

Orchid Island Capital, Inc.  
Form 10-Q  
July 30, 2015

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

FORM 10-Q

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

For the quarterly period ended June 30, 2015

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-35236

Orchid Island Capital, Inc.

(Exact name of registrant as specified in its charter)

Maryland  
(State or other jurisdiction of  
incorporation or organization)

27-3269228  
(I.R.S. Employer  
Identification No.)

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

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

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

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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, 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 ☒

Number of shares outstanding at July 30, 2015: 22,962,493

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## PART I. FINANCIAL INFORMATION

|                                                                                                |    |
|------------------------------------------------------------------------------------------------|----|
| ITEM 1. Financial Statements                                                                   | 1  |
| Balance Sheets as of June 30, 2015 (unaudited) and December 31, 2014                           | 1  |
| Statements of Operations (unaudited) for the six and three months ended June 30, 2015 and 2014 | 2  |
| Statement of Stockholders' Equity (unaudited) for the six months ended June 30, 2015           | 3  |
| Statements of Cash Flows (unaudited) for the six months ended June 30, 2015 and 2014           | 4  |
| ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations  | 21 |
| ITEM 3. Quantitative and Qualitative Disclosures about Market Risk                             | 39 |
| ITEM 4. Controls and Procedures                                                                | 43 |

## PART II. OTHER INFORMATION

|                                                                     |    |
|---------------------------------------------------------------------|----|
| ITEM 1. Legal Proceedings                                           | 44 |
| ITEM 1A. Risk Factors                                               | 44 |
| ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds | 44 |
| ITEM 3. Defaults upon Senior Securities                             | 44 |
| ITEM 4. Mine Safety Disclosures                                     | 44 |
| ITEM 5. Other Information                                           | 44 |
| ITEM 6. Exhibits                                                    | 45 |
| SIGNATURES                                                          | 46 |

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## ORCHID ISLAND CAPITAL, INC.

## BALANCE SHEETS

(\$ in thousands, except per share data)

|                                           | (Unaudited)      |                      |
|-------------------------------------------|------------------|----------------------|
|                                           | June 30,<br>2015 | December<br>31, 2014 |
| <b>ASSETS:</b>                            |                  |                      |
| Mortgage-backed securities, at fair value |                  |                      |
| Pledged to counterparties                 | \$2,115,919      | \$1,517,304          |
| Unpledged                                 | 58,952           | 31,867               |
| Total mortgage-backed securities          | 2,174,871        | 1,549,171            |
| Cash and cash equivalents                 | 100,471          | 93,137               |
| Restricted cash                           | 23,060           | 7,790                |
| Accrued interest receivable               | 8,663            | 6,211                |
| Derivative assets, at fair value          | 65               | 1,217                |
| Other assets                              | 523              | 282                  |
| Total Assets                              | \$2,307,653      | \$1,657,808          |

**LIABILITIES AND STOCKHOLDERS' EQUITY**

|                                          |             |             |
|------------------------------------------|-------------|-------------|
| <b>LIABILITIES:</b>                      |             |             |
| Repurchase agreements                    | \$2,014,071 | \$1,436,651 |
| Payable for unsettled security purchased | 7,623       | -           |
| Accrued interest payable                 | 599         | 628         |
| Due to affiliates                        | 456         | 330         |
| Other liabilities                        | 755         | 2,121       |
| Total Liabilities                        | 2,023,504   | 1,439,730   |

**COMMITMENTS AND CONTINGENCIES****STOCKHOLDERS' EQUITY:**

|                                                                                                                                                                                                  |             |             |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------|-------------|
| Preferred stock, \$0.01 par value; 100,000,000 shares authorized; no shares issued and outstanding as of June 30, 2015 and December 31, 2014                                                     | -           | -           |
| Common Stock, \$0.01 par value; 500,000,000 shares authorized, 22,959,817 shares issued and outstanding as of June 30, 2015 and 16,699,656 shares issued and outstanding as of December 31, 2014 | 230         | 167         |
| Additional paid-in capital                                                                                                                                                                       | 283,919     | 217,419     |
| Retained earnings                                                                                                                                                                                | -           | 492         |
| Total Stockholders' Equity                                                                                                                                                                       | 284,149     | 218,078     |
| Total Liabilities and Stockholders' Equity                                                                                                                                                       | \$2,307,653 | \$1,657,808 |

See Notes to Financial Statements



ORCHID ISLAND CAPITAL, INC.  
STATEMENTS OF OPERATIONS  
(Unaudited)

For the Six and Three Months Ended June 30, 2015 and 2014  
(\$ in thousands, except per share data)

|                                                         | Six Months Ended June<br>30, |           | Three Months Ended June<br>30, |           |
|---------------------------------------------------------|------------------------------|-----------|--------------------------------|-----------|
|                                                         | 2015                         | 2014      | 2015                           | 2014      |
| Interest income                                         | \$31,367                     | \$10,372  | \$16,753                       | \$6,589   |
| Interest expense                                        | (2,863 )                     | (1,087 )  | (1,567 )                       | (676 )    |
| Net interest income                                     | 28,504                       | 9,285     | 15,186                         | 5,913     |
| Realized (losses) gains on mortgage-backed securities   | (1,923 )                     | 3,891     | (1,891 )                       | 2,980     |
| Unrealized (losses) gains on mortgage-backed securities | (7,003 )                     | 10,124    | (13,324 )                      | 8,584     |
| Losses on derivative instruments                        | (13,154 )                    | (7,421 )  | (802 )                         | (5,728 )  |
| Net portfolio income (loss)                             | 6,424                        | 15,879    | (831 )                         | 11,749    |
| Expenses:                                               |                              |           |                                |           |
| Management fees                                         | 1,869                        | 733       | 1,014                          | 430       |
| Accrued incentive compensation                          | 322                          | 225       | 157                            | 225       |
| Directors' fees and liability insurance                 | 482                          | 240       | 234                            | 156       |
| Audit, legal and other professional fees                | 333                          | 245       | 173                            | 172       |
| Direct REIT operating expenses                          | 88                           | 88        | 46                             | 44        |
| Other administrative                                    | 653                          | 118       | 377                            | 87        |
| Total expenses                                          | 3,747                        | 1,649     | 2,001                          | 1,114     |
| Net income (loss)                                       | \$2,677                      | \$14,230  | \$(2,832 )                     | \$10,635  |
| Basic and diluted net income (loss) per share           | \$0.14                       | \$2.01    | \$(0.14 )                      | \$1.17    |
| Weighted Average Shares Outstanding                     | 18,320,359                   | 7,096,838 | 19,751,871                     | 9,078,107 |
| Dividends declared per common share                     | \$1.08                       | \$1.08    | \$0.54                         | \$0.54    |
| See Notes to Financial Statements                       |                              |           |                                |           |

ORCHID ISLAND CAPITAL, INC.  
STATEMENT OF STOCKHOLDERS' EQUITY  
(Unaudited)

For the Six Months Ended June 30, 2015

(\$ in thousands, except per share data)

|                                                                  | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Total     |
|------------------------------------------------------------------|-----------------|----------------------------------|----------------------|-----------|
| Balances, January 1, 2015                                        | \$167           | \$217,419                        | \$492                | \$218,078 |
| Net income                                                       | -               | -                                | 2,677                | 2,677     |
| Cash dividends declared, \$1.08 per share                        | -               | (17,010 )                        | (3,169 )             | (20,179 ) |
| Issuance of common stock pursuant to public offerings            | 63              | 83,212                           | -                    | 83,275    |
| Issuance of common stock pursuant to equity<br>compensation plan | -               | 227                              | -                    | 227       |
| Amortization of equity compensation                              | -               | 71                               | -                    | 71        |
| Balances, June 30, 2015                                          | \$230           | \$283,919                        | \$-                  | \$284,149 |
| See Notes to Financial Statements                                |                 |                                  |                      |           |

ORCHID ISLAND CAPITAL, INC.  
STATEMENTS OF CASH FLOWS  
(Unaudited)

For the Six Months Ended June 30, 2015 and 2014  
(\$ in thousands)

|                                                                                             | 2015              | 2014              |
|---------------------------------------------------------------------------------------------|-------------------|-------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                                |                   |                   |
| Net income                                                                                  | \$2,677           | \$14,230          |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                   |                   |
| Stock based compensation                                                                    | 298               | 55                |
| Realized and unrealized losses (gains) on mortgage-backed securities                        | 8,926             | (14,015 )         |
| Realized and unrealized losses on interest rate swaptions                                   | 1,152             | 1,285             |
| Realized and unrealized losses on forward settling to-be-announced securities               | 31                | -                 |
| Changes in operating assets and liabilities:                                                |                   |                   |
| Accrued interest receivable                                                                 | (2,414 )          | (2,239 )          |
| Other assets                                                                                | (234 )            | (337 )            |
| Accrued interest payable                                                                    | (29 )             | 217               |
| Other liabilities                                                                           | (209 )            | 361               |
| Due to affiliates                                                                           | 126               | 70                |
| <b>NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</b>                                  | <b>10,324</b>     | <b>(373 )</b>     |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                                |                   |                   |
| From mortgage-backed securities investments:                                                |                   |                   |
| Purchases                                                                                   | (1,139,704)       | (951,473 )        |
| Sales                                                                                       | 402,575           | 420,787           |
| Principal repayments                                                                        | 110,081           | 26,749            |
| Increase in restricted cash                                                                 | (15,270 )         | (1,138 )          |
| Payment on net settlement of to-be-announced securities                                     | (31 )             | -                 |
| Purchase of interest rate swaptions, net of margin cash received                            | (1,157 )          | (1,219 )          |
| <b>NET CASH USED IN INVESTING ACTIVITIES</b>                                                | <b>(643,506 )</b> | <b>(506,294 )</b> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                                |                   |                   |
| Proceeds from repurchase agreements                                                         | 7,458,153         | 3,179,550         |
| Principal payments on repurchase agreements                                                 | (6,880,733)       | (2,714,406)       |
| Cash dividends                                                                              | (20,179 )         | (8,439 )          |
| Proceeds from issuance of common stock, net of issuance costs                               | 83,275            | 75,077            |
| <b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>                                            | <b>640,516</b>    | <b>531,782</b>    |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>                                            | <b>7,334</b>      | <b>25,115</b>     |
| <b>CASH AND CASH EQUIVALENTS, beginning of the period</b>                                   | <b>93,137</b>     | <b>8,169</b>      |
| <b>CASH AND CASH EQUIVALENTS, end of the period</b>                                         | <b>\$100,471</b>  | <b>\$33,284</b>   |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>                                    |                   |                   |
| Cash paid during the period for:                                                            |                   |                   |
| Interest                                                                                    | \$2,892           | \$870             |
| <b>SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITIES:</b>                             |                   |                   |

|                                             |         |         |
|---------------------------------------------|---------|---------|
| Securities acquired settled in later period | \$7,623 | \$6,829 |
| See Notes to Financial Statements           |         |         |

ORCHID ISLAND CAPITAL, INC.  
NOTES TO FINANCIAL STATEMENTS  
(Unaudited)  
JUNE 30, 2015

NOTE 1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization and Business Description

Orchid Island Capital, Inc., (“Orchid” or the “Company”), was incorporated in Maryland on August 17, 2010 for the purpose of creating and managing a leveraged investment portfolio consisting of residential mortgage-backed securities (“RMBS”). From incorporation to February 20, 2013 Orchid was a wholly owned subsidiary of Bimini Capital Management, Inc. (“Bimini”). Orchid began operations on November 24, 2010 (the date of commencement of operations). From incorporation through November 24, 2010, Orchid’s only activity was the issuance of common stock to Bimini.

On February 20, 2013, Orchid completed the initial public offering (“IPO”) of its common stock in which it sold approximately 2.4 million shares of its common stock and raised gross proceeds of \$35.4 million. Orchid is an “emerging growth company” as defined in the Jumpstart Our Business Startups Act of 2012 (the “JOBS Act”).

Orchid completed a secondary offering of 1,800,000 common shares on January 23, 2014. The underwriters exercised their overallotment option in full for an additional 270,000 shares on January 29, 2014. The aggregate net proceeds to Orchid were approximately \$24.2 million which were invested in RMBS that are issued and the principal and interest of which are guaranteed by a federally chartered corporation or agency (“Agency RMBS”) on a leveraged basis.

Orchid completed a secondary offering of 3,200,000 common shares on March 24, 2014. The underwriters exercised their overallotment option in full for an additional 480,000 shares on April 11, 2014. The aggregate net proceeds to Orchid were approximately \$44.0 million which were invested in Agency RMBS securities on a leveraged basis.

On June 17, 2014, Orchid entered into an equity distribution agreement (the “June 2014 Equity Distribution Agreement”) with two sales agents pursuant to which the Company could offer and sell, from time to time, up to an aggregate amount of \$35,000,000 of shares of the Company’s common stock in transactions that were deemed to be “at the market” offerings and privately negotiated transactions. The Company issued a total of 2,528,416 shares under the June 2014 Equity Distribution Agreement for aggregate proceeds of approximately \$34.2 million, net of commissions and fees, prior to its termination.

On September 3, 2014, Orchid entered into a second equity distribution agreement (the “September 2014 Equity Distribution Agreement”) with two sales agents pursuant to which the Company could offer and sell, from time to time, up to an aggregate amount of \$75,000,000 of shares of the Company’s common stock in transactions that are deemed to be “at the market” offerings and privately negotiated transactions. The September 2014 Equity Distribution Agreement replaced the June 2014 Equity Distribution Agreement. The Company issued a total of 5,087,646 shares under the September 2014 Equity Distribution Agreement for aggregate proceeds of approximately \$69.1 million, net of commissions and fees, prior to its termination.

On March 2, 2015, Orchid entered into a third equity distribution agreement (the “March 2015 Equity Distribution Agreement”) with two sales agents pursuant to which the Company may offer and sell, from time to time, up to an aggregate amount of \$100,000,000 of shares of the Company’s common stock in transactions that are deemed to be “at the market” offerings and privately negotiated transactions. The March 2015 Equity Distribution Agreement replaced the September 2014 Equity Distribution Agreement. Through June 30, 2015, the Company issued a total of 6,221,102

shares under the March 2015 Equity Distribution Agreement for aggregate proceeds of approximately \$83.1 million, net of commissions and fees.

## Basis of Presentation and Use of Estimates

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 8 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six and three month periods ended June 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.

The balance sheet at December 31, 2014 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements. For further information, refer to the financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014.

The preparation of 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. The significant estimates affecting the accompanying financial statements are the fair values of RMBS, Eurodollar and Treasury note (“T-Note”) futures contracts, to-be-announced (“TBA”) securities, as discussed below, and interest rate swaptions.

## Statement of Comprehensive Income (Loss)

In accordance with the Financial Accounting Standards Board (the “FASB”) Accounting Standards Codification (“ASC”) Topic 220, Comprehensive Income, a statement of comprehensive income (loss) has not been included as the Company has no items of other comprehensive income (loss). Comprehensive income (loss) is the same as net income (loss) for the periods presented.

## Cash and Cash Equivalents and Restricted Cash

Cash and cash equivalents include cash on deposit with financial institutions and highly liquid investments with original maturities of three months or less at the time of purchase. At June 30, 2015, restricted cash consisted of \$8,663,000 of cash held by a broker as margin on Eurodollar futures contracts and \$14,397,000 of cash held on deposit as collateral with repurchase agreement counterparties. At December 31, 2014 restricted cash consisted of approximately \$5,174,000 of cash held by a broker as margin on Eurodollar futures contracts and \$2,616,000 of cash held on deposit as collateral with repurchase agreement counterparties.

The Company maintains cash balances at four banks, and, at times, balances may exceed federally insured limits. The Company has not experienced any losses related to these balances. The Federal Deposit Insurance Corporation insures eligible accounts up to \$250,000 per depositor at each financial institution. At June 30, 2015, the Company’s cash deposits exceeded federally insured limits by approximately \$99.8 million. Restricted cash balances are uninsured, but are held in separate customer accounts that are segregated from the general funds of the counterparty. The Company limits uninsured balances to only large, well-known bank and derivative counterparties and believes that it is not exposed to any significant credit risk on cash and cash equivalents or restricted cash balances.



## Mortgage-Backed Securities

The Company invests primarily in mortgage pass-through (“PT”) certificates, collateralized mortgage obligations, and interest only (“IO”) securities and inverse interest only (“IIO”) securities representing interest in or obligations backed by pools of RMBS. These investments meet the requirements to be classified as available for sale under ASC 320-10-25, Debt and Equity Securities (which requires the securities to be carried at fair value on the balance sheet with changes in fair value charged to other comprehensive income, a component of stockholders’ equity). However, the Company has elected to account for its investment in RMBS under the fair value option. Electing the fair value option requires the Company to record changes in fair value in the statement of operations, which, in management’s view, more appropriately reflects the results of our operations for a particular reporting period and is consistent with the underlying economics and how the portfolio is managed.

The Company records RMBS transactions on the trade date. Security purchases that have not settled as of the balance sheet date are included in the RMBS balance with an offsetting liability recorded, whereas securities sold that have not settled as of the balance sheet date are removed from the RMBS balance with an offsetting receivable recorded.

The fair value of the Company’s investments in RMBS is governed by FASB ASC 820, Fair Value Measurement. The definition of fair value in FASB ASC 820 focuses on the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date. The fair value measurement assumes that the transaction to sell the asset or transfer the liability either occurs in the principal market for the asset or liability, or in the absence of a principal market, occurs in the most advantageous market for the asset or liability. Estimated fair values for RMBS are based on independent pricing sources and/or third party broker quotes, when available.

Income on PT RMBS securities is based on the stated interest rate of the security. Premiums or discounts present at the date of purchase are not amortized. For IO securities, the income is accrued based on the carrying value and the effective yield. The difference between income accrued and the interest received on the security is characterized as a return of investment and serves to reduce the asset’s carrying value. At each reporting date, the effective yield is adjusted prospectively from the reporting period based on the new estimate of prepayments and the contractual terms of the security. For IIO securities, effective yield and income recognition calculations also take into account the index value applicable to the security. Changes in fair value of RMBS during each reporting period are recorded in earnings and reported as unrealized gains or losses on mortgage-backed securities in the accompanying statements of operations.

## Derivative Financial Instruments

The Company uses derivative instruments to manage interest rate risk, facilitate asset/liability strategies and manage other exposures, and it may continue to do so in the future. The principal instruments that the Company has used to date are T-Note and Eurodollar futures contracts and options to enter in interest rate swaps (“interest rate swaptions”), but may enter into other derivatives in the future.

The Company purchases a portion of its Agency RMBS through delayed delivery transactions (forward purchase commitments), including TBA securities. At times when market conditions are conducive, the Company may choose to move the settlement of these TBA securities out to a later date by entering into an offsetting short position, which is then net settled for cash, and simultaneously entering into a substantially similar TBA securities trade for a later settlement date. Such a set of transactions is referred to as a TBA “dollar roll” transaction. The TBA securities purchased at the later settlement date are typically priced at a discount to securities for settlement in the current

month. This difference is referred to as the “price drop.” The price drop represents compensation to us for foregoing net interest margin and is referred to as TBA “dollar roll income.” Specified pools of mortgage loans can also be the subject of a dollar roll transaction, when market conditions allow.

The Company accounts for TBA securities as derivative instruments if either the TBA securities do not settle in the shortest period of time possible or if the Company cannot assert that it is probable at inception and throughout the term of the TBA security that it will take physical delivery of the Agency RMBS for a long position, or make delivery of the Agency RMBS for a short position, upon settlement of the trade. The Company accounts for TBA dollar roll transactions as a series of derivative transactions. Gains, losses and dollar roll income associated with TBA securities and dollar roll transactions are reported in gain (loss) on derivative instruments in the accompanying statements of operations. The fair value of TBA securities is estimated based on similar methods used to value RMBS securities.

The Company has elected to not treat any of its derivative financial instruments as hedges in order to align the accounting treatment of its derivative instruments with the treatment of its portfolio assets under the fair value option election. FASB ASC Topic 815, Derivatives and Hedging, requires that all derivative instruments be carried at fair value. Changes in fair value are recorded in earnings for each period.

Holding derivatives creates exposure to credit risk related to the potential for failure on the part of counterparties to honor their commitments. In addition, the Company may be required to post collateral based on any declines in the market value of the derivatives. In the event of default by a counterparty, the Company may have difficulty recovering its collateral and may not receive payments provided for under the terms of the agreement. To mitigate this risk, the Company uses only well-established commercial banks as counterparties.

#### Financial Instruments

FASB ASC 825, Financial Instruments, requires disclosure of the fair value of financial instruments for which it is practicable to estimate that value, either in the body of the financial statements or in the accompanying notes. RMBS, Eurodollar and T-Note futures contracts, interest rate swaptions and TBA securities are accounted for at fair value in the balance sheets. The methods and assumptions used to estimate fair value for these instruments are presented in Note 11 of the financial statements.

The estimated fair value of cash and cash equivalents, restricted cash, accrued interest receivable, other assets, due to affiliates, repurchase agreements, payable for unsettled security purchased, accrued interest payable and other liabilities generally approximates their carrying values as of June 30, 2015 and December 31, 2014 due to the short-term nature of these financial instruments.

#### Repurchase Agreements

The Company finances the acquisition of the majority of its PT RMBS through the use of repurchase agreements under master repurchase agreements. Pursuant to ASC Topic 860, Transfers and Servicing, the Company accounts for repurchase transactions as collateralized financing transactions, which are carried at their contractual amounts, including accrued interest, as specified in the respective agreements.

#### Manager Compensation

The Company is externally managed by Bimini Advisors, LLC (the “Manager” or “Bimini Advisors”), a Maryland limited liability company and wholly-owned subsidiary of Bimini. The Company’s management agreement with the Manager provides for payment to the Manager of a management fee and reimbursement of certain operating expenses, which are accrued and expensed during the period for which they are earned or incurred. Refer to Note 12 for the terms of the management agreement.

## Earnings Per Share

The Company follows the provisions of FASB ASC 260, Earnings Per Share. Basic earnings per share (“EPS”) is calculated as net income or loss attributable to common stockholders divided by the weighted average number of shares of common stock outstanding or subscribed during the period. Diluted EPS is calculated using the treasury stock or two-class method, as applicable, for common stock equivalents, if any. However, the common stock equivalents are not included in computing diluted EPS if the result is anti-dilutive.

## Income Taxes

Orchid has qualified and elected to be taxed as a real estate investment trust (“REIT”) under the Internal Revenue Code of 1986, as amended (the “Code”). REITs are generally not subject to federal income tax on their REIT taxable income provided that they distribute to their stockholders at least 90% of their REIT taxable income on an annual basis. In addition, a REIT must meet other provisions of the Code to retain its tax status.

Orchid measures, recognizes and presents its uncertain tax positions in accordance with FASB ASC 740, Income Taxes. Under that guidance, Orchid assesses the likelihood, based on their technical merit, that tax positions will be sustained upon examination based on the facts, circumstances and information available at the end of each period. All of Orchid’s tax positions are categorized as highly certain. There is no accrual for any tax, interest or penalties related to Orchid’s tax position assessment. The measurement of uncertain tax positions is adjusted when new information is available, or when an event occurs that requires a change.

## Recent Accounting Pronouncements

In June 2014, the FASB issued Accounting Standard Update (“ASU”) 2014-12, Compensation-Stock Compensation: Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. ASU 2014-12 requires that performance targets that affect vesting and that could be achieved after the requisite service period be treated as performance conditions. The effective date of ASU 2014-12 is for interim and annual reporting periods beginning after December 15, 2015. The ASU is not expected to materially impact the Company’s financial statements.

In June 2014, the FASB issued ASU 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. ASU 2014-11 amends the accounting guidance for repurchase-to-maturity transactions and repurchase agreements executed as repurchase financings, and requires additional disclosure about certain transactions by the transferor. ASU 2014-11 is effective for certain transactions that qualify for sales treatment for the first interim or annual period beginning after December 15, 2014. The new disclosure requirements for repurchase agreements, securities lending transactions and repurchase-to-maturity transactions that qualify for secured borrowing treatment is effective for annual periods beginning after December 15, 2014 and for interim periods beginning after March 15, 2015. The adoption of this ASU did not have a material impact on the Company’s financial statements.

## NOTE 2. MORTGAGE-BACKED SECURITIES

The following table presents the Company’s RMBS portfolio as of June 30, 2015 and December 31, 2014:

(in thousands)

|                                    | June 30,<br>2015 | December<br>31, 2014 |
|------------------------------------|------------------|----------------------|
| Pass-Through RMBS Certificates:    |                  |                      |
| Hybrid Adjustable-rate Mortgages   | \$56,754         | \$70,400             |
| Adjustable-rate Mortgages          | 3,456            | 3,794                |
| Fixed-rate Mortgages               | 1,993,369        | 1,412,593            |
| Total Pass-Through Certificates    | 2,053,579        | 1,486,787            |
| Structured RMBS Certificates:      |                  |                      |
| Interest-Only Securities           | 78,347           | 46,611               |
| Inverse Interest-Only Securities   | 42,945           | 15,773               |
| Total Structured RMBS Certificates | 121,292          | 62,384               |
| Total                              | \$2,174,871      | \$1,549,171          |



The following table summarizes the Company's RMBS portfolio as of June 30, 2015 and December 31, 2014, according to the contractual maturities of the securities in the portfolio. Actual maturities of RMBS investments are generally shorter than stated contractual maturities and are affected by the contractual lives of the underlying mortgages, periodic payments of principal, and prepayments of principal.

(in thousands)

|                                                 | June 30,<br>2015 | December<br>31, 2014 |
|-------------------------------------------------|------------------|----------------------|
| Greater than five years and less than ten years | \$697            | \$967                |
| Greater than or equal to ten years              | 2,174,174        | 1,548,204            |
| Total                                           | \$2,174,871      | \$1,549,171          |

The Company generally pledges its RMBS assets as collateral under repurchase agreements. At June 30, 2015 and December 31, 2014, the Company had unpledged securities totaling \$59.0 million and \$31.9 million, respectively. The unpledged balance at June 30, 2015 includes an unsettled security purchase with a fair value of approximately \$7.6 million that will be pledged as collateral under repurchase agreements on its settlement date in July 2015.

### NOTE 3. REPURCHASE AGREEMENTS

As of June 30, 2015, the Company had outstanding repurchase obligations of approximately \$2,014.1 million with a net weighted average borrowing rate of 0.39%. These agreements were collateralized by RMBS with a fair value, including accrued interest, of approximately \$2,123.6 million and cash pledged to counterparties of approximately \$14.4 million. As of December 31, 2014, the Company had outstanding repurchase obligations of approximately \$1,436.7 million with a net weighted average borrowing rate of 0.36%. These agreements were collateralized by RMBS with a fair value, including accrued interest, of approximately \$1,522.9 million and cash pledged to counterparties of approximately \$2.6 million.

As of June 30, 2015 and December 31, 2014, the Company's repurchase agreements had remaining maturities as summarized below:

(\$ in thousands)

|                                                       | OVERNIGHT<br>(1 DAY OR<br>LESS) | BETWEEN<br>2<br>AND<br>30 DAYS | BETWEEN<br>31<br>AND<br>90 DAYS | GREATER<br>THAN<br>90 DAYS | TOTAL       |
|-------------------------------------------------------|---------------------------------|--------------------------------|---------------------------------|----------------------------|-------------|
| <b>June 30, 2015</b>                                  |                                 |                                |                                 |                            |             |
| Fair market value of securities pledged,<br>including |                                 |                                |                                 |                            |             |
| accrued interest receivable                           | \$ 82,736                       | \$ 1,799,521                   | \$ 241,364                      | \$-                        | \$2,123,621 |
| Repurchase agreement liabilities<br>associated with   |                                 |                                |                                 |                            |             |
| these securities                                      | \$ 80,108                       | \$ 1,709,480                   | \$ 224,483                      | \$-                        | \$2,014,071 |
| Net weighted average borrowing rate                   | 0.36                            | % 0.39                         | % 0.41                          | % -                        | 0.39 %      |
| <b>December 31, 2014</b>                              |                                 |                                |                                 |                            |             |
| Fair market value of securities pledged,<br>including |                                 |                                |                                 |                            |             |

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|                                                                   |      |           |           |         |             |      |   |      |   |
|-------------------------------------------------------------------|------|-----------|-----------|---------|-------------|------|---|------|---|
| accrued interest receivable                                       | \$ - | \$984,823 | \$534,238 | \$3,844 | \$1,522,905 |      |   |      |   |
| Repurchase agreement liabilities associated with these securities | \$ - | \$929,831 | \$502,947 | \$3,873 | \$1,436,651 |      |   |      |   |
| Net weighted average borrowing rate                               | -    | 0.36      | %         | 0.37    | %           | 0.38 | % | 0.36 | % |

If, during the term of a repurchase agreement, a lender files for bankruptcy, the Company might experience difficulty recovering its pledged assets, which could result in an unsecured claim against the lender for the difference between the amount loaned to the Company plus interest due to the counterparty and the fair value of the collateral pledged to such lender, including the accrued interest receivable and cash posted by the Company as collateral. At June 30, 2015, the Company had an aggregate amount at risk (the difference between the amount loaned to the Company, including interest payable, and the fair value of securities and cash pledged (if any), including accrued interest on such securities) with all counterparties of approximately \$122.9 million. The Company did not have an amount at risk with any individual counterparty greater than 10% of the Company's equity at June 30, 2015 and December 31, 2014.

#### NOTE 4. DERIVATIVE FINANCIAL INSTRUMENTS

In connection with its interest rate risk management strategy, the Company economically hedges a portion of the cost of its repurchase agreement funding by entering into derivatives and other hedging contracts. To date, we have entered into Eurodollar and T-Note futures contracts and interest rate swaptions, but may enter into other contracts in the future. The Company has not elected hedging treatment under GAAP, and as such all gains or losses (realized and unrealized) on these instruments are reflected in earnings for all periods presented.

In addition, the Company utilizes TBA securities as a means of investing in and financing Agency RMBS or as a means of reducing its exposure to Agency RMBS, and not as a hedge. The Company accounts for TBA securities as derivative instruments if either the TBA securities do not settle in the shortest period of time possible or if the Company cannot assert that it is probable at inception and throughout the term of the TBA securities that it will take physical delivery of the Agency RMBS for a long position, or make delivery of the Agency RMBS for a short position, upon settlement of the trade.

#### Derivative Assets (Liability), at Fair Value

The table below summarizes fair value information about our derivative assets and liability as of June 30, 2015 and December 31, 2014.

(in thousands)

| Derivative Instruments and Related Accounts       | Balance Sheet Location           | June 30,<br>2015 | December<br>31, 2014 |
|---------------------------------------------------|----------------------------------|------------------|----------------------|
| <b>Assets</b>                                     |                                  |                  |                      |
| Futures contracts - Margin posted to counterparty | Restricted cash                  | \$8,663          | \$5,174              |
| Payer swaptions                                   | Derivative assets, at fair value | 65               | 1,217                |
|                                                   |                                  | \$8,728          | \$6,391              |
| <b>Liability</b>                                  |                                  |                  |                      |
| Payer swaptions - Margin posted by counterparty   | Other liabilities                | \$(207)          | \$(1,364)            |

The tables below present information related to the Company's Eurodollar and T-Note futures positions at June 30, 2015 and December 31, 2014.

(\$ in thousands)

| Expiration Year              | Average<br>Contract<br>Notional<br>Amount | June 30, 2015                        |   |                                          |   | Open<br>Equity(1) |
|------------------------------|-------------------------------------------|--------------------------------------|---|------------------------------------------|---|-------------------|
|                              |                                           | Average<br>Weighted<br>Entry<br>Rate |   | Weighted<br>Average<br>Effective<br>Rate |   |                   |
| Eurodollar Futures Contracts |                                           |                                      |   |                                          |   |                   |
| 2015                         | \$900,000                                 | 0.85                                 | % | 0.45                                     | % | \$(1,819 )        |
| 2016                         | 900,000                                   | 1.51                                 | % | 1.04                                     | % | (4,189 )          |
| 2017                         | 900,000                                   | 2.31                                 | % | 1.81                                     | % | (4,570 )          |
| 2018                         | 900,000                                   | 2.77                                 | % | 2.34                                     | % | (3,887 )          |
| 2019                         | 900,000                                   | 2.56                                 | % | 2.61                                     | % | 124               |
| Total / Weighted Average     | \$900,000                                 | 2.04                                 | % | 1.62                                     | % | \$(14,341 )       |

#### Treasury Note Futures Contracts

|                                       |            |      |   |      |   |            |
|---------------------------------------|------------|------|---|------|---|------------|
| September 2015 10 year T-Note futures |            |      |   |      |   |            |
| (Sep 2015 - Sep 2025 Hedge Period)    | \$ 120,000 | 2.15 | % | 2.07 | % | \$(1,011 ) |

(\$ in thousands)

| Expiration Year              | Average<br>Contract<br>Notional<br>Amount | December 31, 2014                    |   |                                          |   | Open<br>Equity(1) |
|------------------------------|-------------------------------------------|--------------------------------------|---|------------------------------------------|---|-------------------|
|                              |                                           | Weighted<br>Average<br>Entry<br>Rate |   | Weighted<br>Average<br>Effective<br>Rate |   |                   |
| Eurodollar Futures Contracts |                                           |                                      |   |                                          |   |                   |
| 2015                         | \$650,000                                 | 0.79                                 | % | 0.63                                     | % | \$(1,039 )        |
| 2016                         | 800,000                                   | 1.52                                 | % | 1.54                                     | % | 139               |
| 2017                         | 800,000                                   | 2.36                                 | % | 2.23                                     | % | (1,041 )          |
| 2018                         | 800,000                                   | 2.94                                 | % | 2.54                                     | % | (2,361 )          |
| Total / Weighted Average     | \$760,000                                 | 1.88                                 | % | 1.73                                     | % | \$(4,302 )        |

(1) Open equity represents the cumulative gains (losses) recorded on open futures positions from inception.

(2) Treasury Futures Contracts were valued at 126.17 at June 30, 2015. The nominal value of the short position was \$151.4 million.

The table below presents information related to the Company's interest rate swaption positions at June 30, 2015.

(\$ in thousands)

| Expiration | Cost | Option        |                                                | Notional<br>Amount | Underlying Swap      |                            | Weighted<br>Average<br>Term<br>(Years) |
|------------|------|---------------|------------------------------------------------|--------------------|----------------------|----------------------------|----------------------------------------|
|            |      | Fair<br>Value | Weighted<br>Average<br>Months to<br>Expiration |                    | Fixed<br>Pay<br>Rate | Receive<br>Rate<br>(LIBOR) |                                        |

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|                   |         |         |   |           |      |   |         |     |
|-------------------|---------|---------|---|-----------|------|---|---------|-----|
| June 30, 2015     |         |         |   |           |      |   |         |     |
| ≤ 1 year          | \$3,200 | \$65    | 2 | \$175,000 | 3.29 | % | 3 Month | 10  |
| December 31, 2014 |         |         |   |           |      |   |         |     |
| ≤ 1 year          | \$5,350 | \$1,217 | 6 | \$375,000 | 2.79 | % | 3 Month | 7.3 |

12

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# Gain (Loss) From Derivative Instruments, Net

The table below presents the effect of the Company's derivative financial instruments on the statements of operations for the six and three months ended June 30, 2015 and 2014.

(in thousands)

|                                                | Six Months Ended June 30, |            | Three Months Ended June 30, |            |
|------------------------------------------------|---------------------------|------------|-----------------------------|------------|
|                                                | 2015                      | 2014       | 2015                        | 2014       |
| Eurodollar futures contracts (short positions) | \$(10,960 )               | \$(6,136 ) | \$358                       | \$(4,599 ) |
| T-Note futures contracts (short position)      | (1,011 )                  | -          | (1,011 )                    | -          |
| Payer swaptions                                | (1,152 )                  | (1,285 )   | (61 )                       | (1,129 )   |
| Net TBA securities                             | (31 )                     | -          | (88 )                       | -          |
|                                                | \$(13,154 )               | \$(7,421 ) | \$(802 )                    | \$(5,728 ) |

## Credit Risk-Related Contingent Features

The use of derivatives creates exposure to credit risk relating to potential losses that could be recognized in the event that the counterparties to these instruments fail to perform their obligations under the contracts. We minimize this risk by limiting our counterparties for instruments which are not centrally cleared on a registered exchange to major financial institutions with acceptable credit ratings and monitoring positions with individual counterparties. In addition, we may be required to pledge assets as collateral for our derivatives, whose amounts vary over time based on the market value, notional amount and remaining term of the derivative contract. In the event of a default by a counterparty, we may not receive payments provided for under the terms of our derivative agreements, and may have difficulty obtaining our assets pledged as collateral for our derivatives. The cash and cash equivalents pledged as collateral for our derivative instruments are included in restricted cash on our balance sheets.

## NOTE 5. OFFSETTING ASSETS AND LIABILITIES

The Company's derivatives and repurchase agreements are subject to underlying agreements with master netting or similar arrangements, which provide for the right of offset in the event of default or in the event of bankruptcy of either party to the transactions. The Company reports its assets and liabilities subject to these arrangements on a gross basis.

The following table presents information regarding those assets and liabilities subject to such arrangements as if the Company had presented them on a net basis as of June 30, 2015 and December 31, 2014.

(in thousands)

| Offsetting of Assets              |                            |                            | Gross Amount Not Offset in the Balance Sheet |  |                        |            |
|-----------------------------------|----------------------------|----------------------------|----------------------------------------------|--|------------------------|------------|
|                                   |                            | Net Amount                 | Financial                                    |  | Cash                   |            |
| Gross Amount of Recognized Assets | Gross Amount Offset in the | of Assets Presented in the | Instruments Received as Collateral           |  | Received as Collateral | Net Amount |

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|                                        |         | Balance<br>Sheet | Balance<br>Sheet |     |            |     |
|----------------------------------------|---------|------------------|------------------|-----|------------|-----|
| June 30, 2015                          |         |                  |                  |     |            |     |
| Derivative assets - Payer<br>swaptions | \$65    | \$-              | \$65             | \$- | \$(65 )    | \$- |
| December 31, 2014                      |         |                  |                  |     |            |     |
| Derivative asset - Payer<br>swaption   | \$1,217 | \$-              | \$1,217          | \$- | \$(1,217 ) | \$- |

(in thousands)

|                       | Offsetting of Liabilities              |                                          |                                                          | Gross Amount Not Offset in the Balance Sheet |                        |            |
|-----------------------|----------------------------------------|------------------------------------------|----------------------------------------------------------|----------------------------------------------|------------------------|------------|
|                       | Gross Amount of Recognized Liabilities | Gross Amount Offset in the Balance Sheet | Net Amount of Liabilities Presented in the Balance Sheet | Instruments Posted as Collateral             | Cash Posted Collateral | Net Amount |
| June 30, 2015         |                                        |                                          |                                                          |                                              |                        |            |
| Repurchase Agreements | \$2,014,071                            | \$-                                      | \$2,014,071                                              | \$(1,999,674)                                | \$(14,397)             | \$-        |
| December 31, 2014     |                                        |                                          |                                                          |                                              |                        |            |
| Repurchase Agreements | \$1,436,651                            | \$-                                      | \$1,436,651                                              | \$(1,434,035)                                | \$(2,616)              | \$-        |

The amounts disclosed for collateral received by or posted to the same counterparty up to and not exceeding the net amount of the asset or liability presented in the balance sheet. The fair value of the actual collateral received by or posted to the same counterparty typically exceeds the amounts presented. See Notes 3 and 4 for a discussion of collateral posted or received against or for repurchase obligations and derivative instruments.

#### NOTE 6. CAPITAL STOCK

##### Common Stock Issuances

During 2015 and 2014, the Company completed the following public offerings of shares of its common stock.

(\$ in thousands, except per share amounts)

| Type of Offering                  | Period         | Weighted Average Price Received Per Share(1) | Shares     | Net Proceeds(2) |
|-----------------------------------|----------------|----------------------------------------------|------------|-----------------|
| 2015                              |                |                                              |            |                 |
| At the Market Offering Program(3) | First Quarter  | \$13.66                                      | 1,210,487  | \$16,175        |
| At the Market Offering Program(3) | Second Quarter | 13.65                                        | 5,024,530  | 67,100          |
|                                   |                |                                              | 6,235,017  | \$83,275        |
| 2014                              |                |                                              |            |                 |
| Secondary Offering                | First Quarter  | \$12.50                                      | 2,070,000  | \$24,174        |
| Secondary Offering(4)             | First Quarter  | 12.55                                        | 3,680,000  | 43,989          |
| At the Market Offering Program(3) | Second Quarter | 13.14                                        | 537,499    | 6,914           |
| At the Market Offering Program(3) | Third Quarter  | 13.99                                        | 3,389,441  | 46,372          |
| At the Market Offering Program(3) | Fourth Quarter | 13.87                                        | 3,675,207  | 49,846          |
|                                   |                |                                              | 13,352,147 | \$171,295       |

(1) Weighted average price received per share is gross of underwriters' discount, if applicable, and other offering costs.

- (2) Net proceeds are net of the underwriters' discount, if applicable, and other offering costs.
- (3) The Company has entered into three equity distribution agreements, two of which have been cancelled and replaced with the current agreement, to publicly offer and sell shares of the Company's common stock in at the market and privately negotiated transactions from time to time. As of June 30, 2015, shares with a value of \$15.0 million remain available for issuance under the March 2015 Equity Distribution Agreement.
- (4) Includes net proceeds received of \$5.7 million for 480,000 shares issued to the underwriters in April 2014 pursuant to the exercise of their overallotment option related to the March 2014 offering.

## Cash Dividends

The table below presents the cash dividends declared on the Company's common stock during 2015 and 2014.

(in thousands, except per share amount)

| Declaration Date  | Record Date        | Payment Date       | Per Share Amount | Total           |
|-------------------|--------------------|--------------------|------------------|-----------------|
| <b>2015</b>       |                    |                    |                  |                 |
| July 9, 2015(1)   | July 27, 2015      | July 31, 2015      | \$0.14           | \$3,218         |
| June 9, 2015      | June 22, 2015      | June 30, 2015      | 0.18             | 4,057           |
| May 11, 2015      | May 26, 2015       | May 29, 2015       | 0.18             | 3,580           |
| April 9, 2015     | April 27, 2015     | April 30, 2015     | 0.18             | 3,303           |
| March 10, 2015    | March 27, 2015     | March 31, 2015     | 0.18             | 3,205           |
| February 10, 2015 | February 25, 2015  | February 27, 2015  | 0.18             | 3,017           |
| January 13, 2015  | January 26, 2015   | January 30, 2015   | 0.18             | 3,017           |
| <b>Totals</b>     |                    |                    | <b>\$1.22</b>    | <b>\$23,397</b> |
| December 9, 2014  | December 26, 2014  | December 30, 2014  | \$0.18           | \$3,004         |
| November 12, 2014 | November 25, 2014  | November 28, 2014  | 0.18             | 2,737           |
| October 9, 2014   | October 28, 2014   | October 31, 2014   | 0.18             | 2,358           |
| September 9, 2014 | September 25, 2014 | September 30, 2014 | 0.18             | 2,348           |
| August 12, 2014   | August 26, 2014    | August 29, 2014    | 0.18             | 1,999           |
| July 10, 2014     | July 28, 2014      | July 31, 2014      | 0.18             | 1,759           |
| June 11, 2014     | June 25, 2014      | June 30, 2014      | 0.18             | 1,712           |
| May 8, 2014       | May 27, 2014       | May 30, 2014       | 0.18             | 1,641           |
| April 8, 2014     | April 25, 2014     | April 30, 2014     | 0.18             | 1,636           |
| March 11, 2014    | March 26, 2014     | March 31, 2014     | 0.18             | 1,550           |
| February 11, 2014 | February 25, 2014  | February 28, 2014  | 0.18             | 974             |
| January 9, 2014   | January 27, 2014   | January 31, 2014   | 0.18             | 925             |
| <b>Totals</b>     |                    |                    | <b>\$2.16</b>    | <b>\$22,643</b> |

(1) The effect of the dividend declared in July 2015 is not reflected in the Company's financial statements as of June 30, 2015.

## NOTE 7. STOCK INCENTIVE PLAN

In October 2012, the Company's Board of Directors adopted and Bimini, then the Company's sole stockholder, approved, the Orchid Island Capital, Inc. 2012 Equity Incentive Plan (the "Incentive Plan") to recruit and retain employees, directors and other service providers, including employees of the Manager and other affiliates. The Incentive Plan provides for the award of stock options, stock appreciation rights, stock award, performance units, other equity-based awards (and dividend equivalents with respect to awards of performance units and other equity-based awards) and incentive awards. The Incentive Plan is administered by the Compensation Committee of the Company's Board of Directors except that the Company's full Board of Directors will administer awards made to directors who are not employees of the Company or its affiliates. The Incentive Plan provides for awards of up to an aggregate of 10% of the issued and outstanding shares of our common stock (on a fully diluted basis) at the time of the awards, subject to a maximum aggregate 4,000,000 shares of the Company's common stock that may be issued under the Incentive Plan.

## Restricted Stock Awards

On April 25, 2014, the Compensation Committee granted each of our non-employee directors 6,000 shares of restricted common stock subject to a three year vesting schedule whereby 2,000 shares of the award vest on the first, second and third anniversaries of the award date. Directors will have all the rights of a stockholder with respect to the awards, including the right to receive dividends and vote the shares. The awards are subject to forfeiture should the director no longer be a member of the Board of Directors of the Company prior to the respective vesting dates. A total of 8,000 shares of restricted stock vested and were issued during the six months ended June 30, 2015. There were no vested and unissued restricted stock awards at June 30, 2015 and December 31, 2014.

The table below presents information related to the Company's restricted common stock at June 30, 2015 and 2014.

(\$ in thousands, except per share data)

|                                                    | Six Months Ended June 30, |                                                 | 2014   |                                                 |
|----------------------------------------------------|---------------------------|-------------------------------------------------|--------|-------------------------------------------------|
|                                                    | 2015                      | Weighted<br>Average<br>Grant Date<br>Fair Value | 2014   | Weighted<br>Average<br>Grant Date<br>Fair Value |
|                                                    | Shares                    |                                                 | Shares |                                                 |
| Unvested, beginning of period                      | 24,000                    | \$ 12.23                                        | -      | \$-                                             |
| Granted                                            | -                         | -                                               | 24,000 | 12.23                                           |
| Vested and issued                                  | (8,000 )                  | 12.23                                           | -      | -                                               |
| Unvested, end of period                            | 16,000                    | \$ 12.23                                        | 24,000 | \$ 12.23                                        |
| Compensation expense during period                 |                           | \$49                                            |        | \$16                                            |
| Unrecognized compensation expense, end of period   |                           | \$179                                           |        | \$277                                           |
| Intrinsic value, end of period                     |                           | \$179                                           |        | \$313                                           |
| Weighted-average remaining vesting term (in years) |                           | 1.8                                             |        | 2.8                                             |

#### Stock Awards

The Company issues immediately vested common stock under the Incentive Plan to certain executive officers and directors. The following table presents information related to fully vested common stock issued during the six months ended June 30, 2015 and 2014.

(\$ in thousands, except per share data)

|                                                                     | Six Months Ended June 30, |         |
|---------------------------------------------------------------------|---------------------------|---------|
|                                                                     | 2015                      | 2014    |
| Fully vested shares granted(1)(2)                                   | 24,619                    | 2,944   |
| Weighted average grant date price                                   | \$13.28                   | \$13.06 |
| Compensation expense related to fully vested common share awards(1) | \$327                     | \$38    |

- (1) The table above includes 21,715 shares of fully vested shares which were granted in January 2015 with respect to service performed during 2014. Approximately \$288,000 of compensation expense related to these share awards were accrued and recognized in 2014.
- (2) The table above includes 7,475 shares with a fair value of approximately \$100,000 surrendered for the satisfaction of tax withholding obligations.

#### Performance Units

The Company issues performance units under the Incentive Plan to certain executive officers. "Performance Units" vest after the end of a defined performance period, based on satisfaction of the performance conditions set forth in the performance unit agreement. When earned, each Performance Unit will be settled by the issuance of one share of the Company's Common Stock, at which time the Performance Unit will be cancelled. The Performance Units contain dividend equivalent rights which entitle the Participants to receive distributions declared by the Company on Common Stock, but do not include the right to vote the shares. Performance Units are subject to forfeiture should the participant no longer serve as an executive officer for the Company. Compensation expense for the Performance Units are recognized over the remaining vesting period once it becomes probable that the performance conditions will be achieved.



The following table presents information related to Performance Units outstanding during the six months ended June 30, 2015.

(\$ in thousands, except per share data)

|                                                                   |          |
|-------------------------------------------------------------------|----------|
| Performance units granted during the period                       | 7,508    |
| Weighted average grant date price                                 | \$ 13.32 |
| Compensation expense related to performance units                 | \$22     |
| Intrinsic value, at period end                                    | \$84     |
| Unrecognized compensation expense, at period end                  | \$78     |
| Weighted average remaining vesting term (in years), at period end | 1.8      |

#### NOTE 8. COMMITMENTS AND CONTINGENCIES

From time to time, the Company may become involved in various claims and legal actions arising in the ordinary course of business. Management is not aware of any reported or unreported contingencies at June 30, 2015.

#### NOTE 9. INCOME TAXES

The Company will generally not be subject to federal income tax on its REIT taxable income to the extent that it distributes its REIT taxable income to its stockholders and satisfies the ongoing REIT requirements, including meeting certain asset, income and stock ownership tests. A REIT must generally distribute at least 90% of its REIT taxable income to its stockholders, of which 85% generally must be distributed within the taxable year, in order to avoid the imposition of an excise tax. The remaining balance may be distributed up to the end of the following taxable year, provided the REIT elects to treat such amount as a prior year distribution and meets certain other requirements.

#### NOTE 10. EARNINGS PER SHARE (EPS)

The Company had dividend eligible shares of restricted common stock and Performance Units that were outstanding during the six and three months ended June 30, 2015. The basic and diluted per share computations include these unvested shares of restricted common stock and performance units if there is income available to Common Stock, as they have dividend participation rights. The shares of restricted common stock and Performance Units have no contractual obligation to share in losses. Because there is no such obligation, the shares of restricted common stock and Performance Units are not included in the basic and diluted EPS computations when no income is available to Common Stock even though they are considered participating securities.

The table below reconciles the numerator and denominator of EPS for the six and three months ended June 30, 2015 and 2014.

(in thousands, except per-share information)

|                                                       | Six Months Ended June<br>30,<br>2015 |          | Three Months Ended June<br>30,<br>2015 |          |
|-------------------------------------------------------|--------------------------------------|----------|----------------------------------------|----------|
|                                                       | 2015                                 | 2014     | 2015                                   | 2014     |
| Basic and diluted EPS per common share:               |                                      |          |                                        |          |
| Numerator for basic and diluted EPS per common share: |                                      |          |                                        |          |
| Net income (loss) - Basic and diluted                 | \$2,677                              | \$14,230 | \$(2,832)                              | \$10,635 |
| Weighted average common shares:                       |                                      |          |                                        |          |
| Common shares outstanding at the balance sheet date   | 22,960                               | 9,632    | 22,960                                 | 9,632    |

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Unvested dividend eligible share based compensation

|                                           |          |          |           |        |
|-------------------------------------------|----------|----------|-----------|--------|
| outstanding at the balance sheet date     | 24       | 24       | -         | 24     |
| Effect of weighting                       | (4,664 ) | (2,559 ) | (3,208 )  | (578 ) |
| Weighted average shares-basic and diluted | 18,320   | 7,097    | 19,752    | 9,078  |
| Income (loss) per common share:           |          |          |           |        |
| Basic and diluted                         | \$0.14   | \$2.01   | \$(0.14 ) | \$1.17 |

## NOTE 11. FAIR VALUE

Authoritative accounting literature establishes a framework for using fair value to measure assets and liabilities and defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) as opposed to the price that would be paid to acquire the asset or received to assume the liability (an entry price). A fair value measure should reflect the assumptions that market participants would use in pricing the asset or liability, including the assumptions about the risk inherent in a particular valuation technique, the effect of a restriction on the sale or use of an asset and the risk of non-performance. Required disclosures include stratification of balance sheet amounts measured at fair value based on inputs the Company uses to derive fair value measurements. These stratifications are:

- Level 1 valuations, where the valuation is based on quoted market prices for identical assets or liabilities traded in active markets (which include exchanges and over-the-counter markets with sufficient volume),
- Level 2 valuations, where the valuation is based on quoted market prices for similar instruments traded in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market, and
- Level 3 valuations, where the valuation is generated from model-based techniques that use significant assumptions not observable in the market, but observable based on Company-specific data. These unobservable assumptions reflect the Company's own estimates for assumptions that market participants would use in pricing the asset or liability. Valuation techniques typically include option pricing models, discounted cash flow models and similar techniques, but may also include the use of market prices of assets or liabilities that are not directly comparable to the subject asset or liability.

The Company's RMBS, interest rate swaptions and TBA securities are valued using Level 2 valuations, and such valuations currently are determined by the Company based on independent pricing sources and/or third party broker quotes, when available. Because the price estimates may vary, the Company must make certain judgments and assumptions about the appropriate price to use to calculate the fair values. Alternatively, the Company could opt to have the value of all of our positions in RMBS, interest rate swaptions and TBA securities determined by either an independent third-party or do so internally.

RMBS, interest rate swaptions, TBA securities and Eurodollar and T-Note futures contracts were recorded at fair value on a recurring basis during the six and three months ended June 30, 2015 and 2014. When determining fair value measurements, the Company considers the principal or most advantageous market in which it would transact and considers assumptions that market participants would use when pricing the asset. When possible, the Company looks to active and observable markets to price identical assets. When identical assets are not traded in active markets, the Company looks to market observable data for similar assets.

The following table presents financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2015 and December 31, 2014:

(in thousands)

|                                         | Fair Value<br>Measurements | Quoted<br>Prices<br>in Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
|-----------------------------------------|----------------------------|----------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|
| <b>June 30, 2015</b>                    |                            |                                                                                  |                                                           |                                                    |
| Mortgage-backed securities              | \$ 2,174,871               | \$-                                                                              | \$2,174,871                                               | \$ -                                               |
| Eurodollar and T-Note futures contracts | 8,663                      | 8,663                                                                            | -                                                         | -                                                  |
| Payer swaptions                         | 65                         | -                                                                                | 65                                                        | -                                                  |
| <b>December 31, 2014</b>                |                            |                                                                                  |                                                           |                                                    |
| Mortgage-backed securities              | \$ 1,549,171               | \$-                                                                              | \$1,549,171                                               | \$ -                                               |
| Eurodollar futures contracts            | 5,174                      | 5,174                                                                            | -                                                         | -                                                  |
| Payer swaptions                         | 1,217                      | -                                                                                | 1,217                                                     | -                                                  |

During the six and three months ended June 30, 2015 and 2014, there were no transfers of financial assets or liabilities between levels 1, 2 or 3.

## NOTE 12. RELATED PARTY TRANSACTIONS

### Management Agreement

At the completion of its IPO, the Company entered into a management agreement with Bimini Advisors (the “Manager”), which provides for an initial term through February 20, 2016 with automatic one-year extensions and is subject to certain termination rights. Under the terms of the management agreement, Bimini Advisors is responsible for administering the business activities and day-to-day operations of the Company. Bimini Advisors receives a monthly management fee in the amount of:

- One-twelfth of 1.5% of the first \$250 million of the Company’s equity, as defined in the management agreement,
- One-twelfth of 1.25% of the Company’s equity that is greater than \$250 million and less than or equal to \$500 million, and
- One-twelfth of 1.00% of the Company’s equity that is greater than \$500 million.

The Company is obligated to reimburse Bimini Advisors for any direct expenses incurred on its behalf. In addition, Bimini Advisors began allocating to the Company its pro rata portion of certain overhead costs set forth in the management agreement commencing with the calendar quarter beginning July 1, 2014. Should the Company terminate the management agreement without cause, it shall pay to Bimini Advisors a termination fee equal to three times the average annual management fee, as defined in the management agreement, before or on the last day of the initial term or automatic renewal term.

Total expenses recorded during the six months ended June 30, 2015 and 2014 for the management fee and costs incurred were approximately \$2,382,000 and \$733,000, respectively. Total expenses recorded during the three months

ended June 30, 2015 and 2014 for the management fee and costs incurred were approximately \$1,288,000 and \$430,000, respectively.

At June 30, 2015 and December 31, 2014, the net amount due to affiliates was approximately \$456,000 and \$330,000, respectively.

#### Other Relationships with Bimini

John B. Van Heuvelen, one of our independent director nominees, owns shares of common stock of Bimini. Robert Cauley, our Chief Executive Officer and Chairman of our Board of Directors, also serves as Chief Executive Officer and Chairman of the Board of Directors of Bimini and owns shares of common stock of Bimini. Hunter Haas, our Chief Financial Officer, Chief Investment Officer, Secretary and a member of our Board of Directors, also serves as the Chief Financial Officer, Chief Investment Officer and Treasurer of Bimini and owns shares of common stock of Bimini.

#### NOTE 13. SUBSEQUENT EVENT

##### Share Repurchase Program

On July 29, 2015, the Board of Directors passed a resolution authorizing the repurchase of up to 2,000,000 shares of the Company's common stock. As part of the stock repurchase program, shares may be purchased in open market transactions, including through block purchases, through privately negotiated transactions, or pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Open market repurchases will be made in accordance with Exchange Act Rule 10b-18, which sets certain restrictions on the method, timing, price and volume of open market stock repurchases. The timing, manner, price and amount of any repurchases will be determined by the Company in its discretion and will be subject to economic and market conditions, stock price, applicable legal requirements and other factors. The authorization does not obligate the Company to acquire any particular amount of common stock and the program may be suspended or discontinued at the Company's discretion without prior notice.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with the financial statements and notes to those statements included in Item 1 of this Form 10-Q. The discussion may contain certain forward-looking statements that involve risks and uncertainties. Forward-looking statements are those that are not historical in nature. As a result of many factors, such as those set forth under "Risk Factors" in our most recent Annual Report on Form 10-K, our actual results may differ materially from those anticipated in such forward-looking statements.

### Overview

We are a specialty finance company that invests in residential mortgage-backed securities ("RMBS") which are issued and guaranteed by a federally chartered corporation or agency ("Agency RMBS"). Our investment strategy focuses on, and our portfolio consists of, two categories of Agency RMBS: (i) traditional pass-through Agency RMBS ("PT RMBS") and (ii) structured Agency RMBS, such as collateralized mortgage obligations ("CMOs"), interest only securities ("IOs"), inverse interest only securities ("IIOs") and principal only securities ("POs"), among other types of structured Agency RMBS. We were formed by Bimini in August 2010, commenced operations on November 24, 2010 and completed our initial public offering ("IPO") on February 20, 2013. We are externally managed by Bimini Advisors, a registered investment adviser with the Securities and Exchange Commission (the "SEC").

Our business objective is to provide attractive risk-adjusted total returns over the long term through a combination of capital appreciation and the payment of regular monthly distributions. We intend to achieve this objective by investing in and strategically allocating capital between the two categories of Agency RMBS described above. We seek to generate income from (i) the net interest margin on our leveraged pass-through Agency RMBS portfolio and the leveraged portion of our structured Agency RMBS portfolio, and (ii) the interest income we generate from the unleveraged portion of our structured Agency RMBS portfolio. We intend to fund our pass-through Agency RMBS and certain of our structured Agency RMBS through short-term borrowings structured as repurchase agreements. Pass-through Agency RMBS and structured Agency RMBS typically exhibit materially different sensitivities to movements in interest rates. Declines in the value of one portfolio may be offset by appreciation in the other. The percentage of capital that we allocate to our two Agency RMBS asset categories will vary and will be actively managed in an effort to maintain the level of income generated by the combined portfolios, the stability of that income stream and the stability of the value of the combined portfolios. We believe that this strategy will enhance our liquidity, earnings, book value stability and asset selection opportunities in various interest rate environments.

We operate so as to qualify to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code"). We generally will not be subject to U.S. federal income tax to the extent that we currently distribute all of our REIT taxable income to our stockholders and maintain our REIT qualification.

On October 3, 2014, we received approval to list our common stock on the New York Stock Exchange ("NYSE"). The Company's common stock began trading on the NYSE at the commencement of trading on October 8, 2014 under the symbol "ORC".

### Capital Raising Activities

We completed secondary offerings in January and March 2014, raising aggregate net proceeds of approximately \$68.2 million from the sale of 5,750,000 shares of our common stock inclusive of the \$5.7 million of net proceeds received from the exercise of the underwriters' overallotment option granted in the March 2014 offering, which closed in April 2014.



On June 17, 2014, we entered into an equity distribution agreement (the “June 2014 Equity Distribution Agreement”) with two sales agents pursuant to which we could offer and sell, from time to time, up to an aggregate amount of \$35,000,000 of shares of our common stock in transactions that were deemed to be “at the market” offerings and privately negotiated transactions. We issued a total of 2,528,416 shares under the June 2014 Equity Distribution Agreement for aggregate proceeds of approximately \$34.2 million, net of commissions and fees, prior to its termination.

On September 3, 2014, we entered into a second equity distribution agreement (the “September 2014 Equity Distribution Agreement”) with two sales agents pursuant to which we could offer and sell, from time to time, up to an aggregate amount of \$75,000,000 of shares of our common stock in transactions that were deemed to be “at the market” offerings and privately negotiated transactions. The September 2014 Equity Distribution Agreement replaced the June 2014 Equity Distribution Agreement. We issued a total of 5,087,646 shares under the September 2014 Equity Distribution Agreement for aggregate proceeds of approximately \$69.1 million, net of commissions and fees, prior to its termination.

On March 2, 2015, we entered into a third equity distribution agreement (the “March 2015 Equity Distribution Agreement”) with two sales agents pursuant to which we may offer and sell, from time to time, up to an aggregate amount of \$100,000,000 of shares of our common stock in transactions that are deemed to be “at the market” offerings and privately negotiated transactions. The March 2015 Equity Distribution Agreement replaced the September 2014 Equity Distribution Agreement. Through June 30, 2015, we had issued a total of 6,221,102 shares under the March 2015 Equity Distribution Agreement for aggregate proceeds of approximately \$83.1 million, net of commissions and fees.

#### Factors that Affect our Results of Operations and Financial Condition

A variety of industry and economic factors may impact our results of operations and financial condition. These factors include:

- interest rate trends;
- the difference between Agency RMBS yields and our funding and hedging costs;
  - competition for investments in Agency RMBS;
  - actions taken by the Federal Reserve and the U.S. Treasury;
- prepayment rates on mortgages underlying our Agency RMBS, and credit trends insofar as they affect prepayment rates; and
- other market developments.

In addition, a variety of factors relating to our business may also impact our results of operations and financial condition. These factors include:

- our degree of leverage;
- our access to funding and borrowing capacity;
  - our borrowing costs;
  - our hedging activities;
- the market value of our investments; and
- the requirements to qualify as a REIT and the requirements to qualify for a registration exemption under the Investment Company Act.

## Results of Operations

Described below are the Company's results of operations for the six and three months ended June 30, 2015, as compared to the Company's results of operations for the six and three months ended June 30, 2014.

## Net Income (Loss) Summary

Net income for the six months ended June 30, 2015 was \$2.7 million, or \$0.14 per share. Net income for the six months ended June 30, 2014 was \$14.2 million, or \$2.01 per share. Net loss for the three months ended June 30, 2015 was \$2.8 million, or \$0.14 per share. Net income for the three months ended June 30, 2014 was \$10.6 million, or \$1.17 per share. The components of net income (loss) for the six and three months ended June 30, 2015 and 2014, along with the changes in those components are presented in the table below:

(in thousands)

|                                                 | Six Months Ended June 30, |          |             | Three Months Ended, June 30, |          |             |
|-------------------------------------------------|---------------------------|----------|-------------|------------------------------|----------|-------------|
|                                                 | 2015                      | 2014     | Change      | 2015                         | 2014     | Change      |
| Interest income                                 | \$31,367                  | \$10,372 | \$20,995    | \$16,753                     | \$6,589  | \$10,164    |
| Interest expense                                | (2,863 )                  | (1,087 ) | (1,776 )    | (1,567 )                     | (676 )   | (891 )      |
| Net interest income                             | 28,504                    | 9,285    | 19,219      | 15,186                       | 5,913    | 9,273       |
| (Losses) gains on RMBS and derivative contracts | (22,080 )                 | 6,594    | (28,674 )   | (16,017 )                    | 5,836    | (21,853 )   |
| Net portfolio income (loss)                     | 6,424                     | 15,879   | (9,455 )    | (831 )                       | 11,749   | (12,580 )   |
| Expenses                                        | (3,747 )                  | (1,649 ) | (2,098 )    | (2,001 )                     | (1,114 ) | (887 )      |
| Net income (loss)                               | \$2,677                   | \$14,230 | \$(11,553 ) | \$(2,832 )                   | \$10,635 | \$(13,467 ) |

## GAAP and Non-GAAP Reconciliations

## Economic Interest Expense and Economic Net Interest Income

To date, the Company has used derivatives, specifically Eurodollar and T-Note futures contracts and interest rate swaptions, to hedge a portion of the interest rate risk on repurchase agreements in a rising rate environment. Each interest rate futures contract covers a specific period, but the Company typically has many contracts in place at any point in time—usually covering several years in the aggregate. We currently have Eurodollar and T-Note futures contracts and interest rate swaption agreements in place. The interest rate swaptions agreements give us the option to enter into swaps covering future periods. During 2015, we entered into forward settling TBA securities that meet the definition of a derivative under GAAP. We have not entered into these TBA securities as a hedge of our interest rate risk.

The Company has not elected to designate its derivative holdings for hedge accounting treatment under the Financial Accounting Standards Board, (the “FASB”), Accounting Standards Codification, (“ASC”), Topic 815, Derivatives and Hedging. Changes in fair value of these instruments are presented in a separate line item in the Company’s statements of operations and not included in interest expense. As such, for financial reporting purposes, interest expense and cost of funds are not impacted by the fluctuation in value of the derivative instruments. In the future, the Company may use other derivative instruments to hedge its interest expense and/or elect to designate its derivative holdings for hedge accounting treatment.

For the purpose of computing economic net interest income and ratios relating to cost of funds measures, GAAP interest expense has been adjusted to reflect the realized gains or losses on specific derivative instruments that pertain to each period presented. As of June 30, 2015, the Company had Eurodollar and T-Note futures contracts in place covering periods through 2019 and 2025, respectively, and interest rate swaption agreements in place covering periods beginning in 2015 through 2025. Adjusting our interest expense for the periods presented by the gains or losses on all derivative instruments would not accurately reflect our economic interest expense for these periods.

For each period presented, the Company has combined the effects of the derivative financial instruments in place for the respective period with the actual interest expense incurred on repurchase agreements to reflect total expense for the applicable period. Interest expense, including the effect of derivative instruments for the period, is referred to as economic interest expense. Net interest income, when calculated to include the effect of derivative instruments for the period, is referred to as economic net interest income.

However, because the Company has not elected hedging treatment under ASC 815, the gains or losses on all of the Company's derivative instruments held during the period are reflected in our statements of operations. This presentation includes gains or losses on all contracts in effect during the reporting period, covering the current period as well as periods in the future.

The Company believes that economic interest expense and economic net interest income provides meaningful information to consider, in addition to the respective amounts prepared in accordance with GAAP. The non-GAAP measures help the Company to evaluate its financial position and performance without the effects of certain transactions and GAAP adjustments that are not necessarily indicative of its current investment portfolio or operations. The realized and unrealized gains or losses presented in the Company's statements of operations are not necessarily representative of the total interest rate expense that the Company will ultimately realize. This is because as interest rates move up or down in the future, the gains or losses the Company ultimately realizes, and which will affect the Company's total interest rate expense in future periods, may differ from the unrealized gains or losses recognized as of the reporting date.

The Company's presentation of the economic value of its hedging strategy has important limitations. First, other market participants may calculate economic interest expense and economic net interest income differently than the Company calculates them. Second, while the Company believes that the calculation of the economic value of our hedging strategy described above helps to present our financial position and performance, it may be of limited usefulness as an analytical tool. Therefore, the economic value of the Company's investment strategy should not be viewed in isolation and is not a substitute for interest expense and net interest income computed in accordance with GAAP.

The tables below present a reconciliation of the adjustments to interest expense shown for each period relative to our derivative instruments, and the income statement line item, gains (losses) on derivative instruments, calculated in accordance with GAAP for the six months ended June 30, 2015 and 2014 and each quarter during 2015 and 2014.

#### Gains (Losses) on Derivative Instruments

(in thousands)

|                           | Recognized<br>in<br>Income<br>Statement<br>(GAAP) | TBA<br>Securities<br>Income | Funding Hedges<br>Attributed<br>to<br>Current<br>Period<br>(Non-GAAP) | Attributed to<br>Future<br>Periods<br>(Non-GAAP) |
|---------------------------|---------------------------------------------------|-----------------------------|-----------------------------------------------------------------------|--------------------------------------------------|
| <b>Three Months Ended</b> |                                                   |                             |                                                                       |                                                  |
| June 30, 2015             | \$(803 )                                          | \$(88 )                     | \$(595 )                                                              | \$(120 )                                         |
| March 31, 2015            | (12,351 )                                         | 57                          | (306 )                                                                | (12,102 )                                        |
| December 31, 2014         | (9,562 )                                          | -                           | (145 )                                                                | (9,417 )                                         |
| September 30, 2014        | 3,058                                             | -                           | (25 )                                                                 | 3,083                                            |
| June 30, 2014             | (5,728 )                                          | -                           | (3 )                                                                  | (5,725 )                                         |
| March 31, 2014            | (1,693 )                                          | -                           | (30 )                                                                 | (1,663 )                                         |
| <b>Six Months Ended</b>   |                                                   |                             |                                                                       |                                                  |
| June 30, 2015             | \$(13,154 )                                       | \$(31 )                     | \$(901 )                                                              | \$(12,222 )                                      |
| June 30, 2014             | (7,421 )                                          | -                           | (33 )                                                                 | (7,388 )                                         |

# Economic Interest Expense and Economic Net Interest Income

(in thousands)

|                           |                    | Interest Expense on Repurchase<br>Agreements<br>Gains<br>(Losses) on<br>Derivative<br>Instruments |                                       |                                    | Net Interest Income            |                                       |
|---------------------------|--------------------|---------------------------------------------------------------------------------------------------|---------------------------------------|------------------------------------|--------------------------------|---------------------------------------|
|                           | Interest<br>Income | GAAP<br>Interest<br>Expense                                                                       | Attributed<br>to Current<br>Period(1) | Economic<br>Interest<br>Expense(2) | GAAP<br>Net Interest<br>Income | Economic<br>Net Interest<br>Income(3) |
| <b>Three Months Ended</b> |                    |                                                                                                   |                                       |                                    |                                |                                       |
| June 30, 2015             | \$ 16,753          | \$ 1,567                                                                                          | \$(595 )                              | \$ 2,162                           | \$ 15,186                      | \$ 14,591                             |
| March 31, 2015            | 14,614             | 1,296                                                                                             | (306 )                                | 1,602                              | 13,318                         | 13,012                                |
| December 31, 2014         | 12,146             | 1,126                                                                                             | (145 )                                | 1,271                              | 11,020                         | 10,875                                |
| September 30, 2014        | 9,286              | 818                                                                                               | (25 )                                 | 843                                | 8,468                          | 8,443                                 |
| June 30, 2014             | 6,589              | 676                                                                                               | (3 )                                  | 679                                | 5,913                          | 5,910                                 |
| March 31, 2014            | 3,783              | 411                                                                                               | (30 )                                 | 441                                | 3,372                          | 3,342                                 |
| <b>Six Months Ended</b>   |                    |                                                                                                   |                                       |                                    |                                |                                       |
| June 30, 2015             | \$ 31,367          | \$ 2,863                                                                                          | \$(901 )                              | \$ 3,764                           | \$ 28,504                      | \$ 27,603                             |
| June 30, 2014             | 10,372             | 1,087                                                                                             | (33 )                                 | 1,120                              | 9,285                          | 9,252                                 |

(1) Reflects the effect of derivative instrument hedges for only the period presented.

(2) Calculated by subtracting the effect of derivative instrument hedges attributed to the period presented from GAAP interest expense.

(3) Calculated by adding the effect of derivative instrument hedges attributed to the period presented to GAAP net interest income.

## Net Interest Income

During the six months ended June 30, 2015, we generated \$28.5 million of net interest income, consisting of \$31.4 million of interest income from RMBS assets offset by \$2.9 million of interest expense on repurchase liabilities. For the comparable period ended June 30, 2014, we generated \$9.3 million of net interest income, consisting of \$10.4 million of interest income from RMBS assets offset by \$1.1 million of interest expense on repurchase liabilities. The \$21.0 million increase in interest income and \$1.8 million increase in interest expense for the six months ended June 30, 2015 primarily reflects the deployment of the proceeds from our capital raising activities into the RMBS portfolio on a leveraged basis.

On an economic basis, our interest expense on repurchase liabilities for the six months ended June 30, 2015 and 2014 was \$3.8 million and \$1.1 million, respectively, resulting in \$27.6 million and \$9.3 million of economic net interest income, respectively.

During the three months ended June 30, 2015, we generated \$15.2 million of net interest income, consisting of \$16.8 million of interest income from RMBS assets offset by \$1.6 million of interest expense on repurchase liabilities. For the three months ended June 30, 2014, we generated \$5.9 million of net interest income, consisting of \$6.6 million of interest income from RMBS assets offset by \$0.7 million of interest expense on repurchase liabilities. The

deployment of the proceeds from our capital raising activities on a leveraged basis was the main reason for the increase in both interest income and interest expense for the three months ended June 30, 2015 as compared to the same period in 2014.

On an economic basis, our interest expense on repurchase liabilities for the three months ended June 30, 2015 and 2014 was \$2.2 million and \$0.7 million, respectively, resulting in \$14.6 million and \$5.9 million of economic net interest income, respectively.

The tables below provide information on our portfolio average balances, interest income, yield on assets, average repurchase agreement balances, interest expense, cost of funds, net interest income and net interest spread for the six months ended June 30, 2015 and 2014 and each quarter during 2015 and 2014 on both a GAAP and economic basis.

(\$ in thousands)

|                           | Average<br>RMBS<br>Held(1) | Interest<br>Income | Yield<br>on<br>Average<br>RMBS |   | Average<br>Repurchase<br>Agreements(1) | Interest Expense<br>GAAP<br>Basis | Economic<br>Basis(2) | Average Cost of<br>Funds<br>GAAP<br>Basis |   | Economic<br>Basis(3) |   |
|---------------------------|----------------------------|--------------------|--------------------------------|---|----------------------------------------|-----------------------------------|----------------------|-------------------------------------------|---|----------------------|---|
| <b>Three Months Ended</b> |                            |                    |                                |   |                                        |                                   |                      |                                           |   |                      |   |
| June 30, 2015             | \$1,925,747                | \$16,753           | 3.48                           | % | \$ 1,736,781                           | \$1,567                           | \$ 2,162             | 0.36                                      | % | 0.50                 | % |
| March 31, 2015            | 1,612,896                  | 14,614             | 3.62                           | % | 1,448,071                              | 1,296                             | 1,602                | 0.36                                      | % | 0.44                 | % |
| December 31, 2014         | 1,362,352                  | 12,146             | 3.57                           | % | 1,346,314                              | 1,126                             | 1,271                | 0.33                                      | % | 0.38                 | % |
| September 30, 2014        | 1,025,768                  | 9,286              | 3.62                           | % | 1,019,839                              | 818                               | 843                  | 0.32                                      | % | 0.33                 | % |
| June 30, 2014             | 811,881                    | 6,589              | 3.25                           | % | 717,474                                | 676                               | 679                  | 0.38                                      | % | 0.38                 | % |
| March 31, 2014            | 549,490                    | 3,783              | 2.75                           | % | 484,902                                | 411                               | 441                  | 0.34                                      | % | 0.36                 | % |
| <b>Six Months Ended</b>   |                            |                    |                                |   |                                        |                                   |                      |                                           |   |                      |   |
| June 30, 2015             | \$1,769,322                | \$31,367           | 3.55                           | % | \$ 1,592,426                           | \$2,863                           | \$ 3,764             | 0.36                                      | % | 0.47                 | % |
| June 30, 2014             | 680,685                    | 10,372             | 3.05                           | % | 601,188                                | 1,087                             | 1,120                | 0.36                                      | % | 0.37                 | % |

(\$ in thousands)

|                           | Net Interest Income<br>GAAP<br>Basis | Economic<br>Basis(2) | Net Interest Spread<br>GAAP<br>Basis |   | Economic<br>Basis(4) |   |
|---------------------------|--------------------------------------|----------------------|--------------------------------------|---|----------------------|---|
| <b>Three Months Ended</b> |                                      |                      |                                      |   |                      |   |
| June 30, 2015             | \$15,186                             | \$14,591             | 3.12                                 | % | 2.98                 | % |
| March 31, 2015            | 13,318                               | 13,011               | 3.26                                 | % | 3.18                 | % |
| December 31, 2014         | 11,020                               | 10,875               | 3.24                                 | % | 3.19                 | % |
| September 30, 2014        | 8,468                                | 8,443                | 3.30                                 | % | 3.29                 | % |
| June 30, 2014             | 5,913                                | 5,910                | 2.87                                 | % | 2.87                 | % |
| March 31, 2014            | 3,372                                | 3,342                | 2.41                                 | % | 2.39                 | % |
| <b>Six Months Ended</b>   |                                      |                      |                                      |   |                      |   |
| June 30, 2015             | \$28,504                             | \$27,602             | 3.19                                 | % | 3.08                 | % |
| June 30, 2014             | 9,285                                | 9,252                | 2.69                                 | % | 2.68                 | % |

- (1) Portfolio yields and costs of borrowings presented in the tables above and the tables on pages 27 and 28 are calculated based on the average balances of the underlying investment portfolio/repurchase agreement balances and are annualized for the periods presented. Average balances for quarterly periods are calculated using two data points, the beginning and ending balances.
- (2) Economic interest expense and economic net interest income presented in the table above and the tables on page 28 includes the effect of our derivative instrument hedges for only the periods presented.
- (3) Represents interest cost of our borrowings and the effect of derivative instrument hedges attributed to the period divided by Average RMBS.
- (4) Economic Net Interest Spread is calculated by subtracting Average Economic Cost of Funds from Yield on Average RMBS.

### Interest Income and Average Asset Yield

Our interest income for the six months ended June 30, 2015 and 2014 was \$31.4 million and \$10.4 million, respectively. We had average RMBS holdings of \$1,769.3 million and \$680.7 million for the six months ended June 30, 2015 and 2014, respectively. The yield on our portfolio was 3.55% and 3.05% for the six months ended June 30, 2015 and 2014, respectively. For the six months ended June 30, 2015 as compared to the six months ended June 30, 2014, there was a \$21.0 million increase in interest income due to a \$1,088.6 million increase in average RMBS, combined with a 50 basis point increase in the yield on average RMBS. The increase in average RMBS during the six months ended June 30, 2015 reflects the deployment of the proceeds of our capital raising activities, on a leveraged basis.

Our interest income for the three months ended June 30, 2015 and 2014 was \$16.8 million and \$6.6 million, respectively. We had average RMBS holdings of \$1,925.7 million and \$811.9 million for the three months ended June 30, 2015 and 2014, respectively. The yield on our portfolio was 3.48% and 3.25% for the three months ended June 30, 2015 and 2014, respectively. For the three months ended June 30, 2015 as compared to the three months ended June 30, 2014, there was a \$10.2 million increase in interest income due to a \$1,113.9 million increase in average RMBS, combined with a 23 basis point increase in the yield on average RMBS. The increase in average RMBS during the three months ended June 30, 2015 reflects the deployment of the proceeds of our capital raising activities, on a leveraged basis.

The table below presents the average portfolio size, income and yields of our respective sub-portfolios, consisting of structured RMBS and pass-through RMBS ("PT RMBS") for the six months ended June 30, 2015 and 2014 and each quarter during 2015 and 2014.

(\$ in thousands)

|                    | Average RMBS Held |                    |             | Interest Income |                    |          | Realized Yield on Average RMBS |                    |        |  |  |
|--------------------|-------------------|--------------------|-------------|-----------------|--------------------|----------|--------------------------------|--------------------|--------|--|--|
|                    | PT<br>RMBS        | Structured<br>RMBS | Total       | PT<br>RMBS      | Structured<br>RMBS | Total    | PT<br>RMBS                     | Structured<br>RMBS | Total  |  |  |
| Three Months Ended |                   |                    |             |                 |                    |          |                                |                    |        |  |  |
| June 30, 2015      | \$1,824,893       | \$100,854          | \$1,925,747 | \$16,549        | \$204              | \$16,753 | 3.63 %                         | 0.81 %             | 3.48 % |  |  |
| March 31, 2015     | 1,541,497         | 71,399             | 1,612,896   | 14,629          | (15 )              | 14,614   | 3.80 %                         | (0.09 )%           | 3.62 % |  |  |
| December 31, 2014  | 1,298,967         | 63,385             | 1,362,352   | 12,761          | (615 )             | 12,146   | 3.93 %                         | (3.88 )%           | 3.57 % |  |  |
| September 30, 2014 | 969,034           | 56,734             | 1,025,768   | 9,482           | (196 )             | 9,286    | 3.91 %                         | (1.39 )%           | 3.62 % |  |  |
| June 30, 2014      | 764,199           | 47,682             | 811,881     | 7,674           | (1,085 )           | 6,589    | 4.02 %                         | (9.10 )%           | 3.25 % |  |  |
| March 31, 2014     | 514,226           | 35,264             | 549,490     | 4,402           | (619 )             | 3,783    | 3.42 %                         | (7.02 )%           | 2.75 % |  |  |
| Six Months Ended   |                   |                    |             |                 |                    |          |                                |                    |        |  |  |
| June 30, 2015      | \$1,683,195       | \$86,127           | \$1,769,322 | \$31,178        | \$189              | \$31,367 | 3.70 %                         | 0.44 %             | 3.55 % |  |  |
| June 30, 2014      | 639,212           | 41,473             | 680,685     | 12,076          | (1,704 )           | 10,372   | 3.78 %                         | (8.22 )%           | 3.05 % |  |  |

#### Interest Expense and the Cost of Funds

We had average outstanding repurchase agreements of \$1,592.4 million and \$601.2 million and total interest expense of \$2.9 million and \$1.1 million for the six months ended June 30, 2015 and 2014, respectively. Our average cost of funds was 0.36% for both the six months ended June 30, 2015 and 2014. There was a \$991.2 million increase in average outstanding repurchase agreements during the six months ended June 30, 2015 as compared to the six months ended June 30, 2014. The increase in average outstanding repurchase agreements, and the corresponding increase in interest expense, reflects the leveraging of the proceeds of our capital raising.

Our economic interest expense was \$3.8 million and \$1.1 million for the six months ended June 30, 2015 and 2014, respectively. There was an 10 basis point increase in the average economic cost of funds to 0.47% for the six months ended June 30, 2015 from 0.37% for the six months ended June 30, 2014. The increase in economic interest expense was primarily due to the increase in average outstanding repurchase agreements during the six months ended June 30, 2015, combined with losses on futures contracts attributed to the current period.

We had average outstanding repurchase agreements of \$1,736.8 million and \$717.5 million and total interest expense of \$1.6 million and \$0.7 million for the three months ended June 30, 2015 and 2014, respectively. Our average cost of funds was 0.36% and 0.38% for three months ended June 30, 2015 and 2014, respectively. There was a 2 basis point decrease in the average cost of funds and a \$1,019.3 million increase in average outstanding repurchase agreements during the three months ended June 30, 2015 as compared to the three months ended June 30, 2014. The increase in average outstanding repurchase agreements, and the corresponding increase in interest expense, reflects the leveraging of the proceeds of our capital raising activities.

Our economic interest expense was \$2.2 million and \$0.7 million for the three months ended June 30, 2015 and 2014, respectively. There was a 12 basis point increase in the average economic cost of funds to 0.50% for the three months ended June 30, 2015 from 0.38% for the three months ended June 30, 2014. The increase in economic interest expense was primarily due to the increase in average outstanding repurchase agreements during the three months ended June 30, 2015, combined with losses on futures contracts attributed to the current period.

Because all of our repurchase agreements are short-term, changes in market rates directly affect our interest expense. Our average cost of funds calculated on a GAAP basis was 18 basis points above the average one-month LIBOR and 4 basis points below the average six-month LIBOR for the quarter ended June 30, 2015. Our average economic cost of funds was 32 basis points above the average one-month LIBOR and 10 basis points above the average six-month LIBOR for the quarter ended June 30, 2015. The average term to maturity of the outstanding repurchase agreements decreased to 18 days at June 30, 2015 from 27 days at December 31, 2014.

The tables below presents the average balance of repurchase agreements outstanding, interest expense and average cost of funds, and average one-month and six-month LIBOR rates for the six months ended June 30, 2015 and 2014 and each quarter in 2015 and 2014 on both a GAAP and economic basis.

(\$ in thousands)

|                           | Average<br>Balance of<br>Repurchase<br>Agreements | Interest Expense<br>GAAP<br>Basis | Economic<br>Basis | Average Cost of Funds<br>GAAP<br>Basis | Economic<br>Basis |
|---------------------------|---------------------------------------------------|-----------------------------------|-------------------|----------------------------------------|-------------------|
| <b>Three Months Ended</b> |                                                   |                                   |                   |                                        |                   |
| June 30, 2015             | \$ 1,736,781                                      | \$ 1,567                          | \$ 2,162          | 0.36 %                                 | 0.50 %            |
| March 31, 2015            | 1,448,071                                         | 1,296                             | 1,602             | 0.36 %                                 | 0.44 %            |
| December 31, 2014         | 1,346,314                                         | 1,126                             | 1,271             | 0.33 %                                 | 0.38 %            |
| September 30, 2014        | 1,019,839                                         | 818                               | 843               | 0.32 %                                 | 0.33 %            |
| June 30, 2014             | 717,474                                           | 676                               | 679               | 0.38 %                                 | 0.38 %            |
| March 31, 2014            | 484,902                                           | 411                               | 441               | 0.34 %                                 | 0.36 %            |
| <b>Six Months Ended</b>   |                                                   |                                   |                   |                                        |                   |
| June 30, 2015             | \$ 1,592,426                                      | \$ 2,863                          | \$ 3,764          | 0.36 %                                 | 0.47 %            |
| June 30, 2014             | 601,188                                           | 1,087                             | 1,120             | 0.36 %                                 | 0.37 %            |

|                           | Average GAAP Cost of Funds<br>Relative to Average |           |           |          | Average Economic Cost of Funds<br>Relative to Average |        |           |       |
|---------------------------|---------------------------------------------------|-----------|-----------|----------|-------------------------------------------------------|--------|-----------|-------|
|                           | Average LIBOR                                     |           | One-Month |          | One-Month                                             |        | Six-Month |       |
|                           | One-Month                                         | Six-Month | LIBOR     | LIBOR    | LIBOR                                                 | LIBOR  | LIBOR     | LIBOR |
| <b>Three Months Ended</b> |                                                   |           |           |          |                                                       |        |           |       |
| June 30, 2015             | 0.18 %                                            | 0.40 %    | 0.18 %    | (0.04 )% | 0.32 %                                                | 0.10 % |           |       |
| March 31, 2015            | 0.17 %                                            | 0.35 %    | 0.19 %    | 0.01 %   | 0.27 %                                                | 0.09 % |           |       |
| December 31, 2014         | 0.16 %                                            | 0.34 %    | 0.17 %    | (0.01 )% | 0.22 %                                                | 0.04 % |           |       |
| September 30, 2014        | 0.15 %                                            | 0.33 %    | 0.17 %    | (0.01 )% | 0.18 %                                                | 0.00 % |           |       |
| June 30, 2014             | 0.15 %                                            | 0.33 %    | 0.23 %    | 0.05 %   | 0.23 %                                                | 0.05 % |           |       |
| March 31, 2014            | 0.16 %                                            | 0.34 %    | 0.18 %    | 0.00 %   | 0.20 %                                                | 0.02 % |           |       |
| <b>Six Months Ended</b>   |                                                   |           |           |          |                                                       |        |           |       |
| June 30, 2015             | 0.18 %                                            | 0.38 %    | 0.18 %    | (0.02 )% | 0.29 %                                                | 0.09 % |           |       |

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|               |      |   |      |   |      |   |      |   |      |   |      |   |
|---------------|------|---|------|---|------|---|------|---|------|---|------|---|
| June 30, 2014 | 0.16 | % | 0.33 | % | 0.20 | % | 0.03 | % | 0.21 | % | 0.04 | % |
|---------------|------|---|------|---|------|---|------|---|------|---|------|---|

28

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## Gains or Losses

The table below presents our gains or losses for the six and three months ended June 30, 2015 and 2014.

(in thousands)

|                                                   | Six Months Ended June 30, |          |            | Three Months Ended June 30, |          |            |
|---------------------------------------------------|---------------------------|----------|------------|-----------------------------|----------|------------|
|                                                   | 2015                      | 2014     | Change     | 2015                        | 2014     | Change     |
| Realized (losses) gains on sales of RMBS          | \$(1,923 )                | \$3,891  | \$(5,814 ) | \$(1,891 )                  | \$2,980  | \$(4,871 ) |
| Unrealized (losses) gains on RMBS                 | (7,003 )                  | 10,124   | (17,127 )  | (13,324 )                   | 8,584    | (21,908 )  |
| Total (losses) gains on RMBS                      | (8,926 )                  | 14,015   | (22,941 )  | (15,215 )                   | 11,564   | (26,779 )  |
| Losses on Eurodollar and T-Note futures contracts | (11,971 )                 | (6,136 ) | (5,835 )   | (653 )                      | (4,599 ) | 3,946      |
| Losses on payer swaptions                         | (1,152 )                  | (1,285 ) | 133        | (61 )                       | (1,129 ) | 1,068      |
| Losses on TBA securities                          | (31 )                     | -        | (31 )      | (88 )                       | -        | (88 )      |

We invest in RMBS with the intent to earn net income from the realized yield on those assets over their related funding and hedging costs, and not for purposes of making short term gains from sales. However, we have sold, and may continue to sell, existing assets to acquire new assets, which our management believes might have higher risk-adjusted returns in light of current or anticipated interest rates, federal government programs or general economic conditions or to manage our balance sheet as part of our asset/liability management strategy. During the six months ended June 30, 2015 and 2014, we received proceeds of \$402.6 million and \$420.8 million, respectively, from the sales of RMBS. During the three months ended June 30, 2015 and 2014, we received proceeds of \$362.3 million and \$279.5 million, respectively, from the sales of RMBS.

The net realized and unrealized losses on RMBS for the six and three months ended June 30, 2015 were driven in part by an increase in mortgage interest rates in the three months ended June 30, 2015 resulting in decreased RMBS prices. Gains (losses) on Eurodollar and T-Note futures contracts are a result of higher / lower short and intermediate term rates and the resulting impact on implied forward rates during the six and three months ended June 30, 2015 and 2014. The table below presents historical interest rate data for each quarter end during 2015 and 2014.

|                    | 5 Year Treasury Rate(1) |   | 10 Year Treasury Rate(1) |   | 15 Year Fixed-Rate Mortgage Rate(2) |   | 30 Year Fixed-Rate Mortgage Rate(2) |   | Three Month LIBOR(3) |   |
|--------------------|-------------------------|---|--------------------------|---|-------------------------------------|---|-------------------------------------|---|----------------------|---|
| June 30, 2015      | 1.63                    | % | 2.34                     | % | 3.19                                | % | 3.98                                | % | 0.28                 | % |
| March 31, 2015     | 1.38                    | % | 1.93                     | % | 3.04                                | % | 3.77                                | % | 0.27                 | % |
| December 31, 2014  | 1.65                    | % | 2.17                     | % | 3.13                                | % | 3.86                                | % | 0.25                 | % |
| September 30, 2014 | 1.78                    | % | 2.51                     | % | 3.31                                | % | 4.16                                | % | 0.23                 | % |
| June 30, 2014      | 1.63                    | % | 2.52                     | % | 3.27                                | % | 4.16                                | % | 0.23                 | % |
| March 31, 2014     | 1.73                    | % | 2.72                     | % | 3.36                                | % | 4.34                                | % | 0.23                 | % |

(1) Historical 10 Year Treasury Rates are obtained from quoted end of day prices on the Chicago Board Options Exchange.

(2)

Historical 30 Year and 15 Year Fixed Rate Mortgage Rates are obtained from Freddie Mac's Primary Mortgage Market Survey.

(3) Historical LIBOR are obtained from the Intercontinental Exchange Benchmark Administration Ltd.

## Expenses

For the six and three months ended June 30, 2015, the Company's total operating expenses were approximately \$3.7 million and \$2.0 million, respectively, compared to approximately \$1.6 million and \$1.1 million, respectively, for the six and three months ended June 30, 2014. The table below presents a breakdown of operating expenses for the six and three months ended June 30, 2015 and 2014.

(in thousands)

|                                          | Six Months Ended June 30, |         |         | Three Months Ended June 30, |         |        |
|------------------------------------------|---------------------------|---------|---------|-----------------------------|---------|--------|
|                                          | 2015                      | 2014    | Change  | 2015                        | 2014    | Change |
| Management fees                          | \$1,869                   | \$733   | \$1,136 | \$1,014                     | \$430   | \$584  |
| Accrued incentive compensation           | 322                       | 225     | 97      | 157                         | 225     | (68 )  |
| Directors fees and liability insurance   | 482                       | 240     | 242     | 234                         | 156     | 78     |
| Audit, legal and other professional fees | 333                       | 245     | 88      | 173                         | 172     | 1      |
| Other direct REIT operating expenses     | 88                        | 88      | -       | 46                          | 44      | 2      |
| Other expenses                           | 653                       | 118     | 535     | 377                         | 87      | 290    |
| Total expenses                           | \$3,747                   | \$1,649 | \$2,098 | \$2,001                     | \$1,114 | \$887  |

At the completion of our IPO, we entered into a management agreement with Bimini Advisors, LLC, a wholly owned subsidiary of Bimini, which provides for an initial term through February 20, 2016 with automatic one-year extensions and is subject to certain termination rights. Under the terms of the management agreement, Bimini Advisors is responsible for administering the business activities and day-to-day operations of the Company. Bimini Advisors receives a monthly management fee in the amount of:

- One-twelfth of 1.5% of the first \$250 million of the Company's equity, as defined in the management agreement,
- One-twelfth of 1.25% of the Company's equity that is greater than \$250 million and less than or equal to \$500 million, and
- One-twelfth of 1.00% of the Company's equity that is greater than \$500 million.

The Company is obligated to reimburse Bimini Advisors for any direct expenses incurred on its behalf. In addition, beginning July 1, 2014, Bimini Advisors began allocating to the Company its pro rata portion of certain overhead costs in accordance with the management agreement. During the six and three months ended June 30, 2015, the Company recorded overhead allocations of approximately \$0.5 million and \$0.3 million, respectively, and is included in the table above in the caption "other expenses."

## Financial Condition:

## Mortgage-Backed Securities

As of June 30, 2015, our RMBS portfolio consisted of \$2,174.9 million of Agency RMBS at fair value and had a weighted average coupon on assets of 4.15%. During the six months ended June 30, 2015, we received principal repayments of \$110.1 million compared to \$26.7 million for the six months ended June 30, 2014. During the three

months ended June 30, 2015, we received principal repayments of \$67.1 million compared to \$16.4 million for the three months ended June 30, 2014. The average prepayment speeds for the quarters ended June 30, 2015 and 2014 were 15.3% and 8.1%, respectively.

The following table presents the constant prepayment rate (“CPR”) experienced on our structured and PT RMBS sub-portfolios, on an annualized basis, for the quarterly periods presented. CPR is a method of expressing the prepayment rate for a mortgage pool that assumes that a constant fraction of the remaining principal is prepaid each month or year. Specifically, the CPR in the chart below represents the three month prepayment rate of the securities in the respective asset category. Assets that were not owned for the entire quarter have been excluded from the calculation. The exclusion of certain assets during periods of high trading activity can create a very high, and often volatile, reliance on a small sample of underlying loans.

| Three Months Ended | PT RMBS<br>Portfolio<br>(%) | Structured<br>RMBS<br>Portfolio<br>(%) | Total<br>Portfolio<br>(%) |
|--------------------|-----------------------------|----------------------------------------|---------------------------|
| June 30, 2015      | 13.8                        | 17.9                                   | 15.3                      |
| March 31, 2015     | 8.1                         | 14.6                                   | 9.7                       |
| December 31, 2014  | 4.0                         | 14.9                                   | 7.8                       |
| September 30, 2014 | 8.1                         | 18.8                                   | 12.5                      |
| June 30, 2014      | 4.1                         | 15.9                                   | 8.1                       |
| March 31, 2014     | 4.2                         | 14.9                                   | 9.1                       |

The increase in prepayments during the three months ended June 30, 2015 was primarily due to the effects of lower residential mortgage rates in the previous quarter.

The following tables summarize certain characteristics of the Company’s PT RMBS and structured RMBS mortgage related securities as of June 30, 2015 and December 31, 2014:

(\$ in thousands)

| Asset Category                     | Fair<br>Value | Percentage<br>of<br>Entire<br>Portfolio | Weighted<br>Average<br>Coupon | Weighted<br>Average<br>Maturity<br>in<br>Months | Longest<br>Maturity | Weighted<br>Average<br>Reset<br>in<br>Months | Weighted<br>Average<br>Coupon | Weighted<br>Average<br>Lifetime<br>Cap | Weighted<br>Average<br>Periodic<br>Cap |
|------------------------------------|---------------|-----------------------------------------|-------------------------------|-------------------------------------------------|---------------------|----------------------------------------------|-------------------------------|----------------------------------------|----------------------------------------|
| <b>June 30, 2015</b>               |               |                                         |                               |                                                 |                     |                                              |                               |                                        |                                        |
| Adjustable Rate RMBS               | \$ 3,456      | 0.2%                                    | 3.64%                         | 229                                             | 1-Sep-35            | 0.57                                         | 10.07%                        | 2.00%                                  |                                        |
| Fixed Rate RMBS                    | 1,993,369     | 91.7%                                   | 4.17%                         | 325                                             | 1-Jun-45            | NA                                           | NA                            | NA                                     |                                        |
| Hybrid Adjustable Rate RMBS        | 56,754        | 2.6%                                    | 2.56%                         | 331                                             | 1-Aug-43            | 90.84                                        | 7.56%                         | 2.00%                                  |                                        |
| Total Mortgage-backed Pass-through | 2,053,579     | 94.5%                                   | 4.12%                         | 325                                             | 1-Jun-45            | NA                                           | NA                            | NA                                     |                                        |
| Interest-Only Securities           | 78,347        | 3.6%                                    | 3.62%                         | 256                                             | 25-Apr-45           | NA                                           | NA                            | NA                                     |                                        |
| Inverse Interest-Only Securities   | 42,945        | 1.9%                                    | 6.20%                         | 324                                             | 15-Apr-45           | NA                                           | 6.38%                         | NA                                     |                                        |
| Total Structured RMBS              | 121,292       | 5.5%                                    | 4.53%                         | 280                                             | 25-Apr-45           | NA                                           | NA                            | NA                                     |                                        |
| Total Mortgage Assets              | \$ 2,174,871  | 100.0%                                  | 4.15%                         | 322                                             | 1-Jun-45            | NA                                           | NA                            | NA                                     |                                        |
| <b>December 31, 2014</b>           |               |                                         |                               |                                                 |                     |                                              |                               |                                        |                                        |
| Adjustable Rate RMBS               | \$ 3,794      | 0.2%                                    | 3.55%                         | 236                                             | 1-Sep-35            | 4.02                                         | 10.05%                        | 2.00%                                  |                                        |
| Fixed Rate RMBS                    | 1,412,593     | 91.2%                                   | 4.37%                         | 318                                             | 1-Dec-44            | NA                                           | NA                            | NA                                     |                                        |
|                                    | 70,400        | 4.6%                                    | 2.54%                         | 338                                             | 1-Aug-43            | 97.75                                        | 7.54%                         | 2.00%                                  |                                        |

|                             |              |        |       |     |           |    |       |    |
|-----------------------------|--------------|--------|-------|-----|-----------|----|-------|----|
| Hybrid Adjustable Rate RMBS |              |        |       |     |           |    |       |    |
| Total Mortgage-backed       |              |        |       |     |           |    |       |    |
| Pass-through                | 1,486,787    | 96.0%  | 4.28% | 319 | 1-Dec-44  | NA | NA    | NA |
| Interest-Only Securities    | 46,611       | 3.0%   | 3.95% | 248 | 25-Jan-43 | NA | NA    | NA |
| Inverse Interest-Only       |              |        |       |     |           |    |       |    |
| Securities                  | 15,773       | 1.0%   | 6.23% | 308 | 25-Apr-41 | NA | 6.39% | NA |
| Total Structured RMBS       | 62,384       | 4.0%   | 4.52% | 263 | 25-Jan-43 | NA | NA    | NA |
| Total Mortgage Assets       | \$ 1,549,171 | 100.0% | 4.29% | 317 | 1-Dec-44  | NA | NA    | NA |

(\$ in thousands)

| Agency          | June 30, 2015 |                                |   | December 31, 2014 |                                |   |
|-----------------|---------------|--------------------------------|---|-------------------|--------------------------------|---|
|                 | Fair Value    | Percentage of Entire Portfolio |   | Fair Value        | Percentage of Entire Portfolio |   |
| Fannie Mae      | \$1,716,523   | 78.9                           | % | \$1,243,923       | 80.3                           | % |
| Freddie Mac     | 437,182       | 20.1                           | % | 296,203           | 19.1                           | % |
| Ginnie Mae      | 21,166        | 1.0                            | % | 9,045             | 0.6                            | % |
| Total Portfolio | \$2,174,871   | 100.0                          | % | \$1,549,171       | 100.0                          | % |

|                                              | June 30,<br>2015 | December<br>31, 2014 |
|----------------------------------------------|------------------|----------------------|
| Weighted Average Pass-through Purchase Price | \$107.56         | \$107.88             |
| Weighted Average Structured Purchase Price   | \$14.02          | \$13.67              |
| Weighted Average Pass-through Current Price  | \$107.28         | \$108.59             |
| Weighted Average Structured Current Price    | \$15.49          | \$13.65              |
| Effective Duration (1)                       | 3.214            | 2.291                |

(1) Effective duration is the approximate percentage change in price for a 100 basis point change in rates. An effective duration of 3.214 indicates that an interest rate increase of 1.0% would be expected to cause a 3.214% decrease in the value of the RMBS in the Company's investment portfolio at June 30, 2015. An effective duration of 2.291 indicates that an interest rate increase of 1.0% would be expected to cause a 2.291% decrease in the value of the RMBS in the Company's investment portfolio at December 31, 2014. These figures include the structured securities in the portfolio, but do not include the effect of the Company's funding cost hedges. Effective duration quotes for individual investments are obtained from The Yield Book, Inc.

The following table presents a summary of portfolio assets acquired during the six months ended June 30, 2015 and 2014.

(\$ in thousands)

|                   | 2015        |               |                        |   | 2014       |               |                        |    |
|-------------------|-------------|---------------|------------------------|---|------------|---------------|------------------------|----|
|                   | Total Cost  | Average Price | Weighted Average Yield |   | Total Cost | Average Price | Weighted Average Yield |    |
| Pass-through RMBS | \$1,087,707 | \$107.63      | 2.62                   | % | \$926,148  | \$107.50      | 2.99                   | %  |
| Structured RMBS   | 59,583      | 14.55         | 2.80                   | % | 32,154     | 14.65         | (5.02)                 | )% |

#### Repurchase Agreements

As of June 30, 2015, we had established borrowing facilities in the repurchase agreement market with a number of commercial banks and other financial institutions and had borrowings in place with 20 of these counterparties. We believe these facilities provide borrowing capacity in excess of our needs. None of these lenders are affiliated with the Company. These borrowings are secured by the Company's RMBS and cash, and bear interest rates that are based on a spread to LIBOR.

As of June 30, 2015, we had obligations outstanding under the repurchase agreements of approximately \$2,014.1 million with a net weighted average borrowing cost of 0.39%. The remaining maturity of our outstanding repurchase agreements obligations ranged from 1 to 79 days, with a weighted average remaining maturity of 18 days. Securing the repurchase agreement obligations as of June 30, 2015 are RMBS with an estimated fair value, including accrued interest, of approximately \$2,123.6 million and a weighted average maturity of 324 months, and cash pledged to counterparties of approximately \$14.4 million. In June 2015, the Company purchased assets with a fair value of approximately \$7.6 million which settle in July 2015 that are expected to be funded by repurchase agreements. Through July 30, 2015, we have been able to maintain our repurchase facilities with comparable terms to those that existed at June 30, 2015 with maturities through October 6, 2015.



The table below presents information about our period end and average repurchase agreement obligations for each quarter in 2015 and 2014.

(\$ in thousands)

| Three Months Ended | Ending<br>Balance<br>of<br>Repurchase<br>Agreements | Average<br>Balance<br>of<br>Repurchase<br>Agreements | Difference Between<br>Ending<br>Repurchase Agreements<br>and<br>Average Repurchase<br>Agreements |         |      |
|--------------------|-----------------------------------------------------|------------------------------------------------------|--------------------------------------------------------------------------------------------------|---------|------|
|                    |                                                     |                                                      | Amount                                                                                           | Percent |      |
| June 30, 2015      | \$ 2,014,071                                        | \$ 1,736,781                                         | \$ 277,290                                                                                       | 15.97   | %(1) |
| March 31, 2015     | 1,459,490                                           | 1,448,071                                            | 11,419                                                                                           | 0.79    | %    |
| December 31, 2014  | 1,436,651                                           | 1,346,314                                            | 90,337                                                                                           | 6.71    | %    |
| September 30, 2014 | 1,255,978                                           | 1,019,839                                            | 236,139                                                                                          | 23.15   | %(2) |
| June 30, 2014      | 783,701                                             | 717,474                                              | 66,227                                                                                           | 9.23    | %    |
| March 31, 2014     | 651,246                                             | 484,902                                              | 166,344                                                                                          | 34.30   | %(3) |

- (1) The higher ending balance relative to the average balance during the quarter ended June 30, 2015 reflects the deployment of the proceeds, on a leveraged basis, of the Company's share issuances under the at the market equity offerings. During the quarter ended June 30, 2015, the Company's investment in PT RMBS increased \$457.4 million.
- (2) The higher ending balance relative to the average balance during the quarter ended September 30, 2014 reflects the deployment of the proceeds, on a leveraged basis, of the Company's share issuances under the at the market equity offerings. During the quarter ended September 30, 2014, the Company's investment in PT RMBS increased \$284.2 million.
- (3) The higher ending balance relative to the average balance during the quarter ended March 31, 2014 reflects the deployment of the proceeds, on a leveraged basis, of the Company's January and March 2014 equity offerings. During the quarter ended March 31, 2014, the Company's investment in PT RMBS increased \$374.5 million.

## Liquidity and Capital Resources

Liquidity is our ability to turn non-cash assets into cash, purchase additional investments, repay principal and interest on borrowings, fund overhead, fulfill margin calls and pay dividends. Our principal immediate sources of liquidity include cash balances, unencumbered assets and borrowings under repurchase agreements. Our borrowing capacity will vary over time as the market value of our interest earning assets varies. Our balance sheet also generates liquidity on an on-going basis through payments of principal and interest we receive on our RMBS portfolio. Management believes that we currently have sufficient liquidity and capital resources available for (a) the acquisition of additional investments consistent with the size and nature of our existing RMBS portfolio, (b) the repayments on borrowings and (c) the payment of dividends to the extent required for our continued qualification as a REIT. We may also generate liquidity from time to time by selling our equity or debt securities in public offerings or private placements.

Because our PT RMBS portfolio consists entirely of government and agency securities, we do not anticipate having difficulty converting our assets to cash should our liquidity needs ever exceed our immediately available sources of cash. Our structured RMBS portfolio also consists entirely of governmental agency securities, although they typically do not trade with comparable bid / ask spreads as PT RMBS. However, we anticipate that we would be able to

liquidate such securities readily, even in distressed markets, although we would likely do so at prices below where such securities could be sold in a more stable market. To enhance our liquidity even further, we may pledge a portion of our structured RMBS as part of a repurchase agreement funding, but retain the cash in lieu of acquiring additional assets. In this way we can, at a modest cost, retain higher levels of cash on hand and decrease the likelihood we will have to sell assets in a distressed market in order to raise cash.

Our master repurchase agreements have no stated expiration, but can be terminated at any time at our option or at the option of the counterparty. However, once a definitive repurchase agreement under a master repurchase agreement has been entered into, it generally may not be terminated by either party. A negotiated termination can occur, but may involve a fee to be paid by the party seeking to terminate the repurchase agreement transaction.

Under our repurchase agreement funding arrangements, we are required to post margin at the initiation of the borrowing. The margin posted represents the haircut, which is a percentage of the market value of the collateral pledged. To the extent the market value of the asset collateralizing the financing transaction declines, the market value of our posted margin will be insufficient and we will be required to post additional collateral. Conversely, if the market value of the asset pledged increases in value, we would be over collateralized and we would be entitled to have excess margin returned to us by the counterparty. Our lenders typically value our pledged securities daily to ensure the adequacy of our margin and make margin calls as needed, as do we. Typically, but not always, the parties agree to a minimum threshold amount for margin calls so as to avoid the need for nuisance margin calls on a daily basis. Our master repurchase agreements do not specify the haircut; rather haircuts are determined on an individual repurchase transaction basis. Throughout the six months ended June 30, 2015, haircuts on our pledged collateral remained stable and as of June 30, 2015, our weighted average haircut was approximately 5.4% of the value of our collateral.

As discussed earlier, we invest a portion of our capital in structured Agency RMBS. We do not apply leverage to this portion of our portfolio. The leverage inherent in structured securities replaces the leverage obtained by acquiring PT securities and funding them in the repurchase market. This structured RMBS strategy has been a core element of the Company's overall investment strategy since inception. However, we have and may continue to pledge a portion of our structured RMBS in order to raise our cash levels, but generally will not pledge these securities in order to acquire additional assets.

The following table summarizes the effect on our liquidity and cash flows from contractual obligations for repurchase agreements and interest expense on repurchase agreements.

(in thousands)

|                                              | Obligations Maturing |                          |                        |                         |             |
|----------------------------------------------|----------------------|--------------------------|------------------------|-------------------------|-------------|
|                                              | Within One<br>Year   | One to<br>Three<br>Years | Three to<br>Five Years | More than<br>Five Years | Total       |
| Repurchase agreements                        | \$2,014,071          | \$-                      | \$-                    | \$-                     | \$2,014,071 |
| Interest expense on repurchase agreements(1) | 981                  | -                        | -                      | -                       | 981         |
| Unsettled securities purchased               | 7,623                | -                        | -                      | -                       | 7,623       |
| Totals                                       | \$2,022,675          | \$-                      | \$-                    | \$-                     | \$2,022,675 |

(1) Interest expense on repurchase agreements is based on current interest rates as of June 30, 2015 and the remaining term of the liabilities existing at that date.

In future periods, we expect to continue to finance our activities in a manner that is consistent with our current operations via repurchase agreements. As of June 30, 2015, we had cash and cash equivalents of \$100.5 million. We generated cash flows of \$139.0 million from principal and interest payments on our RMBS and had average repurchase agreements outstanding of \$1,592.4 million during the six months ended June 30, 2015. During the three months ended June 30, 2015, we generated cash flows of \$82.0 million from principal and interest payments on our RMBS and had average repurchase agreements outstanding of \$1,736.8 million.

#### Stockholders' Equity

In January 2014, we completed a public offering of 2,070,000 shares of our common stock (including 270,000 shares sold pursuant to the full exercise of the overallotment option granted to the underwriters which closed on January 29, 2014) for aggregate net proceeds of approximately \$24.2 million after deducting underwriters' discounts and

commissions and offering expenses.

In March 2014, we completed a public offering of 3,680,000 shares of our common stock (including 480,000 shares sold pursuant to the full exercise of the overallotment option granted to the underwriters which closed on April 11, 2014) for aggregate net proceeds of approximately \$44.0 million after deducting underwriters' discounts and commissions and offering expenses.

On June 17, 2014, we entered into an equity distribution agreement (the “June 2014 Equity Distribution Agreement”) with two sales agents pursuant to which we could offer and sell, from time to time, up to an aggregate amount of \$35,000,000 of shares of our common stock in transactions that were deemed to be “at the market” offerings and privately negotiated transactions. We issued a total of 2,528,416 shares under the June 2014 Equity Distribution Agreement for aggregate proceeds of approximately \$34.2 million, net of commissions and fees, prior to its termination.

On September 3, 2014, we entered into a second equity distribution agreement (the “September 2014 Equity Distribution Agreement”) with two sales agents pursuant to which we could offer and sell, from time to time, up to an aggregate amount of \$75,000,000 of shares of our common stock in transactions that were deemed to be “at the market” offerings and privately negotiated transactions. The September 2014 Equity Distribution Agreement replaced the June 2014 Equity Distribution Agreement. We issued a total of 5,087,646 shares under the September 2014 Equity Distribution Agreement for aggregate proceeds of approximately \$69.1 million, net of commissions and fees, prior to its termination.

On March 2, 2015, we entered into a third equity distribution agreement (the “March 2015 Equity Distribution Agreement”) with two sales agents pursuant to which we may offer and sell, from time to time, up to an aggregate amount of \$100,000,000 of shares of our common stock in transactions that are deemed to be “at the market” offerings and privately negotiated transactions. The March 2015 Equity Distribution Agreement replaced the September 2014 Equity Distribution Agreement. Through June 30, 2015, we issued a total of 6,221,102 shares under March 2015 Equity Distribution Agreement for aggregate proceeds of approximately \$83.1 million, net of commissions and fees.

## Outlook

### Interest Rates

Volatility in global interest rates continued in the second quarter of 2015. Interest rates rose across all sectors in the global bond markets, thereby depressing bond prices across sectors. Spreads on treasuries of the same durations as Agency RMBS incrementally widened during the second quarter, putting downward pressure on book value for many mortgage REITs. Both U.S. Treasuries and Agency RMBS yields ended the second quarter higher than the close of the first quarter 2015. The rise in rates was led by growing sentiment that the European economies are recovering and the need for continued aggressive monetary stimulus by the European Central Bank (the “ECB”) would diminish somewhat over the next few quarters. However, European markets decreased during the second quarter primarily due to fears stoked by uncertainty over Greek sovereign finances and its future as an ECB member and a member of the Eurozone.

We believe that the U.S. economy appears to be on a trajectory of slow, sustainable growth. The consensus forecast for 2015 economic growth in the U.S. remains at approximately 2.7%, accompanied by moderate growth in payrolls and inflation within the Federal Reserve's target range. The Federal Reserve continues to guide capital markets to anticipate the possibility of an interest rate hike in September or December 2015. Federal Reserve Chair Yellen, in her June 17, 2015 remarks following the June Federal Reserve Open Market Committee (“FOMC”) policy meeting, stated that she anticipates a long period of continued accommodative monetary policy following an initial rise in the Federal Funds Rate later this year. These statements, which Chair Yellen reiterated in Congressional testimony on July 15-16, 2015, generally are in line with market participants' expectations for the balance of 2015. As of June 30, 2015, the bond market appears to have priced in an increase in the federal funds rate in September 2015 and a slow rise over the next few years. With the Federal Reserve ostensibly tying the start of interest rate increases to evidence of further improvement in the economy, data releases remain materially influential events. We believe that data dependency and analysis of the Federal Reserve will continue to drive the direction and volatility of U.S. rates, with the uncertainty that this dynamic creates further enhancing volatility in the interest rate and fixed income markets.



## Recent Regulatory Developments

In March 2015, housing and mortgage financial reform legislation, H.R. 1491, was proposed by congressmen John Delaney (D-MD), John Camey (D-DE) and James A. Himes (D-CT), each of whom is a member of the House Financial Services Committee. The bill is called The Partnership to Strengthen Homeownership Act, and is similar to one introduced by the same congressmen in the last Congress (H.R. 5055), which never made it out of committee. Under this proposed legislation, all government guaranteed single-family and multi-family mortgage-backed securities will be supported by a minimum of 5% private sector capital, which will stand in a first loss position. The remaining 95% of the risk will be shared between Ginnie Mae and a private reinsurer on a pari passu basis. Fees paid to Ginnie Mae for providing these securities will be allocated to affordable housing programs. Under the bill, Freddie Mac and Fannie Mae would be wound down over a five-year period, and their multifamily businesses will be spun out as separate entities. Ginnie Mae would be required to create and implement a workable multifamily guarantee that utilizes private sector pricing consistent with the single family model. The GSEs' current multifamily businesses would continue to function within the new multifamily housing market as purely private organizations with an explicit government guarantee provided by Ginnie Mae and a private sector reinsurer.

In May 2015, Senate Banking Committee Chairman Richard Shelby (R-AL) released a draft bill entitled The Regulatory Relief Bill of 2015 (the "Regulatory Relief Bill"). If enacted, this bill would increase the threshold for a financial institution to be deemed a Systemically Important Financial Institution ("SIFI") from \$50 billion to \$500 billion while giving the Financial Stability Oversight Council discretion to designate banks with greater than \$50 billion in assets as SIFIs, give non-banks an opportunity to file a remedial plan addressing regulators' concerns before being designated as SIFIs, require an affirmative vote every five-years to renew the SIFI designation of non-banks, provide regulatory relief for community banks and broaden the Consumer Financial Protection Bureau Qualified Mortgage rule.

We expect debate and discussion on residential housing and mortgage reform to continue in 2015. However, we cannot be certain if H.R. 1491, the Regulatory Relief Bill or any other housing- and/or mortgage-related bill will be approved by Congress, and if so, what the effect will be.

## Effect on Us

Regulatory developments, movements in interest rates and prepayment rates as well as loan modification programs affect us in many ways, including the following:

### Effects on our Assets

A change in or elimination of the guarantee structure of Agency RMBS may increase our costs (if, for example, guarantee fees increase) or require us to change our investment strategy altogether. For example, the elimination of the guarantee structure of Agency RMBS may cause us to change our investment strategy to focus on non-Agency RMBS, which in turn would require us to significantly increase our monitoring of the credit risks of our investments in addition to interest rate and prepayment risks.

Lower long-term interest rates can affect the value of our Agency RMBS in a number of ways. If prepayment rates are relatively low (due, in part, to the refinancing problems described above), lower long-term interest rates can increase the value of higher-coupon Agency RMBS. This is because investors typically place a premium on assets with yields that are higher than market yields. Although lower long-term interest rates may increase asset values in our portfolio, we may not be able to invest new funds in similarly-yielding assets.



If prepayment levels increase, the value of our Agency RMBS affected by such prepayments may decline. This is because a principal prepayment accelerates the effective term of an Agency RMBS, which would shorten the period during which an investor would receive above-market returns (assuming the yield on the prepaid asset is higher than market yields). Also, prepayment proceeds may not be able to be reinvested in similar-yielding assets. Agency RMBS backed by mortgages with high interest rates are more susceptible to prepayment risk because holders of those mortgages are most likely to refinance to a lower rate. IOs and IIOs, however, may be the types of Agency RMBS most sensitive to increased prepayment rates. Because the holder of an IO or IIO receives no principal payments, the values of IOs and IIOs are entirely dependent on the existence of a principal balance on the underlying mortgages. If the principal balance is eliminated due to prepayment, IOs and IIOs essentially become worthless. Although increased prepayment rates can negatively affect the value of our IOs and IIOs, they have the opposite effect on POs. Because POs act like zero-coupon bonds, meaning they are purchased at a discount to their par value and have an effective interest rate based on the discount and the term of the underlying loan, an increase in prepayment rates would reduce the effective term of our POs and accelerate the yields earned on those assets, which would increase our net income.

Because we base our investment decisions on risk management principles rather than anticipated movements in interest rates, in a volatile interest rate environment we may allocate more capital to structured Agency RMBS with shorter durations, such as short-term fixed and floating rate CMOs. We believe these securities have a lower sensitivity to changes in long-term interest rates than other asset classes. We may attempt to mitigate our exposure to changes in long-term interest rates by investing in IOs and IIOs, which typically have different sensitivities to changes in long-term interest rates than pass-through Agency RMBS, particularly pass-through Agency RMBS backed by fixed-rate mortgages.

We do not believe our investment portfolio will be materially affected by loan modification programs because Agency RMBS backed by loans that would qualify for such programs (e.g., seriously delinquent loans) will be purchased by Fannie Mae and Freddie Mac at their par value prior to the implementation of such programs. However, if Fannie Mae and Freddie Mac were to modify or end their repurchase programs or if the U.S. Government modified its loan modification programs to modify non-delinquent mortgage loans, our investment portfolio could be negatively impacted.

#### Effects on our borrowing costs

We leverage our pass-through Agency RMBS portfolio and a portion of our structured Agency RMBS with principal balances through the use of short-term repurchase agreement transactions. The interest rates on our debt are determined by market levels of both the Federal Funds Rate and LIBOR. An increase in the U.S. Federal Funds Rate or LIBOR would increase our borrowing costs, which could affect our interest rate spread if there is no corresponding increase in the interest we earn on our assets. This would be most prevalent with respect to our Agency RMBS backed by fixed rate mortgage loans because the interest rate on a fixed-rate mortgage loan does not change even though market rates may change.

In order to protect our net interest margin against increases in short-term interest rates, we may enter into interest rate swaps, which effectively convert our floating-rate repurchase agreement debt to fixed-rate debt, or utilize other hedging instruments such as Eurodollar futures contracts or interest rate swaptions.

#### Summary

Over the past several quarters there has been a relatively large spread between short and long-term interest rates has positively affected our net interest margin. However, if prepayment rates remain elevated or accelerate further they

could continue to negatively affect our net interest margin and the value of our assets. Furthermore, increases in the Federal Funds Rate and LIBOR could significant increase our financing costs, which could lower our net interest margin.

### Critical Accounting Policies

Our financial statements are prepared in accordance with GAAP. GAAP requires our management to make some complex and subjective decisions and assessments. Our most critical accounting policies involve decisions and assessments which could significantly affect reported assets, liabilities, revenues and expenses. There have been no changes to our critical accounting policies as discussed in our annual report on Form 10-K for the year ended December 31, 2014.

### Capital Expenditures

At June 30, 2015, we had no material commitments for capital expenditures.

### Off-Balance Sheet Arrangements

At June 30, 2015, we did not have any off-balance sheet arrangements.

### Dividends

In addition to other requirements, to qualify as a REIT, we must pay annual dividends to our stockholders of at least 90% of our REIT taxable income, determined without regard to the deduction for dividends paid and excluding any net capital gains. We intend to pay regular monthly dividends to our stockholders and have declared the following dividends during 2015 and 2014.

(in thousands, except per share amounts)

| Declaration Date  | Record Date        | Payment Date       | Per Share Amount | Total           |
|-------------------|--------------------|--------------------|------------------|-----------------|
| <b>2015</b>       |                    |                    |                  |                 |
| July 9, 2015(1)   | July 27, 2015      | July 31, 2015      | \$0.14           | \$3,218         |
| June 9, 2015      | June 22, 2015      | June 30, 2015      | 0.18             | 4,057           |
| May 11, 2015      | May 26, 2015       | May 29, 2015       | 0.18             | 3,580           |
| April 9, 2015     | April 27, 2015     | April 30, 2015     | 0.18             | 3,303           |
| March 10, 2015    | March 27, 2015     | March 31, 2015     | 0.18             | 3,205           |
| February 10, 2015 | February 25, 2015  | February 27, 2015  | 0.18             | 3,017           |
| January 13, 2015  | January 26, 2015   | January 30, 2015   | 0.18             | 3,017           |
| <b>Totals</b>     |                    |                    | <b>\$1.22</b>    | <b>\$23,397</b> |
| <b>2014</b>       |                    |                    |                  |                 |
| December 9, 2014  | December 26, 2014  | December 30, 2014  | \$0.18           | \$3,004         |
| November 12, 2014 | November 25, 2014  | November 28, 2014  | 0.18             | 2,737           |
| October 9, 2014   | October 28, 2014   | October 31, 2014   | 0.18             | 2,358           |
| September 9, 2014 | September 25, 2014 | September 30, 2014 | 0.18             | 2,348           |
| August 12, 2014   | August 26, 2014    | August 29, 2014    | 0.18             | 1,999           |
| July 10, 2014     | July 28, 2014      | July 31, 2014      | 0.18             | 1,759           |
| June 11, 2014     | June 25, 2014      | June 30, 2014      | 0.18             | 1,712           |
| May 8, 2014       | May 27, 2014       | May 30, 2014       | 0.18             | 1,641           |
| April 8, 2014     | April 25, 2014     | April 30, 2014     | 0.18             | 1,636           |
| March 11, 2014    | March 26, 2014     | March 31, 2014     | 0.18             | 1,550           |

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|                   |                   |                   |        |          |
|-------------------|-------------------|-------------------|--------|----------|
| February 11, 2014 | February 25, 2014 | February 28, 2014 | 0.18   | 974      |
| January 9, 2014   | January 27, 2014  | January 31, 2014  | 0.18   | 925      |
| Totals            |                   |                   | \$2.16 | \$22,643 |

- (1) The effect of the dividend declared in July 2015 is not reflected in the Company's financial statements as of June 30, 2015

## Inflation

Virtually all of our assets and liabilities are interest rate sensitive in nature. As a result, interest rates and other factors influence our performance far more so than does inflation. Changes in interest rates do not necessarily correlate with inflation rates or changes in inflation rates. Our financial statements are prepared in accordance with GAAP and our distributions will be determined by our Board of Directors consistent with our obligation to distribute to our stockholders at least 90% of our REIT taxable income on an annual basis in order to maintain our REIT qualification; in each case, our activities and balance sheet are measured with reference to historical cost and/or fair market value without considering inflation.

## Jumpstart Our Business Startups Act of 2012

We are an “emerging growth company” as defined in the Jumpstart Our Business Startups Act of 2012 (the “JOBS Act”). The JOBS Act permits emerging growth companies to take advantage of an extended transition period to comply with new or revised accounting standards applicable to public companies. We have elected to “opt out” of this provision and, as a result, we will be required to comply with new or revised accounting standards as required when they are adopted. The decision to opt out of the extended transition period under the JOBS Act is irrevocable.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the exposure to loss resulting from changes in market factors such as interest rates, foreign currency exchange rates, commodity prices and equity prices. The primary market risks that we are exposed to are interest rate risk, prepayment risk, spread risk, liquidity risk, extension risk and counterparty credit risk.

### Interest Rate Risk

Interest rate risk is highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control.

Changes in the general level of interest rates can affect our net interest income, which is the difference between the interest income earned on interest-earning assets and the interest expense incurred in connection with our interest-bearing liabilities, by affecting the spread between our interest-earning assets and interest-bearing liabilities. Changes in the level of interest rates can also affect the rate of prepayments of our securities and the value of the RMBS that constitute our investment portfolio, which affects our net income and ability to realize gains from the sale of these assets and impacts our ability to borrow and the amount that we can borrow against these securities.

We may utilize a variety of financial instruments in order to limit the effects of changes in interest rates on our operations. The principal instruments that we use are futures contracts and options to enter into interest rate swaps. These instruments are intended to serve as a hedge against future interest rate increases on our repurchase agreement borrowings. Hedging techniques are partly based on assumed levels of prepayments of our Agency RMBS. If prepayments are slower or faster than assumed, the life of the Agency RMBS will be longer or shorter, which would reduce the effectiveness of any hedging strategies we may use and may cause losses on such transactions. Hedging strategies involving the use of derivative securities are highly complex and may produce volatile returns. Hedging techniques are also limited by the rules relating to REIT qualification. In order to preserve our REIT status, we may be forced to terminate a hedging transaction at a time when the transaction is most needed.

Our profitability and the value of our investment portfolio (including derivatives used for hedging purposes) may be adversely affected during any period as a result of changing interest rates including changes in the forward yield curve.

Our portfolio of PT RMBS is typically comprised of adjustable-rate RMBS, fixed-rate RMBS and hybrid adjustable-rate RMBS. We generally seek to acquire low duration assets that offer high levels of protection from mortgage prepayments provided they are reasonably priced by the market. Although the duration of an individual asset can change as a result of changes in interest rates, we strive to maintain a hedged PT RMBS portfolio with an effective duration of less than 2.0. The stated contractual final maturity of the mortgage loans underlying our portfolio of PT RMBS generally ranges up to 30 years. However, the effect of prepayments of the underlying mortgage loans tends to shorten the resulting cash flows from our investments substantially. Prepayments occur for various reasons, including refinancing of underlying mortgages and loan payoffs in connection with home sales.

The duration of our IO and IIO portfolios will vary greatly depending on the structural features of the securities. While prepayment activity will always affect the cash flows associated with the securities, the interest only nature of IOs may cause their durations to become extremely negative when prepayments are high, and less negative when prepayments are low. Prepayments affect the durations of IIOs similarly, but the floating rate nature of the coupon of IIOs (which is inversely related to the level of one month LIBOR) cause their price movements, and model duration, to be affected by changes in both prepayments and one month LIBOR, both current and anticipated levels. As a result, the duration of IIO securities will also vary greatly.

Prepayments on the loans underlying our RMBS can alter the timing of the cash flows from the underlying loans to us. As a result, we gauge the interest rate sensitivity of our assets by measuring their effective duration. While modified duration measures the price sensitivity of a bond to movements in interest rates, effective duration captures both the movement in interest rates and the fact that cash flows to a mortgage related security are altered when interest rates move. Accordingly, when the contract interest rate on a mortgage loan is substantially above prevailing interest rates in the market, the effective duration of securities collateralized by such loans can be quite low because of expected prepayments.

We face the risk that the market value of our PT RMBS assets will increase or decrease at different rates than that of our structured RMBS or liabilities, including our hedging instruments. Accordingly, we assess our interest rate risk by estimating the duration of our assets and the duration of our liabilities. We generally calculate duration using various third party models. However, empirical results and various third party models may produce different duration numbers for the same securities.

The following sensitivity analysis shows the estimated impact on the fair value of our interest rate-sensitive investments and hedge positions as of June 30, 2015 and December 31, 2014, assuming rates instantaneously fall 100 basis points ("bps"), fall 50 bps, rise 50 bps and rise 100 bps, adjusted to reflect the impact of convexity, which is the measure of the sensitivity of our hedge positions and Agency RMBS' effective duration to movements in interest rates.

All changes in value in the table below are measured as percentage changes from the investment portfolio value and net asset value at the base interest rate scenario. The base interest rate scenario assumes interest rates and prepayment projections as of June 30, 2015 and December 31, 2014. We apply a floor of 0% for the down rate scenarios on our interest bearing liabilities and hedge positions, such that any hypothetical interest rate decrease would have a limited positive impact on our funding costs beyond a certain level.

Actual results could differ materially from estimates, especially in the current market environment. To the extent that these estimates or other assumptions do not hold true, which is likely in a period of high price volatility, actual results will likely differ materially from projections and could be larger or smaller than the estimates in the table below. Moreover, if different models were employed in the analysis, materially different projections could result. Lastly, while the table below reflects the estimated impact of interest rate increases and decreases on a static portfolio, we

may from time to time sell any of our agency securities as a part of our overall management of our investment portfolio.

## Interest Rate Sensitivity(1)

| Change in Interest Rate | Portfolio<br>Market<br>Value(2)(3) |    | Book<br>Value(2)(4) |    |
|-------------------------|------------------------------------|----|---------------------|----|
| As of June 30, 2015     |                                    |    |                     |    |
| -100 Basis Points       | (0.18                              | )% | (1.36               | )% |
| -50 Basis Points        | 0.26                               | %  | 2.01                | %  |
| +50 Basis Points        | (0.92                              | )% | (7.07               | )% |
| +100 Basis Points       | (2.34                              | )% | (17.90              | )% |
| As of December 31, 2014 |                                    |    |                     |    |
| -100 Basis Points       | (0.79                              | )% | (5.63               | )% |
| -50 Basis Points        | (0.13                              | )% | (0.89               | )% |
| +50 Basis Points        | (0.30                              | )% | (2.10               | )% |
| +100 Basis Points       | (0.94                              | )% | (6.64               | )% |

(1) Interest rate sensitivity is derived from models that are dependent on inputs and assumptions provided by third parties as well as by our Manager, and assumes there are no changes in mortgage spreads and assumes a static portfolio. Actual results could differ materially from these estimates.

(2) Includes the effect of derivatives and other securities used for hedging purposes.

(3) Estimated dollar change in investment portfolio value expressed as a percent of the total fair value of our investment portfolio as of such date.

(4) Estimated dollar change in portfolio value expressed as a percent of stockholders' equity as of such date.

In addition to changes in interest rates, other factors impact the fair value of our interest rate-sensitive investments, such as the shape of the yield curve, market expectations as to future interest rate changes and other market conditions. Accordingly, in the event of changes in actual interest rates, the change in the fair value of our assets would likely differ from that shown above and such difference might be material and adverse to our stockholders.

## Prepayment Risk

Because residential borrowers have the option to prepay their mortgage loans at par at any time, we face the risk that we will experience a return of principal on our investments faster than anticipated. Various factors affect the rate at which mortgage prepayments occur, including changes in the level of and directional trends in housing prices, interest rates, general economic conditions, loan age and size, loan-to-value ratio, the location of the property and social and demographic conditions. Additionally, changes to GSE underwriting practices or other governmental programs could also significantly impact prepayment rates or expectations. Generally, prepayments on Agency RMBS increase during periods of falling mortgage interest rates and decrease during periods of rising mortgage interest rates. However, this may not always be the case. We may reinvest principal repayments at a yield that is lower or higher than the yield on the repaid investment, thus affecting our net interest income by altering the average yield on our assets.

## Spread Risk

When the market spread widens between the yield on our Agency RMBS and benchmark interest rates, our net book value could decline if the value of our agency securities fall by more than the offsetting fair value increases on our hedging instruments tied to the underlying benchmark interest rates. We refer to this as "spread risk" or "basis risk." The spread risk associated with our mortgage assets and the resulting fluctuations in fair value of these securities can occur independent of changes in benchmark interest rates and may relate to other factors impacting the mortgage and

fixed income markets, such as actual or anticipated monetary policy actions by the Federal Reserve, market liquidity, or changes in required rates of return on different assets. Consequently, while we use futures contracts and interest rate swaps and swaptions to attempt to protect against moves in interest rates, such instruments typically will not protect our net book value against spread risk.

## Liquidity Risk

The primary liquidity risk for us arises from financing long-term assets with shorter-term borrowings through repurchase agreements. Our assets that are pledged to secure repurchase agreements are Agency RMBS and cash. As of June 30, 2015, we had unrestricted cash and cash equivalents of \$100.5 million and unpledged securities of approximately \$59.0 million (not including securities pledged to us) available to meet margin calls on our repurchase agreements and derivative contracts and for other corporate purposes. However, should the value of our Agency RMBS pledged as collateral or the value of our derivative instruments suddenly decrease, margin calls relating to our repurchase and derivative agreements could increase, causing an adverse change in our liquidity position. Further, there is no assurance that we will always be able to renew (or roll) our repurchase agreements. In addition, our counterparties have the option to increase our haircuts (margin requirements) on the assets we pledge, against repurchase agreements thereby reducing the amount that can be borrowed against an asset even if they agree to renew or roll the repurchase agreement. Significantly higher haircuts can reduce our ability to leverage our portfolio or even force us to sell assets, especially if correlated with asset price declines or faster prepayment rates on our assets.

## Extension Risk

The projected weighted average life and the duration (or interest rate sensitivity) of our investments is based on our Manager's assumptions regarding the rate at which the borrowers will prepay the underlying mortgage loans. In general, we use futures contracts and interest rate swaptions to help manage our funding cost on our investments in the event that interest rates rise. These hedging instruments allow us to reduce our funding exposure on the notional amount of the instrument for a specified period of time.

However, if prepayment rates decrease in a rising interest rate environment, the average life or duration of our fixed-rate assets or the fixed-rate portion of the ARMs or other assets generally extends. This could have a negative impact on our results from operations, as our hedging instrument expirations are fixed and will, therefore, cover a smaller percentage of our funding exposure on our mortgage assets to the extent that their average lives increase due to slower prepayments. This situation may also cause the market value of our agency securities collateralized by fixed rate mortgages or hybrid ARMs to decline by more than otherwise would be the case while most of our hedging instruments would not receive any incremental offsetting gains. In extreme situations, we may be forced to sell assets to maintain adequate liquidity, which could cause us to incur realized losses.

## Counterparty Credit Risk

We are exposed to counterparty credit risk relating to potential losses that could be recognized in the event that the counterparties to our repurchase agreements and derivative contracts fail to perform their obligations under such agreements. The amount of assets we pledge as collateral in accordance with our agreements varies over time based on the market value and notional amount of such assets as well as the value of our derivative contracts. In the event of a default by a counterparty, we may not receive payments provided for under the terms of our agreements and may have difficulty obtaining our assets pledged as collateral under such agreements. Our credit risk related to certain derivative transactions is largely mitigated through daily adjustments to collateral pledged based on changes in market value and we limit our counterparties to major financial institutions with acceptable credit ratings. However, there is no guarantee our efforts to manage counterparty credit risk will be successful and we could suffer significant losses if unsuccessful.



#### ITEM 4. CONTROLS AND PROCEDURES

##### Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report (the “evaluation date”), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer (the “CEO”) and Chief Financial Officer (the “CFO”), of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (“Exchange Act”). Based on this evaluation, the CEO and CFO concluded our disclosure controls and procedures, as designed and implemented, were effective as of the evaluation date (1) in ensuring that information regarding the Company is accumulated and communicated to our management, including our CEO and CFO, by our employees, as appropriate to allow timely decisions regarding required disclosure and (2) in providing reasonable assurance that information we must disclose in its periodic reports under the Exchange Act is recorded, processed, summarized and reported within the time periods prescribed by the SEC’s rules and forms.

##### Changes in Internal Controls over Financial Reporting

There were no significant changes in the Company’s internal control over financial reporting that occurred during the Company’s most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are not party to any material pending legal proceedings as described in Item 103 of Regulation S-K.

ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors disclosed in the “Risk Factors” section of our Annual Report on Form 10-K filed with the SEC on February 24, 2015.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The Company did not issue or sell equity securities that were not registered under the Securities Act during the three months ended June 30, 2015.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

ITEM 5. OTHER INFORMATION

None.

## ITEM 6. EXHIBITS

### Exhibit No.

- 3.1 Articles of Amendment and Restatement of Orchid Island Capital, Inc. (filed as Exhibit 3.1 to the Company's Registration Statement on Amendment No. 1 to Form S-11 (File No.333-184538) filed on November 28, 2012 and incorporated herein by reference).
- 3.2 Amended and Restated Bylaws of Orchid Island Capital, Inc. (filed as Exhibit 3.2 to the Company's Registration Statement on Amendment No. 1 to Form S-11 (File No.333-184538) filed on November 28, 2012 and incorporated herein by reference).
- 10.1 Equity Distribution Agreement, dated March 2, 2015, by and between Orchid Island Capital, Inc., Bimini Advisors, LLC, Ladenburg Thalmann & Co., Inc. and Mitsubishi UFJ Securities (USA), Inc. (incorporated by reference to Exhibit 1.1 to the Registrant's Form 8-K filed with the Securities Exchange Commission on March 2, 2015).
- 31.1 Certification of Robert E. Cauley, Chief Executive Officer and President of the Registrant, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 31.2 Certification of G. Hunter Haas, IV, Chief Financial Officer of the Registrant, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 32.1 Certification of Robert E. Cauley, Chief Executive Officer and President of the Registrant, pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*
- 32.2 Certification of G. Hunter Haas, IV, Chief Financial Officer of the Registrant, pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*

|                      |                                                                       |
|----------------------|-----------------------------------------------------------------------|
| Exhibit 101.INS XBRL | Instance Document ***                                                 |
| Exhibit 101.SCH XBRL | Taxonomy Extension Schema Document ***                                |
| Exhibit 101.CAL XBRL | Taxonomy Extension Calculation Linkbase Document***                   |
| Exhibit 101.DEF XBRL | Additional Taxonomy Extension Definition Linkbase Document Created*** |
| Exhibit 101.LAB XBRL | Taxonomy Extension Label Linkbase Document ***                        |
| Exhibit 101.PRE XBRL | Taxonomy Extension Presentation Linkbase Document ***                 |

|     |                                    |
|-----|------------------------------------|
| *   | Filed herewith.                    |
| **  | Furnished herewith.                |
| *** | Submitted electronically herewith. |

Signatures

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

Orchid Island Capital, Inc.  
Registrant

|       |               |                                                                                                                                                                |
|-------|---------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Date: | July 30, 2015 | By: /s/ Robert E. Cauley<br>Robert E. Cauley<br>Chief Executive Officer, President and Chairman of the Board                                                   |
| Date: | July 30, 2015 | By: /s/ G. Hunter Haas, IV<br>G. Hunter Haas, IV<br>Secretary, Chief Financial Officer, Chief Investment Officer and Director<br>(Principal Financial Officer) |

# INDEX TO EXHIBITS

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