# CAPSTEAD

### **Investor Presentation**

Information as of December 31, 2016

### Safe Harbor Statement -

#### **Private Securities Litigation Reform Act of 1995**



#### **Statement Concerning Forward-looking Statements**

This document contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, without limitation, any statement that may predict, forecast, indicate or imply future results, performance or achievements, and may contain the words "believe," "anticipate," "expect," "estimate," "intend," "will be," "will likely continue," "will likely result," or words or phrases of similar meaning. Forward-looking statements are based largely on the expectations of management and are subject to a number of risks and uncertainties including, but not limited to, the following:

- changes in general economic conditions;
- fluctuations in interest rates and levels of mortgage prepayments;
- the effectiveness of risk management strategies;
- the impact of differing levels of leverage employed;
- liquidity of secondary markets and credit markets;
- the availability of financing at reasonable levels and terms to support investing on a leveraged basis;
- the availability of new investment capital;
- the availability of suitable qualifying investments from both an investment return and regulatory perspective;
- changes in market conditions as a result of federal corporate and individual income tax reform, federal government fiscal

- and individual income tax reform, federal government fiscal challenges and Federal Reserve monetary policy, including policy regarding its holdings of Agency and U.S. Treasury Securities;
- deterioration in credit quality and ratings of existing or future issuances of Fannie Mae, Freddie Mac or Ginnie Mae securities;
- changes in legislation or regulation affecting Fannie Mae,
   Freddie Mac, Ginnie Mae and similar federal government agencies and related guarantees;
- changes in legislation or regulation affecting exemptions for mortgage REITs from regulation under the Investment Company Act of 1940;
- other changes in legislation or regulation affecting the mortgage and banking industries; and
- increases in costs and other general competitive factors.

In addition to the above considerations, actual results and liquidity are affected by other risks and uncertainties which could cause actual results to be significantly different from those expressed or implied by any forward-looking statements included herein. It is not possible to identify all of the risks, uncertainties and other factors that may affect future results. In light of these risks and uncertainties, the forward-looking events and circumstances discussed herein may not occur and actual results could differ materially from those anticipated or implied in the forward-looking statements. Forward-looking statements speak only as of the date the statement is made and the Company undertakes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Accordingly, readers of this document are cautioned not to place undue reliance on any forward-looking statements included herein.

## **Overview of Capstead Mortgage Corporation**



#### **Company Summary**

- Founded in 1985, Capstead is the oldest publicly-traded residential mortgage REIT.
- Our <u>sole</u> focus is on managing a leveraged portfolio of short-duration\* agency-guaranteed (i.e. Fannie Mae, Freddie
  Mac and Ginnie Mae) residential ARM securities that is appropriately hedged and can earn attractive risk-adjusted
  returns over the long term, with little, if any, credit risk.
- At December 31, 2016, our agency-guaranteed ARM securities portfolio stood at \$13.32 billion, supported by \$1.35 billion in long-term investment capital levered 9.02 times.

Proven Strategy of
Efficiently Managing
a Leveraged
Portfolio of
Short-Duration
Agency-Guaranteed
ARM Securities

- Our short-duration strategy differentiates us from our peers because the adjustable-rate mortgages underlying our portfolio reset to more current interest rates within a relatively short period of time:
  - allowing us to benefit from future recoveries in financing spreads that typically contract during periods of rising interest rates, and
  - resulting in smaller fluctuations in portfolio values from changes in interest rates compared to portfolios containing a significant amount of longer-duration ARM or fixed-rate mortgage securities.
- By virtue of being internally-managed and with our sole focus on agency-guaranteed securities, we are arguably the most efficient mortgage REIT in the industry.

Experienced
Management Team
Aligned with
Stockholders

- Our top three executive officers have a combined 75 years of mortgage finance industry experience.
- We are internally-managed with low operating costs and a strong focus on performance-based compensation.
- This structure greatly enhances the alignment of management interests with those of our stockholders.

Straight-forward
Investment
Strategy and
Transparent
Reporting

- This singular and straight-forward investment strategy, together with our use of cash flow hedge accounting allows for easily understood, transparent financial reporting, with limited use of non-GAAP financial measures.
- Additional transparency is evident by virtue of our internally-managed structure our compensation-related decisions and costs are fully disclosed and subject to annual say-on-pay approvals.
- We make every effort to provide additional analysis in our earnings reports, SEC filings and analyst presentations that tells our story in a complete and straight-forward fashion.

Duration is a measure of market price sensitivity to interest rate movements. A shorter duration generally indicates less interest rate risk.

## **Market Snapshot**

(dollars in thousands, except per share amounts)



Capstead's \$1.35 billion in long-term investment capital consists of \$1.05 billion of our common equity trading on the NYSE, \$199 million of our 7.50% Series E perpetual preferred capital also trading on the NYSE, and \$98 million in privately-placed unsecured borrowings maturing in 2035 and 2036.

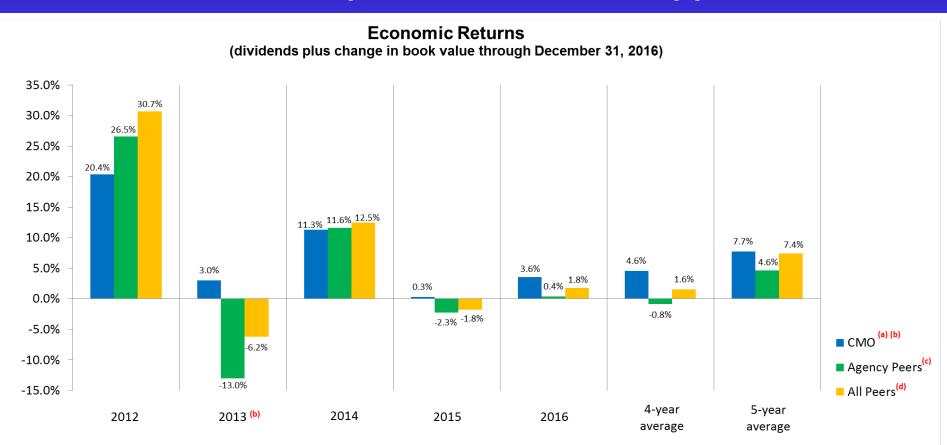
	Common	7.50% Series E Preferred	Long-Term Unsecured Borrowings	Total Long-Term Investment Capital
NYSE Stock Ticker	СМО	CMOPRE		
Shares outstanding <sup>(a)</sup>	95,989	8,234		
Cost of preferred capital		7.76%	7.77%	7.76%
Price as of March 6, 2017	\$10.55	\$24.33		
Book Value per common share <sup>(a)</sup>	\$10.85			
Price as a multiple of December 31, 2016 book value	97.2%			
Recorded value <sup>(a)</sup>	\$1,048,628	\$199,059	\$ 98,090	\$1,345,777
Market capitalization as of March 6, 2017	\$1,012,684	\$200,333	\$ 98,090	\$1,311,107

(a) As of December 31, 2016.

## **Capstead's Economic Returns**



Our agency-only, short-duration ARM strategy typically leads to outperformance during periods of rising interest rates and/or worsening credit conditions relative to other mortgage REITs.



<sup>(</sup>a) CMO economic returns exclude the effect of \$(0.03) per share in separation of service charges associated with the July 2016 resignation of the Company's former chief executive officer. Including this unusual charge, our economic returns would have been lower by 26 basis points in 2016, and by 7 and 5 basis points for the 4- and 5-year averages, respectively.

<sup>(</sup>b) Excludes \$(0.28) per share one-time effect of preferred capital redemption and issuance transactions on book value in 2013. Including this unusual charge, our economic returns would have been lower by 52 and 41 basis points for the 4- and 5-year averages, respectively.

<sup>(</sup>c) Agency Peers: AGNC, AI, ANH, ARR, CYS, EARN, HTS, NLY, ORC.

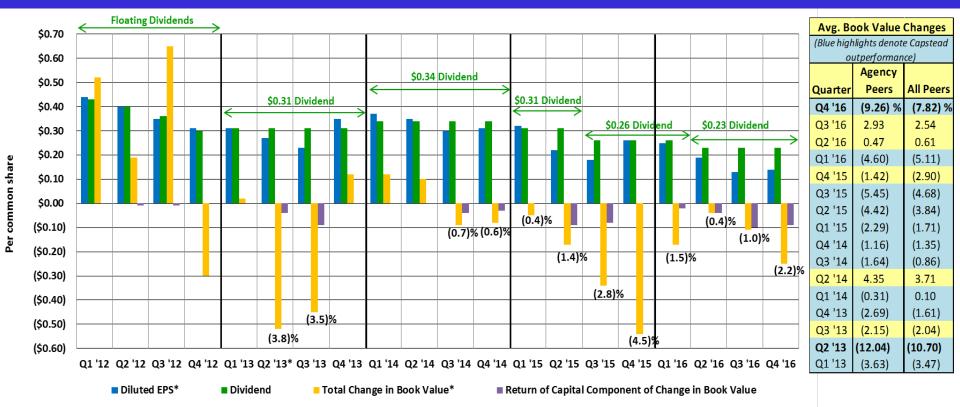
<sup>(</sup>d) All Peers: Agency peers plus AMTG, CIM, DX, IVR, JMI, MFA, MITT, MTGE, NYMT, OAKS, RWT, TWO, WMC.

# Components of our Economic Returns Quarterly Earnings, Dividends and Changes in Book Value



Our quarterly earnings are affected by the impact of changes in interest rates on mortgage refinancing activity and our borrowing costs. Quarterly earnings can also fluctuate with seasonal factors, most notably higher mortgage prepayment levels typically experienced during the summer house-selling season. We reassess the common dividend periodically based largely on how these factors are impacting expected future earnings.

Our book value per common share is directly impacted by changes in interest rates and other market conditions as our portfolio and our hedge instruments are marked-to-market through stockholders' equity. Book value has also been impacted to the extent common dividends exceeded earnings resulting in returns of capital to our stockholders.

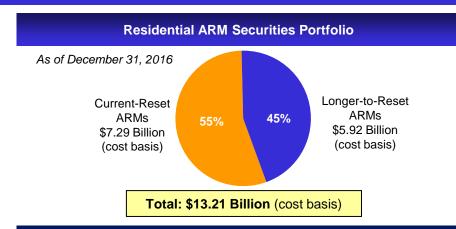


For presentation purposes, we adjusted our Q2 2013 diluted EPS and related change in book value to exclude certain one-time effects of preferred capital redemption and issuance transactions totaling \$(0.23) and \$(0.28), respectively. These transactions replaced higher-cost preferred equity to the benefit of future earnings. See page 19 for further information and a reconciliation of diluted EPS to this presentation.

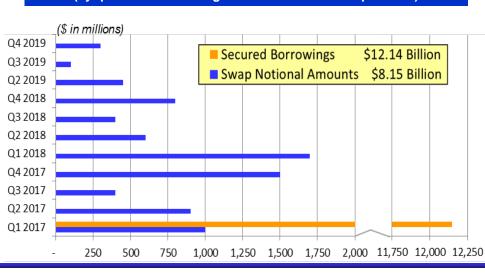
## Capstead's Proven Short-Duration Investment Strategy



We finance our agency-guaranteed residential ARM securities primarily with 30- to 90-day repurchase arrangements augmented with relatively low-cost two- and three-year interest rate swap agreements and longer-dated secured borrowings when available at attractive levels.



Secured Borrowings & Swap Notional Amounts (by quarter of borrowing maturities / contract expirations)



- Our portfolio of agency-guaranteed ARM securities have little, if any, credit risk and are either currently resetting to more current rates at least annually or will begin doing so in five years or less. Our Current-Reset ARMs reset in rate in less than 18 months and our Longer-to-Reset ARMs reset in less than five years.
- With an asset duration\* of approximately 11½ months at yearend, the value of our portfolio is naturally less exposed to changes in interest rates than portfolios containing longer duration ARM or fixed-rate securities. This relative stability affords us more flexibility in managing through periods of market stress.
- We have long-term relationships with a variety of domestic and foreign lending counterparties. At year-end we had borrowings outstanding with 21 counterparties.
- We routinely borrow for 30 to 90 days and extend the duration of our borrowings using relatively low-cost two- and three-year payfixed interest rate swap agreements. When available at attractive levels, we may also enter into longer-dated secured borrowings.
- Together with our portfolio-related swap agreements, our secured borrowings had a duration of approximately 8½ months at year-end, resulting in a net duration gap of approximately 3 months.

<sup>\*</sup> Duration is a common measure of market price sensitivity to interest rate movements. A shorter duration generally indicates less interest rate risk.

## Capstead's Appropriate Use of Leverage



In our view, borrowing at current levels represents an appropriate use of leverage for a short-duration, agency-guaranteed ARM securities portfolio in today's market conditions.



## **Financing Spread Analysis**

As of December 31, 2016 (unaudited)



Cash yields continue to benefit from higher coupon interest rates as mortgage loans underlying our current-reset ARM securities reset to higher rates primarily due to increases in the underlying indices (principally 12-month LIBOR, six-month LIBOR and one-year CMT).

Mortgage prepayment levels directly impact our financing spreads because purchased investment premiums are amortized to earnings as portfolio yield adjustments. Mortgage prepayments are influenced by housing market conditions, including prevailing mortgage interest rates, as well as seasonal factors, in particular the summer home selling season. We experienced refinancing waves in both 2016 and 2015.

Unhedged borrowing have trended higher largely because of market expectations for higher short-term interest rates culminating with the Federal Reserve's December 2016 and 2015 quarter point increases in the Federal Funds Rate. Hedged borrowing rates have generally trended higher as older, lower-rate swaps were replaced at higher rates, although beginning in the third quarter of 2016, these rates benefited from higher variable-rate receipts due to higher LIBOR rates.

		20	016		2015				
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1	
Total financing spreads: (a)	•	•			•	•	•		
Yields on all interest-earning assets	1.49%	1.45%	1.53%	1.69%	1.62%	1.40%	1.42%	1.66%	
Borrowing rates on all interest-paying liabilities	0.94	0.89	0.89	0.87	0.79	0.74	0.68	0.65	
Total financing spreads	0.55	0.56	0.64	0.82	0.83	0.66	0.74	1.01	
Financing spreads on residential mortgage investments, a non-GAAP financial measure:									
<b>Cash yields</b> on residential mortgage investments <sup>(b)</sup>	2.55%	2.52%	2.50%	2.47%	2.44%	2.42%	2.41%	2.42%	
Investment premium amortization (b)	(1.05)	(1.06)	(0.96)	(0.75)	(0.81)	(0.99)	(0.95)	(0.72)	
Yields on residential mortgage investments	1.50	1.46	1.54	1.72	1.63	1.43	1.46	1.70	
Unhedged secured borrowing rates (c)	0.79	0.69	0.67	0.65	0.48	0.45	0.41	0.38	
Hedged secured borrowing rates (c)	0.95	0.93	0.96	0.93	0.87	0.84	0.77	0.75	
Secured borrowing rates	0.89	0.84	0.84	0.82	0.73	0.69	0.62	0.59	
Financing spreads on residential									
mortgage investments	0.61	0.62	0.70	0.90	0.90	0.74	0.84	1.11	
CPR	25.59	25.80	23.19	18.23	19.62	23.21	21.98	16.66	

<sup>(</sup>a) All interest-earning assets include residential mortgage investments, overnight investments and cash collateral receivable from interest rate swap counterparties. All interest-paying liabilities include unsecured borrowings and cash collateral payable to interest rate swap counterparties.

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<sup>(</sup>b) Cash yields are based on the cash component of interest income. Investment premium amortization is determined using the interest method which incorporates actual and anticipated future mortgage prepayments. Both are expressed as a percentage calculated on average amortized cost basis for the indicated periods.

<sup>(</sup>c) Unhedged borrowing rates represent average rates on secured borrowings, before consideration of interest rate swap agreements held for portfolio hedging purposes. Hedged borrowing rates represent the average fixed-rate payments made on these swaps adjusted for differences between LIBOR-based variable-rate payments received and unhedged borrowing rates, as well as the effects of any hedge ineffectiveness. Average fixed-rate swap payments were 0.80%, 0.75%, 0.73% and 0.69% for the fourth, third, second and first quarters of 2016, respectively, while average variable-rate payment adjustments were 0.15%, 0.18%, 0.23% and 0.24% for the same periods, respectively. During 2016 and 2015, fixed-rate swap payments averaged 0.74% and 0.57% while variable-rate payment adjustments averaged 0.20% and 0.24%, respectively.

## **Changes in Interest Rates Affecting Capstead's Earnings**



The ten-year Treasury rate can be viewed as a proxy for mortgage interest rates. After declining this spring and summer, the ten-year rate has increased significantly, particularly post-election. One-month LIBOR also has increased due to money market reform and anticipation of Federal Reserve actions to increase the Federal Funds Rate.

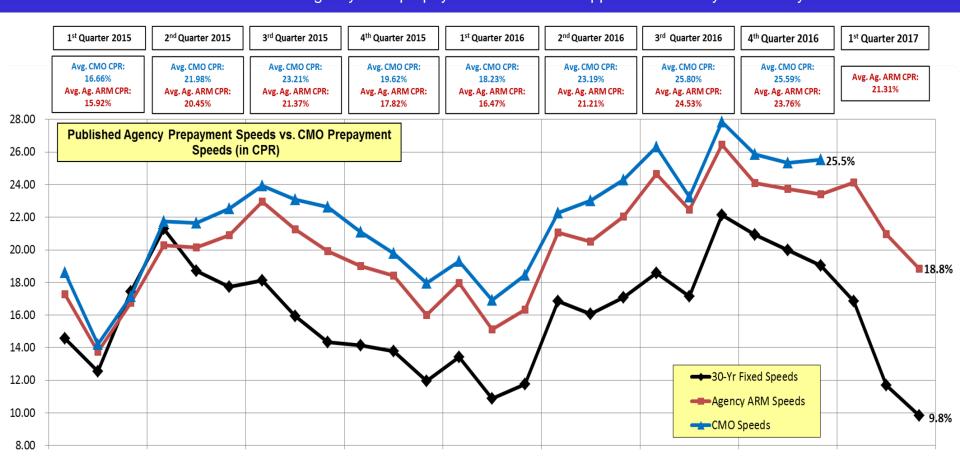
The primary indices underlying our residential ARM securities portfolio began increasing in 2015, in large part due to market expectations for Federal Reserve action to increase the Federal Funds Rate. Additionally, six- and 12-month LIBOR increased considerably during the latter part of 2016 in response to money market reform. All three indices have continued increasing post year-end (indices presented through March 6, 2017).



# Agency Mortgage Prepayment Speeds versus Capstead Prepayment Speeds



Similar to what occurred in 2015, Capstead experienced high prepayment levels during the summer months of 2016 reflecting declines in prevailing interest rates and seasonal factors. While the 2016 refinancing wave peaked in September, declines in prepayment rates on ARM securities lagged declines in prepayment rates on fixed-rate mortgage securities during the fourth quarter and in January 2017. However, with the sharp increase in interest rates post-election, opportunities for homeowners to refinance at lower rates have diminished and Agency ARM prepayment rates have dropped considerably in February and March.



## **Key Elements of Capstead's ARM Portfolio**

As of December 31, 2016 (dollars in thousands, unaudited)



The 2016 year-end Net WAC\* on our current-reset ARMs was 25 basis points higher than at year-end 2015. These securities' Fully-Indexed WAC\* was 38 basis points higher. This is primarily the result of increases in the underlying indices. These indices have increased further since year-end. With these higher rates, ARM loans underlying the current-reset component of our portfolio can be expected to continue increasing in coupon in the coming quarters.

	Principal	In	vestment	Amortized C	ost Basis	F	air Market	Net		Fully- Indexed	Average Net	Months to
	Balance	P	remiums	(\$)	%		Value	WAC*		WAC*	Margins	Roll
Current-reset ARMs:												
Fannie Mae Agency Securities	\$ 3,867,294	\$	114,375	\$ 3,981,669	102.96	\$	4,074,538	2.77%		3.13%	1.70%	5.8
Freddie Mac Agency Securities	1,538,730		49,879	1,588,609	103.24		1,626,167	2.84		3.31	1.81	6.9
Ginnie Mae Agency Securities	1,662,262		55,573	1,717,835	103.34		1,722,965	2.25		2.38	1.51	6.6
Residential Mortgage Loans	1,839		9	1,848	100.49		1,874	3.80		3.10	2.08	4.9
(55% of total)	7,070,125		219,836	7,289,961	103.11		7,425,544	2.66	+0.33	2.99	1.68	6.2
						Ye	ear-end 2015	2.41	+0.20	2.61		
Longer-to-reset ARMs:												
Fannie Mae Agency Securities	2,594,168		84,060	2,678,228	103.24		2,667,048	2.67		3.31	1.62	42.7
Freddie Mac Agency Securities	2,057,569		66,485	2,124,054	103.23		2,115,614	2.71		3.34	1.66	43.2
Ginnie Mae Agency Securities	1,080,898		34,727	1,115,625	103.21		1,105,323	2.92		2.36	1.51	38.9
(45% of total)	5,732,635		185,272	5,917,907	103.23		5,887,985	2.73	+0.41	3.14	1.61	42.2
						Ye	ear-end 2015	2.77	- 0.13	2.64		
<u>.</u>	\$ 12,802,760	\$	405,108	\$ 13,207,868	103.16	<u>\$</u>	13,313,529	2.69	+0.37	3.06	1.65	22.3
						Ye	ear-end 2015	2.57	+0.05	2.62		

Gross WAC (rate paid by borrowers)\* 3.29

<sup>\*</sup> Net WAC, or weighted average coupon, is the weighted average interest rate of the mortgage loans underlying the indicated investments, net of servicing and other fees, as of December 31, 2016. Net WAC is expressed as a percentage calculated on an annualized basis on the unpaid principal balances of the mortgage loans underlying these investments. As such it is similar to cash yield on the portfolio which is calculated using amortized cost basis. Fully indexed WAC represents the weighted average coupon upon one or more resets using interest rate indexes and net margins in effect, as of December 31, 2016. Gross WAC is the weighted average interest rate of the mortgage loans underlying the indicated investments, including servicing and other fees paid by borrowers, as of December 31, 2016.

## Capstead's Stockholder Friendly Structure



Capstead is a leader among our mortgage REIT peers in terms of operating cost efficiency.

We are internally-managed with low operating costs compared to our mortgage REIT peers.

Our executives' pay structure is variable through compensation elements that focus on "pay for performance" as opposed to fees paid to an external manager that are based solely on capital under management. Additionally, our board of directors and our senior executives hold a significant amount of Capstead stock.

As a result, we are incented to grow the Company by raising capital only when it is accretive to book value and earnings rather than for the purpose of increasing compensation or external management fees. Conversely, we are also not conflicted regarding whether or not to repurchase shares when appropriate.

	Quarter Ended Dec. 31, 2016 <sup>(a)</sup>	Year Ended Dec. 31, 2016 <sup>(a)</sup>	
Compensation-related expenses:			
Fixed:			
Salaries and related savings plan matching,			
payroll taxes, insurance and other benefits	0.25%	0.26%	
Variable:			
Short-term incentive compensation:			
Performance-based cash compensation program	0.31	0.20	
Dividend equivalent rights	0.03	0.04	The majority of compensation-related
Long-term incentive compensation, principally			expenses are performance-based.
performance-based equity awards	0.03	0.11	опропосовно реполивное жасов.
Related savings plan matching and payroll taxes	0.03	0.02	
	0.40	0.37	
	0.65	0.63	
Other platform expenses	0.32	0.34	
	0.97%	0.97%	

<sup>(</sup>a) Expressed on an annualized basis as a percentage of average long-term investment capital, excluding the effects of third and fourth quarter separation of service charges of \$2.7 million and \$225,000, respectively, associated with the July resignation of the Company's former chief executive officer.

# CAPSTEAD

**Appendix** 

## Capstead's Fourth Quarter 2016 Highlights



- Generated earnings of \$17.5 million or \$0.14 per diluted common share
- Paid common dividend of \$0.23 per common share
- Book value decreased by 1.4% (\$0.16) due to changes in unrealized gains and losses on the portfolio and interest rate swaps held for hedging purposes, and by 0.8% (\$0.09) due to capital returned to stockholders in the form of dividends in excess of reported earnings, ending the quarter at \$10.85 per common share
- Yields on residential mortgage investments increased four basis points to 1.50% while rates on related secured borrowings increased by five basis points to 0.89%
- Total financing spreads decreased one basis point to 0.55% while financing spreads on residential mortgage investments, a non-GAAP financial measure, also decreased one basis point to 0.61%
- Agency-guaranteed residential ARM portfolio and related leverage ended the quarter at \$13.32 billion and 9.02 times long-term investment capital, respectively
- Management remarks from our January 25, 2017 earnings press release:

"Earnings for the fourth quarter were hampered by slower than anticipated declines in mortgage prepayment levels. As a result, portfolio yields did not improve as much as expected. While the 2016 refinancing wave peaked in September, declines in prepayment rates on ARM securities have lagged declines in prepayment rates on fixed-rate mortgage securities during the fourth quarter and in January 2017. However, with the sharp increase in interest rates post-election, opportunities for homeowners to refinance at lower rates have diminished considerably. This is expected to lead to lower mortgage prepayment levels in the coming months, benefiting portfolio yields and earnings.

"Additionally, we expect cash yields to continue increasing in 2017 as coupon interest rates on mortgage loans underlying our portfolio reset to higher rates based on higher prevailing six- and 12-month interest rate indices. Our borrowing costs are also currently benefiting from higher variable rate swap receipts due to higher short-term LIBOR rates relative to our unhedged borrowing rates. However, future actions by the Federal Reserve to increase the level of short-term interest rates will put upward pressure on unhedged borrowing rates and fixed-rate swap payment requirements on new swap agreements. Provided the Federal Reserve does not move to increase short-term interest rates at a considerably faster pace than the financial markets currently anticipate, and longer term interest rates remain benign, we anticipate reporting improved earnings in the coming quarters.

"During the fourth quarter of 2016, longer-term interest rates moved significantly higher, as illustrated by the ten-year Treasury rate increasing 85 basis points to end the year at 2.45%. As a consequence, longer duration mortgage-backed securities lost considerable value. For instance, Fannie Mae 30-year fixed 3.0% mortgage securities declined in price by approximately 4.75% during this period. In contrast, Capstead's ARM securities portfolio performed relatively well, experiencing a decline in overall portfolio pricing of just 0.49%.

"This translated into a fourth quarter book value decline of only 1.4% due to changes in unrealized gains and losses on the portfolio and interest rate swaps held for hedging purposes. As a result, our fourth quarter economic return (change in book value plus dividends) is expected to significantly outpace the performance of our mortgage REIT peers holding longer duration portfolios that will be reporting in the coming weeks.

"We remain confident in our strategy of cost-effectively managing a leveraged portfolio of agency-guaranteed residential ARM securities that can produce attractive risk-adjusted returns over the long term while reducing, but not eliminating, sensitivity to changes in interest rates."

## **Capstead's Quarterly Income Statements**



(dollars in thousands, except per share amounts, unaudited)

	Quarter Ended									
	December 2016		September 2016			June 2016	March 2016		December 2015	
Interest income:										
Residential mortgage investments	\$	50,040	\$	49,845	\$	53,309	\$	59,500	\$	57,518
Other		143		174		128		192		60
		50,183		50,019		53,437		59,692		57,578
Interest expense:										
Secured borrowings		(27,421)		(26,636)		(27,014)		(26,582)		(23,937)
Unsecured borrowings	-	(1,910)		(1,970)		(1,976)		(1,977)		(2,087)
		(29,331)		(28,606)		(28,990)		(28,559)		(26,024)
		20,852		21,413		24,447		31,133	-	31,554
Other revenue (expense):										
Compensation-related expense		(2,219)		(1,299)		(2,042)		(3,224)		(2,627)
Separation of service charge		(225)		(2,740)		-		-		-
Other general and administrative expense		(1,117)		(1,239)		(1,157)		(1,169)		(1,170)
Miscellaneous other revenue		159		305		382		613		600
	-	(3,402)	-	(4,973)		(2,817)		(3,780)		(3,197)
Net income	\$	17,450	\$	16,440	\$	21,630	\$	27,353	\$	28,357
Net income available to common stockholders:										
Net income	\$	17,450	\$	16,440	\$	21,630	\$	27,353	\$	28,357
Less preferred stock dividends		(3,857)		(3,846)	_	(3,843)		(3,826)	_	(3,821)
	\$	13,593	\$	12,594	\$	17,787	\$	23,527	\$	24,536
Net income per diluted common share		\$0.14		\$0.13		\$0.19		\$0.25		\$0.26
Average long-term investment capital	\$	1,369,928	\$	1,380,006	\$	1,388,476	\$	1,398,043	\$	1,431,338
Average balance of mortgage assets		13,320,407		13,629,220		13,837,817		13,848,718		14,115,691
Investment premium amortization		34,945		36,076		33,052		26,011		28,732
Average constant prepayment rate, or CPR		25.59%		25.80%		23.19%		18.23%		19.62%
Average total financing spreads		0.55		0.56		0.64		0.82		0.83
Average financing spreads on residential mortgage investments <sup>(a)</sup>		0.61		0.62		0.70		0.90		0.90

# Capstead's Annual Income Statements – Five Years Ended 2016



(dollars in thousands, except per share amounts, unaudited)

					,	Year Ended				
		December December			December	December		I	December	
		2016		2015		2014		2013		2012
Interest income:										
Residential mortgage investments	\$	212,694	\$	215,989	\$	226,749	\$	215,137	\$	255,931
Other		637		341		315		322		698
		213,331		216,330		227,064		215,459		256,629
Interest expense:		(407.050)		(05.504)		(05.455)		(00.000)		(00.404)
Secured borrowings		(107,653)		(85,521)		(65,155)		(66,368)		(69,101)
Unsecured borrowings		(7,833)		(8,454)		(8,488) (73,643)		(8,736) (75,104)		(8,747)
		(115,486) 97,845	-	(93,975) 122,355		153,421		140,355	-	(77,848) 178,781
		,		<u>,                                     </u>		,		· · · · · · · · · · · · · · · · · · ·		,
Other revenue (expense):						4		4		
Compensation-related expense		(8,784)		(10,200)		(8,302)		(9,341)		(10,972)
Separation of service charge		(2,965)		- (4.700)		- (4.157)		- (4 476)		- (4.071)
Other general and administrative expense Miscellaneous other revenue (expense)		(4,682) 1,459		(4,798) 968		(4,157) (142)		(4,476) (300)		(4,271) (171)
iviscellarieous other revenue (expense)		(14,972)		(14,030)		(12,601)		(14,117)		(15,414)
Income before equity in earnings of unconsolidated affiliates		82,873		108,325		140,820		126,238		163,367
Equity in earnings of unconsolidated affiliates		-		-		-		249		259
Net income	\$	82,873	\$	108,325	\$	140,820	\$	126,487	\$	163,626
Net income per diluted common share		\$0.70		\$0.97		\$1.33		\$0.93		\$1.50
Core earnings per diluted common share (a)		Ψ3σ		ψ0.0.		ψσσ		\$1.16		ψσσ
	<b>c</b>	4 204 074	Φ.	4 470 050	æ	4 400 050	æ	,	æ	4 504 070
Average long-term investment capital	\$	1,384,074	\$	1,476,953	\$	1,498,252	\$	1,545,350	\$	1,564,872
Average balance of mortgage assets		13,658,034		13,922,698		13,424,149		13,550,511		13,190,380
Investment premium amortization		130,084		121,190		101,872		125,872		96,677
Average constant prepayment rate, or CPR		23.20%		20.37%		17.28%		21.45%		17.60%
Average total financing spreads		0.64		0.81		1.06		0.96		1.26
Average financing spreads on residential mortgage investments <sup>(a)</sup>		0.72		0.89		1.17		1.07		1.38

# Capstead's Comparative Balance Sheets (dollars in thousands, except per share amounts, unaudited)

	December 31, 2016	December 31, 2015	December 31, 2014	December 31, 2013	December 31, 2012
Assets					
Residential mortgage investments	\$ 13,316,282	\$ 14,154,737	\$13,908,104	\$ 13,475,874	\$ 13,860,158
Cash collateral receivable from interest rate swap counterparties	29,660	50,193	53,139	25,502	49,972
Interest rate swap agreements at fair value	24,709	7,720	1,657	5,005	169
Cash and cash equivalents	56,732	54,185	307,526	413,356	425,445
Receivables and other assets	149,493	179,531	116,525	94,014	128,086
Investments in unconsolidated affiliates	-	-			3,117
	\$ 13,576,876	\$ 14,446,366	\$14,386,951	\$ 14,013,751	\$ 14,466,947
Liabilities					
Secured borrowings	\$ 12,145,346	\$ 12,958,394	\$12,806,843	\$ 12,482,900	\$ 12,784,238
Interest rate swap agreements at fair value	24,417	26,061	27,034	11,304	32,868
Unsecured borrowings	98,090	97,986	97,882	97,783	100,779
Common stock dividend payable	22,634	25,979	34,054	30,872	29,512
Accounts payable and accrued expenses	38,702	39,622	30,367	25,109	22,425
	12,329,189	13,148,042	12,996,180	12,647,968	12,969,822
Stockholders' Equity					
Preferred stock	199,059	197,172	183,936	165,756	188,992
Common stock	942,842	965,057	979,413	980,884	1,014,223
Accumulated other comprehensive income	105,786	136,095	227,422	219,143	293,910
	1,247,687	1,298,324	1,390,771	1,365,783	1,497,125
	\$ 13,576,876	\$ 14,446,366	\$14,386,951	\$ 14,013,751	\$ 14,466,947
<b>Book value per common share</b> (based on outstanding shares of common stock and calculated assuming liquidation preferences for preferred stock) (unaudited)	\$10.85	\$11.42	\$12.52	\$12.47	\$13.58
Long-term investment capital (stockholders' equity and unsecured borrowings, net of investments in related unconsolidated affiliates prior their dissolution in December 2013) (unaudited)	\$1,345,777	\$1,396,310	<b>\$1,488,653</b>	\$1,463,566	\$1,594,787
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Portfolio leverage (secured borrowings divided by long-term investment capital) (unaudited)	9.02:1	9.28:1	8.60:1	8.53:1	8.02:1

### **Non-GAAP Financial Measures**

As of December 31, 2016 (unaudited)



Financing spreads on residential mortgage investments, a non-GAAP financial measure, differs from total financing spreads, an all-inclusive GAAP measure, that is based on all interest-earning assets and all interest-paying liabilities. We believe presenting financing spreads on residential mortgage investments provides useful information for evaluating the performance of the Company's portfolio.

Core earnings per diluted common share is a non-GAAP financial measure that differs from the related GAAP measure of net income per diluted common share by excluding certain one-time effects of second quarter 2013 transactions to redeem then-outstanding high-cost convertible preferred capital and issue our 7.50% Series E preferred shares. We believe presenting this metric on a core earnings basis provides useful, comparative information for evaluating the Company's performance.

		20	016		2015					
Quarter Ended:	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1		
Total financing spreads	0.55%	0.56%	0.64%	0.82%	0.83%	0.66%	0.74%	1.01%		
Impact of yields on other interest-earning assets	0.01	0.01	0.01	0.03	0.01	0.03	0.04	0.04		
Impact of borrowing rates on other interest-paying liabilities	0.05	0.05	0.05	0.05	0.06	0.05	0.06	0.06		
Financing spreads on residential mortgage investments	0.61	0.62	0.70	0.90	0.90	0.74	0.84	1.11		
Year Ended:	2016	2015	2014	2013	2012					
Total financing spreads	0.64%	0.81%	1.06%	0.96%	1.26%					
Impact of yields on other interest-earning assets	0.02	0.03	0.05	0.04	0.06					
Impact of borrowing rates on other interest-paying										
liabilities	0.06	0.05	0.06	0.07	0.06					
Financing spreads on residential mortgage investments	0.72	0.89	1.17	1.07	1.38					

Core earnings available to common stockholders and core earnings per diluted common share:	Quarter E June 30,		Year Ended December 31, 2013		
Net income available to common stockholders Redemption preference premiums paid Convertible preferred dividends accruing from the Series E preferred	\$ 4,103	\$0.04	\$ 89,027	\$0.93	
	19,924	0.21	19,924	0.21	
stock issue date to the convertible preferred redemption date Core earnings available to common stockholders	1,741	0.02	1,741	<u>0.02</u>	
	\$ 25,768	\$0.27	\$110,692	<u>\$1.16</u>	

## **Experienced Management Team**



Our top three executive officers have a combined 75 years of mortgage finance industry experience.

#### Phillip A. Reinsch – President and Chief Executive Officer, Director, Chief Financial Officer and Secretary

- Appointed President, Chief Executive Officer and Director in July 2016
- Served as Chief Financial Officer since 2003, and has served in other executive positions at Capstead since 1993
- Formerly employed by Ernst & Young LLP focusing on mortgage banking and asset securitization
- A CPA and member of the NAREIT Mortgage REIT Council, the FEI Dallas Chapter Real Estate Steering Committee and the NACD

#### Robert R. Spears – Executive Vice President, Chief Investment Officer

- Has served in asset and liability management positions at Capstead since 1994
- Formerly Vice President of secondary marketing with NationsBanc Mortgage Corporation

#### Roy S. Kim – Senior Vice President, Asset and Liability Management and Treasurer

- Joined Capstead in April 2015 augmenting our asset and liability management capabilities with primary responsibility for liability management
- Has over 20 years experience in the mortgage finance industry, primarily in trading capacities with JP Morgan and Bank of America