ANNALY CAPITAL MANAGEMENT INC
Form 10-Q
May 05, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED: MARCH 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: 1-13447

ANNALY CAPITAL MANAGEMENT, INC.
(Exact name of registrant as specified in its charter)

MARYLAND 22-3479661
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

1211 AVENUE OF THE AMERICAS
NEW YORK, NEW YORK 10036 ……
(Address of principal executive offices) (Zip Code) ……..

(212) 696-0100
(Registrant’s telephone number, including area code)

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer 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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the last practicable date:

Class	Outstanding at April 30, 2016
Common Stock, $.01 par value	924,862,679

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PART I - FINANCIAL INFORMATION

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(dollars in thousands, except per share data)

	March 31, 2016 (Unaudited)	December 31, 2015 [1]
ASSETS		
Cash and cash equivalents (including cash pledged as collateral of $2,223,009 and $1,584,686, respectively) [2]	$2,416,136	$1,769,258
Investments, at fair value:		
Agency mortgage-backed securities (including pledged assets of $60,742,440 and $60,678,548, respectively)	65,439,824	65,718,224
Agency debentures (including pledged assets of $0 and $0, respectively)	157,035	152,038
Credit risk transfer securities (including pledged assets of $150,479 and $184,160, respectively)	501,167	456,510
Non-Agency mortgage-backed securities (including pledged assets of $1,057,282 and $744,783, respectively)	1,157,507	906,722
Commercial real estate debt investments (including pledged assets of $4,401,725 and $2,911,828, respectively) [3]	4,401,725	2,911,828
Commercial real estate debt and preferred equity, held for investment (including pledged assets of $523,787 and $578,820, respectively) [4]	1,177,468	1,348,817
Loans held for sale	278,600	278,600
Investments in commercial real estate	527,786	535,946
Corporate debt	639,481	488,508
Interest rate swaps, at fair value	93,312	19,642
Other derivatives, at fair value	77,449	22,066
Receivable for investments sold	2,220	121,625
Accrued interest and dividends receivable	232,180	231,336
Other assets	234,407	119,422
Goodwill	71,815	71,815
Intangible assets, net	35,853	38,536
Total assets	$77,443,965	$75,190,893
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Repurchase agreements	$54,448,141	$56,230,860
Other secured financing	3,588,326	1,845,048
Securitized debt of consolidated VIEs [5]	3,802,682	2,540,711
Participation sold	13,182	13,286
Mortgages payable	334,765	334,707
Interest rate swaps, at fair value	2,782,961	1,677,571

Other derivatives, at fair value	69,171	49,963
Dividends payable	277,456	280,779
Payable for investments purchased	250,612	107,115
Accrued interest payable	163,983	151,843
Accounts payable and other liabilities	54,679	53,088
Total liabilities	65,785,958	63,284,971
Stockholders' Equity:		
7.875% Series A Cumulative Redeemable Preferred Stock:		
7,412,500 authorized, issued and outstanding	177,088	177,088
7.625% Series C Cumulative Redeemable Preferred Stock:		
12,650,000 authorized, 12,000,000 issued and outstanding	290,514	290,514
7.50% Series D Cumulative Redeemable Preferred Stock:		
18,400,000 authorized, issued and outstanding	445,457	445,457
Common stock, par value $0.01 per share, 1,956,937,500 authorized,		
924,853,133 and 935,929,561 issued and outstanding, respectively	9,249	9,359
Additional paid-in capital	14,573,760	14,675,768
Accumulated other comprehensive income (loss)	640,366	(377,596)
Accumulated deficit	(4,487,982)	(3,324,616)
Total stockholders' equity	11,648,452	11,895,974
Noncontrolling interest	9,555	9,948
Total equity	11,658,007	11,905,922
Total liabilities and equity	$77,443,965	$75,190,893

(1) Derived from the audited consolidated financial statements at December 31, 2015.

(2) Includes cash of consolidated VIEs of $50.7 million and $48.5 million at March 31, 2016 and December 31, 2015, respectively.

(3) Includes senior securitized commercial mortgage loans of consolidated VIEs carried at fair value of $4.0 billion and $2.6 billion at March 31, 2016 and December 31, 2015, respectively.

(4) Includes senior securitized commercial mortgage loans of a consolidated VIE with a carrying value of $211.9 million and $262.7 million carried at amortized cost, net of an allowance for losses of $0, at March 31, 2016 and December 31, 2015, respectively.

(5) Includes securitized debt of consolidated VIEs carried at fair value of $3.7 billion and $2.4 billion at March 31, 2016 and December 31, 2015, respectively.

See notes to consolidated financial statements.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(dollars in thousands, except per share data)
(Unaudited)

	For the Quarters Ended	
	March 31, 2016	March 31, 2015
Net interest income:		
Interest income	$388,143	$519,114
Interest expense	147,447	129,420
Net interest income	240,696	389,694
Realized and unrealized gains (losses):		
Realized gains (losses) on interest rate swaps[1]	(147,475)	(158,239)
Realized gains (losses) on termination of interest rate swaps	-	(226,462)
Unrealized gains (losses) on interest rate swaps	(1,031,720)	(466,202)
Subtotal	(1,179,195)	(850,903)
Net gains (losses) on disposal of investments	(1,675)	62,356
Net gains (losses) on trading assets	125,189	(6,906)
Net unrealized gains (losses) on financial instruments measured at fair value through earnings	128	(33,546)
Subtotal	123,642	21,904
Total realized and unrealized gains (losses)	(1,055,553)	(828,999)
Other income (loss):		
Investment advisory income	-	10,464
Dividend income from affiliate	-	4,318
Other income (loss)	(6,115)	(1,024)
Total other income (loss)	(6,115)	13,758
General and administrative expenses:		
Compensation and management fee	36,997	38,629
Other general and administrative expenses	10,948	12,309
Total general and administrative expenses	47,945	50,938
Income (loss) before income taxes	(868,917)	(476,485)
Income taxes	(837)	14
Net income (loss)	(868,080)	(476,499)
Net income (loss) attributable to noncontrolling interest	(162)	(90)
Net income (loss) attributable to Annaly	(867,918)	(476,409)
Dividends on preferred stock	17,992	17,992
Net income (loss) available (related) to common stockholders	$(885,910)	$(494,401)
Net income (loss) per share available (related) to common stockholders:		
Basic	$(0.96)	$(0.52)
Diluted	$(0.96)	$(0.52)

Weighted average number of common shares outstanding:		
Basic	926,813,588	947,669,831
Diluted	926,813,588	947,669,831
Dividends Declared Per Share of Common Stock	$0.30	$0.30
Net income (loss)	$(868,080)	$(476,499)
Other comprehensive income (loss):		
Unrealized gains (losses) on available-for-sale securities	1,017,707	631,472
Reclassification adjustment for net (gains) losses included in net income (loss)	255	(62,356)
Other comprehensive income (loss)	1,017,962	569,116
Comprehensive income (loss)	$149,882	$92,617
Comprehensive income (loss) attributable to noncontrolling interest	(162)	(90)
Comprehensive income (loss) attributable to Annaly	150,044	92,707
Dividends on preferred stock	17,992	17,992
Comprehensive income (loss) attibutable to common stockholders	$132,052	$74,715

(1) Consists of interest expense on interest rate swaps.

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ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(dollars in thousands, except per share data)
(Unaudited)

	7.875% Series A Cumulative Redeemable Preferred Stock	7.625% Series C Cumulative Redeemable Preferred Stock	7.50% Series D Cumulative Redeemable Preferred Stock	Common stock par value	Additional paid-in capital	Accumulated other comprehensive income (loss)	Accumulated deficit	Total stockholders' equity	Nonco interes
BALANCE, December 31, 2014	$177,088	$290,514	$445,457	$9,476	$14,786,509	$204,883	$(2,585,436)	$13,328,491	$5,290
Net income (loss) attributable to Annaly	-	-	-	-	-	-	(476,409)	(476,409)	-
Net income (loss) attributable to noncontrolling interest	-	-	-	-	-	-	-	-	(90
Unrealized gains (losses) on available-for-sale securities	-	-	-	-	-	631,472	-	631,472	-
Reclassification adjustment for net (gains) losses included in net income (loss)	-	-	-	-	-	(62,356)	-	(62,356)	-
Stock compensation expense	-	-	-	-	39	-	-	39	-
Net proceeds from direct purchase and dividend reinvestment	-	-	-	1	569	-	-	570	-
Equity contributions from (distributions to) noncontrolling interest	-	-	-	-	-	-	-	-	(115
Preferred Series A dividends, declared $0.492	-	-	-	-	-	-	(3,648)	(3,648)	-

per share									
Preferred Series C dividends, declared $0.477 per share	-	-	-	-	-	-	(5,719)	(5,719)	-
Preferred Series D dividends, declared $0.469 per share	-	-	-	-	-	-	(8,625)	(8,625)	-
Common dividends declared, $0.30 per share	-	-	-	-	-	-	(284,310)	(284,310)	-
BALANCE, March 31, 2015	$177,088	$290,514	$445,457	$9,477	$14,787,117	$773,999	$(3,364,147)	$13,119,505	$5,08
BALANCE, December 31, 2015	$177,088	$290,514	$445,457	$9,359	$14,675,768	$(377,596)	$(3,324,616)	$11,895,974	$9,94
Net income (loss) attributable to Annaly	-	-	-	-	-	-	(867,918)	(867,918)	-
Net income (loss) attributable to noncontrolling interest	-	-	-	-	-	-	-	-	(162
Unrealized gains (losses) on available-for-sale securities	-	-	-	-	-	1,017,707	-	1,017,707	-
Reclassification adjustment for net (gains) losses included in net income (loss)	-	-	-	-	-	255	-	255	-
Stock compensation expense	-	-	-	-	69	-	-	69	-
Net proceeds from direct purchase and dividend reinvestment	-	-	-	1	523	-	-	524	-
Buyback of common stock	-	-	-	(111)	(102,600)	-	-	(102,711)	-
Equity contributions from (distributions to) noncontrolling interest	-	-	-	-	-	-	-	-	(231
	-	-	-	-	-	-	(3,648)	(3,648)	-

Preferred Series A dividends, declared $0.492 per share									
Preferred Series C dividends, declared $0.477 per share	-	-	-	-	-	-	(5,719)	(5,719)	-
Preferred Series D dividends, declared $0.469 per share	-	-	-	-	-	-	(8,625)	(8,625)	-
Common dividends declared, $0.30 per share	-	-	-	-	-	-	(277,456)	(277,456)	-
BALANCE, March 31, 2016	$177,088	$290,514	$445,457	$9,249	$14,573,760	$640,366	$(4,487,982)	$11,648,452	$9,55

See notes to consolidated financial statements

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ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)
(Unaudited)

	For the Quarters Ended March 31,	
	2016	2015
Cash flows from operating activities:		
Net income (loss)	$(868,080)	$(476,499)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Amortization of Residential Investment Securities premiums and discounts, net	355,671	284,777
Amortization of commercial real estate investment premiums and discounts, net	(247)	(160)
Amortization of intangibles	2,429	1,195
Amortization of deferred financing costs	520	2,914
Amortization of net origination fees and costs, net	(1,737)	(1,190)
Amortization of contingent beneficial conversion feature and equity component of Convertible Senior Notes	-	11,758
Depreciation expense	4,570	2,823
Net (gains) losses on sales of Residential Investment Securities	1,675	(62,356)
Stock compensation expense	69	39
Unrealized (gains) losses on interest rate swaps	1,031,720	466,202
Net unrealized (gains) losses on financial instruments measured at fair value through earnings	(128)	33,546
Equity in net income from unconsolidated joint ventures	3,147	-
Net (gains) losses on trading assets	(125,189)	6,906
Proceeds from repurchase agreements of RCap	466,225,000	386,000,000
Payments on repurchase agreements of RCap	(466,825,000)	(391,250,000)
Proceeds from reverse repurchase agreements	14,550,000	15,325,000
Payments on reverse repurchase agreements	(14,550,000)	(15,325,000)
Net payments on derivatives	91,358	(66,604)
Due to / from brokers	(5)	-
Other assets	(66,389)	(2,627)
Accrued interest and dividends receivable	(1,547)	28,886
Receivable for investment advisory income	-	134
Accrued interest payable	12,140	(25,425)
Accounts payable and other liabilities	26,530	3,709
Net cash provided by (used in) operating activities	(133,493)	(5,041,972)
Cash flows from investing activities:		
Payments on purchases of Residential Investment Securities	(4,644,731)	(5,065,764)
Proceeds from sales of Residential Investment Securities	3,596,677	13,973,224
Principal payments on Agency mortgage-backed securities	1,946,498	2,596,964
Payments on purchases of corporate debt	(181,079)	(63,015)
Principal payments on corporate debt	30,578	1,733

Purchases of commercial real estate debt investments	(76,862)	(185,925)
Sales of commercial real estate debt investments	-	41,016
Purchase of securitized loans at fair value	(1,489,268)	(1,370,011)
Origination of commercial real estate investments, net	(179,099)	(61,502)
Principal payments on commercial real estate debt investments	1,374	-
Principal payments on securitized loans at fair value	52,287	-
Principal payments on commercial real estate investments	351,930	82,408
Purchase of investments in real estate	(610)	-
Distributions in excess of cumulative earnings from unconsolidated joint ventures	1,053	-
Purchase of equity securities	(88,062)	(3,602)
Proceeds from sales of equity securities	16,112	-
Net cash provided by (used in) investing activities	(663,202)	9,945,526

Statements continued on following page.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

Cash flows from financing activities:		
Proceeds from repurchase agreements	43,970,988	57,776,249
Principal payments on repurchase agreements	(45,153,707)	(63,410,797)
Payments on maturity of convertible senior notes	-	(107,541)
Proceeds from other secured financing	2,146,084	90,000
Payments on other secured financing	(402,806)	-
Proceeds from issuance of securitized debt	1,381,640	1,267,914
Principal repayments on securitized debt	(96,861)	(37,680)
Payment of deferred financing cost	(400)	(641)
Net proceeds from direct purchases and dividend reinvestments	524	569
Principal payments on participation sold	(77)	(76)
Principal payments on mortgages payable	(99)	(69)
Distributions to noncontrolling interests	(230)	(115)
Net payment on share repurchase	(102,712)	-
Dividends paid	(298,771)	(302,285)
Net cash provided by (used in) financing activities	1,443,573	(4,724,472)
Net (decrease) increase in cash and cash equivalents	646,878	179,082
Cash and cash equivalents, beginning of period	1,769,258	1,920,326
Cash and cash equivalents, end of period	$2,416,136	$2,099,408
Supplemental disclosure of cash flow information:		
Interest received	$726,930	$815,765
Dividends received	$-	$4,048
Investment advisory income received	$-	$10,992
Interest paid (excluding interest paid on interest rate swaps)	$127,449	$124,673
Net interest paid on interest rate swaps	$152,458	$176,395
Taxes paid	$244	$643
Noncash investing activities:		
Receivable for investments sold	$2,220	$2,009,937
Payable for investments purchased	$250,612	$5,205
Net change in unrealized gains (losses) on available-for-sale securities, net of reclassification adjustment	$1,017,962	$569,116
Dividends declared, not yet paid	$277,456	$284,310

See notes to consolidated financial statements.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. DESCRIPTION OF BUSINESS

Annaly Capital Management, Inc. (the "Company" or "Annaly") is a Maryland corporation that commenced operations on February 18, 1997. The Company owns a portfolio of real estate related investments, including mortgage pass-through certificates, collateralized mortgage obligations, Agency debentures, credit risk transfer ("CRT") securities, other securities representing interests in or obligations backed by pools of mortgage loans, commercial real estate assets and corporate debt. The Company's principal business objectives are to generate net income for distribution to its stockholders from its investments and capital preservation. The Company is externally managed by Annaly Management Company LLC (the "Manager").
The Company's business operations are primarily comprised of the following:

- Annaly, the parent company, which invests primarily in Agency mortgage-backed securities and related derivatives to hedge these investments. Its portfolio also includes residential credit investments such as CRT and non-Agency mortgage-backed securities.
- Annaly Commercial Real Estate Group, Inc. ("ACREG," formerly known as CreXus Investment Corp.), a wholly-owned subsidiary that was acquired during the second quarter of 2013 which specializes in acquiring, financing and managing commercial real estate loans and other commercial real estate debt, commercial mortgage-backed securities and other commercial real estate-related assets.
- Annaly Middle Market Lending LLC ("MML," formerly known as Charlesfort Capital Management LLC), a wholly-owned subsidiary which engages in corporate middle market lending transactions.
- RCap Securities, Inc. ("RCap"), a wholly-owned subsidiary, which operates as a broker-dealer and is a member of the Financial Industry Regulatory Authority ("FINRA").

The Company has elected to be taxed as a Real Estate Investment Trust ("REIT") as defined under the Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder (the "Code").

2. BASIS OF PRESENTATION

The accompanying consolidated financial statements and related notes of the Company have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP").
The accompanying consolidated financial statements and related notes are unaudited and should be read in conjunction with the audited consolidated financial statements included in the Company's most recent annual report on Form 10-K. The consolidated financial information as of December 31, 2015 has been derived from audited consolidated financial statements not included herein.
In the opinion of management, all normal, recurring adjustments have been included for a fair presentation of this interim financial information. Interim period operating results may not be indicative of the operating results for a full year.

3. SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation – The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and consolidated variable interest entities. All intercompany balances and transactions have been eliminated in consolidation. The Company reclassified previously presented financial information so that amounts previously presented conform to the current period presentation.

The Company has evaluated all of its investments in legal entities in order to determine if they are variable interests in Variable Interest Entities ("VIEs"). A VIE is defined as an entity in which equity investors (i) do not have the characteristics of a controlling financial interest, and/or (ii) do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. A variable interest is an investment or other interest that will absorb portions of a VIE's expected losses or receive portions of the entity’s expected residual returns. A VIE is required to be consolidated by its primary beneficiary, which is defined as the party that (i) has the power to direct the activities that most significantly impact the VIE’s economic performance and (ii) has the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

To assess whether the Company has the power to direct the activities of a VIE that most significantly impact the VIE's economic performance, the Company considers all facts and circumstances, including the Company's role in establishing the VIE and the Company's ongoing rights and responsibilities. This assessment includes first, identifying the activities that most significantly impact the VIE's economic performance; and second, identifying which party, if any, has power over those activities. In general, the parties that make the most significant decisions affecting the VIE or have the right to unilaterally remove those decision makers are deemed to have the power to direct the activities of a VIE.

To assess whether the Company has the obligation to absorb losses of the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE, the Company applies significant judgment and considers all of its economic interests, including debt and equity investments and other arrangements deemed to be variable interests, both explicit and implicit, in the VIE. This assessment requires that the Company applies judgment in determining whether these interests, in the aggregate, are considered potentially significant to the VIE. Factors considered in assessing significance include: the design of the VIE, including its capitalization structure; subordination of interests; payment priority; relative share of interests held across various classes within the VIE's capital structure; and the reasons why the interests are held by the Company.

The Company performs ongoing reassessments of whether changes in the facts and circumstances regarding the Company's involvement with a VIE causes the Company's consolidation conclusion regarding the VIE to change.

Cash and Cash Equivalents – Cash and cash equivalents include cash on hand, cash held in money market funds on an overnight basis and cash pledged as collateral with counterparties. Cash deposited with clearing organizations is carried at cost, which approximates fair value. The Company also maintains collateral in the form of cash on margin with counterparties to its interest rate swaps and other derivatives. RCap is a member of various clearing organizations with which it maintains cash required to conduct its day-to-day clearance activities. Cash and securities deposited with clearing organizations and collateral held in the form of cash on margin with counterparties to the Company's interest rate swaps and other derivatives totaled approximately $2.2 billion and $1.6 billion at March 31, 2016 and December 31, 2015, respectively.

Fair Value Measurements – The Company reports various financial instruments at fair value. A complete discussion of the methodology utilized by the Company to estimate the fair value of certain financial instruments is included in these Notes to Consolidated Financial Statements.

Revenue Recognition – The revenue recognition policy by asset class is discussed below.

Agency Mortgage-Backed Securities, Agency Debentures, Non-Agency Mortgage-Backed Securities and CRT Securities – The Company invests in mortgage pass-through certificates, collateralized mortgage obligations and other mortgage-backed securities representing interests in or obligations backed by pools of mortgage loans and certificates guaranteed by the Government National Mortgage Association ("Ginnie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac") or the Federal National Mortgage Association ("Fannie Mae") (collectively, "Agency mortgage-backed securities"). These Agency mortgage-backed securities may include forward contracts for Agency mortgage-backed securities purchases or sales of a generic pool, on a to-be-announced basis ("TBA securities"). The Company also invests in Agency debentures issued by the Federal Home Loan Banks, Freddie Mac and Fannie Mae, as well as CRT securities. CRT securities are risk sharing instruments issued by Fannie Mae and Freddie Mac, and similarly structured transactions arranged by third party market participants. CRT securities are designed to synthetically transfer mortgage credit risk from Fannie Mae, Freddie Mac and/or third parties to private investors. The Company also invests in non-Agency mortgage-backed securities, such as those issued in non-performing loan ("NPL") and re-performing loan (“RPL”) securitizations.

Agency mortgage-backed securities, Agency debentures, non-Agency mortgage-backed securities and CRT securities are referred to herein as “Residential Investment Securities.” Although the Company generally intends to hold most of its Residential Investment Securities until maturity, it may, from time to time, sell any of its Residential Investment Securities as part of the overall management of its portfolio. Residential Investment Securities classified as available-for-sale are reported at fair value with unrealized gains and losses reported as a component of other comprehensive income (loss). The fair value of Residential Investment Securities classified as available-for-sale is estimated by management and is compared to independent sources for reasonableness. Residential Investment Securities transactions are recorded on trade date, including TBA securities that meet the regular-way securities scope exception from derivative accounting. The Company previously changed its accounting policy for determining the realized gains and losses on sales of Residential Investment Securities from the average cost method to

the specific identification method. The Company determined that the specific identification method was preferable because it more accurately matches gains or losses with costs and is the methodology predominantly used by its industry peers, among other considerations. The impact of the change was immaterial to the consolidated financial statements and prior periods.
The Company elected the fair value option for interest-only mortgage-backed securities, non-Agency mortgage-backed securities and certain CRT securities. Interest-only securities and inverse interest-only securities are collectively referred to as "interest-only securities." These interest-only mortgage-backed securities represent the Company's right to receive a specified proportion of the contractual interest flows of specific mortgage-backed securities. Interest-only mortgage-backed securities, non-Agency mortgage-backed securities and certain CRT securities are measured at fair value with changes in fair value recorded as Net unrealized gains (losses) on financial instruments measured at fair value through earnings in the Company's Consolidated Statements of Comprehensive Income (Loss). The interest-only securities are included in Agency mortgage-backed securities at fair value on the accompanying Consolidated Statements of Financial Condition.

Interest income from coupon payments is accrued based on the outstanding principal amounts of the Residential Investment Securities and their contractual terms. In addition, the Company recognizes income under the retrospective method on a substantial portion of its Residential Investment Securities classified as available-for-sale. Premiums and discounts associated with the purchase of Residential Investment Securities are amortized or accreted into income over the remaining projected lives of the securities. Using a third-party supplied model and market information to project future cash flows and expected remaining lives of securities, the effective interest rate determined for each security is applied as if it had been in place from the date of the security's acquisition. The amortized cost of the investment is then adjusted to the amount that would have existed had the new effective yield been applied since the acquisition date. The adjustment to amortized cost is offset with a charge or credit to interest income. Changes in interest rates and other market factors will impact prepayment speed projections and the amount of premium amoritization recognized in any given period.
Equity Securities – The Company may invest in equity securities that are classified as available-for-sale or trading. Equity securities classified as available-for-sale are reported at fair value, based on market quotes, with unrealized gains and losses reported as a component of other comprehensive income (loss). Equity securities classified as trading are reported at fair value, based on market quotes, with unrealized gains and losses reported in the Consolidated Statements of Comprehensive Income (Loss) as Net gains (losses) on trading assets. Dividends are recorded in earnings based on the declaration date.

Derivative Instruments – The Company may use a variety of derivative instruments to economically hedge some of its exposure to market risks, including interest rate and prepayment risk. These instruments include, but are not limited to, interest rate swaps, options to enter into interest rate swaps ("swaptions"), TBA contracts without intent to accept delivery ("TBA derivatives"), options on TBA contracts ("MBS options") and U.S. Treasury and Eurodollar futures contracts. The Company may also invest in other types of mortgage derivatives such as interest-only securities and synthetic total return swaps, such as the Markit IOS Synthetic Total Return Swap Index. Derivatives are accounted for in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 815, Derivatives and Hedging, which requires recognition of all derivatives as either assets or liabilities at fair value in the Consolidated Statements of Financial Condition with changes in fair value recognized in the Consolidated Statements of Comprehensive Income (Loss). None of the Company's derivative transactions have been designated as hedging instruments for accounting purposes.

Some derivative agreements contain provisions that allow for netting or setting off by counterparty; however, the Company elected to present related assets and liabilities on a gross basis in the Consolidated Statements of Financial Condition.

Interest rate swap agreements - Interest rate swaps are the primary instrument used to mitigate interest rate risk. In particular, the Company uses interest rate swaps to manage its exposure to changing interest rates on its repurchase agreements by economically hedging cash flows associated with these borrowings. Swap agreements may or may not be cleared through a derivatives clearing organization ("DCO"). Uncleared swaps are fair valued using internal pricing models and compared to the counterparty market values. Centrally cleared swaps are fair valued using internal pricing models and compared to the DCO's market values.

Interest rate swaptions - Interest rate swaptions are purchased/sold to mitigate the potential impact of increases or decreases in interest rates. Interest rate swaptions provide the option to enter into an interest rate swap agreement for a predetermined notional amount, stated term and pay and receive interest rates in the future. They are not centrally cleared. The premium paid/received for interest rate swaptions is reported as an

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asset/liability in the Consolidated Statements of Financial Condition. The difference between the premium and the fair value of the swaption is reported in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss). If a swaption expires unexercised, the realized gain (loss) on the swaption would be equal to the premium received/paid. If the Company sells or exercises a swaption, the realized gain or loss on the swaption would be equal to the difference between the cash received or the fair value of the underlying interest rate swap received and the premium paid.

The fair value of interest rate swaptions is estimated using internal pricing models and compared to the counterparty market value.

TBA Dollar Rolls - TBA dollar roll transactions are accounted for as a series of derivative transactions. The fair value of TBA derivatives is based on similar methods used to value Agency mortgage-backed securities with gains and losses recorded in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss).

MBS Options – MBS options are generally options on TBA contracts, which help manage mortgage market risks and volatility while providing the potential to enhance returns. MBS options are over-the-counter traded instruments and those written on current-coupon mortgage-backed securities are typically the most liquid. MBS options are measured at fair value using internal pricing models and compared to the counterparty market value at the valuation date with gains and losses recorded in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss).

Futures Contracts - Futures contracts are derivatives that track the prices of specific assets. Short sales of futures contracts help mitigate the potential impact of changes in interest rates on the portfolio performance. The Company maintains margin accounts that are settled daily with Futures Commission Merchants (“FCMs”). The margin requirement varies based on the market value of the open positions and the equity retained in the account. Futures contracts are measured at fair value based on exchange pricing with gains and losses recorded in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss).

Repurchase Agreements – The Company finances the acquisition of a significant portion of its Agency mortgage-backed securities with repurchase agreements. The Company examines each of the specified criteria in ASC 860, Transfers and Servicing, at the inception of each transaction and has determined that each of the financings meet the specified criteria in this guidance.

Reverse repurchase agreements and repurchase agreements with the same counterparty and the same maturity are presented net in the Consolidated Statements of Financial Condition when the terms of the agreements meet the criteria to permit netting. The Company reports cash flows on repurchase agreements as financing activities in the Consolidated Statements of Cash Flows. The Company reports cash flows on reverse repurchase and repurchase agreements entered into by RCap as operating activities in the Consolidated Statements of Cash Flows.

Goodwill and Intangible Assets – The Company’s acquisitions are accounted for using the acquisition method. Under the acquisition method, net assets and results of operations of acquired companies are included in the consolidated financial statements from the date of acquisition. The purchase prices are allocated to the assets acquired, including identifiable intangible assets, and the liabilities assumed based on their estimated fair values at the date of acquisition. The excess of purchase price over the fair value of the net assets acquired is recognized as goodwill. Conversely, any excess of the fair value of the net assets acquired over the purchase price is recognized as a bargain purchase gain. The Company tests goodwill for impairment on an annual basis and at interim periods when events or circumstances may make it more likely than not that an impairment has occurred. If a qualitative analysis indicates that there may be an impairment, a quantitative analysis is performed. The quantitative impairment test for goodwill utilizes a two-step approach, whereby the Company compares the carrying value of each identified reporting unit to its fair value. If the carrying value of the reporting unit is greater than its fair value, the second step is performed, where the implied fair value of goodwill is compared to its carrying value. The Company recognizes an impairment charge for the amount by which the carrying amount of goodwill exceeds its fair value. An impairment of the goodwill associated with the Company's acquisition of Fixed Income Discount Advisory Company ("FIDAC") was recorded during the year ended December 31, 2015.

Intangible assets with an estimated useful life are amortized over their expected useful lives.

Convertible Senior Notes – The Company recorded the 4% Convertible Senior Notes and 5% Convertible Senior Notes (collectively, the "Convertible Senior Notes") at their contractual amounts, adjusted by the effects of a beneficial conversion feature and a contingent beneficial conversion feature (collectively, the "Conversion Features"). The Conversion Features' intrinsic value is included in "Additional paid-in capital" on the Company's Consolidated Statements of Financial

Condition and reduces the recorded liability amount associated with the Convertible Senior Notes. A Conversion Feature may be recognized as a result of adjustments to the conversion price for dividends declared to common stockholders. The 4% and 5% Convertible Senior Notes matured in February 2015 and May 2015, respectively.

Stock Based Compensation – The Company is required to measure and recognize in the consolidated financial statements the compensation cost relating to share-based payment transactions. The Company recognizes compensation expense on a straight-line basis over the requisite service period for the entire award.

Income Taxes – The Company has elected to be taxed as a REIT and intends to comply with the provisions of the Code, with respect thereto. Accordingly, the Company will not be subject to federal income tax to the extent of its distributions to stockholders and as long as certain asset, income and stock ownership tests are met. The Company and certain of its direct and indirect subsidiaries, including FIDAC, RCap and certain subsidiaries of ACREG, have made separate joint elections to treat these subsidiaries as taxable REIT subsidiaries ("TRSs"). As such, each of these TRSs is taxable as a domestic C corporation and subject to federal, state and local income taxes based upon their taxable income.
The provisions of ASC 740, Income Taxes, ("ASC 740") clarify the accounting for uncertainty in income taxes recognized in financial statements and prescribe a recognition threshold and measurement attribute for uncertain tax positions taken or expected to be taken on a tax return. ASC 740 also requires that interest and penalties related to unrecognized tax benefits be recognized in the financial statements. The Company does not have any unrecognized tax benefits that would affect its financial position. Thus, no accruals for penalties and interest were necessary as of March 31, 2016 and December 31, 2015.

Use of Estimates – The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Commercial Real Estate Investments

Commercial Real Estate Debt Investments - The Company's commercial real estate debt investments are comprised of commercial mortgage-backed securities and loans held by consolidated collateralized financing entities. Commercial mortgage-backed securities are classified as available-for-sale and reported at fair value with unrealized gains and losses reported as a component of other comprehensive income (loss). Management evaluates commercial mortgage-backed securities for other-than-temporary impairment at least quarterly. See the "Commercial Real Estate Investments" footnote for additional information regarding the consolidated collateralized financing entities.

Commercial Real Estate Loans – The Company's commercial real estate loans are comprised of fixed-rate and adjustable-rate loans. The Company designates loans as held for investment if it has the intent and ability to hold the loans until maturity or payoff. The difference between the principal amount of a loan and proceeds at acquisition is recorded as either a discount or premium. If the Company intends to sell or securitize the loans and the financing vehicle is not expected to be consolidated, they are classified as held for sale. Commercial real estate loans that are designated as held for sale are carried at the lower of amortized cost or fair value and recorded as Loans held for sale in the accompanying Consolidated Statements of Financial Condition. Any deferred origination fees and costs or purchase premiums or discounts are deferred and recognized upon sale. The Company determines the fair value of commercial real estate loans held for sale on an individual loan basis. Commercial real estate loans that are designated as held for investment and are originated or purchased by the Company are carried at their outstanding principal balance, net of unamortized origination fees and costs, premiums or discounts, less a reserve for estimated losses if necessary. The Company has elected the fair value option for multi-family mortgage loans held in securitization trusts that it was required to consolidate. Preferred equity interests are designated as held for investment and are carried at their outstanding principal balance, net of unamortized origination fees and costs, premiums or discounts, less a reserve for estimated losses if necessary. See “Commercial Real Estate Investments” footnote for additional information.

Investments in Commercial Real Estate – Investments in commercial real estate are carried at historical cost less accumulated depreciation. Historical cost includes all costs necessary to bring the asset to the condition and location necessary for its intended use, including financing during the construction period. Costs directly related to acquisitions deemed to be business combinations are expensed. Ordinary repairs and maintenance which are not reimbursed by tenants are expensed as incurred. Major replacements and improvements that extend the useful life of the asset are capitalized and depreciated over their useful life.

Investments in commercial real estate are depreciated using the straight-line method over the estimated useful lives of the assets, summarized as follows:

Category	Term
Building	30 - 40 years
Site improvements	1 - 28 years

The Company follows the acquisition method of accounting for acquisitions of operating real estate held for investment, where the purchase price of operating real estate is allocated to tangible assets such as land, building, site improvements and other identified intangibles such as above/below market and in-place leases.

The Company applies the equity method of accounting for its investments in joint ventures where it is not considered to have a controlling financial interest. Under the equity method of accounting, the Company will recognize its share of earnings or losses of the investee in the period in which they are reported by the investee. The Company also considers whether there are any indicators of other-than-temporary impairment of joint ventures accounted for under the equity method.

The Company evaluates whether real estate acquired in connection with a foreclosure ("REO") or UCC/deed in lieu of foreclosure (herein collectively referred to as a foreclosure) constitutes a business and whether business combination accounting is applicable. Upon foreclosure of a property, the excess of the carrying value of a loan, if any, over the estimated fair value of the property, less estimated costs to sell, is charged to provision for loan losses.

Investments in commercial real estate, including REO, that do not meet the criteria to be classified as held for sale are separately presented in the Consolidated Statements of Financial Condition as held for investment. Real estate held for sale is reported at the lower of its carrying value or its estimated fair value less estimated costs to sell. Once a property is determined to be held for sale, depreciation is no longer recorded.

The Company's real estate portfolio (REO and real estate held for investment) is reviewed on a quarterly basis, or more frequently as necessary, to assess whether there are any indicators that the value of its operating real estate may be impaired or that its carrying value may not be recoverable. A property's value is considered impaired if the Company's estimate of the aggregate future undiscounted cash flows to be generated by the property is less than the carrying value of the property. In conducting this review, the Company considers U.S. macroeconomic factors, including real estate sector conditions, together with asset specific and other factors. To the extent impairment has occurred and is considered to be other than temporary, the loss will be measured as the excess of the carrying amount of the property over the calculated fair value of the property.

Revenue Recognition – Commercial Real Estate Investments - Interest income is accrued based on the outstanding principal amount of the commercial real estate loans and preferred equity interests held for investment (collectively referred to as "CRE Debt and Preferred Equity Investments") and their contractual terms. Premiums and discounts associated with the purchase of CRE Debt and Preferred Equity Investments are amortized or accreted into interest income over the projected lives of the CRE Debt and Preferred Equity Investments using the interest method.

Corporate Debt

Corporate Loans – The Company's investments in corporate debt that are loans are designated as held for investment when the Company has the intent and ability to hold the investment until maturity or payoff. These investments are carried at their principal balance outstanding plus any premiums or discounts less allowances for loan losses. Interest income from coupon payments is accrued based upon the outstanding principal amounts of the debt and its contractual terms. Premiums and discounts are amortized or accreted into interest income using the interest method. These investments typically take the form of senior secured loans primarily in first lien and second lien loans. The Company's senior secured loans generally have stated maturities of three to eight years. In connection with these senior secured loans the Company receives a security interest in certain of the assets of the borrower and such assets support repayment of such loans. Senior secured loans are generally exposed to the least amount of credit risk given their seniority to scheduled principal and interest and priority of security in the assets of the borrower. To date, the majority of the Company's investments have been funded term loans versus debt securities.

Corporate Debt Securities – The Company's investments in corporate debt securities are designated as held-to-maturity when the Company has the intent and ability to hold the investments until maturity. These investments are carried at their principal balance outstanding plus any premiums or discounts less other-than-temporary impairment. Interest income from coupon payments is accrued based upon the outstanding principal amounts of the debt and its contractual terms. Premiums

and discounts are amortized or accreted into interest income using the interest method.
Other-Than-Temporary Impairment – Management evaluates available-for-sale securities and held-to-maturity debt securities for other-than-temporary impairment at least quarterly, and more frequently when economic or market conditions warrant such evaluation. When the fair value of an available-for-sale security is less than its amortized cost the security is considered impaired. For securities that are impaired, the Company determines if it (1) has the intent to sell the security, (2) is more likely than not that it will be required to sell the security before recovery of its amortized cost basis, or (3) does not expect to recover the entire amortized cost basis of the security. Further, the security is analyzed for credit loss (the difference between the present value of cash flows expected to be collected and the amortized cost basis). The credit loss, if any, will then be recognized in the Consolidated Statements of Comprehensive Income (Loss), while the balance of losses related to other factors will be recognized as a component of other comprehensive income (loss). If the fair value is less than the cost of a held-to-maturity security, the Company performs an analysis to determine whether it expects to recover the entire cost basis of the security. There was no other-than-temporary impairment recognized for the quarters ended March 31, 2016 and 2015.
Allowance for Losses – The Company evaluates the need for a loss reserve on its CRE Debt and Preferred Equity Investments and its corporate loans. A provision for losses related to CRE Debt and Preferred Equity Investments and corporate loans, including those accounted for under ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, may be established when it is probable the Company will not collect amounts contractually due or all amounts previously estimated to be collectable. Management assesses the credit quality of the portfolio and adequacy of loan loss reserves on a quarterly basis, or more frequently as necessary. Significant judgment is required in this analysis. Depending on the expected recovery of its investment, the Company considers the estimated net recoverable value of the CRE Debt and Preferred Equity Investments as well as other factors, including but not limited to the fair value of any collateral, the amount and the status of any senior debt, the prospects for the borrower and the competitive landscape where the borrower conducts business. To determine if loan loss allowances are required on investments in corporate debt, the Company reviews the monthly and/or quarterly financial statements of the borrowers, verifies loan compliance packages if applicable and analyzes current results relative to budgets and sensitivities performed at inception of the investment. Because these determinations are based upon projections of future
economic events, which are inherently subjective, the amounts ultimately realized may differ materially from the carrying value as of the reporting date.
The Company may be exposed to various levels of credit risk depending on the nature of its investments and credit enhancements, if any, supporting its assets. The Company’s core investment process includes procedures related to the initial approval and periodic monitoring of credit risk and other risks associated with each investment. The Company’s investment underwriting procedures include evaluation of the underlying borrowers’ ability to manage and operate their respective properties or companies. Management reviews loan-to-value metrics upon either the origination or the acquisition of a new investment but generally does not update the loan-to-value metrics in the course of quarterly surveillance. Management generally reviews the most recent financial information produced by the borrower, which may include, but is not limited to, net operating income (“NOI”), debt service coverage ratios, property debt yields (net cash flow or NOI divided by the amount of outstanding indebtedness), loan per unit and rent rolls relating to each of the Company’s CRE Debt and Preferred Equity Investments, and may consider other factors management deems important. Management also reviews market pricing to determine each borrower’s ability to refinance their respective assets at the maturity of each loan. Management also reviews economic trends, both macro and those affecting the property specifically, and the supply and demand of competing projects in the sub-market in which each subject property is located. Management monitors the financial condition and operating results of its corporate borrowers and continually assesses the future outlook of the borrower’s financial performance in light of industry developments, management changes and company-specific considerations.
In connection with the quarterly surveillance review process, loans are assigned an internal risk rating. Effective December 31, 2015, the loan risk ratings were enhanced and considered guidance provided by the Office of the

Controller of the Currency for commercial real estate lending. The initial internal risk ratings (“Initial Ratings”) are based on loan-to-values and the NOI debt yields of the underlying collateral of the Company’s CRE Debt and Preferred Equity Investments and based upon leverage and cash flow coverages of the borrowers’ debt and operating obligations. The final internal risk ratings are influenced by other quantitative and qualitative factors that can result in an adjustment to the Initial Ratings, subject to review and approval by the respective committee. The internal risk rating categories include “Performing”, “Closely Monitored”, “Special Mention”, “Substandard”, “Doubtful” or “Loss”. Performing loans meet all present contractual obligations.

Closely Monitored loans are transitional or could be exhibiting some weakness in both leverage and liquidity, which if not corrected, could jeopardize timely repayment. Special Mention loans exhibit potential weakness that deserves management’s close attention and if uncorrected, may result in deterioration of repayment prospects. Substandard loans are inadequately protected by sound worth and paying capacity of the obligor or of the collateral pledged with a distinct possibility that loss will be sustained if some of the deficiencies are not corrected. Doubtful loans are Substandard loans whereby collection of all contractual principal and interest is highly questionable or improbable. Loss loans are considered uncollectible. The presentation of prior period internal risk ratings have been revised to conform to the current period presentation.

No allowance for loan losses was deemed necessary as of March 31, 2016 and December 31, 2015.

Broker Dealer Activities

In January 2014, RCap ceased its trading activity in U.S. Treasury securities, derivatives and securities borrowed and loaned transactions.

Reverse Repurchase Agreements – RCap enters into reverse repurchase agreements and repurchase agreements as part of its matched book trading activity. Reverse repurchase agreements are recorded on settlement date at the contract amount and are collateralized by mortgage-backed or other securities. Margin calls are made by RCap as necessary based on the daily valuation of the underlying collateral as compared to the contract price. RCap generates income from the spread between what is earned on the reverse repurchase agreements and what is paid on the matched repurchase agreements. RCap’s policy is to obtain possession of collateral with a market value in excess of the principal amount loaned under reverse repurchase agreements. To ensure that the market value of the underlying collateral remains sufficient, collateral is valued daily, and RCap requires counterparties to deposit additional collateral, when necessary. All reverse repurchase activities are transacted under master repurchase agreements that give RCap the right, in the event of default, to liquidate collateral held and in some instances, to offset receivables and payables with the same counterparty. Substantially all of RCap's repurchase and reverse repurchase activity is with affiliated entities.

Recent Accounting Pronouncements

The following table provides a brief description of recent accounting pronouncements that could potentially impact the Company’s consolidated financial statements:

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

Standard	Description	Date of Adoption	Effect on the financial statements or other significant matters
Standards that are not yet adopted			
ASU 2016-02 Leases (Topic 842)	The amendments require lessees to recognize a right-of-use asset and a liability to make lease payments in the statement of financial position for most leases. The accounting for lessors is largely unchanged.	January 1, 2019 (early adoption permitted)	Not expected to have a significant impact on the consolidated financial statements.
ASU 2016-01 Financial Instruments - Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities	The amendments address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments.	January 1, 2018 (early adoption permitted for a provision related presentation of instrument-specific credit risk of liabilities accounted for under the fair value option)	Expected to impact disclosures only and not have a significant impact on the consolidated finanical statements.
ASU 2014-15, Presentation of Financial Statements – Going Concern (Subtopic 205-04) Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern	This ASU requires management to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company’s ability to continue as a going concern within one year after the date the financial statements are issued.	January 1, 2017 (early adoption permitted)	Not expected to have an impact on the consolidated financial statements.
ASU 2014-09, Revenue from Contracts with Customers	This guidance applies to contracts with customers to transfer goods or services and contracts to transfer nonfinancial assets unless those contracts are within the scope of other standards (for example, lease transactions).	January 1, 2018	Not expected to have a significant impact on the consolidated financial statements.

Standard	Description	Date of Adoption	Effect on the financial statements or other significant matters

Standards that were adopted			
ASU 2015-16 Business Combinations (Topic 805) Simplifying the Accounting Measurement-Period Adjustments	This amendment removed the requirement to present adjustments to provisional amounts retrospectively. The update required that an acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to provisional amounts.	January 1, 2016 (early adoption permitted)	Did not have a significant impact on the consolidated financial statements.
ASU 2015-15, Interest - Imputation of Interest (Subtopic 835-30) Simplifying the Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting (SEC Update)	This amendment provided SEC guidance that it would not object to filers presenting debt issue costs related to line-of-credit arrangements as an asset and ratably amortizing the costs over the term of the arrangement.	June 18, 2015 (early adoption permitted)	Did not have an impact on the consolidated financial statements.
ASU 2015-10, Technical Corrections and Improvements	This perpetual project updated the codification for technical corrections and improvements.	January 1, 2016 (early adoption permitted), for amendments subject to transition guidance	Did not have a significant impact on the consolidated financial statements.
ASU 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)	This update removed the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient and also removes certain disclosure requirements for these investments.	January 1, 2016 (early adoption permitted)	Did not have an impact on the consolidated financial statements.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement	This update clarified that customers should determine whether a cloud computing arrangement includes the license of software by applying the same guidance cloud service providers use. The guidance also eliminated the current requirement that customers analogize to the leasing standard when determining the asset acquired in a software licensing arrangement.	January 1, 2016 (early adoption permitted)	Did not have a significant impact on the consolidated financial statements.
ASU 2015-03, Interest - Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs	This ASU required that debt issue costs are presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The recognition and measurement of debt issue costs were not affected.	January 1, 2016 (early adoption permitted)	Impacted presentation only and did not have a significant impact on the consolidated financial statements.
ASU 2015-02, Consolidation (Topic 810) Amendments to the Consolidation Analysis	This update affected the following areas of the consolidation analysis: limited partnerships and similar entities, evaluation of fees paid to a decision maker or service provider as a variable interest and in determination of the primary beneficiary, effect of related parties on the primary beneficiary determination and for certain investment funds.	January 1, 2016 (early adoption permitted)	Did not have a significant impact on the consolidated financial statements.
ASU 2015-01, Income Statement - Extraordinary and Unusual Items (Subtopic 225-20)	This update eliminated from GAAP the concept of extraordinary items.	January 1, 2016 (early adoption permitted)	Did not have an impact on the consolidated financial statements.
ASU 2014-16, Derivatives and Hedging (Topic 815) Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or Equity	This ASU provided additional guidance for evaluating whether conversion rights, redemption rights, voting rights, liquidation rights and dividend payment preferences and other features embedded in a share, including preferred stock, contain embedded derivatives requiring bifurcation. The update requires that an entity determine the nature of the host contract by considering all stated and implied terms and features in a hybrid instrument.	January 1, 2016 (early adoption permitted)	Did not have a significant impact on the consolidated financial statements.
ASU 2014-13, Consolidation (Topic 810) Measuring the Financial Assets and the Financial Liabilities of a Consolidated Collateralized Financing Entity	This update provided a practical expedient to measure the fair value of the financial assets and financial liabilities of a consolidated collateralized financing entity, which the reporting entity has	January 1, 2016 (early adoption permitted)	The Company adopted this ASU and applied the guidance to commercial mortgage backed securitization

	elected to or is required to measure on a fair value basis.		transactions. See "Commercial Real Estate Investments" footnote for further disclosure.
ASU 2014-11, Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosure	This update made limited amendments to the guidance in ASC 860 on accounting for certain repurchase agreements.	January 1, 2015	Impacted disclosures only and did not have a significant impact on the consolidated financial statements.
ASU 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity	This ASU raised the threshold for a disposal to be treated as discontinued operations.	April 1, 2015	Did not have a significant impact on the consolidated financial statements.
ASU 2014-04 Receivables–Troubled Debt Restructurings by Creditors, Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure	This update clarified that an in-substance repossession or foreclosure has occurred, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, when the creditor obtains legal title to the property upon completion of a foreclosure or the borrower conveys all interest in the property to the creditor through a deed in lieu of foreclosure or similar arrangement.	January 1, 2015	Did not have a significant impact on the consolidated financial statements.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

4. RESIDENTIAL INVESTMENT SECURITIES

The following tables present the Company's Residential Investment Securities portfolio carried at fair value as of March 31, 2016 and December 31, 2015:

	March 31, 2016						
	Principal / Notional	Remaining Premium	Remaining Discount	Amortized Cost	Unrealized Gains(1)	Unrealized Losses(1)	Estimated Fair Value
Agency	(dollars in thousands)						
Fixed-rate pass-through	$56,120,429	$3,093,155	$(2,392)	$59,211,192	$765,776	$(204,912)	$59,772,056
Adjustable-rate pass-through	3,064,341	68,241	(6,974)	3,125,608	70,485	(220)	3,195,873
CMO	922,196	24,962	(387)	946,771	16,943	(4,417)	959,297
Debentures	158,803	-	(638)	158,165	-	(1,130)	157,035
Interest-only	9,362,596	1,614,332	-	1,614,332	33,802	(135,536)	1,512,598
Total Agency investments	$69,628,365	$4,800,690	$(10,391)	$65,056,068	$887,006	$(346,215)	$65,596,859
Residential Credit							
CRT	$517,207	$1,586	$(14,763)	$504,030	$3,138	$(6,001)	$501,167
Legacy(2)	484,784	879	(52,182)	433,481	1,251	(4,306)	430,426
NPL/RPL	428,656	50	(1,579)	427,127	153	(941)	426,339
New issue	280,060	1,233	(1,446)	279,847	3,713	-	283,560
New issue interest-only	1,114,234	17,823	-	17,823	324	(965)	17,182
Total residential credit securities	$2,824,941	$21,571	$(69,970)	$1,662,308	$8,579	$(12,213)	$1,658,674
Total Residential Investment Securities	$72,453,306	$4,822,261	$(80,361)	$66,718,376	$895,585	$(358,428)	$67,255,533

	December 31, 2015						
	Principal / Notional	Remaining Premium	Remaining Discount	Amortized Cost	Unrealized Gains(1)	Unrealized Losses(1)	Estimated Fair Value
Agency	(dollars in thousands)						
Fixed-rate pass-through	$57,339,705	$3,270,521	$(2,832)	$60,607,394	$400,350	$(824,862)	$60,182,882
Adjustable-rate pass-through	2,894,192	61,781	(6,427)	2,949,546	70,849	(10,317)	3,010,078
CMO	964,095	27,269	(477)	990,887	9,137	(12,945)	987,079
Debentures	158,802	-	(648)	158,154	-	(6,116)	152,038
Interest-only	9,499,332	1,634,312	-	1,634,312	18,699	(114,826)	1,538,185
Total Agency investments	$70,856,126	$4,993,883	$(10,384)	$66,340,293	$499,035	$(969,066)	$65,870,262

Residential Credit							
CRT	$476,084	$2,225	$(12,840)	$465,469	$250	$(9,209)	$456,510
Legacy[2]	378,527	773	(37,150)	342,150	698	(1,140)	341,708
NPL/RPL	354,945	19	(1,270)	353,694	19	(1,172)	352,541
New issue	197,695	566	-	198,261	-	(1,060)	197,201
New issue interest-only	811,245	15,430	-	15,430	-	(158)	15,272
Total residential credit securities	$2,218,496	$19,013	$(51,260)	$1,375,004	$967	$(12,739)	$1,363,232
Total Residential Investment Securities	$73,074,622	$5,012,896	$(61,644)	$67,715,297	$500,002	$(981,805)	$67,233,494

(1) Unrealized gains and losses on Agency investments, excluding interest-only investments, are reported as a component of other comprehensive income (loss). Unrealized gains and losses on residential credit securities and Agency interest-only investments are generally reported in Net unrealized gains (losses) on financial instruments measured at fair value through earnings in the Consolidated Statements of Comprehensive Income (Loss).
(2) Legacy residential credit refers to securities whose underlying collateral was securitized prior to 2009.

The following tables present the Company's Agency mortgage-backed securities portfolio by issuing Agency concentration as of March 31, 2016 and December 31, 2015:

Investment Type	March 31, 2016	December 31, 2015
	(dollars in thousands)	
Fannie Mae	$41,990,479	$42,647,075
Freddie Mac	23,341,571	22,960,595
Ginnie Mae	107,774	110,554
Total	$65,439,824	$65,718,224

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Actual maturities of the Company's Residential Investment Securities portfolio are generally shorter than stated contractual maturities because actual maturities of the portfolio are affected by periodic payments and prepayments of principal on underlying mortgages. The
following table summarizes the Company's available-for-sale Residential Investment Securities as of March 31, 2016 and December 31, 2015, according to their estimated weighted average life classifications:

	March 31, 2016		December 31, 2015	
Weighted Average Life	Estimated Fair Value	Amortized Cost	Estimated Fair Value	Amortized Cost
	(dollars in thousands)			
Less than one year	$72,348	$73,220	$37,862	$37,850
Greater than one year through five years	46,745,799	46,268,066	20,278,111	20,066,435
Greater than five years through ten years	20,238,032	20,176,740	46,473,701	47,174,319
Greater than ten years	199,354	200,350	443,820	436,693
Total	$67,255,533	$66,718,376	$67,233,494	$67,715,297

The weighted average lives of the Agency mortgage-backed securities at March 31, 2016 and December 31, 2015 in the table above are based upon projected principal prepayment rates. The actual weighted average lives of the Agency mortgage-backed securities could be materially longer or shorter than projected.
The following table presents the gross unrealized losses and estimated fair value of the Company's Agency mortgage-backed securities by length of time that such securities have been in a continuous unrealized loss position at March 31, 2016 and December 31, 2015.

	March 31, 2016			December 31, 2015		
	Estimated Fair Value(1)	Gross Unrealized Losses(1)	Number of Securities(1)	Estimated Fair Value(1)	Gross Unrealized Losses(1)	Number of Securities(1)
	(dollars in thousands)					
Less than 12 Months	$2,633,437	$(7,176)	67	$20,072,072	$(164,259)	463
12 Months or More	20,732,579	(203,503)	188	21,705,764	(689,981)	189
Total	$23,366,016	$(210,679)	255	$41,777,836	$(854,240)	652

(1) Excludes interest-only mortgage-backed securities.

The decline in value of these securities is solely due to market conditions and not the quality of the assets. Substantially all of the Agency mortgage-backed securities are "AAA" rated or carry an implied "AAA" rating. The investments are not considered to be other-than-temporarily impaired because the Company currently has the ability and intent to hold the investments to maturity or for a period of time sufficient for a forecasted market price recovery up to or beyond the cost of the investments, and it is not more likely than not that the Company will be required to sell the investments before recovery of the amortized cost bases, which may be maturity. Also, the Company
is guaranteed payment of the principal amount of the securities by the respective issuing government agency.

During the quarter ended March 31, 2016, the Company disposed of $3.5 billion of Residential Investment Securities, resulting in a net realized loss of ($1.7) million.

During the quarter ended March 31, 2015, the Company disposed of $14.9 billion of Residential Investment Securities, resulting in a net realized gain of $62.3 million.

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5. COMMERCIAL REAL ESTATE INVESTMENTS

On December 11, 2015, the Company originated a $335.0 million recapitalization financing with respect to eight class A/B office properties in Orange County, California. As of March 31, 2016, such financing is comprised of a $280.0 million senior mortgage loan ($278.6 million, net of origination fees), and mezzanine loan with an initial principal balance of $55.0 million ($52.7 million, net of origination) and a future funding component of $30.0 million. The senior mortgage loan was held for sale as of March 31, 2016
and December 31, 2015. In April 2016, the Company sold $115.0 million of the senior loan to an unrelated third party at carrying value, accordingly, no gain or loss was recorded in connection with the sale. The balance of the senior loan of $165.0 million remains held for sale.

The following tables present commercial real estate investments held for investment at March 31, 2016 and December 31, 2015.

CRE Debt and Preferred Equity Investments

	March 31, 2016			December 31, 2015		
	Outstanding Principal	Carrying Value(1)	Percentage of Loan Portfolio(2)	Outstanding Principal	Carrying Value(1)	Percentage of Loan Portfolio(2)
	(dollars in thousands)					
Senior mortgages	$477,302	$474,559	40.3 %	$387,314	$385,838	28.6 %
Senior securitized mortgages(3)	212,072	211,855	17.9 %	263,072	262,703	19.4 %
Mezzanine loans	486,081	482,101	41.0 %	582,592	578,503	43.0 %
Preferred equity	9,000	8,953	0.8 %	122,444	121,773	9.0 %
Total (4)	$1,184,455	$1,177,468	100.0 %	$1,355,422	$1,348,817	100.0 %

(1) Carrying value includes unamortized origination fees of $7.1 million and $6.9 million as of March 31, 2016 and December 31, 2015, respectively.
(2) Based on outstanding principal.
(3) Assets of consolidated VIEs.
(4) Excludes Loans held for sale.

	March 31, 2016				
	Senior Mortgages	Senior Securitized Mortgages(1)	Mezzanine Loans	Preferred Equity	Total
	(dollars in thousands)				
Beginning balance	$385,838	$ 262,703	$578,503	$121,773	$1,348,817
Originations & advances (principal)	155,065	-	25,897	-	180,962
Principal payments	(65,077)	(51,000)	(122,408)	(113,445)	(351,930)
Sales (principal)	-	-	-	-	-
Amortization & accretion of (premium) discounts	(34)	-	(221)	-	(255)

Net (increase) decrease in origination fees	(1,578)	-	(285)	-	(1,863)
Amortization of net origination fees	345	152	615	625	1,737
Transfers	-	-	-	-	-
Allowance for loan losses	-	-	-	-	-
Net carrying value (2)	$474,559	$ 211,855	$482,101	$8,953	$1,177,468

(1) Assets of consolidated VIE.
(2) Excludes Loans held for sale.

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	December 31, 2015				
	Senior Mortgages	Senior Securitized Mortgages(1)	Mezzanine Loans	Preferred Equity	Total
	(dollars in thousands)				
Beginning balance	$383,895	$ 398,634	$522,731	$212,905	$1,518,165
Originations & advances (principal)	293,925	-	195,312	-	489,237
Principal payments	(243,270)	(136,469)	(153,693)	(92,210)	(625,642)
Sales (principal)	(46,945)	-	-	-	(46,945)
Amortization & accretion of (premium) discounts	(142)	-	(232)	517	143
Net (increase) decrease in origination fees	(3,702)	(279)	(4,806)	-	(8,787)
Amortization of net origination fees	2,077	817	691	561	4,146
Transfers	-	-	18,500	-	18,500
Allowance for loan losses	-	-	-	-	-
Net carrying value (2)	$385,838	$ 262,703	$578,503	$121,773	$1,348,817

(1) Assets of consolidated VIE.
(2) Excludes Loans held for sale.

Internal CRE Debt and Preferred Equity Investment Ratings

	March 31, 2016									
		Percentage of CRE Debt and Preferred Equity	Internal Ratings							
Investment Type	Outstanding Principal (1)	Portfolio	Performing	Closely-Monitored	Special Mention	Substandard	Doubtful	Loss	Total
	(dollars in thousands)								
Senior mortgages	$477,302	40.3 %	$91,321	$ 243,681	$142,300	$ -	$ -	$ -	$477,302
Senior securitized mortgages(2)	212,072	17.9 %	55,770	15,500	140,802	-	-	-	212,072
Mezzanine loans	486,081	41.0 %	295,950	160,814	29,317	-	-	-	486,081
Preferred equity	9,000	0.8 %	-	-	9,000	-	-	-	9,000
	$1,184,455	100.0 %	$443,041	$ 419,995	$321,419	$ -	$ -	$ -	$1,184,455

(1) Excludes Loans held for sale.
(2) Assets of consolidated VIE.

	December 31, 2015								
		Percentage of CRE Debt and Preferred Equity	Internal Ratings						
Investment Type	Outstanding Principal (1)	Portfolio	Performing	Closely-Monitored	Special Mention	Substandard	Doubtful	Loss	Total

	(dollars in thousands)								
Senior mortgages	$387,314	28.6 %	$71,000	$ 283,148	$33,166	$ -	$ -	$ -	$387,314
Senior securitized mortgages(2)	263,072	19.4 %	106,770	15,500	140,802	-	-	-	263,072
Mezzanine loans	582,592	43.0 %	342,493	219,969	20,130	-	-	-	582,592
Preferred equity	122,444	9.0 %	-	81,944	40,500	-	-	-	122,444
	$1,355,422	100.0 %	$520,263	$ 600,561	$234,598	$ -	$ -	$ -	$1,355,422

(1) Excludes Loans held for sale.
(2) Assets of consolidated VIE.

Real Estate Investments

There were no acquisitions of new real estate holdings during the quarter ended March 31, 2016.
The following table summarizes real estate held for investment as of March 31, 2016:

Date of Acquisition	Type	Location	Purchase Price	Remaining Lease Term (Years) (1)
(dollars in thousands)				
July 2015	Multi Tenant Retail	Ohio	$11,000	4.6
August 2015	Multi Tenant Retail	Florida	$18,900	5.1
October 2015	Multifamily Property	Washington, DC	$75,000	0.3
October 2015	Multi Tenant Retail	California	$37,750	3.0
November 2015	Multi Tenant Retail	Texas	$131,950	4.3

The weighted average amortization period for intangible assets and liabilities as of March 31, 2016 is 7.2 years. Above market leases and leasehold intangible assets are included in Intangible assets, net and below market leases are included in Accounts payable and other liabilities in the Consolidated Statements of Financial Condition.

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Investments in Commercial Real Estate

	March 31, 2016	December 31, 2015
	(dollars in thousands)	
Real estate held for investment, at amortized cost		
Land	$113,494	$113,494
Buildings and improvements	374,213	373,603
Subtotal	487,707	487,097
Less: accumulated depreciation	(21,456)	(16,886)
Total real estate held for investment, at amortized cost, net	466,251	470,211
Equity in unconsolidated joint ventures	61,535	65,735
Investments in commercial real estate, net	$527,786	$535,946

Depreciation expense was $4.6 million and $2.8 million for the quarters ended March 31, 2016 and 2015, respectively and is included in Other income (loss) in the Consolidated Statements of Comprehensive Income (Loss).

Rental Income
The minimum rental amounts due under leases are generally either subject to scheduled fixed increases or adjustments. The leases generally also require that the tenants reimburse us for certain operating costs. Approximate future minimum rents payments under non-cancelable operating leases in effect at March 31, 2016 for consolidated investments in real estate are as follows:

	March 31, 2016 (dollars in thousands)
2016 (remaining)	$ 26,105
2017	30,305
2018	26,238
2019	22,157
2020	17,848
Later years	53,326
	$ 175,979

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Mortgage loans payable as of March 31, 2016 and December 31, 2015, were as follows:

March 31, 2016

Property	Mortgage Carrying Value	Mortgage Principal	Interest Rate	Fixed/Floating Rate	Maturity Date	Priority
(dollars in thousands)						
Joint Ventures	$292,821	$296,325	2.30% to 4.61%	Floating (1)	2016 and 2025	First liens
Tennessee	12,236	12,350	4.01 %	Fixed	6/6/2019	First liens
Virginia	11,012	11,025	3.58 %	Fixed	9/6/2019	First liens
Arizona	16,271	16,227	3.50 %	Fixed	1/1/2017	First liens
Nevada	2,425	2,419	3.45 %	Floating (2)	3/29/2017	First liens
	$334,765	$338,346				

(1) Includes a mortgage with a fixed rate via an interest rate swap (pay fixed 4.31%, receive floating rate of L+215).
(2) Includes a mortgage with a fixed rate via an interest rate swap (pay fixed 3.45%, receive floating rate of L+200).

December 31, 2015

Property	Mortgage Carrying Value	Mortgage Principal	Interest Rate	Fixed/Floating Rate	Maturity Date	Priority
(dollars in thousands)						
Joint Ventures	$292,658	$296,325	2.30% to 4.61%	Floating (1)	2016 and 2025	First liens
Tennessee	12,228	12,350	4.01 %	Fixed	6/6/2019	First liens
Virginia	11,012	11,025	3.58 %	Fixed	9/6/2019	First liens
Arizona	16,365	16,308	3.50 %	Fixed	1/1/2017	First liens
Nevada	2,444	2,436	3.45 %	Floating (2)	3/29/2017	First liens
	$334,707	$338,444				

(1) Includes a mortgage with a fixed rate via an interest rate swap (pay fixed 4.31%, receive floating rate of L+215).
(2) Includes a mortgage with a fixed rate via an interest rate swap (pay fixed 3.45%, receive floating rate of L+200).

The following table details future mortgage loan principal payments as of March 31, 2016:

	Mortgage Loan Principal Payments (dollars in thousands)

2016 (remaining)	$ 7,502
2017	18,344
2018	-
2019	23,375
2020	-
Later years	289,125
	$ 338,346

VIEs

Securitization

In January 2014, the Company closed NLY Commercial Mortgage Trust 2014-FL1 (the "Trust"), a $399.5 million securitization financing transaction which provides permanent, non-recourse financing collateralized by floating-rate first mortgage debt investments originated or co-originated by the Company and is not subject to margin calls. A total of $260.7 million of investment grade bonds were issued by the Trust, representing an advance rate of 65.3% at a weighted average coupon of LIBOR plus 1.74% at closing. The Company used the proceeds to originate commercial real estate investments. The Company retained bonds rated below investment grade and the interest-only bond issued by the Trust, which are referred to as the subordinate bonds.

The Company incurred approximately $4.3 million of costs in connection with the securitization that have been capitalized and are being amortized to interest expense. Deferred financing costs are included in Securitized debt of consolidated VIEs in the accompanying Consolidated Statements of Financial Condition.

As of March 31, 2016 the carrying value of the Trust's assets was $211.9 million, net of $0.2 million of unamortized origination fees, which are included in Commercial real estate debt and preferred equity in the accompanying Consolidated Statements of Financial Condition. As of March 31, 2016, the carrying value of the Trust's liabilities was $125.6 million, net of $0.2 million of deferred financing costs, classified as Securitized debt of consolidated VIEs in the accompanying Consolidated Statements of Financial Condition.

In February 2015, the Company purchased the junior-most tranche, Class C Certificate of the Freddie Mac securitization, FREMF Mortgage Trust 2015-KLSF ("FREMF 2015-KLSF") for $102.1 million. The underlying portfolio is a pool of 11 floating rate multifamily mortgage loans with a cut-off principal balance of $1.4 billion. The Company was required to consolidate the FREMF 2015-KLSF Trust's assets and liabilities of $1.3 billion and $1.2 billion, respectively, at March 31, 2016.

In April 2015, the Company purchased the junior-most tranche, Class C Certificate of the Freddie Mac securitization, FREMF Mortgage Trust 2015-KF07 ("FREMF 2015-KF07") for $89.4 million. The underlying portfolio is a pool of 40 floating rate multifamily mortgage loans with a cut-off principal balance of $1.2 billion. The Company was required to consolidate the FREMF 2015-KF07 Trust's assets and liabilities of $1.1 billion and $1.0 billion, respectively, at March 31, 2016.

In February 2016, the Company purchased the junior-most tranche, Class C Certificate of the Freddie Mac securitization, FREM Mortgage Trust 2016-KLH1 ("FREM 2016-KLH1") for $107.6 million, net of a $4.4 million discount to face value of $112.0 million. The underlying portfolio is a pool of 28 floating rate multifamily mortgage loans with a cut-off principal balance of $1.5 billion. The Company was required to consolidate the FREM 2016-KLH1 Trust's assets and liabilities of $1.5 billion and $1.4 billion, respectively, at March 31, 2016. FREMF 2015-KLSF, FREMF 2015-KF07 and FREM 2016-KLH1 are collectively referred to herein as the FREMF Trusts.

The FREMF Trusts are structured as pass-through entities that receive principal and interest on the underlying collateral and distribute those payments to the certificate holders. The FREMF Trusts are VIEs and the Company is considered to be the primary beneficiary as a result of its ability to replace the special servicer without cause through its ownership of the Class C Certificates and its current designation as the directing certificate holder. The Company's exposure to the obligations of the VIEs is generally
limited to the Company's investment in the FREMF Trusts of $291.0 million. Assets of the FREMF Trusts may only be used to settle obligations of the FREMF Trusts. Creditors of the FREMF Trusts have no recourse to the general credit of the Company. The Company is not contractually required to provide and has not provided any form of financial support to the FREMF Trusts. No gain or loss was recognized upon initial consolidation of the FREMF Trusts, but $0.2 million and $0.8 million of related costs were expensed during the quarter ended March 31, 2016 and the year ended December 31, 2015, respectively. The FREMF Trusts' assets are included in Commercial real estate debt investments and the FREMF Trusts' liabilities are included in Securitized debt of consolidated VIEs in the accompanying Consolidated Statements of Financial Condition.

Upon consolidation, the Company elected the fair value option for the financial assets and liabilities of the FREMF Trusts in order to avoid an accounting mismatch, and to more accurately represent the economics of its interest in the entities. The fair value option requires that changes in fair value be reflected in the Company's Consolidated Statements of Comprehensive Income (Loss). The Company has adopted ASU 2014-13 and applied the practical expedient fair value measurement whereby the Company determines whether the fair value of the financial assets or financial liabilities is more observable as a basis for measuring the less observable financial instruments. The Company has determined that the fair value of the financial liabilities of the FREMF Trusts is more observable, since the prices for these liabilities are primarily available from third-party pricing services utilized for multifamily mortgage-backed securities, while the fair value of the individual assets of the trusts are inherently less capable of precise measurement given their illiquid nature and the limitations on available information related to these assets. Given that the Company's methodology for valuing the financial assets of the FREMF Trusts is an aggregate fair value derived from the fair value of the financial liabilities, the Company has determined that the fair value of each of the financial assets in their entirety should be classified in Level 2 of the fair value measurement hierarchy.

The statement of financial condition of the FREMF Trusts that is reflected in the Company's Consolidated Statements of Financial Condition at March 31, 2016 is as follows:

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	March 31, 2016 (dollars in thousands)
Assets	
Senior securitized commercial mortgages carried at fair value	$3,968,118
Accrued interest receivable	8,351
Total assets	$3,976,469
Liabilities	
Securitized debt (non-recourse) at fair value	$3,677,079
Accrued interest payable	4,311
Total liabilities	$3,681,390

The FREMF Trusts mortgage loans had an unpaid principal balance of $4.0 billion at March 31, 2016. As of March 31, 2016 there are no loans 90 days or more past due or on nonaccrual status. There is no gain or loss attributable to instrument-specific credit risk of the underlying loans or securitized debt securities as of March 31, 2016 based upon the
Company's process of monitoring events of default on the underlying mortgage loans.

The statement of comprehensive income (loss) of the FREMF Trusts that is reflected in the Company's Consolidated Statements of Comprehensive Income (Loss) for the quarter ended March 31, 2016 is as follows:

	For the Quarter Ended March 31, 2016 (dollars in thousands)
Net interest income:	
Interest income	$ 21,030
Interest expense	7,876
Net interest income	13,154
Other income (loss):	
Unrealized gain (loss) on financial instruments at fair value [1]	147
Guarantee fees and servicing costs	(5,297)
Other income (loss)	(5,150)
General and administration expenses	2
Net income	$ 8,002

(1) Included in Net unrealized gains (losses) on financial instruments measured at fair value through earnings.

The geographic concentrations of credit risk exceeding 5% of the total loan balances related to the FREMF Trusts as of March 31, 2016 are as follows:

Securitized Loans at Fair Value
Geographic Concentration of Credit Risk

Property Location	Principal Balance	% of Balance
	(dollars in thousands)	
Texas	$749,569	18.8 %
North Carolina	537,375	13.5 %
Maryland	499,495	12.5 %
Florida	456,663	11.4 %
Other	1,751,963	43.8 %
Total	$3,995,065	100.0 %

6. CORPORATE DEBT

The Company invests in corporate loans and corporate debt securities through the MML subsidiary. The industry and interest rate characteristics of the portfolio as of March 31, 2016 are as follows:

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	Industry Dispersion		
	Fixed Rate	Floating Rate	Total
	(dollars in thousands)		
Healthcare	$-	$173,896	$173,896
Security services	74,700	-	74,700
Technology	-	93,292	93,292
Business services	4,359	134,515	138,874
Agriculture and protein processing	-	41,576	41,576
Food & beverage	-	27,930	27,930
Mining & minerals	-	24,671	24,671
Consumer products	-	23,230	23,230
Manufacturing	-	7,477	7,477
Education services	-	21,168	21,168
Packaging	-	12,667	12,667
Total	$79,059	$560,422	$639,481

The table below reflects the Company's aggregate positions by their respective place in the capital structure of the borrowers as of March 31, 2016.

	March 31, 2016 (dollars in thousands)
First lien loans	$397,693
Second lien loans	162,729
Second lien notes	74,700
Subordinated notes	4,359
Total	$639,481

7. FAIR VALUE MEASUREMENTS

The Company follows fair value guidance in accordance with GAAP to account for its financial instruments. The fair value of a financial instrument is the amount 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.

GAAP requires classification of financial instruments into a three-level hierarchy based on the priority of the inputs to the valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument. Financial assets and liabilities recorded at fair value on the Consolidated Statements of Financial Condition or disclosed in the related notes are categorized based on the inputs to the valuation techniques as follows:
Level 1– inputs to the valuation methodology are quoted prices (unadjusted) for identical assets and liabilities in active markets.

Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 – inputs to the valuation methodology are unobservable and significant to overall fair value.

The Company designates its financial instruments as trading, available for sale or held to maturity depending upon the type of instrument and the Company's intent and ability to hold such instrument to maturity. Instruments classified as available for sale and trading are reported at fair value on a recurring basis.

The following is a description of the valuation methodologies used for instruments carried at fair value. These methodologies are applied to assets and liabilities across the three-level fair value hierarchy,

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with the observability of inputs determining the appropriate level.

Futures contracts are valued using quoted prices for identical instruments in active markets. Residential Investment Securities, interest rate swaps, swaptions and other derivatives are valued using quoted prices or internally estimated prices for similar assets using internal models. The Company incorporates common market pricing methods, including a spread measurement to the Treasury curve as well as underlying characteristics of the particular security including coupon, prepayment speeds, periodic and life caps, rate reset period and expected life of the security in its estimates of fair value. Management reviews and indirectly corroborates its estimates of the fair value derived using internal models by comparing its results to independent prices provided by dealers in the securities and/or third party pricing services. Certain liquid asset classes, such as Agency fixed-rate pass-throughs, may be priced using independent sources such as quoted prices for TBA securities.
The Residential Investment Securities, interest rate swap and swaption markets are considered to be active markets such that participants transact with sufficient frequency and volume to provide transparent pricing information on an ongoing basis. The liquidity of the Residential Investment Securities, interest rate swaps, swaptions, TBA derivatives and MBS options markets and the similarity of the Company's securities to those actively traded enable the Company to observe quoted prices in the market and utilize those prices as a basis for formulating fair value measurements. Consequently, the Company has classified Residential Investment Securities, interest rate swaps, swaptions, TBA derivatives and MBS options as Level 2 inputs in the fair value hierarchy. Additionally, as discussed in the "Commercial Real Estate Investments" footnote, Commercial real estate debt investments carried at fair value are classified as Level 2.

The following table presents the estimated fair values of financial instruments measured at fair value on a recurring basis.

	Level 1	Level 2	Level 3	Total
March 31, 2016	(dollars in thousands)			
Assets:				
Agency mortgage-backed securities	$-	65,439,824	$ -	$65,439,824
Agency debentures	-	157,035	-	157,035
Credit risk transfer securities	-	501,167	-	501,167
Non-Agency mortgage-backed securities	-	1,157,507	-	1,157,507
Commercial real estate debt investments	-	4,401,725	-	4,401,725
Interest rate swaps	-	93,312	-	93,312
Other derivatives	717	76,732	-	77,449
Total assets	$717	$71,827,302	$ -	$71,828,019
Liabilities:				
Securitized debt of consolidated VIEs	$-	3,677,079	$ -	$3,677,079
Interest rate swaps	-	2,782,961	-	2,782,961
Other derivatives	69,171	-	-	69,171
Total liabilities	$69,171	$6,460,040	$ -	$6,529,211

	Level 1	Level 2	Level 3	Total
December 31, 2015	(dollars in thousands)			
Assets:				
Agency mortgage-backed securities	$-	$65,718,224	$ -	$65,718,224

Agency debentures	-	152,038	-	152,038
Credit risk transfer securities	-	456,510	-	456,510
Non-Agency mortgage-backed securities	-	906,722	-	906,722
Commercial real estate debt investments	-	2,911,828	-	2,911,828
Interest rate swaps	-	19,642	-	19,642
Other derivatives	12,443	9,623	-	22,066
Total assets	$12,443	$70,174,587	$ -	$70,187,030
Liabilities:				
Securitized debt of consolidated VIEs	$-	$2,366,878	$ -	$2,366,878
Interest rate swaps	-	1,677,571	-	1,677,571
Other derivatives	32,778	17,185	-	49,963
Total liabilities	$32,778	$4,061,634	$ -	$4,094,412

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GAAP requires disclosure of fair value information about financial instruments, whether or not recognized in the financial statements, for which it is practical to estimate the value. In cases where quoted market prices are not available, fair values are based upon discounted cash flows using market yields, methodologies that incorporate market-based transactions or other valuation methodologies. Considerable judgment is necessary to interpret market data and develop estimated fair values. Accordingly, fair values are not necessarily indicative of the amount the Company would realize on disposition of the financial instruments. The use of different market assumptions or estimation methodologies could have a material effect on the estimated fair value amounts.

The carrying value of short-term instruments, including cash and cash equivalents, reverse repurchase agreements, repurchase agreements and other secured financing whose term is less than twelve months, generally approximates fair value due to the short-term nature of the instruments.

The estimated fair value of commercial real estate debt and preferred equity investments takes into consideration changes in credit spreads and interest rates from the date of origination or purchase to the reporting date. The fair value also reflects consideration of asset-specific maturity dates and other items that could have an impact on the fair value as of the reporting date.

Estimates of fair value of corporate debt require the use of judgments and inputs including, but not limited to, the enterprise value of the borrower (i.e., an estimate of the total fair value of the borrower's debt and equity), the nature and realizable value of any collateral, the borrower's ability to make payments when due and its earnings history. Management also considers factors that affect the macro and local economic markets in which the borrower operates.

The fair value of repurchase agreements with remaining maturities greater than one year or with embedded optionality are valued as structured notes, with term to maturity, LIBOR rates and the Treasury curve being primary determinants of estimated fair value.

The fair value of mortgages payable is calculated using the estimated yield of a new par loan to value the remaining terms in place. A par loan is created using the identical terms of the existing loan; however, the coupon is derived by using the original spread against the interpolated Treasury. The fair value of mortgages payable also reflects consideration of the value of the underlying collateral and changes in credit risk from the time the debt was originated.

The carrying value of participation sold is based on the loan's amortized cost. The fair value of participation sold is based on the fair value of the underlying related commercial loan.

The fair value of securitized debt of consolidated VIEs is determined using the average of external vendor pricing services.

The following table summarizes the estimated fair value for financial assets and liabilities as of March 31, 2016 and December 31, 2015.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements

		March 31, 2016		December 31, 2015	
	Level in Fair Value Hierarchy	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:		(dollars in thousands)			
Cash and cash equivalents	1	$2,416,136	$2,416,136	$1,769,258	$1,769,258
Agency mortgage-backed securities	2	65,439,824	65,439,824	65,718,224	65,718,224
Agency debentures	2	157,035	157,035	152,038	152,038
Credit risk transfer securities	2	501,167	501,167	456,510	456,510
Non-Agency mortgage-backed securities	2	1,157,507	1,157,507	906,722	906,722
Commercial real estate debt investments	2	4,401,725	4,401,725	2,911,828	2,911,828
Commercial real estate debt and preferred equity, held for investment	3	1,177,468	1,170,280	1,348,817	1,350,968
Loans held for sale	3	278,600	278,600	278,600	278,600
Corporate debt (1)	2	639,481	626,486	488,508	470,894
Interest rate swaps	2	93,312	93,312	19,642	19,642
Other derivatives	1,2	77,449	77,449	22,066	22,066
Financial liabilities:					
Repurchase agreements	1,2	$54,448,141	$54,562,824	$56,230,860	$56,361,623
Other secured financing	1,2	3,588,326	3,590,225	1,845,048	1,846,095
Securitized debt of consolidated VIEs	2	3,802,682	3,802,898	2,540,711	2,541,193
Participation sold	2	13,182	12,691	13,286	13,138
Mortgage payable	3	334,765	350,599	334,707	339,849
Interest rate swaps	2	2,782,961	2,782,961	1,677,571	1,677,571
Other derivatives	1,2	69,171	69,171	49,963	49,963

(1) Includes a held-to-maturity debt security carried at amortized cost of $74.7 million as of March 31, 2016 and December 31, 2015. The held-to-maturity debt security had a fair value of $66.8 million and $61.3 million as of March 31, 2016 and December 31, 2015, respectively.

8. SECURED FINANCING

The Company had outstanding $54.4 billion and $56.2 billion of repurchase agreements with weighted average borrowing rates of 1.87% and 1.83%, after giving effect to the Company's interest rate swaps used to hedge cost of funds, and weighted average
remaining maturities of 136 days and 151 days as of March 31, 2016 and December 31, 2015, respectively.

At March 31, 2016 and December 31, 2015, the repurchase agreements had the following remaining maturities, collateral types and weighted average rates:

March 31, 2016

	Repurchase Agreements by Collateral Type						
	Agency Mortgage-backed Securities	Debentures	CRTs	Non-Agency Mortgage-backed Securities	Commercial Loans	Total Repurchase Agreements	Weighted Average Rate
	(dollars in thousands)						
1 day	$8,050,000	$ -	$-	$ -	$ -	$8,050,000	0.62 %
2 to 29 days	12,466,595	-	54,656	320,677	-	12,841,928	0.75 %
30 to 59 days	4,663,011	-	59,313	156,354	-	4,878,678	0.82 %
60 to 89 days	9,118,832	-	-	146,165	-	9,264,997	0.96 %
90 to 119 days	4,270,155	-	-	-	-	4,270,155	0.95 %
Over 120 days(1)	14,954,590	-	-	-	187,793	15,142,383	1.46 %
Total	$53,523,183	$ -	$113,969	$ 623,196	$ 187,793	$54,448,141	0.99 %

December 31, 2015

	Repurchase Agreements by Collateral Type						
	Agency Mortgage-backed Securities	Debentures	CRTs	Non-Agency Mortgage-backed Securities	Commercial Loans	Total Repurchase Agreements	Weighted Average Rate
	(dollars in thousands)						
1 day	$-	$ -	$-	$ -	$ -	$-	0.00 %
2 to 29 days	20,123,464	-	83,664	260,359	-	20,467,487	0.69 %
30 to 59 days	7,898,646	-	59,189	65,374	-	8,023,209	0.74 %
60 to 89 days	4,046,593	-	-	78,833	-	4,125,426	0.74 %
90 to 119 days	4,846,580	-	-	-	-	4,846,580	0.60 %
Over 120 days(1)	18,557,715	-	-	31,015	179,428	18,768,158	1.33 %
Total	$55,472,998	$ -	$142,853	$			