedom Mortgage. Pursuant to this agreement, Freedom Mortgage will attempt to refinance certain mortgage loans underlying Aurora's MSR portfolio as directed by Aurora. If a loan is refinanced, Aurora will pay Freedom Mortgage a fee for its origination services. Freedom Mortgage will be entitled to sell the loan for its own benefit and will transfer the related MSR to Aurora. The agreement has an initial term of one year, subject to automatic renewals of one year each and subject to termination by either party upon 60 days prior notice. All new loans must qualify for sale to Fannie Mae or Freddie Mac and meet other conditions set forth in the agreement. As of December 31, 2016, MSR's on 36 loans with an aggregate unpaid principal balance of approximately \$9.8 million had been received from Freedom Mortgage which generated approximately \$20,500 in fees due to Freedom Mortgage.

On November 15, 2016, the Company completed the sale of the Pool 1 Excess MSR's and the Pool 2014 Excess MSR's to Freedom Mortgage. At the closing, the Company received cash proceeds of approximately \$38.0 million, repaid \$12.0 million of outstanding borrowings drawn on our \$25 million term loan facility with NexBank SSB, or the NexBank term loan, with a portion of the cash proceeds and released our security interests arising under the Pool 1 Agreement and the Flow Agreement. The Company invested the remaining cash proceeds in Agency RMBS and expects to redeploy those proceeds into future MSR acquisitions. See Note 19 for information regarding the sale of the Pool 2 Excess MSR's. In connection with the transactions described

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above, Freedom Mortgage agreed to make 12 monthly yield maintenance payments to the Company beginning in December 2016 aggregating \$3.0 million which are intended to mitigate the reduction in yield on the remaining assets.

Other Transactions with Affiliated Entities

The Company, through one of its subsidiaries, has entered into an uncommitted master repurchase agreement with Freedom Mortgage pursuant to which the Company may, from time to time, purchase a newly issued Ginnie Mae RMBS, subject to Freedom Mortgage's agreement to repurchase the security at a future date, generally no more than 90 days later. The Company simultaneously re-hypothecates the security to one of its counterparties with whom it has a repurchase agreement, for an identical term. There were no transactions outstanding at December 31, 2016 or 2015.

See Note 5 for a discussion of the co-investments in Excess MSRs with Freedom Mortgage and the services provided by Freedom Mortgage during the period prior to transfer to Freedom Mortgage of the direct servicing obligations for the MSRs. See Note 10 for a discussion of the Acknowledgement Agreement among the Company, Freedom Mortgage and Ginnie Mae entered into in connection with the co-investments in Excess MSRs.

For the year ended December 31, 2016, the Company earned approximately \$1.7 million in income and had a corresponding expense of approximately \$593,000 which are included in "Interest income" and "Interest expense", respectively, on the consolidated statements of income. No such related income or expense was earned or incurred during the year ended December 31, 2015. There were no such assets, or related liabilities, as of December 31, 2016 and December 31, 2015.

Note 8 — Derivative Instruments

Interest Rate Swap Agreements, Swaptions, TBAs and Treasury Futures

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

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

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

Non-hedge derivatives	December 31, 2016	December 31, 2015
Notional amount of interest rate swaps	\$ 415,850	\$ 300,300
Notional amount of swaptions	70,000	85,000
Notional amount of TBAs, net	(6,000)	—
Notional amount of Treasury Futures	50,000	—
Notional amount of options on Treasury Futures	20,000	—
Total notional amount	\$ 549,850	\$ 385,300

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

	Notional Amount	Weighted Average Pay Rate	Weighted Average Receive Rate	Weighted Average Years to Maturity
December 31, 2016	\$ 415,850	1.46%	0.90%	4.8
December 31, 2015	\$ 300,300	1.71%	0.37%	4.3

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

	Notional Amount	Weighted Average Pay Rate	Weighted Average Receive Rate ^(A)	Weighted Average Years to Maturity
December 31, 2016	\$ 70,000	2.74%	LIBOR-BBA%	10.9
December 31, 2015	\$ 85,000	3.15%	LIBOR-BBA%	10.9

(A) Floats in accordance with LIBOR.

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

Realized Gains (Losses) on Derivatives

Non-Hedge Derivatives	Income Statement Location	Year Ended December 31		
		2016	2015	2014
Interest rate swaps	Realized gain/(loss) on derivative assets	\$ (6,600)	\$ (2,128)	\$ (686)
Swaptions	Realized gain/(loss) on derivative assets	(884)	(1,036)	(1,910)
TBAs	Realized gain/(loss) on derivative assets	(316)	(400)	60
Treasury futures	Realized gain/(loss) on derivative assets	(163)	(349)	(107)
Total		\$ (7,963)	\$ (3,913)	\$ (2,643)

Offsetting Assets and Liabilities

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

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

Offsetting Assets and Liabilities

As of December 31, 2016

	Gross Amounts of Recognized Assets or Liabilities	Gross Amounts Offset in the Consolidated Balance Sheet	Net Amounts of Assets Presented in the Consolidated Balance Sheet	Gross Amounts Not Offset in the Consolidated Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received (Pledged)	
Assets						
Interest rate swaps	\$ 7,639	\$ —	\$ 7,639	\$ (7,639)	\$ —	\$ —
Swaptions	1,482	—	1,482	(1,482)	—	—
TBAs	—	—	—	—	—	—
Treasury futures	—	—	—	—	—	—
Total Assets	\$ 9,121	\$ —	\$ 9,121	\$ (9,121)	\$ —	\$ —
Liabilities						
Repurchase agreements	\$ 594,615	\$ —	\$ 594,615	\$ (574,181)	\$ (20,434)	\$ —
Interest rate swaps	339	—	339	—	(339)	—
Swaptions	—	—	—	—	—	—
TBAs	75	—	75	(75)	—	—
Treasury futures	280	—	280	526	(806)	—
Total Liabilities	\$ 595,309	\$ —	\$ 595,309	\$ (573,730)	\$ (21,579)	\$ —

As of December 31, 2015

	Gross Amounts of Recognized Assets or Liabilities	Gross Amounts Offset in the Consolidated Balance Sheet	Net Amounts of Assets Presented in the Consolidated Balance Sheet	Gross Amounts Not Offset in the Consolidated Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received (Pledged)	
Assets						
Interest rate swaps	\$ 51	\$ —	\$ 51	\$ (51)	\$ —	\$ —
Swaptions	371	—	371	(371)	—	—
TBAs	—	—	—	—	—	—
Treasury futures	—	—	—	—	(84)	—
Total Assets	\$ 422	\$ —	\$ 422	\$ (422)	\$ (84)	\$ —
Liabilities						
Repurchase agreements	\$ 385,560	\$ —	\$ 385,560	\$ (381,386)	\$ (4,174)	\$ —
Interest rate swaps	4,595	—	4,595	—	(4,595)	—
Swaptions	—	—	—	—	—	—
TBAs	—	—	—	—	—	—
Treasury futures	—	—	—	—	—	—
Total Liabilities	\$ 390,155	\$ —	\$ 390,155	\$ (381,386)	\$ (8,769)	\$ —

Note 9 – Fair Value

Fair Value Measurements

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

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

- Level 1 Inputs are quoted prices in active markets for identical assets or liabilities as of the measurement date under current market conditions. Additionally, the entity must have the ability to access the active market and the quoted prices cannot be adjusted by the entity.
- Level 2 Inputs include quoted prices in active markets for similar assets or liabilities; quoted prices in inactive markets for identical or similar assets or liabilities; or inputs that are observable or can be corroborated by observable market data by correlation or other means for substantially the full-term of the assets or liabilities.
- Level 3 Unobservable inputs are supported by little or no market activity. The unobservable inputs represent the assumptions that management believes market participants would use to price the assets and liabilities, including risk. Generally, Level 3 assets and liabilities are valued using pricing models, discounted cash flow methodologies, or similar techniques that require significant judgment or estimation. Following are descriptions of the valuation methodologies used to measure material assets and liabilities at fair value and details of the valuation models, key inputs to those models and significant assumptions utilized.

Recurring Fair Value Measurements

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

RMBS

The Company holds a portfolio of RMBS that are classified as available for sale and are carried at fair value in the consolidated balance sheets. The Company determines the fair value of its RMBS based upon prices obtained from third-party pricing providers. The third-party pricing providers use pricing models that generally incorporate such factors as coupons, primary and secondary mortgage rates, rate reset period, issuer, prepayment speeds, credit enhancements and expected life of the security. As a result, the Company classified 100% of its RMBS as Level 2 fair value assets at December 31, 2016 and December 31, 2015.

Excess MSRs

The Company holds a portfolio of Excess MSRs that are reported at fair value in the consolidated balance sheets. The Company uses a discounted cash flow model to estimate the fair value of these assets. Although Excess MSR transactions are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels and discount rates). As a result, the Company classified 100% of its Excess MSRs as Level 3 fair value assets at December 31, 2016 and December 31, 2015.

MSRs

The Company holds a portfolio of MSRs that are reported at fair value in the consolidated balance sheets. The Company uses a discounted cash flow model to estimate the fair value of these assets. Although MSR transactions are observable in the marketplace, the valuation includes unobservable market data inputs (prepayment speeds, delinquency levels, costs to service and discount rates). As a result, the Company classified 100% of its MSRs as Level 3 fair value assets at December 31, 2016 and December 31, 2015.

Derivative Instruments

The Company enters into a variety of derivative financial instruments as part of its economic hedging strategies. The Company executes interest rate swaps, swaptions, TBAs and treasury futures. The Company utilizes third-party pricing providers to value its financial derivative instruments. As a result, the Company classified 100% of the derivative instruments as Level 2 fair value assets and liabilities at December 31, 2016 and December 31, 2015.

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

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

Recurring Fair Value Measurements

As of December 31, 2016

	Level 1	Level 2	Level 3	Carrying Value
Assets				
RMBS				
Fannie Mae	\$ —	\$ 448,937	\$ —	\$ 448,937
Freddie Mac	—	198,103	—	198,103
CMOs	—	24,864	—	24,864
RMBS total	—	671,904	—	671,904
Derivative assets				
Interest rate swaps	—	7,639	—	7,639
Interest rate swaptions	—	1,482	—	1,482
TBAs	—	—	—	—
Treasury Futures	—	—	—	—
Derivative assets total	—	9,121	—	9,121
Servicing related assets	—	—	61,263	61,263
Total Assets	\$ —	\$ 681,025	\$ 61,263	\$ 742,288
Liabilities				
Derivative liabilities				
Interest rate swaps	—	339	—	339
TBAs	—	75	—	75
Treasury Futures	—	280	—	280
Derivative liabilities total	—	694	—	694
Total Liabilities	\$ —	\$ 694	\$ —	\$ 694

As of December 31, 2015

	Level 1	Level 2	Level 3	Carrying Value
Assets				
RMBS				
Fannie Mae	\$ —	\$ 308,772	\$ —	\$ 308,772
Freddie Mac	—	193,411	—	193,411
CMOs	—	6,059	—	6,059
RMBS total	—	508,242	—	508,242
Derivative assets				
Interest rate swaps	—	51	—	51
Interest rate swaptions	—	371	—	371
TBAs	—	—	—	—
Treasury Futures	—	—	—	—
Derivative assets total	—	422	—	422
Servicing related assets	—	—	97,803	97,803
Total Assets	\$ —	\$ 508,664	\$ 97,803	\$ 606,467
Liabilities				
Derivative liabilities				
Interest rate swaps	—	4,595	—	4,595
TBAs	—	—	—	—
Treasury Futures	—	—	—	—
Derivative liabilities total	—	4,595	—	4,595
Total Liabilities	\$ —	\$ 4,595	\$ —	\$ 4,595

The Company may be required to measure certain assets or liabilities at fair value from time to time. These periodic fair value measures typically result from application of certain impairment measures under GAAP. These items would constitute nonrecurring fair value measures under ASC 820. As of December 31, 2016 and December 31, 2015, the Company did not have any assets or liabilities measured at fair value on a nonrecurring basis in the periods presented.

Level 3 Assets and Liabilities

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

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

Changes in market conditions, as well as changes in the assumptions or methodology used to determine fair value, could result in a significant change to estimated fair values. It should be noted that minor changes in assumptions or estimation methodologies can have a material effect on these derived or estimated fair values, and that the fair values reflected below are indicative of the interest rate and credit spread environments as of December 31, 2016 and December 31, 2015 and do not take into consideration the effects of subsequent changes in market or other factors.

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

Level 3 Fair Value Measurements

As of December 31, 2016

	Level 3 ^(A)				
	Excess MSR			MSRs	Total
	Pool 1	Pool 2	Pool 2014		
Balance at December 31, 2015	\$ 43,482	\$ 33,054	\$ 1,506	\$ 19,761	\$ 97,803
Purchases and principal paydowns:					
Purchases	—	—	—	16,179	16,179
Sales	(39,916)	—	(1,179)	—	(41,095)
Proceeds from principal paydowns	(3,566)	(3,911)	(327)	—	(7,804)
Other Changes ^(B)	—	—	—	(784)	(784)
Purchases and principal paydowns:	\$ (43,482)	\$ (3,911)	\$ (1,506)	\$ 15,395	\$ (33,504)
Changes in Fair Value due to:					
Changes in valuation inputs or assumptions used in valuation model	—	249	—	227	476
Other changes in fair value ^(C)	—	—	—	(3,512)	(3,512)
Unrealized gain (loss) included in Net Income	\$ —	\$ 249	\$ —	\$ (3,285)	\$ (3,036)
Balance at December 31, 2016	\$ —	\$ 29,392	\$ —	\$ 31,871	\$ 61,263

As of December 31, 2015

	Level 3 ^(A)				
	Excess MSR			MSRs	Total
	Pool 1	Pool 2	Pool 2014		
Balance at December 31, 2014	\$ 54,798	\$ 34,938	\$ 1,586	\$ —	\$ 91,322
Purchases and principal paydowns:					
Purchases	—	—	—	20,884	20,884
Sales	—	—	—	—	—
Proceeds from principal paydowns	(8,825)	(4,186)	(250)	—	(13,261)
Other Changes ^(B)	—	—	—	—	—
Purchases and principal paydowns:	\$ (8,825)	\$ (4,186)	\$ (250)	\$ 20,884	\$ 7,623
Changes in Fair Value due to:					
Changes in valuation inputs or assumptions used in valuation model	(2,491)	2,302	170	(707)	(726)
Other changes in fair value ^(C)	—	—	—	(416)	(416)
Unrealized gain (loss) included in Net Income	\$ (2,491)	\$ 2,302	\$ 170	\$ (1,123)	\$ (1,142)
Balance at December 31, 2015	\$ 43,482	\$ 33,054	\$ 1,506	\$ 19,761	\$ 97,803

(A) Includes the recapture agreement for each respective pool.

(B) Represents purchase price adjustments, principally contractual prepayment protection, and changes due to the Company's repurchase of the underlying collateral.

(C) Represents changes due to realization of expected cash flows.

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

Fair Value Measurements

As of December 31, 2016

	<u>Fair Value</u>	<u>Valuation Technique</u>	<u>Unobservable Input^(A)</u>	<u>Range</u>	<u>Weighted Average</u>
Excess MSR Pool					
2	\$ 29,392	Discounted cash flow	Constant prepayment speed	7.8% - 31.9%	14.3%
			Uncollected Payments	8.3% - 13.1%	11.9%
			Discount rate	—	16.2%
MSRs	\$ 31,871	Discounted cash flow	Constant prepayment speed	7.1% - 24.9%	10.6%
			Uncollected payments	0.8% - 1.4%	1.3%
			Discount rate	—	9.3%
			Annual cost to service, per loan		\$ 64
TOTAL	\$ 61,263	Discounted cash flow			

As of December 31, 2015

	<u>Fair Value</u>	<u>Valuation Technique</u>	<u>Unobservable Input^(A)</u>	<u>Range</u>	<u>Weighted Average</u>
Excess MSR Pool					
1	\$ 43,482	Discounted cash flow	Constant prepayment speed	4.0% - 19.0%	10.5%
			Uncollected Payments	2.9% - 7.0%	6.2%
			Discount rate		12.3%
Excess MSR Pool					
2	\$ 33,054	Discounted cash flow	Constant prepayment speed	8.3% - 42.3%	14.9%
			Uncollected Payments	10.4% - 13.9%	13.0%
			Discount rate		16.7%
Excess MSR Pool					
2014	\$ 1,506	Discounted cash flow	Constant prepayment speed	3.9% - 22.3%	11.2%
			Uncollected Payments	5.9% - 7.1%	6.8%
			Discount rate		11.9%
MSRs	\$ 19,761	Discounted cash flow	Constant prepayment speed	0.0% - 13.8%	9.7%
			Uncollected payments	1.2% - 3.4%	1.6%
			Discount rate		8.3%
			Annual cost to service, per loan		\$ 73
TOTAL	\$ 97,803	Discounted cash flow			

(A) Significant increases (decreases) in any of the inputs in isolation may result in significantly lower (higher) fair value measurement. A change in the assumption used for discount rates may be accompanied by a directionally similar change in the assumption used for the probability of uncollected payments and a directionally opposite change in the assumption used for prepayment rates.

Fair Value of Financial Instruments not Carried at Fair Value in Balance Sheets

In accordance with ASC 820, the Company is required to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized in the consolidated balance sheets, for which fair value can be estimated. The following describes the Company's methods for estimating the fair value for financial instruments.

- RMBS available for sale securities, Servicing Related Assets, derivative assets and derivative liabilities are recurring fair value measurements; carrying value equals fair value. See discussion of valuation methods and assumptions within the "Fair Value Measurements" section of this footnote.

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- Cash and cash equivalents and restricted cash have a carrying value which approximates fair value because of the short maturities of these instruments.
- The carrying value of repurchase agreements and corporate debt that mature in less than one year generally approximates fair value due to the short maturities. The Company does not hold any repurchase agreements that are considered long-term.

Corporate debt that matures in more than one year, with a floating rate generally approximates fair value.

Note 10 — Commitments and Contingencies

The following represents commitments and contingencies of the Company as of December 31, 2016 and December 31, 2015:

Management Agreement

The Company pays the Manager a quarterly management fee, calculated and payable quarterly in arrears, equal to the product of one quarter of the 1.5% Management Fee Annual Rate and the stockholders' equity, adjusted as set forth in the Management Agreement as of the end of such fiscal quarter. The Company relies on resources of Freedom Mortgage to provide the Manager with the necessary resources to conduct Company operations. For further discussion regarding the Management Fee, see Note 7.

Legal and Regulatory

From time to time the Company may be subject to potential liability under laws and government regulations and various claims and legal actions arising in the ordinary course of business. Liabilities are established for legal claims when payments associated with the claims become probable and the costs can be reasonably estimated. The actual costs of resolving legal claims may be substantially higher or lower than the amounts established for those claims. Based on information currently available, management is not aware of any legal or regulatory claims that would have a material effect on the Company's consolidated financial statements, and, therefore, no accrual is required as of December 31, 2016 and December 31, 2015.

Commitments to Purchase/Sell RMBS

As of December 31, 2016 and December 31, 2015, the Company held forward TBA purchase and sale commitments, respectively, with counterparties, which are forward RMBS trades, whereby the Company committed to purchasing a pool of securities at a particular interest rate. As of the date of the trade, the mortgage-backed securities underlying the pool that will be delivered to fulfill a TBA trade are not yet designated. The securities are typically "to be announced" 48 hours prior to the established trade settlement date. As of December 31, 2016 the Company was not obligated to purchase any securities and was obligated to sell approximately \$6.0 million of securities and has been classified within "payables for unsettled trades" on the consolidated balance sheets. As of December 31, 2015 the Company was not obligated to purchase any securities and was not obligated to sell securities.

Acknowledgement Agreements

In order to have Ginnie Mae acknowledge our interest in Excess MSR's related to FHA and VA mortgage loans that have been pooled into securities guaranteed by Ginnie Mae, the Company entered into an acknowledgment agreement with Ginnie Mae and Freedom Mortgage. Under that agreement, if Freedom Mortgage failed to make a required payment to the holders of the Ginnie Mae-guaranteed RMBS, the Company would have been obligated to make that payment even though the payment may relate to loans for which the Company did not own any Excess MSR's. The Company's failure to make that payment would have resulted in liability to Ginnie Mae for any losses or claims that it suffers as a result. This agreement was terminated in connection with the sale of the Pool 2 Excess MSR's in February 2017. See Note 19.

Management has determined, that as of December 31, 2016 and December 31, 2015, the risk of material loss to be remote and thus no liability has been accrued.

In connection with the MSR Financing Facility entered into by Aurora and QRS III, those parties also entered into an acknowledgment agreement with Fannie Mae. Pursuant to that agreement, Fannie Mae consented to the pledge by Aurora and QRS III of their respective interests in MSR's for loans owned or securitized by Fannie Mae, and acknowledged the security interest of the lender in those MSR's. See Note 13.

Note 11 – Repurchase Agreements

The Company had outstanding approximately \$594.6 million and \$385.6 of repurchase agreements as of December 31, 2016 and December 31, 2015, respectively. The Company’s obligations under these agreements had weighted average remaining maturities of 65 days and 47 days as of December 31, 2016 and December 31, 2015 respectively. RMBS and cash have been pledged as collateral under these repurchase agreements (see Note 4).

The repurchase agreements had the following remaining maturities and weighted average rates (after giving effect to the Company’s interest rate swaps) as of the dates indicated (dollars in thousands):

Repurchase Agreements Characteristics

As of December 31, 2016

	Repurchase Agreements	Weighted Average Rate
Less than one month	\$ 60,690	1.14%
One to three months	456,502	0.91%
Greater than three months	77,423	0.90%
Total/Weighted Average	\$ 594,615	0.93%

As of December 31, 2015

	Repurchase Agreements	Weighted Average Rate
Less than one month	\$ 93,926	0.55%
One to three months	284,687	0.56%
Greater than three months	6,947	0.52%
Total/Weighted Average	\$ 385,560	0.56%

Note 12 – FHLBI Advances

The Company had no outstanding advances from the FHLBI as of December 31, 2016. The Company had outstanding approximately \$62.3 million of FHLBI advances, with a weighted average borrowing rate of 0.54% as of December 31, 2015. The Company’s obligations under these advances had a weighted average remaining maturity of 94 days as of December 31, 2015. Agency RMBS and FHLBI stock had been pledged as collateral for these advances (dollars in thousands). As of December 31, 2016, the Company’s captive insurance subsidiary had withdrawn from membership in the FHLBI and had been dissolved.

Federal Home Loan Bank Advance Characteristics

As of December 31, 2015

	Federal Home Loan Bank Advances	Weighted Average Rate
Less than one month	\$ 15,000	0.44%
One to three months	—	—%
Greater than three months	47,250	0.57%
Total/Weighted Average Federal Home Loan Bank Advances	\$ 62,250	0.54%

Note 13 – Notes Payable

At December 31, 2016 and December 31, 2015, the Company had outstanding borrowings of \$8.9 million and \$24.3 million, respectively, on a \$25.0 million Term Loan. The outstanding borrowings bear interest at a weighted average interest rate of 5.57% per annum and are secured by the pledge of the Company’s existing

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portfolio of Excess MSR. The principal payments on the borrowings are due monthly, beginning in September 2015, based on a 10-year amortization schedule with a maturity date in April 2020. Prior to September 2015, only interest was payable monthly. The Term Loan was paid in full in connection with the sale of the Excess MSR to Freedom Mortgage. See Notes 7 and 19.

In September 2016, Aurora and QRS III entered into a loan and security agreement (the “MSR Financing Facility”), pursuant to which Aurora and QRS III pledged their respective rights in all existing and future MSR for loans owned or securitized by Fannie Mae to secure borrowings up to a maximum of \$25.0 million outstanding at any one time. The facility has a two-year revolving period, subject to extension by agreement, during which only interest payments are due. Borrowings bear interest at a spread over one month LIBOR. At the end of the revolving period, the outstanding amount will be converted to a three-year term loan with monthly payments of interest (calculated as a spread over the rate for one-year interest rate swaps) and principal (calculated on a ten-year amortization schedule). At December 31 2016, \$14.0 million was outstanding under the MSR Financing Facility.

The outstanding long-term borrowings had the following remaining maturities as of the dates indicated (dollars in thousands):

Long-Term Borrowings Repayment Characteristics

		As of December 31, 2016					
		2017	2018	2019	2020	2021	Total
Term Loan							
	Borrowings under Term Loan facility	\$ 2,841	\$ 3,005	\$ 3,040	\$ —	\$ —	\$ 8,886
MSR Financing Facility							
	Borrowings under MSR Financing facility	\$ —	\$ 271	\$ 1,118	\$ 1,175	\$ 11,436	\$ 14,000

		As of December 31, 2015					
		2016	2017	2018	2019	2020	Total
Term Loan							
	Borrowings under Term Loan facility	\$ 1,958	\$ 2,074	\$ 2,192	\$ 2,317	\$ 15,762	\$ 24,303

Note 14 – Receivables and Other Assets

The assets comprising “Receivables and other assets” as of December 31, 2016 and December 31, 2015 are summarized in the following table (dollars in thousands):

Receivables and Other Assets

	December 31, 2016	December 31, 2015
Excess servicing income receivable	\$ 5,598	\$ 2,159
Servicing advances	1,432	787
Interest receivable	2,069	1,497
Federal Home Loan Bank stock	—	3,261
Deferred tax receivable	—	203
Repurchased loans held for sale	1,570	—
Other receivables	1,628	1,421
Total other assets	\$ 12,297	\$ 9,328

As a condition to membership in the FHLBI, CHMI Insurance was required to purchase and hold a certain amount of FHLBI stock, which was based, in part, upon the outstanding principal balance of advances from the FHLBI. At December 31, 2015, CHMI Insurance had stock in the FHLBI totaling approximately \$3.3 million, which is included in Other Assets on the consolidated balance sheets. FHLBI stock is considered a non-marketable, long-term investment, is carried at cost and is subject to recoverability testing under applicable accounting standards. This stock can only be redeemed or sold at its par value, and only to the FHLBI.

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Accordingly, when evaluating FHLBI stock for impairment, the Company considers the ultimate recoverability of the par value rather than recognizing temporary declines in value. As of December 31, 2016, CHMI Insurance had withdrawn from membership in the FHLBI and its FHLBI stock has been redeemed.

The Company only records as an asset those servicing advances that the Company deems recoverable.

As a result of the Company's investments in MSRs, it is obligated from time to time to repurchase an underlying loan from the Agency for which it is being serviced due to an alleged breach of a representation or warranty. Loans acquired in this manner are recorded at the purchase price less any principal recoveries and are then offered for sale in the scratch and dent market. In the year ended December 31, 2016 the Company purchased five loans, with an aggregate UPB of approximately \$1.64 million at the time of purchase, as required by the applicable Agency. None of those loans have been sold. The repurchased loans are considered Level 2 Assets and are expected to be liquidated in 2017.

Note 15 – Summarized Quarterly Results (Unaudited)

The following tables present information about the Company's quarterly operating results for the periods indicated below (dollars in thousands):

Summarized Quarterly Results

	2016			
	December 31,	September 30,	June 30,	March 31,
Income				
Interest income	\$ 11,242	\$ 7,157	\$ 7,135	\$ 5,188
Interest expense	2,389	1,877	1,885	1,657
Net interest income	8,853	5,280	5,250	3,531
Servicing fee income	2,145	2,365	1,574	1,495
Servicing costs	1,018	641	501	402
Net servicing income (loss)	1,127	1,724	1,073	1,093
Other income (loss)				
Realized gain (loss) on RMBS, net	74	770	235	320
Realized gain (loss) on investments in Excess MSRs, net	1,520	—	—	—
Realized gain (loss) on derivatives, net	(4,056)	(2,147)	(299)	(1,461)
Realized gain (loss) on acquired assets, net	—	—	—	—
Unrealized gain (loss) on derivatives, net	15,307	3,199	(1,228)	(5,198)
Unrealized gain (loss) on investments in Excess MSRs	2,588	117	(149)	(2,307)
Unrealized gain (loss) on investments in MSRs	3,870	(1,847)	(3,076)	(2,232)
Total Income	29,283	7,096	1,806	(6,254)
Expenses				
General and administrative expense	790	864	822	808
Management fee to affiliate	764	802	690	690
Total Expenses	1,554	1,666	1,512	1,498
Income (Loss) Before Income Taxes	27,729	5,430	294	(7,752)
Provision for corporate business taxes	1,127	(89)	10	(590)
Net Income (Loss)	26,602	5,519	284	(7,162)
Net (income) loss allocated to noncontrolling interests	(432)	(76)	(2)	99
Net Income (Loss) Applicable to Common Stockholders	\$ 26,170	\$ 5,443	\$ 282	\$ (7,063)
Net income (Loss) Per Share of Common Stock				
Basic	\$ 3.48	\$ 0.72	\$ 0.04	\$ (0.94)
Diluted	\$ 3.48	\$ 0.72	\$ 0.04	\$ (0.94)
Weighted Average Number of Shares of Common Stock Outstanding				
Basic	7,519,038	7,511,653	7,509,543	7,509,543
Diluted	7,525,348	7,528,188	7,520,616	7,519,038

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	2015			
	December 31,	September 30,	June 30,	March 31,
Income				
Interest income	\$ 7,984	\$ 5,813	\$ 8,088	\$ 5,827
Interest expense	1,759	1,643	1,346	1,235
Net interest income	6,225	4,170	6,742	4,592
Servicing fee income	1,100	463	156	—
Servicing costs	301	366	94	—
Net servicing income (loss)	799	97	62	—
Other income (loss)				
Realized gain (loss) on RMBS, net	393	269	(115)	307
Realized gain (loss) on investments in Excess MSR, net	—	—	—	—
Realized gain (loss) on derivatives, net	(1,672)	(947)	(52)	(1,242)
Realized gain (loss) on acquired assets, net	275	—	174	—
Unrealized gain (loss) on derivatives, net	4,634	(4,986)	2,835	(2,542)
Unrealized gain (loss) on investments in Excess MSR	1,219	(2,059)	2,938	(2,117)
Unrealized gain (loss) on investments in MSR	(560)	(541)	(22)	—
Total Income	11,313	(3,997)	12,562	(1,002)
Expenses				
General and administrative expense	1,083	622	634	742
Management fee to affiliate	713	690	690	690
Total Expenses	1,796	1,312	1,324	1,432
Income (Loss) Before Income Taxes	9,517	(5,309)	11,238	(2,434)
Provision for corporate business taxes	(134)	(139)	(70)	—
Net Income (Loss)	9,651	(5,170)	11,308	(2,434)
Net (income) loss allocated to noncontrolling interests	(106)	46	(103)	22
Net Income (Loss) Applicable to Common Stockholders	\$ 9,545	\$ (5,124)	\$ 11,205	\$ (2,412)
Net income (Loss) Per Share of Common Stock				
Basic	\$ 1.27	\$ (0.68)	\$ 1.49	\$ (0.32)
Diluted	\$ 1.27	\$ (0.68)	\$ 1.49	\$ (0.32)
Weighted Average Number of Shares of Common Stock Outstanding				
Basic	7,509,543	7,509,543	7,509,543	7,509,543
Diluted	7,519,038	7,511,653	7,509,543	7,509,543

Note 16 – Income Taxes

The Company has elected to be taxed as a REIT under Code Sections 856 through 860 beginning with its short taxable year ended December 31, 2013. As a REIT, the Company generally will not be subject to U.S. federal income tax to the extent that it distributes its taxable income to its stockholders. To maintain qualification as a REIT, the Company must distribute at least 90% of its annual REIT taxable income to its stockholders and meet certain other requirements such as assets it may hold, income it may generate and its stockholder composition. It is the Company's policy to distribute all or substantially all of its REIT taxable income. To the extent there is any undistributed REIT taxable income at the end of a year, the Company can elect to distribute such shortfall within the next year as permitted by the Code.

Effective January 1, 2014, CHMI Solutions has elected to be taxed as a corporation for U.S. federal income tax purposes; prior to this date, CHMI Solutions was a disregarded entity for U.S. federal income tax purposes. CHMI Solutions has jointly elected with the Company, the ultimate beneficial owner of CHMI Solutions, to be treated as a TRS of the Company, and all activities conducted through CHMI Solutions and its wholly-owned

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subsidiary, Aurora, are subject to federal and state income taxes. CHMI Solutions files a consolidated tax return with Aurora Financial Group Inc., its wholly owned subsidiary, and is fully taxed as a U.S. C-Corporation.

The state and local tax jurisdictions for which the Company is subject to tax-filing obligations recognize the Company's status as a REIT, and therefore, the Company generally does not pay income tax in such jurisdictions. CHMI Solutions and Aurora are subject to U.S. federal, state and local income taxes.

The components of the Company's income tax expense (benefit) are as follows for the periods indicated below (dollars in thousands):

	Year Ended December 31,		
	2016	2015	2014
Current federal income tax expense	\$ 575	\$ —	\$ —
Current state income tax expense	83	—	6
Deferred federal income tax expense (benefit)	(198)	(309)	(124)
Deferred state income tax expense (benefit)	(2)	(34)	(22)
Total Income Tax Expense	\$ 458	\$ (343)	\$ (140)

The following is a reconciliation of the statutory federal rate to the effective rate, for the periods indicated below (dollars in thousands):

	Year Ended December 31,					
	2016		2015		2014	
Computed income tax (benefit) expense at federal rate	\$ 8,995	35.0%	\$ 4,554	35.0%	\$ 824	35.0%
State taxes, net of federal benefit, if applicable	50	0.2%	(34)	(0.0)%	92	3.9%
Permanent differences in taxable income from GAAP pre-tax income	140	0.6%	(157)	(1.4)%	4,874	207.2%
REIT income not subject to tax	(8,727)	(34.0)%	(4,706)	(36.2)%	(5,930)	(252.0)%
(Benefit from) Provision for Income Taxes/Effective Tax Rate^(A)	\$ 458	1.8%	\$ (343)	(2.6)%	\$ (140)	(5.9)%

(A) The provision for income taxes is recorded at the TRS level.

The Company's consolidated balance sheets, at December 31, 2016, December 31, 2015 and December 31, 2014, contain the following current and deferred tax liabilities and assets, which are recorded at the TRS level (dollars in thousands):

	Year Ended December 31,		
	2016	2015	2014
Income taxes payable			
Federal income taxes payable	\$ 575	\$ —	\$ —
State and local income taxes payable	84	—	—
Income taxes payable	\$ 659	\$ —	\$ —
	December 31, 2016	December 31, 2015	December 31, 2014
Deferred tax assets (liabilities)			
Deferred tax - organizational expenses	\$ 53	\$ 72	\$ 84
Deferred tax - mortgage servicing rights	340	(121)	—
Deferred tax - net operating loss	—	252	62
Total net deferred tax assets (liabilities)	\$ 393	\$ 203	\$ 146

The deferred tax assets as of December 31, 2016 was primarily related to mortgage servicing rights. The deferred tax assets as of December 31, 2015 and December 31, 2014 primarily consisted of net operating loss carryforwards and acquisition related costs capitalized for tax purposes. CHMI Solutions' federal and state net operating loss carryforwards at December 31, 2015 and December 31, 2014 were approximately \$693,000 and \$154,000, respectively, and are available to offset future taxable income and expire in 2035 and 2034, respectively. Management has determined that it is more likely than not that all of CHMI Solutions' deferred tax

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assets will be realized in the future. Accordingly, no valuation allowance has been established at December 31, 2016 and December 31, 2015. As of December 31, 2016, the deferred tax liability is included in “Accrued expenses and other liabilities” in the consolidated balance sheets. As of December 31, 2015, the deferred tax asset is included in “Receivables and other assets” in the consolidated balance sheets.

Based on the Company’s evaluation, the Company has concluded that there are no significant uncertain tax positions requiring recognition in the Company’s consolidated financial statements. Additionally, there were no amounts accrued for penalties or interest as of or during the periods presented in these consolidated financial statements.

The Company’s 2015, 2014 and 2013 federal, state and local income tax returns remain open for examination by the relevant authorities.

Note 17 – Business Combinations

On May 29, 2015 (the acquisition date), CHMI Solutions acquired 100% of the outstanding voting stock of Aurora. The results of Aurora’s operations have been included in the consolidated financial statements since that date. Aurora is a licensed mortgage origination and servicing company. Aurora is a seller/servicer for Fannie Mae and Freddie Mac and an issuer for Ginnie Mae.

The acquisition-date fair value of the consideration transferred totaled approximately \$3.9 million, which consisted of cash. Twenty percent (20%) of the consideration was deposited in an escrow account to provide a source of funds for the seller’s indemnification obligations. Transaction-related costs of approximately \$95,400 were expensed as incurred as of September 30, 2015, and are included in “General and administrative expenses” on the consolidated income statement.

In the Aurora acquisition agreement, the parties agreed to fix the valuation of the MSR portfolio, as a percentage of par, based on third party appraisals obtained at the end of January 2015. The agreement also provided that the UPB of the portfolio would be fixed 90 days after the agreement was signed. Due to the increase in interest rates between January and the closing date at the end of May 2015, the value of the MSR portfolio increased. In addition, the UPB of the portfolio declined between the end of April and the closing date in May. Valuation adjustments for intangible assets and loan loss reserves also contributed to bargain purchase in the amount of approximately \$734,000 as of September 30, 2015 and has been classified within “Realized gain (loss) on acquired assets, net” on the consolidated statements of income.

The following represents the pro forma consolidated income statement as if Aurora had been included in the consolidated results of the Company for each of the last three calendar years. The unaudited pro forma information is intended for informational purposes only and is not necessarily indicative of the Company’s future operating results or operating results that would have occurred had the Aurora acquisition been completed at the beginning of 2015. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies or asset dispositions (dollars in thousands):

Pro Forma Consolidated Income Statement

	Year Ended December 31,		
	2016	2015	2014
Revenue	\$ 31,931	\$ 18,871	\$ 7,811
Earnings (loss)	\$ 24,832	\$ 13,460	\$ 2,398
Earnings (Loss) Per Share of Common Stock			
Basic	\$ 3.31	\$ 1.79	\$ 0.32
Diluted	\$ 3.30	\$ 1.79	\$ 0.32
Weighted Average Number of Shares of Common Stock Outstanding			
Basic	7,512,444	7,509,543	7,505,546
Diluted	7,523,297	7,512,444	7,508,827

These amounts have been calculated after applying the Company’s accounting policies and adjusting the results of Aurora primarily to reflect the exclusion of the bargain purchase and transaction costs together with the consequential tax effects.

Note 18 – CHMI Insurance Company

The Company's indirectly owned subsidiary, CHMI Insurance Company LLC, or CHMI Insurance, became a member of the FHLBI on June 26, 2015. As a member of the FHLBI, CHMI Insurance had access to a variety of products and services offered by the FHLBI, including secured advances. As of December 31, 2015, CHMI Insurance had approximately \$62.3 million of outstanding advances from the FHLBI and had stock in the FHLBI totaling approximately \$3.3 million, which is included in Other Assets on the consolidated balance sheet. In January 2016, the Federal Housing Finance Agency issued a final regulation that requires the Federal Home Loan Banks to terminate the memberships of their captive insurance company members within one year or five years after the rule becomes effective. As a result of this rule, CHMI Insurance withdrew from membership in the FHLBI and dissolved in December 2016.

Note 19 – Subsequent Events

We completed the sale of the Pool 2 Excess MSR to Freedom Mortgage on February 1, 2017. In payment of the purchase price Freedom Mortgage transferred to Aurora Ginnie Mae MSRs with a weighted average servicing fee of approximately 30 basis points. As is required for all transfers of Ginnie Mae MSRs, Aurora and Freedom Mortgage received the approval of this transaction from Ginnie Mae. The Ginnie Mae MSRs relate to a pool consisting primarily of newly originated Ginnie Mae conforming mortgage loans that had an aggregate unpaid principal balance of approximately \$4.5 billion as of January 31, 2017. At the closing of the sale of the Pool 2 Excess MSR, we repaid the remaining outstanding borrowings drawn on the Term Loan with cash on hand, released our security interest arising under the Excess MSR 2 Agreement and terminated that agreement. In addition, the Acknowledgment Agreement that we and Freedom Mortgage entered into with Ginnie Mae at the time of our IPO was terminated.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures. The Company's President and its Chief Financial Officer, have evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. The Company's disclosure controls and procedures are designed to provide reasonable assurance that information is recorded, processed, summarized and reported accurately and on a timely basis. Based on such evaluation, the Company's President and the Company's Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective.

Management's Report on Internal Control Over Financial Reporting. Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act as a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements

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Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control - Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in Internal Control Integrated Framework, our management concluded that our internal control over financial reporting was effective as of December 31, 2016.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Changes in Internal Control Over Financial Reporting. There have been no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information required by this item is incorporated herein by reference to the Company's Definitive Proxy Statement on Schedule 14A relating to its annual meeting of stockholders (the "Proxy Statement"), to be filed with the SEC within 120 days after December 31, 2016.

Item 11. Executive Compensation

The information required by this item is incorporated herein by reference to the Proxy Statement to be filed with the SEC within 120 days after December 31, 2016.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this item is incorporated herein by reference to the Proxy Statement to be filed with the SEC within 120 days after December 31, 2016.

Item 13. Certain Relationships and Related Transactions and Director Independence

The information required by this item is incorporated herein by reference to the Proxy Statement to be filed with the SEC within 120 days after December 31, 2016.

Item 14. Principal Accountant Fees and Services

The information required by this item is incorporated herein by reference to the Proxy Statement to be filed with the SEC within 120 days after December 31, 2016.

PART IV

Item 15. Exhibits and Financial Statement Schedules

Documents filed as part of the report

The following documents are filed as part of this Annual Report on Form 10-K:

(1) Financial Statements.

The consolidated financial statements of the Company, together with the independent registered public accounting firm’s report thereon, are set forth in this Annual Report on Form 10-K and are incorporated herein by reference. See “Item 8. Consolidated Financial Statements and Supplementary Data,” filed herewith, for a list of financial statements.

(2) Financial Statement Schedule.

All financial statement schedules have been omitted because the required information is not applicable or deemed not material, or the required information is presented in the consolidated financial statements and/or in the notes to consolidated financial statements filed in response to Item 8 of this Annual Report on Form 10-K.

(3) Exhibits.

Exhibit Number	Description
3.1	Articles of Amendment and Restatement of Cherry Hill Mortgage Investment Corporation (incorporated by reference to Exhibit 3.1 to Amendment No. 2 to the Company’s Registration Statement on Form S-11 (Registration No. 333-188214) on June 10, 2013).
3.2	Amended and Restated Bylaws of Cherry Hill Mortgage Investment Corporation (incorporated by reference to Exhibit 3.2 to Amendment No. 2 to the Company’s Registration Statement on Form S-11 (Registration No. 333-188214) on June 10, 2013).
4.1	Specimen Common Stock Certificate. (incorporated by reference to Exhibit 4.1 to Amendment No. 1 to the Company’s Registration Statement on Form S-11 (Registration No. 333- 188214) on May 28, 2013).
4.2	Registration Rights Agreement between Stanley Middleman and Cherry Hill Mortgage Investment Corporation (incorporated by reference to Exhibit 99.2 to the Schedule 13D filed by Stanley Middleman on October 11, 2013 (incorporated by reference to actual agreement).
10.1	Flow and Bulk Excess MSR Acquisition Agreement, dated October 9, 2013, by and between Cherry Hill Mortgage Investment Corporation and Freedom Mortgage Corporation (incorporated by reference from Exhibit 10.2 of the Company’s Form 8-K filed with the SEC on October 15, 2013).
10.2	Pool 1 Excess MSR Acquisition and Recapture Agreement, dated October 9, 2013, by and between Cherry Hill Mortgage Investment Corporation and Freedom Mortgage Corporation (incorporated by reference from Exhibit 10.3 of the Company’s Form 8-K filed with the SEC on October 15, 2013).
10.3	Pool 2 Excess MSR Acquisition and Recapture Agreement, dated October 9, 2013, by and between Cherry Hill Mortgage Investment Corporation and Freedom Mortgage Corporation (incorporated by reference from Exhibit 10.4 of the Company’s Form 8-K filed with the SEC on October 15, 2013).

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Exhibit Number	Description
10.5	Amendment No. 1, dated as of October 22, 2015, to Amended and Restated Management Agreement, dated as of September 24, 2013, by and among Cherry Hill Mortgage Investment Corporation and its consolidated subsidiaries and Cherry Hill Mortgage Management, LLC (incorporated by reference from Exhibit 10.1 to the Current Report on Form 8-K filed by Cherry Mortgage Investment Corporation on October 23, 2015).
10.6	Services Agreement, dated May 1, 2013, between Cherry Hill Mortgage Management, LLC and Freedom Mortgage Corporation (incorporated by reference to Exhibit 10.5 to Amendment No. 1 to the Company's Registration Statement on Form S-11 (Registration No. 333- 188214) on May 28, 2013).
10.7	Form of Indemnification Agreement (incorporated by reference to Exhibit 10.6 to Amendment No. 1 to the Company's Registration Statement on Form S-11 (Registration No. 333- 188214) on May 28, 2013).
10.8	2013 Equity Incentive Plan (incorporated by reference to Exhibit 10.9 to Amendment No. 2 to the Company's Registration Statement on Form S-11 (Registration No. 333- 188214) on June 10, 2013).
10.9	Agreement of Limited Partnership of Cherry Hill Operating Partnership, LP. (incorporated by reference to Exhibit 99.1 to the Company's Registration Statement on Form S-11, 2013).
10.10	Form of LTIP Unit Vesting Agreement (incorporated by reference to Exhibit 10.9 to Amendment No. 2 to the Company's Registration Statement on Form S-11 (Registration No. 333- 188214) on June 10, 2013).
10.13	Form of Unrestricted Non-Employee Director Stock Award Agreement (Without Forfeiture Restrictions) (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on January 27, 2014).
10.14	Form of Unrestricted Non-Employee Director Stock Award Agreement (With Forfeiture Restrictions) (incorporated by reference to the Company's Current Report on Form 8-K filed on January 27, 2014).
10.15	Letter agreement, dated November 1, 2016, between Cherry Hill Mortgage Investment Corporation and Freedom Mortgage Corporation.
10.16	Amendment, dated January 9, 2017, to the letter agreement, dated November 1, 2016, between Cherry Hill Mortgage Investment Corporation and Freedom Mortgage Corporation.
12.1*	Statement of Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends.
21.1*	Subsidiaries of Cherry Hill Mortgage Investment Corporation.
23.1*	Consent of Ernst & Young LLP.
31.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934.

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Exhibit Number	Description
31.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934.
32.1*	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Definition Linkbase
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

* Filed herewith.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Cherry Hill Mortgage Investment Corporation

Date: March 14, 2017

By: /s/ Jeffrey Lown II
Name: Jeffrey Lown II
Title: President and Director (Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date: March 14, 2017

By: /s/ Jeffrey Lown II
Name: Jeffrey Lown II
Title: President and Director (Principal Executive Officer)

Date: March 14, 2017

By: /s/ Martin Levine
Martin Levine
Chief Financial Officer, Secretary and Treasurer
(Principal Financial and Accounting Officer)

Date: March 14, 2017

By: /s/ Joseph Murin
Joseph Murin
Director

Date: March 14, 2017

By: /s/ Regina M. Lowrie
Regina M. Lowrie
Director

By: _____
Stanley C. Middleman

Cherry Hill Mortgage Investment Corporation
Statement of Computation of Ratio of Earnings to Combined Fixed Charges
and Preferred Stock Dividends
(Dollars in Thousands)

	Year Ended December 31,		
	2015	2014	2013
Fixed charges ⁽¹⁾	\$ 5,983	\$ 4,307	\$ 867
Preferred stock dividends ⁽²⁾	—	—	—
Combined fixed charges and preferred stock dividends	\$ 5,983	\$ 4,307	\$ 867
Combined fixed charges and preferred stock dividends	\$ 5,983	\$ 4,307	\$ 867
Net income (loss)	13,355	2,375	21,202
Earnings (deficit)	\$ 19,338	\$ 6,682	\$ 22,069
Ratio of earnings to combined fixed charges and preferred stock dividends	3.23x	1.55x	25.45x

(1) Fixed charges consist of interest expense.

(2) There were no shares of preferred stock issued and outstanding in each period presented.

Net income for the year ended December 31, 2015 includes an unrealized loss on derivatives, net, of \$59, an unrealized loss on investments in Excess MSR of \$19 and an unrealized loss on investments in MSR of \$1,123. Net income for the year ended December 31, 2014 includes an unrealized loss on derivatives, net, of \$6,564 and an unrealized loss on investments in Excess MSR of \$5,100. Certain prior period amounts have been reclassified to conform to current period presentation. Excluding unrealized gains and losses on derivatives, net, and unrealized gains and losses on investments in MSR, Excess MSR, adjusted earnings and the ratio of adjusted earnings to combined fixed charges and preferred stock dividends would have been as follows:

	Year Ended December 31,		
	2015	2014	2013
Fixed charges ⁽¹⁾	\$ 5,983	\$ 4,307	\$ 867
Preferred stock dividends ⁽²⁾	—	—	—
Combined fixed charges and preferred stock dividends	\$ 5,983	\$ 4,307	\$ 867
Combined fixed charges and preferred stock dividends	\$ 5,983	\$ 4,307	\$ 867
Net income (loss)	13,355	2,375	21,202
Earnings (deficit)	19,338	6,682	22,069
Unrealized (gains)/losses on derivatives, net	59	6,564	(2,747)
Unrealized (gains)/losses on investments in Excess MSR ⁽³⁾	19	5,100	(14,894)
Unrealized (gains)/losses on investments in MSR	1,123	—	—
Adjusted earnings	\$ 20,539	\$ 18,346	\$ 4,428
Ratio of adjusted earnings to combined fixed charges and preferred stock dividends	3.43x	4.26x	5.11x

(1) Fixed charges consist of interest expense.

(2) There were no shares of preferred stock issued and outstanding in each period presented.

(3) Certain prior period amounts have been reclassified to conform to current period presentation.

Subsidiaries of the Registrant

<u>Subsidiary</u>	<u>Jurisdiction of Formation</u>
Cherry Hill Operating Partnership, LP	Delaware
Cherry Hill QRS I, LLC	Delaware
Cherry Hill QRS II, LLC	Delaware
Cherry Hill QRS III, LLC	Delaware
CHMI Solutions, Inc.	Delaware
Aurora Financial Group Inc.	New Jersey
CHMI Insurance Company, LLC	Michigan

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statements on Form S-8 (File No. 333-191600) and Forms S-3 (File No. 333-200151 and File No. 333-200152) of our report dated March 14, 2017, with respect to the consolidated financial statements of Cherry Hill Mortgage Investment Corporation, included in this Annual Report (Form 10-K) for the year ended December 31, 2016.

/s/ Ernst & Young LLP
New York, New York
March 14, 2017

CERTIFICATIONS

I, Jeffrey Lown, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cherry Hill Mortgage Investment Corporation (the “Registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s most recent fiscal quarter (the Registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting; and
5. The Registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant’s auditors and the audit committee of the Registrant’s board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant’s ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant’s internal control over financial reporting.

Date: March 14, 2017

By: /s/ Jeffrey Lown II

Name: Jeffrey Lown II

Title: President, Chief Investment Officer and Director
(Principal Executive Officer)

CERTIFICATIONS

I, Martin Levine, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cherry Hill Mortgage Investment Corporation (the “Registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s most recent fiscal quarter (the Registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting; and
5. The Registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant’s auditors and the audit committee of the Registrant’s board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant’s ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant’s internal control over financial reporting.

Date: March 14, 2017

4. The Registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:

Date: March 14, 2017

By: /s/ Martin Levine

Martin Levine

Chief Financial Officer, Secretary and Treasurer

**CERTIFICATION
PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002, 18 U.S.C. SECTION 1350**

In connection with the annual report on Form 10-K of Cherry Hill Mortgage Investment Corporation (the "Company") for the year ended December 31, 2016 to be filed with Securities and Exchange Commission on or about the date hereof (the "report"), I, Jeffrey Lown II, President, Chief Investment Officer and Director of the Company, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

1. The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

It is not intended that this statement be deemed to be filed for purposes of the Securities Exchange Act of 1934.

Date: March 14, 2017

By: /s/ Jeffrey Lown II

Name: Jeffrey Lown II

Title: President and Director (Principal Executive Officer)

**CERTIFICATION
PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002, 18 U.S.C. SECTION 1350**

In connection with the annual report on Form 10-K of Cherry Hill Mortgage Investment Corporation (the "Company") for the year ended December 31, 2016 to be filed with Securities and Exchange Commission on or about the date hereof (the "report"), I, Martin Levine, Chief Financial Officer, Secretary and Treasurer of the Company, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

1. The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

It is not intended that this statement be deemed to be filed for purposes of the Securities Exchange Act of 1934.

Date: March 14, 2017

By: /s/ Martin Levine

Martin Levine

Chief Financial Officer, Secretary and Treasurer
