

BIMINI CAPITAL MANAGEMENT, INC.  
Form 10-K  
March 31, 2009

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2008

Commission File Number: 001-32171

BIMINI CAPITAL MANAGEMENT, INC.

(Exact name of registrant as specified in its charter)

Maryland  
(State or other jurisdiction of  
incorporation or organization)

72-1571637  
(I.R.S. Employer  
Identification No.)

3305 Flamingo Drive, Vero Beach, FL 32963  
(Address of principal executive offices - Zip Code)

772-231-1400  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

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

Title of Each Class  
Class A Common Stock, \$0.001 par value

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

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated  
filer  Smaller Reporting Company

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

As of March 30, 2009, there were 26,941,606 shares of the Registrant's Class A Common Stock outstanding. The aggregate market value of the Class A Common Stock held by non-affiliates of the Registrant (24,406,309 shares) at June 30, 2008 was approximately \$6.6 million. The aggregate market value was calculated by using the last sale price of the Class A Common Stock as of that date. As of June 30, 2008, all of the Registrant's Class B Common Stock was held by affiliates of the Registrant. As of June 30, 2008, the aggregate market value of the Registrant's Class C Common Stock held by non-affiliates (319,388 shares) was \$319, which value is based on the initial purchase price of the Class C Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement for its 2009 Annual Meeting of Stockholders are incorporated by reference into Part III of this Annual Report on Form 10-K.

BIMINI CAPITAL MANAGEMENT, INC.

INDEX

PART I

ITEM 1. Business.	2
ITEM 1A. Risk Factors	18
ITEM 1B. Unresolved Staff Comments.	28
ITEM 2. Properties.	28
ITEM 3. Legal Proceedings.	28
ITEM 4. Submission of Matters to a Vote of Security Holders.	29

PART II

ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.	30
ITEM 6. Selected Financial Data.	32
ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.	33
ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk.	46
ITEM 8. Financial Statements and Supplementary Data.	47
ITEM 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.	83
ITEM 9A. Controls and Procedures.	83
ITEM 9A (T). Controls and Procedures.	83
ITEM 9B. Other Information.	83

PART III

ITEM 10. Directors, Executive Officers and Corporate Governance.	84
ITEM 11. Executive Compensation.	84
ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.	84
ITEM 13. Certain Relationships and Related Transactions, and Director Independence.	84
ITEM 14. Principal Accountant Fees and Services.	84

PART IV

ITEM 15. Exhibits, Financial Statement Schedules.	85
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## PART I

### ITEM 1. BUSINESS

#### Overview

Bimini Capital Management, Inc., a Maryland corporation (“Bimini Capital” and, collectively with its subsidiaries, the “Company,” “we” or “us”), is primarily in the business of investing in mortgage-backed securities. We are organized and operate as a real estate investment trust, or REIT, for federal income tax purposes, and our corporate structure includes a taxable REIT subsidiary (“TRS”). Bimini Capital’s website is located at <http://www.biminicapital.com>.

From November 3, 2005 to June 30, 2007 we operated a mortgage banking business through a taxable REIT subsidiary. This entity ceased originating mortgages through two of their production channels during the second quarter of 2007 and the third, the retail loan production channel, was sold. No mortgage loans were originated beyond June 30, 2007.

#### History

We were originally formed in September 2003 as Bimini Mortgage Management, Inc. (“Bimini Mortgage”) for the purpose of creating and managing a leveraged investment portfolio consisting of residential mortgage backed securities (“MBS”). Through November 2, 2005, we operated solely as a REIT.

- On November 3, 2005, Bimini Mortgage acquired Opteum Financial Services, LLC (“OFS”). This entity was renamed Orchid Island TRS, LLC (“OITRS”) effective July 3, 2007. Hereinafter, any historical mention, discussion or references to Opteum Financial Services, LLC or to OFS (such as in previously filed documents or Exhibits) now means Orchid Island TRS, LLC or “OITRS.” Upon closing of the transaction, OITRS became a wholly-owned taxable REIT subsidiary of the Company. Under the terms of the transaction, the Company issued 3.7 million shares of Class A Common Stock and 1.2 million shares of Class A Redeemable Preferred Stock to the former members of OITRS.
- On February 10, 2006, the Company changed its name to Opteum Inc. (“Opteum”). At the Company’s 2006 Annual Meeting of Stockholders, the shares of Class A Redeemable Preferred Stock issued to the former members of OITRS were converted into shares of the Company’s Class A Common Stock on a one-for-one basis following the approval of such conversion by the Company’s stockholders.
- On December 21, 2006, Bimini Capital sold to Citigroup Global Markets Realty Corp. (“Citigroup Realty”) a Class B non-voting limited liability company membership interest in OITRS, representing 7.5% of all of OITRS’s outstanding limited liability company membership interests, for \$4.1 million. In connection with the transaction, the Company also granted Citigroup Realty the option, exercisable on or before December 20, 2007, to acquire additional Class B non-voting limited liability company membership interests in OITRS representing 7.49% of all of OITRS’s outstanding limited liability company membership interests. This option was not exercised. On May 27, 2008, Bimini Capital repurchased the 7.5% interest for \$0.05 million.
- On April 18, 2007, the Board of Managers of OITRS, at the recommendation of the Board of Directors of the Company, approved the closure of OITRS’ wholesale and conduit mortgage loan origination channels in the second quarter of 2007. Also, during the second and third quarters of 2007, substantially all of the other operating assets of OITRS were sold and the proceeds were primarily used to repay secured indebtedness.

- On September 28, 2007, the Company changed its name to Bimini Capital Management, Inc.

## Structure

We have elected to be taxed as a real estate investment trust ("REIT") under Sections 856 and 859 of the Internal Revenue Code of 1986, as amended (the "Code"). Our qualification as a REIT depends upon our ability to meet, on an annual or in some cases quarterly basis, various complex requirements under the Internal Revenue Code relating to, among other things, the sources of our gross income, the composition and values of our assets, our distribution levels and the diversity of ownership of our shares. We have elected to treat OITRS as a taxable REIT subsidiary (TRS).

As used in this document, discussions related to "Bimini Capital," the parent company, the registrant, and the REIT qualifying activities or the general management of our portfolio of mortgage backed securities ("MBS") refer to "Bimini Capital Management, Inc." Further, discussions related to our taxable REIT subsidiary or non-REIT eligible assets refer to OITRS and its consolidated subsidiaries. Discussions relating to the "Company" refer to the consolidated entity (the combination of Bimini Capital and OITRS). The assets and activities that are not REIT eligible, such as mortgage origination, acquisition and servicing activities, were formerly conducted by OITRS and are now reported as discontinued operations.

## Description of Our Business

In general, under our current business strategy, we expect to maximize the operational and tax benefits provided by our REIT structure. We seek to generate net interest income from our portfolio of mortgage-backed securities, which is the difference between (1) the interest income we receive from mortgage-backed securities and (2) the interest we pay on the debt used to finance these investments, plus certain administrative expenses.

## Mortgage-Backed Securities Portfolio

### Investment Strategy

Our current investment strategy, which is subject to change at any time without notice to our stockholders, is to realize net interest income from our investment in mortgage-backed securities ("MBS"). Our MBS portfolio may consist of pass-through certificates, collateralized mortgage obligations (CMOs) and agency MBS derivatives.

Pass-through certificates are securities representing interests in pools of mortgage loans secured by residential real property in which payments of both interest and principal on the securities are generally made monthly. In effect, these securities pass through the monthly payments made by the individual borrowers on the mortgage loans that underlie the securities, net of fees paid to the issuer or guarantor of the securities. Pass-through certificates can be divided into various categories based on the characteristics of the underlying mortgages, such as the term or whether the interest rate is fixed or variable. The mortgage loans underlying pass-through certificates can generally be classified in the following categories:

- **Adjustable-Rate Mortgages.** Adjustable-Rate Mortgages, or ARMs, are mortgages for which the borrower pays an interest rate that varies over the term of the loan. The interest rate usually resets based on market interest rates, although the adjustment of such an interest rate may be subject to certain limitations. Traditionally, interest rates reset periodically. We refer to such ARMs as "traditional" ARMs. Since interest rates on ARMs fluctuate based on market conditions, ARMs tend to have interest rates that do not deviate from current market rates by a large amount. This in turn can mean that ARMs have less price sensitivity to interest rates. We classify ARMs as those

securities whose coupons reset within one year.

- **Fixed-Rate Mortgages.** Fixed-Rate mortgages allow each borrower to pay an interest rate that is constant throughout the term of the loan. Traditionally, most fixed-rate mortgages have an original term of 30 years. However, shorter terms (also referred to as final maturity dates) have become common in recent years. Because the interest rate on the loan never changes, even when market interest rates change, over time there can be a divergence between the interest rate on the loan and current market interest rates. This in turn can make a fixed-rate mortgage price sensitive to market fluctuations in interest rates. In general, the longer the remaining term on the mortgage loan, the greater the price sensitivity.
- **Hybrid Adjustable-Rate Mortgages.** Hybrid ARMs have a fixed-rate for the first few years of the loan, often three, five, or seven years, and thereafter reset periodically like traditional ARMs. Effectively, such mortgages are hybrids, combining the features of a pure fixed-rate mortgage and a "traditional" ARM. Hybrid ARMs have price sensitivity to interest rates similar to that of a fixed-rate mortgage during the period when the interest rate is fixed and similar to that of an ARM when the interest rate is in its periodic reset stage. However, even though hybrid ARMs usually have a short time period in which the interest rate is fixed, during such period the price sensitivity may be high.
- **Balloon Maturity Mortgages.** Balloon maturity mortgages are a type of fixed-rate mortgage where all or most of the principal amount is due at maturity, rather than paid in periodic equal installments, or amortized, over the life of the loan. These mortgages have a static interest rate for the life of the loan. However, the term of the loan is usually quite short, typically less than seven years. As the balloon maturity mortgage approaches its maturity date, the price sensitivity of the mortgage declines.

In addition to pass-through certificates, we may also invest in agency MBS derivatives. A mortgage derivative is a collateralized mortgage obligation ("CMO") class with leveraged exposure to prepayments on the underlying collateral. The coupon on the class can either be fixed or floating. Mortgage derivatives offer a wide range of duration, curve shape, and convexity exposures. Mortgage derivatives can generally be classified as follows:

- **Floater.** A floater is a CMO whose coupon periodically resets at a specified spread over a specified index, subject to a cap and a floor. Usually, floaters have low durations, low negative convexity, and reduced exposure to prepayment risks relative to the underlying collateral. In addition, they typically also have negative duration exposure to the short-end of the yield curve because of the floater cap. When short-term rates increase, the value of the floater decreases and vice-versa. In contrast, an inverse floater has a coupon with an inverse linear relationship to its index. Inverse floaters generally have longer durations, higher negative convexity, and higher exposure to prepayment risks relative to the underlying collateral.
- **Interest Only.** An interest only (IO) CMO is created by stripping the interest cash flows of the underlying mortgage collateral. An IO pays interest on a notional principal amount and has a coupon formula similar to that of a floater, with the exception that IOs don't receive principal payments. In contrast, an inverse IO (IIO) has a coupon with an inverse linear relationship to its index. IIOs typically have large positive short-end durations and large negative long-end durations. The value of an IIO typically falls if short-term rates move up, primarily due to a decline in the IIO's coupon as rates rise. The value of an IIO typically increases as long-term rates rise, primarily due to the accompanying decline in prepayments. IIOs usually benefit when the yield curve steepens and are hurt when the curve flattens.
- **Principal Only.** A principal only (PO) CMO is created by stripping the principal cash flows of the underlying mortgage collateral. Total payments to a PO are fixed – all that is uncertain is the timing of those payments. Because of this POs usually have high durations. Prepayments are desirable because the holder receives the money earlier; therefore, the value of a PO tends to rise with declining interest rates.

The following table shows the breakdown of mortgage loans underlying the mortgage backed securities portfolio as of December 31, 2008 and 2007:

(in thousands)

	December 31,			
	2008		2007	
	Carrying Value	% of Total	Carrying Value	% of Total
<b>Pass-Through Certificates:</b>				
Adjustable Rate Mortgages	\$ 70,632	41.0	\$ 177,608	25.7
Fixed Rate Mortgages	24,884	14.5	113,989	16.5
Hybrid ARMs	63,068	36.6	398,982	57.8
<b>Total Pass-Through Certificates</b>	<b>158,584</b>	<b>92.1</b>	<b>690,579</b>	<b>100.0</b>
<b>Mortgage Derivative Certificates:</b>				
Inverse IO MBS	13,524	7.9	-	-
<b>Totals</b>	<b>\$ 172,108</b>	<b>100.0</b>	<b>\$ 690,579</b>	<b>100.0</b>

As of December 31, 2008, 82.1% and 17.9% of our portfolio was issued by Fannie Mae and Freddie Mac, respectively. As of December 31, 2008, our portfolio had a weighted average coupon of 5.19%. The constant prepayment rate (CPR) for the portfolio, which reflects the annualized proportion of principal that was prepaid, was 5.76% for December 2008. The effective duration for the portfolio was 1.279 as of December 31, 2008. Duration measures the price sensitivity of a fixed income security to movements in interest rates. Effective duration captures both the movement in interest rates and the fact that the cash flows of a mortgage related security are altered when interest rates move.

In evaluating our MBS portfolio assets and their performance, we primarily evaluate the following critical factors:

- asset performance in differing interest rate environments,
  - duration of the particular MBS asset,
  - yield to maturity,
- potential for prepayment of principal, and
  - the market price of the investment.

We seek to minimize the effects on our income caused by prepayments on the mortgage loans underlying our securities at a rate materially different than anticipated. Toward that end, we have positioned our portfolio to include securities with prepayment characteristics that we expect to result in less interest rate sensitive and, therefore, more stable prepayments. We believe that MBS collateralized by the following types of loan pools achieves this goal.

- Borrowers with low loan balances have a lower economic incentive to refinance and have historically prepaid at lower rates than borrowers with larger loan balances. The reduced incentive to refinance has two parts: borrowers with low loan balances will have smaller interest savings because overall interest payments are smaller on their loans; and closing costs for refinancing, which are generally not proportionate to the size of a loan, make refinancing of smaller loans less attractive as it takes a longer period of time for the interest savings to cover the cost of refinancing.
- Mortgage loans backed by the U.S. Government or Government Sponsored Agencies where borrowers have slightly impaired credit histories or loan-to-value ratios greater than 80%. Borrowers with this profile have proportionately higher delinquency rates than typical Fannie Mae, Freddie Mac or Ginnie Mae borrowers, resulting in a higher than market interest rate because of the increased default and delinquency risk. Prepayment rates on these securities are lower than average because refinancing is more difficult for delinquent, recently delinquent or high LTV loans.
- Agency pools collateralized by loans against investment properties generally result in slower prepayments because borrowers financing investment properties are required to pay an upfront premium. Payment of this premium requires a larger rate movement for the borrower to achieve the same relative level of savings upon refinancing.

We have created a diversified portfolio to avoid undue geographic, loan originator, and other types of concentrations. By maintaining essentially all of our MBS portfolio in AAA rated, government or government-sponsored or chartered enterprises and government or federal agencies, which may include an implied guarantee of the federal government as to payment of principal and interest, management believes it can significantly reduce its exposure to losses from credit risk. Legislation may be proposed to change the relationship between certain agencies, such as Fannie Mae and the federal government. This may have the effect of reducing the actual or perceived credit quality of mortgage related securities issued by these agencies. As a result, such legislation could increase the risk of loss on investments in Fannie Mae and/or Freddie Mac MBS. The Company currently intends to continue to invest in such securities, even if such agencies' relationships with the federal government change.

#### Leverage Strategy

Our mortgage-backed securities portfolio is partially funded through borrowings in the repurchase market. In addition, we use leverage in an attempt to increase potential returns to our stockholders. However, the use of leverage may also have the effect of increasing losses when economic conditions are unfavorable. Under normal market conditions, we generally seek to borrow between eight and twelve times the amount of our equity, although our investment policies require no minimum or maximum leverage. For purposes of this calculation, we treat our trust



preferred securities as an equity capital equivalent. We use repurchase agreements to borrow against existing mortgage related securities and use the proceeds to acquire additional mortgage related securities.

When market conditions become severely disrupted, as they are currently, our leverage strategy will be affected. Under such conditions we may not leverage our portfolio to the point we would under more normal market conditions due to the inability to obtain sufficient financing, a desire to reduce the risk exposure of the portfolio, or both. Currently, the Company's access to financing has been limited by the lenders and our leverage has been reduced. To compensate, we may, and have, employed derivative mortgage backed securities to increase returns. Such securities are not financed.

We seek to structure the financing in such a way as to limit the effect of fluctuations in short-term rates on our interest rate spread. In general, our borrowings are short-term and we actively manage, on an aggregate basis, both the interest rate indices and interest rate adjustment periods of our borrowings against the interest rate indices and interest rate adjustment periods on our mortgage related securities in order to limit our liquidity and interest rate related risks.

We generally borrow at short-term rates from various lenders through various contractual agreements including repurchase agreements. Repurchase agreements are generally, but not always, short-term in nature. Under these repurchase agreements, we sell securities to a lender and agree to repurchase those securities in the future for a price that is higher than the original sales price. The difference between the sales price we receive and the repurchase price we pay represents interest paid to the lender. This is determined by reference to an interest rate index (such as the London Interbank Offered Rate or, LIBOR) plus an interest rate spread. Although structured as a sale and repurchase obligation, a repurchase agreement operates as a financing under which we effectively pledge our securities as collateral to secure a short-term loan equal in value to a specified percentage of the market value of the pledged collateral. While used as collateral, we retain beneficial ownership of the pledged collateral, including the right to distributions. At the maturity of a repurchase agreement, we are required to repay the loan and concurrently receive our pledged collateral from the lender or, with the consent of the lender, renew such agreement at the then prevailing financing rate. Our repurchase agreements may require us to pledge additional assets to the lender in the event the market value of the existing pledged collateral declines. At December 31, 2008, repurchase agreements outstanding totaled approximately \$148.7 million.

We have engaged AVM, L.P., a securities broker-dealer, to provide us with repurchase agreement trading, clearing and administrative services. AVM, L.P. acts as our agent and adviser in arranging for third parties to enter into repurchase agreements with us, executes and maintains records of our repurchase transactions and assists in managing the margin arrangements between us and our counterparties for each of our repurchase agreements.

#### Risk Management Approach

Our investment strategy exposes the Company to several types of risk. Interest Rate Risk Management

We believe the primary risk inherent in our portfolio investments is the effect of movements in interest rates. This risk arises because the effects of interest rate changes on our borrowings will not be perfectly correlated with the effects of interest rate changes on the income from, or value of, our portfolio investments. We therefore follow an interest rate risk management program designed to offset the potential adverse effects resulting from the rate adjustment limitations on our mortgage related securities. Under normal market conditions, the Company seeks to minimize differences between interest rate indices and interest rate adjustment periods of our adjustable-rate MBS and related borrowings by matching the terms of assets and related liabilities both as to maturity and to the underlying interest rate index used to calculate interest rate charges.

To the extent the Company has the flexibility to adjust borrowing terms, our interest rate risk management program encompasses a number of procedures, including the following:

- monitoring and adjusting, if necessary, the interest rate sensitivity of our mortgage related securities compared with the interest rate sensitivities of our borrowings.
- structuring our repurchase agreements that fund our purchases of adjustable-rate MBS to have varying maturities and interest rate adjustment periods in order to match the reset dates on our adjustable-rate MBS.
- actively managing, on an aggregate basis, the interest rate indices and interest rate adjustment periods of our mortgage related securities and comparing them to the interest rate indices and adjustment periods of our borrowings. Our liabilities under our repurchase agreements are all LIBOR based, and we select our adjustable-rate MBS to favor LIBOR indexes, among other considerations.

Through the use of these procedures, under normal market conditions, we attempt to reduce the risk of differences between interest rate adjustment periods of our adjustable-rate MBS and our related borrowings. However, no assurances can be given that our interest rate risk management strategies can successfully be implemented.

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We may from time to time use derivative financial instruments to hedge all or a portion of the interest rate risk associated with our borrowings. We may enter into swap or cap agreements, option, put or call agreements, futures contracts, forward rate agreements or similar financial instruments to hedge indebtedness that we may incur or plan to incur. These contracts would be intended to more closely match the effective maturity of, and the interest received on, our assets with the effective maturity of, and the interest owed on, its liabilities. We may also use derivative financial instruments in an attempt to protect our MBS portfolio against declines in the market value of our assets that result from general trends in debt markets. The inability to match closely the maturities and interest rates of our assets and liabilities or the inability to protect adequately against declines in the market value of our assets could result in losses. Derivative instruments will not be used for speculative purposes.

- Credit Risk Management

We invest in a limited universe of mortgage related securities, primarily, but not limited to, those issued by Fannie Mae, Freddie Mac and Ginnie Mae. Payment of principal and interest underlying securities issued by Ginnie Mae is guaranteed by the U.S. Government. Fannie Mae and Freddie Mac mortgage related securities are guaranteed as to payment of principal and interest by the respective entity issuing the security.

- Prepayment Risk Management

A key feature of most mortgage loans is the ability of the borrower to repay principal earlier than scheduled. This is called a prepayment. Prepayments arise primarily due to sale of the underlying property, refinancing, or foreclosure. Prepayments result in a return of principal to pass-through certificate holders. This may result in a lower or higher rate of return upon reinvestment of principal. This is generally referred to as prepayment uncertainty. If a security purchased at a premium prepays at a higher-than-expected rate, then the value of the premium would be eroded at a faster-than-expected rate. Similarly, if a discount mortgage prepays at a lower-than-expected rate, the amortization towards par would be accumulated at a slower-than-expected rate. The possibility of these undesirable effects is sometimes referred to as "prepayment risk."

In general, declining interest rates tend to increase prepayments, and rising interest rates tend to result in fewer prepayments. Like other fixed-income securities, when interest rates rise, the value of mortgage related securities generally declines. The rate of prepayments on underlying mortgages will affect the price and volatility of mortgage related securities and may shorten or extend the effective maturity of the security beyond what was anticipated at the time of purchase. If interest rates rise, our holdings of mortgage related securities may experience reduced returns if the borrowers of the underlying mortgages pay off their mortgages later than anticipated. This is generally referred to as "extension risk."

We seek to manage the risk of prepayments of the underlying mortgages by creating a diversified portfolio with a variety of prepayment characteristics.

- Capital Risk Management

Since all of the elements of risk that our investment strategy exposes the Company to have the potential to negatively affect the prices of our assets or the level of our earnings, they ultimately pose a risk to our capital. Under normal market conditions, and to the extent the Company has access to sufficient levels of funding, our primary means of protecting our capital is through the management of the amount of leverage we employ. When market conditions deteriorate and ready access to funding is not available, we obtain leverage through the assets we acquire. In such

instances the Company will acquire derivative MBS assets that have leverage imbedded in them through the structural features of the security. Examples would be interest only or inverse interest only securities. In an effort to determine the appropriate amount of leverage to employ, we focus on the characteristics of the securities we apply leverage to and to the aggregate characteristics of our portfolio. There are four primary characteristics of both our securities and our portfolio that we focus on. The characteristics are:

- effective duration,
  - convexity,
- expected return and
- the slope of the yield curve.

"Effective duration" measures the sensitivity of a security's price to movements in interest rates. "Convexity" measures the sensitivity of a security's effective duration to movements in interest rates. "Expected return" captures the market's assessment of the risk of a security. We generally assume markets are efficient with respect to the pricing of risk.

While these three risk components primarily address the price