

STARWOOD PROPERTY TRUST, INC.

Form 10-K

February 23, 2017

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10 K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016

or

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

For the transition period from            to

Commission file number 001 34436

Starwood Property Trust, Inc.

(Exact name of registrant as specified in its charter)

Maryland	27 0247747
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
591 West Putnam Avenue	
Greenwich, Connecticut	06830
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code (203) 422 7700

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

Title of each class	Name of each exchange on which registered
Common Stock, \$0.01 par value per share	New York Stock Exchange

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

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

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

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

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

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

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

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

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

As of June 30, 2016, the aggregate market value of the voting stock held by non affiliates was \$4,766,928,850 based on the reported last sale price of our common stock on June 30, 2016. Shares of our common stock held by affiliates, which includes officers and directors of the registrant, have been excluded from this calculation. This calculation does not reflect a determination that persons are affiliates for any other purposes.

The number of shares of the issuer's common stock, \$0.01 par value, outstanding as of February 16, 2017 was 259,278,525.

#### DOCUMENTS INCORPORATED BY REFERENCE

Documents Incorporated By Reference: The information required by Part III of this Form 10 K, to the extent not set forth herein or by amendment, is incorporated by reference from the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A on or prior to May 1, 2017.



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Special Note Regarding Forward Looking Statements

This Annual Report on Form 10-K contains certain forward-looking statements, including without limitation, statements concerning our operations, economic performance and financial condition. These forward-looking statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are developed by combining currently available information with our beliefs and assumptions and are generally identified by the words “believe,” “expect,” “anticipate” and other similar expressions. Forward-looking statements do not guarantee future performance, which may be materially different from that expressed in, or implied by, any such statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their respective dates.

These forward-looking statements are based largely on our current beliefs, assumptions and expectations of our future performance taking into account all information currently available to us. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to us or within our control, and which could materially affect actual results, performance or achievements. Factors that may cause actual results to vary from our forward-looking statements include, but are not limited to:

- factors described in this Annual Report on Form 10 K, including those set forth under the captions “Risk Factors” and “Business”;
- defaults by borrowers in paying debt service on outstanding indebtedness;
- impairment in the value of real estate property securing our loans or in which we invest;
- availability of mortgage origination and acquisition opportunities acceptable to us;
- potential mismatches in the timing of asset repayments and the maturity of the associated financing agreements;
- national and local economic and business conditions;
- general and local commercial and residential real estate property conditions;
- changes in federal government policies;
- changes in federal, state and local governmental laws and regulations;
- increased competition from entities engaged in mortgage lending and securities investing activities;
- changes in interest rates; and
- the availability of, and costs associated with, sources of liquidity.

In light of these risks and uncertainties, there can be no assurances that the results referred to in the forward-looking statements contained in this Annual Report on Form 10-K will in fact occur. Except to the extent required by applicable law or regulation, we undertake no obligation to, and expressly disclaim any such obligation to, update or revise any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, changes to future results over time or otherwise.

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PART I

Item 1. Business.

The following description of our business should be read in conjunction with the information included elsewhere in this Annual Report on Form 10 K for the year ended December 31, 2016. This discussion contains forward looking statements that involve risks and uncertainties. Actual results could differ significantly from the results discussed in the forward looking statements due to the factors set forth in “Risk Factors” and elsewhere in this Annual Report on Form 10 K. References in this Annual Report on Form 10 K to “we,” “our,” “us,” or the “Company” refer to Starwood Property Trust, Inc. and its subsidiaries.

General

Starwood Property Trust, Inc. (“STWD” and, together with its subsidiaries, “we” or the “Company”) is a Maryland corporation that commenced operations in August 2009, upon the completion of our initial public offering (“IPO”). We are focused primarily on originating, acquiring, financing and managing commercial mortgage loans and other commercial real estate debt investments, commercial mortgage backed securities (“CMBS”), and other commercial real estate investments in both the U.S. and Europe. We refer to the following as our target assets: commercial real estate mortgage loans, preferred equity interests, CMBS and other commercial real estate related debt investments. Our target assets may also include residential mortgage backed securities (“RMBS”), certain residential mortgage loans, distressed or non performing commercial loans, commercial properties subject to net leases and equity interests in commercial real estate. As market conditions change over time, we may adjust our strategy to take advantage of changes in interest rates and credit spreads as well as economic and credit conditions.

We have three reportable business segments as of December 31, 2016:

- Real estate lending (the “Lending Segment”)—engages primarily in originating, acquiring, financing and managing commercial first mortgages, subordinated mortgages, mezzanine loans, preferred equity, CMBS, RMBS and other real estate and real estate-related debt investments in both the U.S. and Europe that are held-for-investment.
- Real estate investing and servicing (the “Investing and Servicing Segment”)—includes (i) a servicing business in the U.S. that manages and works out problem assets, (ii) an investment business that selectively acquires and manages unrated, investment grade and non-investment grade rated CMBS, including subordinated interests of securitization and resecuritization transactions, (iii) a mortgage loan business which originates conduit loans for the primary purpose of selling these loans into securitization transactions, and (iv) an investment business that selectively acquires commercial real estate assets, including properties acquired from CMBS trusts. This segment excludes the consolidation of securitization variable interest entities (“VIEs”).
- Real estate property (the “Property Segment”)—engages primarily in acquiring and managing equity interests in stabilized commercial real estate properties, including multi-family properties, that are held for investment.

On January 31, 2014, we completed the spin off of our former single family residential (“SFR”) segment to our stockholders as discussed further in Note 3 of our consolidated financial statements included herein (our “Consolidated Financial Statements”).

On April 19, 2013, we acquired the equity of LNR Property LLC (“LNR”) and certain of its subsidiaries for \$730.5 million. LNR represents our Investing and Servicing Segment.

We are organized and conduct our operations to qualify as a real estate investment trust (“REIT”) under the Internal Revenue Code of 1986, as amended (the “Code”). As such, we will generally not be subject to U.S. federal corporate income tax on that portion of our net income that is distributed to stockholders if we distribute at least 90% of our taxable income to our stockholders by prescribed dates and comply with various other requirements. We also operate

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our business in a manner that will permit us to maintain our exemption from registration under the Investment Company Act of 1940 as amended (the “Investment Company Act” or “1940 Act”).

We are organized as a holding company and conduct our business primarily through our various wholly owned subsidiaries. We are externally managed and advised by SPT Management, LLC (our “Manager”) pursuant to the terms of a management agreement. Our Manager is controlled by Barry Sternlicht, our Chairman and Chief Executive Officer. Our Manager is an affiliate of Starwood Capital Group, a privately held private equity firm founded and controlled by Mr. Sternlicht.

Our corporate headquarters office is located at 591 West Putnam Avenue, Greenwich, Connecticut 06830, and our telephone number is (203) 422 7700.

## Investment Strategy

We seek to attain attractive risk adjusted returns for our investors over the long term by sourcing and managing a diversified portfolio of target assets, financed in a manner that is designed to deliver attractive returns across a variety of market conditions and economic cycles. Our investment strategy focuses on a few fundamental themes:

- origination and acquisition of real estate debt assets with an implied basis sufficiently low to weather declines in asset values;
- acquisition of equity interests in commercial real estate properties that generate stable current returns, increase the duration of our investment portfolio and provide potential for capital appreciation;
- focus on real estate markets and asset classes with strong supply and demand fundamentals and/or barriers to entry;
- structuring and financing each transaction in a manner that reflects the risk of the underlying asset’s cash flow stream and credit risk profile, and efficiently managing and maintaining the transaction’s interest rate and currency exposures at levels consistent with management’s risk objectives;
- seeking situations where our size, scale, speed, and sophistication allow us to position ourselves as a “one stop” lending solution for real estate owner/operators;
- utilizing the skills, expertise, and contacts developed by our Manager over the past 20 plus years as one of the premier global real estate investment managers to correctly anticipate trends and identify attractive risk adjusted investment opportunities in U.S. and European real estate markets; and
- utilizing the skills, expertise, and infrastructure we acquired through our acquisition of LNR, a market leading diversified real estate investment management and loan servicing company, to expand and diversify our presence in various segments of real estate, including:
  - origination of small and medium sized loan transactions (\$10 million to \$50 million) for both investment and securitization/gain on sale;
  - investment in CMBS;
  - investment in commercial real estate; and
  - special servicing of commercial real estate loans in commercial real estate securitization transactions.

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In order to capitalize on the changing sets of investment opportunities that may be present in the various points of an economic cycle, we may expand or refocus our investment strategy by emphasizing investments in different parts of the capital structure and different sectors of real estate. Our investment strategy may be amended from time to time, if recommended by our Manager and approved by our board of directors, without the approval of our stockholders. In addition to our Manager making direct investments on our behalf, we may enter into joint venture, management or other agreements with persons that have special expertise or sourcing capabilities.

### Financing Strategy

Subject to maintaining our qualification as a REIT for U.S. federal income tax purposes and our exemption from registering under the 1940 Act, we may finance the acquisition of our target assets, to the extent available to us, through the following methods:

- sources of private and government sponsored financing, including long and short term repurchase agreements, warehouse and bank credit facilities, and mortgage loans on equity interests in commercial real estate properties;
- loan sales, syndications, and/or securitizations; and
- public or private offerings of our equity and/or debt securities.

We may also utilize other sources of financing to the extent available to us.

### Our Target Assets

We invest in target assets secured primarily by U.S. or European collateral. We focus primarily on originating or opportunistically acquiring commercial mortgage whole loans, B Notes, mezzanine loans, preferred equity and mortgage backed securities ("MBS"). We may invest in performing and non performing mortgage loans and other real estate related loans and debt investments. We may acquire target assets through portfolio or other acquisitions. Our Manager targets desirable markets where it has expertise in the real estate collateral underlying the assets being acquired. Our target assets include the following types of loans and other investments with respect to commercial real estate:

- Whole mortgage loans: loans secured by a first mortgage lien on a commercial property that provide mortgage financing to commercial property developers or owners generally having maturity dates ranging from three to ten years;
- B Notes: typically a privately negotiated loan that is secured by a first mortgage on a single large commercial property or group of related properties and subordinated to an A Note secured by the same first mortgage on the same property or group;
- Mezzanine loans: loans made to commercial property owners that are secured by pledges of the borrower's ownership interests in the property and/or the property owner, subordinate to whole mortgage loans secured by first or second mortgage liens on the property and senior to the borrower's equity in the property;
- Construction or rehabilitation loans: mortgage loans and mezzanine loans to finance the cost of construction or rehabilitation of a commercial property;
- CMBS: securities that are collateralized by commercial mortgage loans, including:
  - senior and subordinated investment grade CMBS,
  - below investment grade CMBS, and

· unrated CMBS;

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- Corporate bank debt: term loans and revolving credit facilities of commercial real estate operating or finance companies, each of which are generally secured by such companies' assets;
- Equity: equity interests in commercial real estate properties, including commercial properties purchased from CMBS trusts; and
- Corporate bonds: debt securities issued by commercial real estate operating or finance companies that may or may not be secured by such companies' assets, including:
  - investment grade corporate bonds,
  - below investment grade corporate bonds, and
  - unrated corporate bonds.

We have also invested in the following types of loans and other debt investments relating to residential real estate:

- Non Agency RMBS: securities collateralized by residential mortgage loans that are not guaranteed by any U.S. Government agency or federally chartered corporation; and
- Residential mortgage loans: loans secured by a first mortgage lien on residential property.

In addition, we may invest in the following real estate-related investments:

- Net leases: commercial properties subject to net leases, which leases typically have longer terms than gross leases, require tenants to pay substantially all of the operating costs associated with the properties and often have contractually specified rent increases throughout their terms; and
- Agency RMBS: RMBS for which a U.S. government agency or a federally chartered corporation guarantees payments of principal and interest on the securities.

Business Segments

We currently operate our business in three reportable segments: the Lending Segment, the Investing and Servicing Segment and the Property Segment. Refer to Note 23 of our Consolidated Financial Statements for our results of operations and financial position by business segment.

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## Lending Segment

The following table sets forth the amount of each category of investments we owned across various property types within our Lending Segment as of December 31, 2016 and 2015 (dollars in thousands):

	Face Amount	Carrying Value	Asset Specific Financing	Net Investment	Vintage	Unlevered Return on Asset	
December 31, 2016							
First mortgages (1)	\$ 4,861,214	\$ 4,845,552	\$ 1,910,078	\$ 2,935,474	1989-2016	6.4	%
Subordinated mortgages	293,925	278,032	4,021	274,011	1998-2015	11.5	%
Mezzanine loans (1)	714,608	713,757	—	713,757	2006-2016	10.7	%
Loans transferred as secured borrowings	35,000	35,000	35,000	—	N/A		
Loan loss allowance	—	(9,788)	—	(9,788)	N/A		
RMBS	399,883	253,915	38,832	215,083	2003-2007	10.3	%
HTM securities (2)	515,027	509,980	305,531	204,449	2013-2015	6.0	%
Equity security	11,275	12,177	—	12,177	N/A		
Investments in unconsolidated entities	N/A	30,874	—	30,874	N/A		
	\$ 6,830,932	\$ 6,669,499	\$ 2,293,462	\$ 4,376,037			
December 31, 2015							
First mortgages (1)	\$ 4,776,576	\$ 4,723,852	\$ 2,154,287	(3) \$ 2,569,565	1989-2015	6.9	%
Subordinated mortgages	416,713	392,563	6,021	386,542	1998-2015	11.2	%
Mezzanine loans (1)	850,024	862,693	—	862,693	2006-2015	10.9	%
Loans transferred as secured borrowings	88,000	86,573	88,000	(1,427)	N/A		
Loan loss allowance	—	(6,029)	—	(6,029)	N/A		
RMBS	233,976	176,224	2,000	174,224	2003-2007	11.9	%
HTM securities (2)	321,193	321,244	179,589	141,655	2013-2015	6.5	%
Equity security	13,471	14,498	—	14,498	N/A		
Investments in unconsolidated entities	N/A	30,827	—	30,827	N/A		
	\$ 6,699,953	\$ 6,602,445	\$ 2,429,897	\$ 4,172,548			

(1) First mortgages include first mortgage loans and any contiguous mezzanine loan components because as a whole, the expected credit quality of these loans is more similar to that of a first mortgage loan. The application of this methodology resulted in mezzanine loans with carrying values of \$964.1 million and \$930.0 million being classified as first mortgages as of December 31, 2016 and 2015, respectively.

(2)

CMBS held-to-maturity (“HTM”) and mandatorily redeemable preferred equity interests in commercial real estate entities.

- (3) Reflects amounts reclassified in accordance with Accounting Standards Update (“ASU”) 2015-03 as discussed in Note 2 to the Consolidated Financial Statements.

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As of December 31, 2016 and 2015, our Lending Segment's investment portfolio, excluding RMBS and other investments, had the following characteristics based on carrying values:

Collateral Property Type	As of December 31,	
	2016	2015
Office	35.8 %	39.4 %
Hospitality	22.9 %	28.2 %
Multi-family	15.3 %	9.0 %
Mixed Use	15.1 %	12.8 %
Retail	7.0 %	6.4 %
Industrial	2.0 %	1.9 %
Residential	1.9 %	2.3 %
	100.0 %	100.0 %

Geographic Location	As of December 31,	
	2016	2015
North East	37.7 %	28.8 %
West	21.5 %	23.2 %
South East	11.6 %	17.3 %
International	9.5 %	13.1 %
South West	8.9 %	7.1 %
Midwest	7.3 %	6.4 %
Mid Atlantic	3.5 %	4.1 %
	100.0 %	100.0 %

Our investment process includes sourcing and screening of investment opportunities, assessing investment suitability, conducting interest rate and prepayment analysis, evaluating cash flow and collateral performance, and reviewing legal structure and servicer and originator information and investment structuring, as appropriate, to seek an attractive return commensurate with the risk we are bearing. Upon identification of an investment opportunity, the investment will be screened and monitored by us to determine its impact on maintaining our REIT qualification and our exemption from registration under the 1940 Act. We will seek to make investments in sectors where we have strong core competencies and believe market risk and expected performance can be reasonably quantified.

We evaluate each one of our investment opportunities based on its expected risk adjusted return relative to the returns available from other, comparable investments. In addition, we evaluate new opportunities based on their relative expected returns compared to comparable positions held in our portfolio. The terms of any leverage available to us for use in funding an investment purchase are also taken into consideration, as are any risks posed by illiquidity or correlations with other securities in the portfolio. We also develop a macro outlook with respect to each target asset class by examining factors in the broader economy such as gross domestic product, interest rates, unemployment rates and availability of credit, among other things. We also analyze fundamental trends in the relevant target asset class sector to adjust/maintain our outlook for that particular target asset class.

Our primary focus has been to build a portfolio of commercial mortgage and mezzanine loans with attractive risk adjusted returns by focusing on the underlying real estate fundamentals and credit analysis of the borrowers. We continually monitor borrower performance and complete a detailed, loan by loan formal credit review on a quarterly

basis. The results of this review are incorporated into our quarterly assessment of the adequacy of the allowance for loan losses.

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The weighted average coupon for first mortgages and mezzanine loans originated and acquired by the Lending Segment during the year ended December 31, 2016 was 5.4% and 10.8%, respectively. No subordinated mortgages were originated or acquired during the year ended December 31, 2016. The following table summarizes the activity in the Lending Segment's loan portfolio and the associated changes in future funding commitments associated with these loans during the year ended December 31, 2016 (amounts in thousands):

	Carrying Value	Future Funding Commitments
Balance at January 1, 2016	\$ 6,059,652	\$ 1,503,889
Acquisitions/originations	2,222,373	753,088
Additional funding and expired commitments	609,503	(639,018)
Capitalized interest (1)	80,992	—
Basis of loans sold	(382,520)	(49,604)
Loan maturities/principal repayments	(2,724,844)	(156,576)
Discount accretion/premium amortization	48,384	—
Unrealized foreign currency remeasurement loss	(47,906)	(52,336)
Change in loan loss allowance, net	(3,759)	—
Transfer to/from other asset classifications	678	—
Balance at December 31, 2016	\$ 5,862,553	\$ 1,359,443

(1) Represents accrued interest income on loans whose terms do not require current payment of interest.

As of December 31, 2016, the Lending Segment's loans held for investment and HTM securities had a weighted average maturity of 2.2 years, inclusive of extension options that management believes are probable of exercise. The table below shows the carrying value expected to mature annually for our loans held for investment and HTM securities (amounts in thousands, except number of investments maturing).

Year of Maturity	Number of Investments Maturing (1)	Carrying Value (1)	% of Total
2017	77	\$ 1,288,084	20.3 %
2018	78	2,014,387	31.7 %
2019	86	1,694,139	26.7 %
2020	39	853,756	13.5 %
2021	2	178,115	2.8 %
2022	—	—	— %
2023	4	53,807	0.8 %
2024	17	223,401	3.5 %
2025	1	41,632	0.7 %
2026 and thereafter	—	—	— %

Total	304	\$ 6,347,321	100.0 %
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(1) Excludes loans transferred as secured borrowings, RMBS, equity security and investments in unconsolidated entities. Carrying value also excludes loan loss allowance.

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## Investing and Servicing Segment

The following table sets forth the amount of each category of investments we owned within our Investing and Servicing Segment as of December 31, 2016 and 2015 (amounts in thousands):

	Face Amount	Carrying Value	Asset Specific Financing	Net Investment
December 31, 2016				
CMBS, fair value option	\$ 4,459,655	\$ 990,570 (1)	\$ 206,651	\$ 783,919
Intangible assets - servicing rights	N/A	89,320 (2)	—	89,320
Lease intangibles, net	N/A	29,676	—	29,676
Loans held-for-sale, fair value option	63,065	63,279	33,131	30,148
Loans held-for-investment	20,442	20,442	—	20,442
Investment in unconsolidated entities	N/A	56,376	—	56,376
Properties, net	N/A	277,612	186,901	90,711
	\$ 4,543,162	\$ 1,527,275	\$ 426,683	\$ 1,100,592
December 31, 2015				
CMBS, fair value option	\$ 4,704,136	\$ 1,038,200(1)	\$ 193,944	\$ 844,256
Intangible assets - servicing rights	N/A	134,153 (2)	—	134,153
Lease intangibles, net	N/A	14,621	—	14,621
Loans held-for-sale, fair value option	203,710	203,865	145,803 (3)	58,062
Investment in unconsolidated entities	N/A	53,145	—	53,145
Properties, net	N/A	150,497	82,513 (3)	67,984
	\$ 4,907,846	\$ 1,594,481	\$ 422,260	\$ 1,172,221

(1) Includes \$959.0 million and \$825.2 million of CMBS reflected in “VIE liabilities” in accordance with Accounting Standards Codification (“ASC”) 810 as of December 31, 2016 and 2015, respectively.

(2) Includes \$34.2 million and \$11.8 million of servicing rights intangibles reflected in “VIE assets” in accordance with ASC 810 as of December 31, 2016 and 2015, respectively.

(3) Reflects amounts reclassified in accordance with ASU 2015-03 as discussed in Note 2 to the Consolidated Financial Statements.

As of December 31, 2016, the Investing and Servicing Segment’s CMBS had a weighted average expected maturity of 7.3 years. The table below shows the CMBS carrying value expected to mature annually (amounts in thousands, except number of investments maturing).

Number of

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Year of Maturity	Investments Maturing	Carrying Value	% of Total	
2017	84	\$ 99,282	10.0	%
2018	36	63,128	6.4	%
2019	30	52,282	5.3	%
2020	7	10,366	1.0	%
2021	4	6,297	0.6	%
2022	3	7,322	0.7	%
2023	25	167,215	16.9	%
2024	20	84,109	8.5	%
2025	49	164,111	16.6	%
2026 and thereafter	143	336,458	34.0	%
Total	401	\$ 990,570	100.0	%

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Our Investing and Servicing Segment's REO Portfolio, as defined in Note 3 to the Consolidated Financial Statements, had the following characteristics based on carrying values of \$283.5 million and \$140.9 million as of December 31, 2016 and 2015, respectively:

Property Type	As of December 31,	
	2016	2015
Retail	45.8 %	71.4 %
Office	23.9 %	— %
Multi-family	18.1 %	18.9 %
Mixed Use	7.5 %	— %
Self-storage	4.7 %	9.7 %
	100.0 %	100.0 %

Geographic Location	As of December 31,	
	2016	2015
South East	51.0 %	35.3 %
North East	17.3 %	35.7 %
Mid Atlantic	9.4 %	— %
Midwest	8.0 %	10.5 %
West	7.3 %	3.6 %
South West	7.0 %	14.9 %
	100.0 %	100.0 %

## Property Segment

The following table sets forth the amount of each category of investments, which are comprised of properties, intangible lease assets and liabilities and our equity investment in four regional shopping malls (the "Retail Fund") held within our Property Segment as of December 31, 2016 and 2015 (amounts in thousands):

	As of December 31,	
	2016	2015
Properties, net	\$ 1,667,108	\$ 768,728
Lease intangibles, net	122,124	58,658
Investment in unconsolidated entities	124,977	122,454
	\$ 1,914,209	\$ 949,840

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The following table sets forth our net investment and other information regarding the Property Segment's properties and intangible lease assets and liabilities as of December 31, 2016 (dollars in thousands):

	Carrying Value	Asset Specific Financing	Net Investment	Occupancy Rate	Weighted Average Remaining Lease Term
Office—Medical Office Portfolio	\$ 767,826	\$ 480,252	\$ 287,574	93.8 %	6.8 years
Office—Ireland Portfolio	459,410	294,932	164,478	97.7 %	9.7 years
Multi-family residential—Ireland Portfolio	16,477	10,705	5,772	100.0 %	0.5 years
Multi-family residential—Woodstar Portfolio	609,823	410,941	198,882	97.4 %	0.5 years
Subtotal—undepreciated carrying value	1,853,536	1,196,830	656,706		
Accumulated depreciation and amortization	(64,304)	—	(64,304)		
Net carrying value	\$ 1,789,232	\$ 1,196,830	\$ 592,402		

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As of December 31, 2016 and 2015, our Property Segment's investment portfolio had the following geographic characteristics based on carrying values:

Geographic Location	As of December 31,	
	2016	2015
Europe	25.2 %	58.2 %
U.S. Regions:		
South East	39.7 %	41.8 %
North East	13.0 %	— %
South West	8.7 %	— %
West	7.2 %	— %
Midwest	6.2 %	— %
	100.0 %	100.0 %

Refer to Schedule III included in Item 8 of this Annual Report on Form 10-K for a detailed listing of the properties held by the Company, including their respective geographic locations.

#### Regulation

Our operations are subject, in certain instances, to supervision and regulation by state and federal governmental authorities and may be subject to various laws and judicial and administrative decisions imposing various requirements and restrictions, which, among other things: (1) regulate credit granting activities; (2) establish maximum interest rates, finance charges and other charges; (3) require disclosures to customers; (4) govern secured transactions; (5) set collection, foreclosure, repossession and claims handling procedures and other trade practices; and (6) regulate affordable housing rental activities. Although most states do not regulate commercial finance, certain states impose limitations on interest rates and other charges and on certain collection practices and creditor remedies, and require licensing of lenders and financiers and adequate disclosure of certain contract terms. We are also required to comply with certain provisions of the Equal Credit Opportunity Act that are applicable to commercial loans and the Fair Housing Act. We intend to conduct our business so that neither we nor any of our subsidiaries are required to register as an investment company under the 1940 Act.

#### Competition

We are engaged in a competitive business. In our investment activities, we compete for opportunities with numerous public and private investment vehicles, including financial institutions, specialty finance companies, mortgage banks, pension funds, opportunity funds, hedge funds, insurance companies, REITs and other institutional investors, as well as individuals. Many competitors are significantly larger than we are, have well established operating histories and may have greater access to capital, more resources and other advantages over us. These competitors may be willing to accept lower returns on their investments or to compromise underwriting standards and, as a result, our origination volume and profit margins could be adversely affected.

#### Our Manager

We are externally managed and advised by our Manager and benefit from the personnel, relationships and experience of our Manager's executive team and other personnel of Starwood Capital Group. Pursuant to the terms of a management agreement between our Manager and us, our Manager provides us with our management team and

appropriate support personnel. Pursuant to an investment advisory agreement between our Manager and Starwood Capital Group Management, LLC, our Manager has access to the personnel and resources of Starwood Capital Group necessary for the implementation and execution of our business strategy.

Our Manager is an affiliate of Starwood Capital Group, a privately held private equity firm founded and controlled by Mr. Sternlicht. Starwood Capital Group has invested in most major classes of real estate, directly and indirectly, through operating companies, portfolios of properties and single assets, including multifamily, office, retail, hotel, residential entitled land and communities, senior housing, mixed use and golf courses. Starwood Capital Group

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invests at different levels of the capital structure, including equity, preferred equity, mezzanine debt and senior debt, depending on the asset risk profile and return expectation.

Our Manager draws upon the experience and expertise of Starwood Capital Group's team of professionals and support personnel operating in nine cities across three countries. Our Manager also benefits from Starwood Capital Group's dedicated asset management group operating in offices located in the U.S. and abroad. We also benefit from Starwood Capital Group's portfolio management, finance and administration functions, which address legal, compliance, investor relations and operational matters, asset valuation, risk management and information technologies in connection with the performance of our Manager's duties.

## Employees

As of December 31, 2016, the Company has 340 full time employees, the majority of which are real estate professionals located throughout the U.S.

## Taxation of the Company

We have elected to be taxed as a REIT under the Code for federal income tax purposes. We generally must distribute annually at least 90% of our taxable income, subject to certain adjustments and excluding any net capital gain, in order for federal corporate income tax not to apply to our earnings that we distribute. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our taxable income, we will be subject to federal corporate income tax on our undistributed taxable income. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we pay out to our stockholders in a calendar year is less than a minimum amount specified under federal tax laws. Our qualification as a REIT also depends on our ability to meet various other requirements imposed by the Code, which relate to organizational structure, diversity of stock ownership and certain restrictions with regard to owned assets and categories of income. If we qualify for taxation as a REIT, we will generally not be subject to U.S. federal corporate income tax on our taxable income that is currently distributed to stockholders.

Even if we qualify as a REIT, we may be subject to certain federal excise taxes and state and local taxes on our income and property. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income taxes at regular corporate rates (including any applicable alternative minimum tax) and will not be able to qualify as a REIT for four subsequent taxable years. REITs are subject to a number of organizational and operational requirements under the Code.

We utilize taxable REIT subsidiaries ("TRSs") to reduce the impact of the prohibited transaction tax and to avoid penalty for the holding of assets not qualifying as real estate assets for purposes of the REIT asset tests. Any income associated with a TRS is fully taxable because a TRS is subject to federal and state income taxes as a domestic C corporation based upon its net income.

See Item 1A—"Risk Factors—Risks Related to Our Taxation as a REIT" for additional tax status information.

## Leverage Policies

Refer to Item 7—"Management's Discussion and Analysis of Financial Condition and Results of Operations—Leverage Policies."

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### Investment Guidelines

Our board of directors has adopted the following investment guidelines:

- our investments will be in our target assets unless otherwise approved by our board of directors;
- no investment shall be made that would cause us to fail to qualify as a REIT for federal income tax purposes;
- no investment shall be made that would cause us or any of our subsidiaries to be required to be registered as an investment company under the 1940 Act;
- not more than 25% of our equity will be invested in any individual asset without the consent of a majority of our independent directors; and
- (a) any investment that is less than \$150 million will require approval of our Chief Executive Officer; (b) any investment that is equal to or in excess of \$150 million but less than \$250 million will require approval of our Manager's investment committee; (c) any investment that is equal to or in excess of \$250 million but less than \$400 million will require approval of each of the investment committee of our board of directors and our Manager's investment committee; and (d) any investment that is equal to or in excess of \$400 million will require approval of each of our board of directors and our Manager's investment committee.

These investment guidelines may be changed from time to time by our board of directors without the approval of our stockholders. In addition, both our Manager and our board of directors must approve any change in our investment guidelines that would modify or expand the types of assets in which we invest.

### Available Information

Our website address is [www.starwoodpropertytrust.com](http://www.starwoodpropertytrust.com). We make available free of charge through our website our Annual Reports on Form 10 K, Quarterly Reports on Form 10 Q, Current Reports on Form 8 K, all amendments to those reports and other filings as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission (the "SEC"), and also make available on our website the charters for the Audit, Compensation and Nominating and Corporate Governance Committees of our board of directors and our Code of Business Conduct and Ethics and Code of Ethics for Principal Executive Officer and Senior Financial Officers, as well as our corporate governance guidelines. Copies in print of these documents are available upon request to our Corporate Secretary at the address indicated on the cover of this report. The information on our website is not a part of, nor is it incorporated by reference into, this Annual Report on Form 10 K.

We intend to post on our website any amendment to, or waiver of, a provision of our Code of Business Conduct and Ethics or Code of Ethics for Principal Executive Officer and Senior Financial Officers that applies to our Chief Executive Officer, Chief Financial Officer or persons performing similar functions and that relates to any element of the code of ethics definition set forth in Item 406 of Regulation S K of the Securities Act of 1933, as amended.

To communicate with our board of directors electronically, we have established an e mail address, [BoardofDirectors@stwdreit.com](mailto:BoardofDirectors@stwdreit.com), to which stockholders may send correspondence to our board of directors or any such individual directors or group or committee of directors.

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Item 1A. Risk Factors.

Risks Related to Our Relationship with Our Manager

We are dependent on Starwood Capital Group, including our Manager, and their key personnel, who provide services to us through the management agreement, and we may not find a suitable replacement for our Manager and Starwood Capital Group if the management agreement is terminated, or for these key personnel if they leave Starwood Capital Group or otherwise become unavailable to us.

Our Manager has significant discretion as to the implementation of our investment and operating policies and strategies. Accordingly, we believe that our success depends to a significant extent upon the efforts, experience, diligence, skill and network of business contacts of the officers and key personnel of our Manager. The officers and key personnel of our Manager evaluate, negotiate, close and monitor a substantial portion of our investments; therefore, our success depends on their continued service. The departure of any of the officers or key personnel of our Manager could have a material adverse effect on our performance.

We offer no assurance that our Manager will remain our investment manager or that we will continue to have access to our Manager's officers and key personnel. The initial term of our management agreement with our Manager, and the initial term of the investment advisory agreement between our Manager and Starwood Capital Group Management, LLC, expired on August 17, 2012, with automatic one year renewals thereafter; provided, however, that our Manager may terminate the management agreement annually upon 180 days prior notice. If the management agreement and the investment advisory agreement are terminated and no suitable replacement is found to manage us, we may not be able to continue to execute our business plan.

There are various conflicts of interest in our relationship with Starwood Capital Group, including our Manager, which could result in decisions that are not in the best interests of our stockholders.

We are subject to conflicts of interest arising out of our relationship with Starwood Capital Group, including our Manager. Specifically, Mr. Sternlicht, our Chairman and Chief Executive Officer, Jeffrey G. Dishner, one of our directors, and certain of our executive officers are executives of Starwood Capital Group.

Our Manager and executive officers may have conflicts between their duties to us and their duties to, and interests in, Starwood Capital Group and its other investment funds. Currently, Starwood Global Opportunity Fund X (the "Starwood Private Real Estate Fund") has a right to invest 25% of the equity capital proposed to be invested by any investment vehicle managed by an entity controlled by Starwood Capital Group in debt interests relating to real estate. There can be no assurance that our Manager and Starwood Capital Group will allocate to us all or any portion of the remaining 75% of any co investment opportunity in our target asset classes. Our independent directors do not approve each co investment by the Starwood Private Real Estate Fund and us unless the amount of capital we invest in the proposed co-investment otherwise requires the review and approval of our independent directors pursuant to our investment guidelines. Pursuant to the exclusivity provisions of the Starwood Private Real Estate Fund, our investment strategy may not include either (i) equity interests in real estate or (ii) "near term loan to own" investments, in each case (of both (i) and (ii)) if such investments are expected, at the time such investment is made, to produce an internal rate of return ("IRR") in excess of 14%. Therefore, our board of directors does not have the flexibility to expand our investment strategy to include equity interests in real estate or "near term loan to own" investments with such an IRR expectation.

Our Manager, Starwood Capital Group and their respective affiliates may sponsor or manage a U.S. publicly traded investment vehicle that invests generally in real estate assets but not primarily in our "target assets" (as defined in our co-investment and allocation agreement) (a "potential competing vehicle"). Our Manager and Starwood Capital Group

have also agreed in our co-investment and allocation agreement that for so long as the management agreement is in effect and our Manager and Starwood Capital Group are under common control, no entity controlled by Starwood Capital Group will sponsor or manage a potential competing vehicle or private or foreign competing vehicle unless Starwood Capital Group adopts a policy that either (i) provides for the fair and equitable allocation of investment opportunities in our “target assets” (as defined in our co-investment and allocation agreement) among all such vehicles and us or (ii) provides us the right to co invest with respect to any “target assets” (as defined in our co-investment and

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allocation agreement) with such vehicles, in each case subject to the suitability of each investment opportunity for the particular vehicle and us and each such vehicle's and our availability of cash for investment.

To the extent that our Manager and Starwood Capital Group adopt the investment allocation policy described in the preceding paragraph in the future, we may nonetheless compete with one or more of these vehicles for investment opportunities sourced by our Manager and Starwood Capital Group. As a result, we may either not be presented with the opportunity or may have to compete with these vehicles to acquire these investments. Some or all of our executive officers, the members of the investment committee of our Manager and other key personnel of our Manager would likely be responsible for selecting investments for these vehicles and they may choose to allocate favorable investments to one or more of these vehicles instead of to us.

Our board of directors has adopted a policy with respect to any proposed investments by our directors or officers or the officers of our Manager, which we refer to as the covered persons, in any of our target asset classes. This policy provides that any proposed investment by a covered person for his or her own account in any of our target asset classes will be permitted if the capital required for the investment does not exceed the personal investment limit. To the extent that a proposed investment exceeds the personal investment limit, we expect that our board of directors will only permit the covered person to make the investment (i) upon the approval of the disinterested directors or (ii) if the proposed investment otherwise complies with terms of any other related party transaction policy our board of directors has adopted. Subject to compliance with all applicable laws, these individuals may make investments for their own account in our target assets which may present certain conflicts of interest not addressed by our current policies.

We pay our Manager substantial base management fees regardless of the performance of our portfolio. Our Manager's entitlement to a base management fee, which is not based upon performance metrics or goals, might reduce its incentive to devote its time and effort to seeking investments that provide attractive risk-adjusted returns for our portfolio. This in turn could hurt both our ability to make distributions to our stockholders and the market price of our common stock.

Excluding our operating subsidiaries, we do not have any employees except for Andrew Sossen, our Chief Operating Officer, Executive Vice President, General Counsel and Chief Compliance Officer, and Rina Paniry, our Chief Financial Officer, Treasurer and Chief Accounting Officer, whom Starwood Capital Group has seconded to us exclusively. Mr. Sossen and Ms. Paniry are also employees of other entities affiliated with our Manager and, as a result, are subject to potential conflicts of interest in service as our employees and as employees of such entities.

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

Certain of our executive officers and two of our six directors are executives of Starwood Capital Group. Our management agreement with our Manager was negotiated between related parties and its terms, including fees payable, may not be as favorable to us as if it had been negotiated with an unaffiliated third party.

Termination of the management agreement with our Manager without cause is difficult and costly. Our independent directors will review our Manager's performance and the management fees annually and the management agreement may be terminated annually upon the affirmative vote of at least two-thirds of our independent directors based upon: (i) our Manager's unsatisfactory performance that is materially detrimental to us, or (ii) a determination that the management fees payable to our Manager are not fair, subject to our Manager's right to prevent termination based on unfair fees by accepting a reduction of management fees agreed to by at least two-thirds of our independent directors. Our Manager will be provided 180 days prior notice of any such a termination. Additionally, upon such a termination, the management agreement provides that we will pay our Manager a termination fee equal to three times the sum of the average annual base management fee and incentive fee received by our Manager during the prior 24-month period.

before such termination, calculated as of the end of the most recently completed fiscal quarter. These provisions may increase the cost to us of terminating the management agreement and adversely affect our ability to terminate our Manager without cause.

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The initial term of our management agreement with our Manager, and the initial term of the investment advisory agreement between our Manager and Starwood Capital Group Management, LLC, expired on August 17, 2012, with automatic one year renewals thereafter; provided, however, that our Manager may terminate the management agreement annually upon 180 days prior notice. If the management agreement is terminated and no suitable replacement is found to manage us, we may not be able to continue to execute our business plan.

Pursuant to the management agreement, our Manager does not assume any responsibility other than to render the services called for thereunder and is not responsible for any action of our board of directors in following or declining to follow its advice or recommendations. Our Manager maintains a contractual as opposed to a fiduciary relationship with us. Under the terms of the management agreement, our Manager, its officers, members, personnel, any person controlling or controlled by our Manager and any person providing sub advisory services to our Manager will not be liable to us, any subsidiary of ours, our directors, our stockholders or any subsidiary's stockholders or partners for acts or omissions performed in accordance with and pursuant to the management agreement, except because of acts constituting bad faith, willful misconduct, gross negligence, or reckless disregard of their duties under the management agreement. In addition, we have agreed to indemnify our Manager, its officers, stockholders, members, managers, directors, personnel, any person controlling or controlled by our Manager and any person providing sub advisory services to our Manager with respect to all expenses, losses, damages, liabilities, demands, charges and claims arising from acts or omissions of our Manager not constituting bad faith, willful misconduct, gross negligence, or reckless disregard of duties, performed in good faith in accordance with and pursuant to the management agreement.

The incentive fee payable to our Manager under the management agreement is payable quarterly and is based on our core earnings and, therefore, may cause our Manager to select investments in more risky assets to increase its incentive compensation.

Our Manager is entitled to receive incentive compensation based upon our achievement of targeted levels of core earnings. In evaluating investments and other management strategies, the opportunity to earn incentive compensation based on core earnings may lead our Manager to place undue emphasis on the maximization of core earnings at the expense of other criteria, such as preservation of capital, in order to achieve higher incentive compensation. Investments with higher yield potential are generally riskier or more speculative. This could result in increased risk to the value of our investment portfolio.

Core earnings is not a measure calculated in accordance with accounting principles generally accepted in the United States of America ("GAAP") and is defined within Item 7 – Non-GAAP Financial Measures in this Annual Report on Form 10-K.

Certain agreements with Colony Starwood Homes (formerly known as Starwood Waypoint Residential Trust) may not reflect terms that would have resulted from arm's length negotiations among unaffiliated third parties.

On January 31, 2014, we distributed all of the common shares of Colony Starwood Homes (formerly known as Starwood Waypoint Residential Trust), our former wholly-owned subsidiary, to our stockholders of record on January 24, 2014, which completed the spin-off of our former SFR segment. The terms of the agreements related to the separation, including a separation and distribution agreement, dated January 16, 2014 (the "Separation Agreement"), were negotiated in the context of the separation while Colony Starwood Homes was still a part of us and, accordingly, may not reflect terms that would have resulted from arm's length negotiations among unaffiliated third parties.

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In the Separation Agreement, we agreed to indemnify Colony Starwood Homes and its affiliates and representatives against losses arising from: (a) any liability of ours or our subsidiaries (excluding any liabilities related to Colony Starwood Homes); (b) any failure of us and our subsidiaries (other than Colony Starwood Homes and its subsidiaries) (collectively, the “Starwood Group”) to pay, perform or otherwise promptly discharge any liability listed under (a) above in accordance with their respective terms, whether prior to, at or after the time of effectiveness of the Separation Agreement; (c) any breach by any member of the Starwood Group of any provision of the Separation Agreement and any agreements ancillary thereto (if any), subject to any limitations of liability provisions and other provisions applicable to any such breach set forth therein; and (d) any untrue statement or alleged untrue statement of a material fact or omission or alleged omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, with respect to all information contained in Colony Starwood Homes’ information statement or the registration statement of which Colony Starwood Homes’ information statement is a part that relates solely to any assets owned, directly or indirectly by us, other than Colony Starwood Homes’ initial portfolio of assets, which included all of our single family rental homes and distressed and non performing residential mortgage loans and certain cash transferred to Colony Starwood Homes or its subsidiaries by us. Any indemnification payments that we may be required to make could have a significantly negative effect on our liquidity and results of operations.

Our conflicts of interest policy may not adequately address all of the conflicts of interest that may arise with respect to our investment activities and also may limit the allocation of investments to us.

In order to avoid any actual or perceived conflicts of interest with our Manager, Starwood Capital Group, any of their affiliates or any investment vehicle sponsored or managed by Starwood Capital Group or any of its affiliates, which we refer to as the Starwood parties, we have adopted a conflicts of interest policy to specifically address some of the conflicts relating to our investment opportunities. Although under this policy the approval of a majority of our independent directors is required to approve (i) any purchase of our assets by any of the Starwood parties and (ii) any purchase by us of any assets of any of the Starwood parties, there is no assurance that this policy will be adequate to address all of the conflicts that may arise or will address such conflicts in a manner that results in the allocation of a particular investment opportunity to us or is otherwise favorable to us. In addition, the Starwood Private Real Estate Fund currently, and additional competing vehicles may in the future, participate in some of our investments, possibly at a more senior level in the capital structure of the underlying borrower and related real estate than our investment. Our interests in such investments may also conflict with the interests of these entities in the event of a default or restructuring of the investment. Participating investments will not be the result of arm’s length negotiations and will involve potential conflicts between our interests and those of the other participating entities in obtaining favorable terms. Since certain of our executives are also executives of Starwood Capital Group, the same personnel may determine the price and terms for the investments for both us and these entities and there can be no assurance that any procedural protections, such as obtaining market prices or other reliable indicators of fair value, will prevent the consideration we pay for these investments from exceeding their fair value or ensure that we receive terms for a particular investment opportunity that are as favorable as those available from an independent third party.

Our board of directors has approved very broad investment guidelines for our Manager and does not approve each investment and financing decision made by our Manager unless required by our investment guidelines.

Our Manager is authorized to follow very broad investment guidelines which enable our Manager to make investments on our behalf in a wide array of assets. Our board of directors will periodically review our investment guidelines and our investment portfolio but will not, and will not be required to, review all of our proposed investments, except that any investment that is equal to or in excess of \$250 million but less than \$400 million will require approval of the investment committee of our board of directors and any investment that is equal to or in excess of \$400 million will require approval of our board of directors. In addition, in conducting periodic reviews, our board of directors may rely and may make investments through affiliates primarily on information provided to them by our

Manager. Furthermore, our Manager may use complex strategies, and transactions entered into by our Manager may be costly, difficult or impossible to unwind by the time they are reviewed by our board of directors. Our Manager (or such affiliates) has great latitude within the broad parameters of our investment guidelines in determining the types and amounts of target assets it decides are attractive investments for us, which could result in investment returns that are substantially below expectations or that result in losses, which would materially and adversely affect our business operations and results. Further, decisions made and investments and financing arrangements entered into by our Manager

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may not fully reflect the best interests of our stockholders.

New investments may not be profitable (or as profitable as we expect), may increase our exposure to certain industries, may increase our exposure to interest rate, foreign currency, real estate market or credit market fluctuations, may divert managerial attention from more profitable opportunities, and may require significant financial resources. A change in our investment strategy may also increase any guarantee obligations we agree to incur or increase the number of transactions we enter into with affiliates. Moreover, new investments may present risks that are difficult for us to adequately assess, given our lack of familiarity with a particular type of investment or other reasons. The risks related to new investments or the financing risks associated with such investments could adversely affect our results of operations, financial condition and liquidity, and could impair our ability to make distributions to our stockholders.

### Risks Related to Our Company

Our board of directors has in the past and may in the future at any time change one or more of our investment strategy or guidelines, financing strategy or leverage policies without stockholder consent.

Our board of directors has in the past and may in the future at any time change one or more of our investment strategy or guidelines, financing strategy or leverage policies with respect to investments, acquisitions, growth, operations, indebtedness, capitalization and distributions without the consent of our stockholders, which could result in an investment portfolio with a different risk profile. Any change in our investment strategy may increase our exposure to interest rate risk, default risk and real estate market fluctuations. These changes could adversely affect our financial condition, results of operations, the market price of our common stock and our ability to make distributions to our stockholders.

We are highly dependent on information systems and systems failures could significantly disrupt our business, which may, in turn, negatively affect the market price of our common stock and our ability to make distributions to our stockholders.

Our business is highly dependent on communications and information systems of Starwood Capital Group. Any failure or interruption of Starwood Capital Group's systems could cause delays or other problems, which could have a material adverse effect on our operating results and negatively affect the market price of our common stock and our ability to make distributions to our stockholders.

Terrorist attacks and other acts of violence or war may affect the real estate industry and our business, financial condition and results of operations.

The terrorist attacks on September 11, 2001 disrupted the U.S. financial markets, including the real estate capital markets, and negatively impacted the U.S. economy in general. Any future terrorist attacks, the anticipation of any such attacks, the consequences of any military or other response by the U.S. and its allies, and other armed conflicts could cause consumer confidence and spending to decrease or result in increased volatility in the U.S. and worldwide financial markets and economy. The economic impact of these events could also adversely affect the credit quality of some of our loans and investments and the properties underlying our interests.

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We may suffer losses as a result of the adverse impact of any future attacks and these losses may adversely impact our performance and may cause the market value of our common stock to decline or be more volatile. A prolonged economic slowdown, a recession or declining real estate values could impair the performance of our investments and harm our financial condition and results of operations, increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us. We cannot predict the severity of the effect that potential future terrorist attacks would have on us. Losses resulting from these types of events may not be fully insurable.

We have not established a minimum distribution payment level and no assurance can be given that we will be able to make distributions to our stockholders in the future at current levels or at all.

We are generally required to distribute to our stockholders at least 90% of our taxable income each year for us to qualify as a REIT under the Code, which requirement we currently intend to satisfy through quarterly distributions of all or substantially all of our REIT taxable income in such year, subject to certain adjustments. We have not established a minimum distribution payment level, and our ability to pay distributions may be adversely affected by a number of factors, including the risk factors contained in this Annual Report on Form 10-K. Although we have made, and anticipate continuing to make, quarterly distributions to our stockholders, our board of directors has the sole discretion to determine the timing, form and amount of any future distributions to our stockholders, and such determination will depend on our earnings, our financial condition, debt covenants, maintenance of our REIT qualification and other factors as our board of directors may deem relevant from time to time. We believe that a change in any one of the following factors could adversely affect our results of operations and impair our ability to continue to pay distributions to our stockholders:

- the profitability of the investment of the net proceeds from our equity offerings;
- our ability to make profitable investments;
- margin calls or other expenses that reduce our cash flow;
- defaults in our asset portfolio or decreases in the value of our portfolio; and
- the fact that anticipated operating expense levels may not prove accurate, as actual results may vary from estimates.

As a result, no assurance can be given that we will be able to continue to make distributions to our stockholders in the future or that the level of any future distributions we do make to our stockholders will achieve a market yield or increase or even be maintained over time, any of which could materially and adversely affect us.

In addition, distributions that we make to our stockholders are generally taxable to our stockholders as ordinary income. However, a portion of our distributions may be designated by us as long term capital gains to the extent that they are attributable to capital gain income recognized by us or may constitute a return of capital to the extent that they exceed our earnings and profits as determined for tax purposes. A return of capital is not taxable, but has the effect of reducing the basis of a stockholder's investment in our common stock.

Changes in accounting rules could occur at any time and could impact us in significantly negative ways that we are unable to predict or protect against.

As has been widely publicized, the SEC, the Financial Accounting Standards Board and other regulatory bodies that establish the accounting rules applicable to us have proposed or enacted a wide array of changes to accounting rules over the last several years. Moreover, in the future these regulators may propose additional changes that we do not

currently anticipate. Changes to accounting rules that apply to us could significantly impact our business or our reported financial performance in negative ways that we cannot predict or protect against. We cannot predict whether any changes to current accounting rules will occur or what impact any codified changes will have on our business, results of operations, liquidity or financial condition.

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Failure to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes Oxley Act could have a material adverse effect on our business and stock price.

As a public company, we are required to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes Oxley Act of 2002. Internal control over financial reporting is complex and may be revised over time to adapt to changes in our business or changes in applicable accounting rules. We cannot assure you that our internal control over financial reporting will be effective in the future or that a material weakness will not be discovered with respect to a prior period for which we believe that internal controls were effective. If we are not able to maintain or document effective internal control over financial reporting, our independent registered public accounting firm may not be able to certify as to the effectiveness of our internal control over financial reporting as of the required dates. Matters impacting our internal controls may cause us to be unable to report our financial information on a timely basis, or may cause us to restate previously issued financial information, and thereby subject us to adverse regulatory consequences, including sanctions or investigations by the SEC, or violations of applicable stock exchange listing rules. There could also be a negative reaction in the financial markets due to a loss of investor confidence in us and the reliability of our financial statements. Confidence in the reliability of our financial statements is also likely to suffer if we or our independent registered public accounting firm reports a material weakness in our internal control over financial reporting. This could materially and adversely affect us by, for example, leading to a decline in our stock price and impairing our ability to raise capital.

### Risks Related to Sources of Financing

Our access to sources of financing may be limited and thus our ability to maximize our returns may be adversely affected.

Our financing sources currently include our credit agreements, our master repurchase agreements, our convertible senior notes, our 5.00% Senior Notes due 2021 (the “2021 Notes”), our mortgage debt on certain investment properties and common stock and debt offerings. Subject to market conditions and availability, we may seek additional sources of financing in the form of bank credit facilities (including term loans and revolving facilities), repurchase agreements, warehouse facilities, structured financing arrangements, public and private equity and debt issuances and derivative instruments, in addition to transaction or asset specific funding arrangements.

Our access to additional sources of financing will depend upon a number of factors, over which we have little or no control, including:

- general market conditions;
- the market’s view of the quality of our assets;
- the market’s perception of our growth potential;
- our current and potential future earnings and cash distributions; and
- the market price of the shares of our common stock.

A dislocation and/or weakness in the capital and credit markets could adversely affect one or more private lenders and could cause one or more of our private lenders to be unwilling or unable to provide us with financing or to increase the costs of that financing. In addition, if regulatory capital requirements imposed on our private lenders change, they may be required to limit, or increase the cost of, financing they provide to us. In general, this could potentially increase our financing costs and reduce our liquidity or require us to sell assets at an inopportune time or price.

To the extent structured financing arrangements are unavailable, we may have to rely more heavily on additional equity issuances, which may be dilutive to our stockholders, or on less efficient forms of debt financing that require a larger portion of our cash flow from operations, thereby reducing funds available for our operations, future

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business opportunities, cash distributions to our stockholders and other purposes. We cannot assure you that we will have access to such equity or debt capital on favorable terms (including, without limitation, cost and term) at the desired times, or at all, which may cause us to curtail our asset acquisition activities and/or dispose of assets, which could negatively affect our results of operations.

Our significant indebtedness subjects us to increased risk of loss and may reduce cash available for distributions to our stockholders.

We currently have a significant amount of indebtedness outstanding. As of December 31, 2016, our total consolidated indebtedness was approximately \$6.2 billion (excluding accounts payable, accrued expenses, other liabilities, VIE liabilities and unfunded commitments). Our outstanding indebtedness currently includes our credit agreements, our repurchase agreements, our convertible senior notes, the 2021 Notes and mortgage debt on certain investment properties. Subject to market conditions and availability, we may incur additional debt through bank credit facilities (including term loans and revolving facilities), repurchase agreements, warehouse facilities, structured financing arrangements, public and private debt issuances and derivative instruments, in addition to transaction or asset specific funding arrangements. The percentage of leverage we employ will vary depending on our available capital, our ability to obtain and access financing arrangements with lenders and the lenders' and rating agencies' estimate of the stability of our investment portfolio's cash flow. Our governing documents contain no limitation on the amount of debt we may incur. We may significantly increase the amount of leverage we utilize at any time without approval of our board of directors. However, under our current repurchase agreements and bank credit facilities, our total leverage may not exceed 75% of total assets (as defined therein), as adjusted to remove the impact of bona fide loan sales that are accounted for as financings and the consolidation of VIEs pursuant to GAAP. Moreover, the indenture governing the 2021 Notes contains covenants that, subject to a number of exceptions and adjustments, among other things, limit our ability to incur additional indebtedness and require that we maintain total unencumbered assets (as defined therein) of not less than 120% of the aggregate principal amount of our outstanding unsecured indebtedness (as defined therein). In addition, we may leverage individual assets at substantially higher levels. Incurring substantial debt subjects us to many risks that, if realized, would materially and adversely affect us, including the risk that:

- our cash flow from operations may be insufficient to make required payments of principal of and interest on the debt or we may fail to comply with all of the other covenants contained in the debt, which is likely to result in (i) acceleration of such debt (and any other debt containing a cross default or cross acceleration provision) that we may be unable to repay from internal funds or to refinance on favorable terms, or at all, (ii) our inability to borrow unused amounts under our financing arrangements, even if we are current in payments on borrowings under those arrangements and/or (iii) the loss of some or all of our assets to foreclosure or sale;
- our debt may increase our vulnerability to adverse economic and industry conditions with no assurance that investment yields will increase with higher financing costs;
- we may be required to dedicate a substantial portion of our cash flow from operations to payments on our debt, thereby reducing funds available for operations, future business opportunities, stockholder distributions or other purposes; and
- we may not be able to refinance debt that matures prior to the investment it was used to finance on favorable terms, or at all.

We are subject to margin calls from our lenders under our credit facilities.

Subject to certain conditions, the lenders under our credit facilities retain the sole discretion over the market value of loans and/or securities that serve as collateral for the borrowings under our credit facilities for purposes of determining

whether we are required to pay margin to such lenders.

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Interest rate fluctuations could significantly decrease our results of operations and cash flows and the market value of our investments.

Our primary interest rate exposures relate to the following:

- changes in interest rates may affect the yield on our investments and the financing cost of our debt, as well as the performance of our interest rate swaps that we utilize for hedging purposes, which could result in operating losses for us should interest expense exceed interest income;
- declines in interest rates may reduce the yield on existing floating rate assets and/or the yield on prospective investments;
- changes in the level of interest rates may affect our ability to source investments;
- increases in the level of interest rates may negatively impact the value of our investments and our ability to realize gains from the disposition of assets;
- increases in the level of interest rates may (x) increase the credit risk of our assets by negatively impacting the ability of our borrowers to pay debt service on our floating rate loan assets or our ability to refinance our assets upon maturity, and (y) negatively impact the value of the real estate supporting our investments (or that we own directly) through the impact such increases can have on property valuation capitalization rates; and
- changes in interest rates and/or the differential between U.S. dollar interest rates and those of non dollar currencies in which we invest can adversely affect the value of our non dollar assets and/or associated currency hedging transactions.

Our warehouse facilities may limit our ability to acquire assets, and we may incur losses if the collateral is liquidated.

We utilize warehouse facilities pursuant to which we accumulate mortgage loans in anticipation of a securitization financing, which assets are pledged as collateral for such facilities until the securitization transaction is consummated. In order to borrow funds to acquire assets under any additional warehouse facilities, we expect that our lenders thereunder would have the right to review the potential assets for which we are seeking financing. We may be unable to obtain the consent of a lender to acquire assets that we believe would be beneficial to us and we may be unable to obtain alternate financing for such assets. In addition, no assurance can be given that a securitization transaction would be consummated with respect to the assets being warehoused. If the securitization is not consummated, the lender could liquidate the warehoused collateral and we would then have to pay any amount by which the original purchase price of the collateral assets exceeds its sale price, subject to negotiated caps, if any, on our exposure. In addition, regardless of whether the securitization is consummated, if any of the warehoused collateral is sold before the consummation, we would have to bear any resulting loss on the sale. No assurance can be given that we will be able to obtain additional warehouse facilities on favorable terms, or at all.

The utilization of any of our repurchase agreements is subject to the pre approval of the lender.

We utilize repurchase agreements to finance the purchase of certain investments. In order for us to borrow funds under a repurchase agreement, our lender must have the right to review the potential assets for which we are seeking financing and approve such assets in its sole discretion. Accordingly, we may be unable to obtain the consent of a lender to finance an investment and alternate sources of financing for such asset may not exist.

A failure to comply with restrictive covenants in our financing arrangements would have a material adverse effect on us, and any future financings may require us to provide additional collateral or pay down debt.

We are subject to various restrictive covenants contained in our existing financing arrangements and may become subject to additional covenants in connection with future financings. Our credit agreements contain covenants that restrict our ability to incur additional debt or liens, make certain investments or acquisitions, merge, consolidate or

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transfer or dispose of substantially all of our assets or otherwise dispose of property and assets, pay dividends and make certain other restricted payments, change the nature of our business, or enter into transactions with affiliates. Our credit agreements, as well as our master repurchase agreements, each requires us to maintain compliance with various financial covenants, including a minimum tangible net worth and cash liquidity, and specified financial ratios, such as total debt to total assets and EBITDA to fixed charges. In addition, the indenture governing the 2021 Notes contains covenants that, subject to a number of exceptions and adjustments, among other things: limit our ability to incur additional indebtedness; require that we maintain total unencumbered assets (as defined therein) of not less than 120% of the aggregate principal amount of our outstanding unsecured indebtedness (as defined therein); and impose certain requirements in order for us to merge or consolidate with another person. Certain of these covenants will be automatically suspended if the 2021 Notes have investment grade credit ratings from each of two specified rating agencies and no default or event of default has occurred and is continuing, subject to automatic reinstatement if the 2021 Notes cease to have an investment grade credit rating from both of those two rating agencies.

These covenants may limit our flexibility to pursue certain investments or incur additional debt. If we fail to meet or satisfy any of these covenants, we would be in default under these agreements and our indebtedness could be declared due and payable. In addition, our lenders could terminate their commitments, require the posting of additional collateral and enforce their interests against existing collateral. We may also be subject to cross default and acceleration rights and, with respect to collateralized debt, the posting of additional collateral and foreclosure rights upon default. Further, this could also make it difficult for us to satisfy the distribution requirements necessary to maintain our status as a REIT for U.S. federal income tax purposes.

Our credit agreements and master repurchase agreements also involve the risk that the market value of the loans pledged or sold by us to the repurchase agreement counterparty or provider of the bank credit facility may decline in value, in which case the lender may require us to provide additional collateral or to repay all or a portion of the funds advanced. We may not have the funds available to repay our debt at that time, which would likely result in defaults unless we are able to raise the funds from alternative sources, which we may not be able to achieve on favorable terms or at all. Posting additional collateral would reduce our liquidity and limit our ability to leverage our assets. If we cannot meet these requirements, the lender could accelerate our indebtedness, increase the interest rate on advanced funds and terminate our ability to borrow funds from them, which could materially and adversely affect our financial condition and ability to continue to implement our business plan. In addition, in the event that the lender files for bankruptcy or becomes insolvent, our loans may become subject to bankruptcy or insolvency proceedings, thus depriving us, at least temporarily, of the benefit of these assets. Such an event could restrict our access to bank credit facilities and increase our cost of capital.

If one or more of our Manager's executive officers are no longer employed by our Manager, the financial institutions providing us financing may not provide future financing to us, which could materially and adversely affect us.

If financial institutions with whom we seek to finance our investments require that one or more of our Manager's executives continue to serve in such capacity and if one or more of our Manager's executives are no longer employed by our Manager, it may constitute an event of default and the financial institution providing the arrangement may have acceleration rights with respect to outstanding borrowings and termination rights with respect to our ability to finance our future investments with that institution. If we are unable to obtain financing for our accelerated borrowings and for our future investments under such circumstances, we could be materially and adversely affected.

We directly or indirectly utilize non recourse securitizations, and such structures expose us to risks that could result in losses to us.

We utilize non recourse securitizations of our investments in mortgage loans to the extent consistent with the maintenance of our REIT qualification and exemption from the Investment Company Act in order to generate cash for

funding new investments and/or to leverage existing assets. In most instances, this involves us transferring our loans to a special purpose securitization entity in exchange for cash. In some sale transactions, we also retain a subordinated interest in the loans sold. The securitization of our portfolio investments might magnify our exposure to losses on those portfolio investments because the subordinated interest we retain in the loans sold would be subordinate to the senior interest in the loans sold, and we would, therefore, absorb all of the losses sustained with respect to a loan sold before the

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owners of the senior interest experience any losses. Moreover, we cannot be assured that we will be able to access the securitization market in the future, or be able to do so at favorable rates. The inability to consummate securitizations of our portfolio investments to finance our investments on a long term basis could require us to seek other forms of potentially less attractive financing or to liquidate assets at an inopportune time or price, which could adversely affect our performance and our ability to continue to grow our business.

We may not have the ability to raise funds on acceptable terms necessary to settle conversions of our outstanding convertible senior notes or to purchase our outstanding convertible senior notes upon a fundamental change.

As of December 31, 2016, we had \$1.4 billion in principal amount of convertible senior notes outstanding. If a fundamental change within the meaning of our outstanding convertible senior notes occurs, holders of those notes will have the right to require us to purchase for cash any or all of their notes. The fundamental change purchase price will equal 100% of the principal amount of the notes to be purchased, plus accrued and unpaid interest thereon. In addition, upon conversion of the convertible senior notes, we will be required to make cash payments in respect of the notes being converted, unless we elect to settle the conversion entirely in shares of our common stock. However, we may not have sufficient funds at the time we are required to purchase the notes surrendered therefor or to make cash payments on the notes being converted, and we may not be able to arrange necessary financing on acceptable terms. If we were unable to raise necessary funding on acceptable terms, our operating results and financial position could be negatively impacted if we were required to repurchase the notes or to pay cash upon conversion.

## Risks Related to Hedging

We enter into hedging transactions that could expose us to contingent liabilities in the future.

Subject to maintaining our qualification as a REIT, part of our investment strategy involves entering into hedging transactions that require us to fund cash payments in certain circumstances (such as the early termination of the hedging instrument caused by an event of default or other early termination event, or the decision by a counterparty to request margin securities it is contractually owed under the terms of the hedging instrument). The amount due would be equal to the unrealized loss of the open swap positions with the respective counterparty and could also include other fees and charges. These economic losses will be reflected in our results of operations, and our ability to fund these obligations will depend on the liquidity of our assets and access to capital at the time, and the need to fund these obligations could adversely impact our financial condition.

Hedging may adversely affect our earnings, which could reduce our cash available for distribution to our stockholders.

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

- interest rate, currency and/or credit hedging can be expensive and may result in us receiving less interest income;
- available interest rate hedges may not correspond directly with the interest rate risk for which protection is sought;
- due to a credit loss, prepayment or asset sale, the duration of the hedge may not match the duration of the related asset or liability;
- the amount of income that a REIT may earn from hedging transactions (other than hedging transactions that satisfy certain requirements of the Code or that are done through a TRS) to offset losses is limited by U.S. federal tax

provisions governing REITs;

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

In addition, we may fail to recalculate, readjust or execute hedges in an efficient manner.

Any hedging activity in which we engage may materially and adversely affect our results of operations and cash flows. Therefore, while we may enter into such transactions seeking to reduce risks, unanticipated changes in interest rates, credit spreads or currencies may result in poorer overall investment performance than if we had not engaged in any such hedging transactions. In addition, the degree of correlation between price movements of the instruments used in a hedging strategy and price movements in the portfolio positions or liabilities being hedged may vary materially. Moreover, for a variety of reasons, we may not seek to establish a perfect correlation between such hedging instruments and the portfolio positions or liabilities being hedged. Any such imperfect correlation may prevent us from achieving the intended hedge and expose us to risk of loss.

Hedging instruments often are not traded on regulated exchanges, guaranteed by an exchange or its clearing house, or regulated by any U.S. or foreign governmental authorities and involve risks and costs that could result in material losses.

The cost of using hedging instruments increases as the period covered by the instrument increases and during periods of rising and volatile interest rates. In addition, some hedging instruments involve risk because they often are not traded on regulated exchanges, guaranteed by an exchange or its clearing house, or regulated by any U.S. or foreign governmental authorities. Consequently, in many cases, there are no requirements with respect to record keeping, financial responsibility or segregation of customer funds and positions. Furthermore, the enforceability of agreements underlying hedging transactions may depend on compliance with applicable securities, commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. The business failure of a hedging counterparty with whom we enter into a hedging transaction that is not cleared on a regulated centralized clearing house will most likely result in its default. Default by a party with whom we enter into a hedging transaction may result in the loss of unrealized profits and force us to cover our commitments, if any, at the then current market price. Although generally we will seek to reserve the right to terminate our hedging positions, it may not always be possible to dispose of or close out a hedging position without the consent of the hedging counterparty and we may not be able to enter into an offsetting contract in order to cover our risk. We cannot assure you that a liquid secondary market will exist for hedging instruments purchased or sold, and we may be required to maintain a position until exercise or expiration, which could result in significant losses.

We may fail to qualify for, or choose not to elect, hedge accounting treatment.

We record derivative and hedging transactions in accordance with GAAP. Under these standards, we may fail to qualify for, or choose not to elect, hedge accounting treatment for a number of reasons, including if we use instruments that do not meet the definition of a derivative (such as short sales), we fail to satisfy hedge documentation and hedge effectiveness assessment requirements or our instruments are not highly effective. If we fail to qualify for, or choose not to elect, hedge accounting treatment, our operating results may be volatile because changes in the fair value of the derivatives that we enter into may not be offset by a change in the fair value of the related hedged transaction or item.

We enter into derivative contracts that could expose us to contingent liabilities in the future.

Subject to maintaining our qualification as a REIT, we enter into derivative contracts that could require us to fund cash payments in the future under certain circumstances (e.g., the early termination of the derivative agreement caused by an event of default or other early termination event, or the decision by a counterparty to request margin securities it is contractually owed under the terms of the derivative contract). The amount due would be equal to the unrealized loss of the open swap positions with the respective counterparty and could also include other fees and charges. These economic losses may materially and adversely affect our results of operations and cash flows.

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### Risks Related to Our Investments

We may not be able to identify additional assets that meet our investment objective.

We cannot assure you that we will be able to identify additional assets that meet our investment objective, that we will be successful in consummating any investment opportunities we identify or that one or more investments we may make will yield attractive risk adjusted returns. Our inability to do any of the foregoing likely would materially and adversely affect our results of operations and cash flows and our ability to make distributions to our stockholders.

The lack of liquidity in our investments may adversely affect our business.

The lack of liquidity of our investments in real estate loans and investments, other than certain of our investments in mortgage backed securities (“MBS”), may make it difficult for us to sell such investments if the need or desire arises. Many of the securities we purchase are not registered under the relevant securities laws, resulting in a prohibition against their transfer, sale, pledge or their disposition except in a transaction that is exempt from the registration requirements of, or otherwise in accordance with, those laws. In addition, certain investments such as B Notes, mezzanine loans and bridge and other loans are also particularly illiquid investments due to their short life, their potential unsuitability for securitization and/or the greater difficulty of recovery in the event of a borrower default. As a result, many of our current investments are, and our future investments will be, illiquid and if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our investments. Further, we may face other restrictions on our ability to liquidate an investment in a business entity to the extent that we or our Manager has or could be attributed with material non public information regarding such business entity. As a result, our ability to vary our portfolio in response to changes in economic and other conditions may be relatively limited, which could adversely affect our results of operations and financial condition.

Our investments may be concentrated and are subject to risk of default.

While we seek to diversify our portfolio of investments, we are not required to observe specific diversification criteria, except as may be set forth in the investment guidelines adopted by our board of directors. Therefore, our investments in our target assets may at times be concentrated in certain property types that are subject to higher risk of foreclosure, or secured by properties concentrated in a limited number of geographic locations. To the extent that our portfolio is concentrated in any one region or type of asset, downturns relating generally to such region or type of asset may result in defaults on a number of our investments within a short time period, which may reduce our net income and the value of our common stock and accordingly reduce our ability to make distributions to our stockholders.

Difficult conditions in the mortgage, commercial and residential real estate markets may cause us to experience market losses related to our holdings.

Our results of operations are materially affected by conditions in the real estate markets, the financial markets and the economy generally. Concerns about the real estate market, as well as inflation, energy costs, geopolitical issues and the availability and cost of credit, have contributed to increased volatility and diminished expectations for the economy and markets going forward. The residential mortgage market has been affected by changes in the lending landscape and there is no assurance that these conditions have stabilized or that they will not worsen. The disruption in the residential mortgage market has an impact on new demand for homes, which weigh on future home price performance. There is a strong correlation between home price growth rates and mortgage loan delinquencies. Deterioration in the real estate market may cause us to experience losses related to our assets and to sell assets at a loss. Declines in the market values of our investments may adversely affect our results of operations and credit availability, which may reduce earnings and, in turn, cash available for distribution to our stockholders.

Our preferred equity investments involve a greater risk of loss than conventional debt financing.

We make preferred equity investments. These investments involve a higher degree of risk than conventional debt financing due to a variety of factors, including their non-collateralized nature and subordinated ranking to other loans and liabilities of the entity in which such preferred equity is held. Accordingly, if the issuer defaults on our

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investment, we would only be able to proceed against such entity in accordance with the terms of the preferred security, and not against any property owned by such entity. Furthermore, in the event of bankruptcy or foreclosure, we would only be able to recoup our investment after all lenders to, and other creditors of, such entity are paid in full. As a result, we may lose all or a significant part of our investment, which could result in significant losses.

Our commercial construction lending may expose us to increased lending risks.

Our commercial construction lending may expose us to increased lending risks. At December 31, 2016, our loan portfolio consisted of \$1.0 billion of commercial real estate construction loans. Construction loans generally expose a lender to greater risk of non payment and loss than permanent commercial mortgage loans because repayment of the loans often depends on the borrower's ability to secure permanent "take out" financing, which requires the successful completion of construction and stabilization of the project, or operation of the property with an income stream sufficient to meet operating expenses, including debt service on such replacement financing. For construction loans, increased risks include the accuracy of the estimate of the property's value at completion of construction and the estimated cost of construction—all of which may be affected by unanticipated construction delays and cost over runs. Such loans typically involve an expectation that the borrower's sponsors will contribute sufficient equity funds in order to keep the loan "in balance," and the sponsors' failure or inability to meet this obligation could result in delays in construction or an inability to complete construction. Commercial construction loans also expose the lender to additional risks of contractor non performance, or borrower disputes with contractors resulting in mechanic's or materialmen's liens on the property and possible further delay in construction. In addition, since such loans generally entail greater risk than mortgage loans on income producing property, we may need to increase our allowance for loan losses in the future to account for the likely increase in probable incurred credit losses associated with such loans. Further, as the lender under a construction loan, we may be obligated to fund all or a significant portion of the loan at one or more future dates. We may not have the funds available at such future date(s) to meet our funding obligations under the loan. In that event, we would likely be in breach of the loan unless we are able to raise the funds from alternative sources, which we may not be able to achieve on favorable terms or at all. In addition, many of our construction loans have multiple lenders and if another lender fails to fund we could be faced with the choice of either funding for that defaulting lender or suffering a delay or protracted interruption in the progress of construction.

We operate in a highly competitive market for investment opportunities and competition may limit our ability to acquire desirable investments in our target assets and could also affect the pricing of these investment opportunities.

We operate in a highly competitive market for investment opportunities. Our profitability depends, in large part, on our ability to acquire our target assets at attractive prices. In acquiring our target assets, we compete with a variety of institutional investors, including other REITs, commercial and investment banks, specialty finance companies, public and private funds (including other funds managed by Starwood Capital Group), commercial finance and insurance companies and other financial institutions. Many of our competitors are substantially larger and have considerably greater financial, technical, marketing and other resources than we do. Several other REITs have raised significant amounts of capital and may have investment objectives that overlap with ours, which may create additional competition for investment opportunities. Some competitors may have a lower cost of funds and access to funding sources that may not be available to us, such as funding from the U.S. government, if we are not eligible to participate in programs established by the U.S. government. Many of our competitors are not subject to the operating constraints associated with REIT tax compliance or maintenance of an exemption from the Investment Company Act. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than we do. Furthermore, competition for investments in our target assets may lead to the price of such assets increasing, which may further limit our ability to generate desired returns. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations. Also, as a result of this competition, desirable investments in our target assets may be limited in the future and we may not be able to continue to take advantage of

attractive investment opportunities from time to time, as we can provide no assurance that we will be able to identify and make additional investments that are consistent with our investment objectives.

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The commercial mortgage loans we originate or acquire and the mortgage loans underlying our CMBS investments are subject to the ability of the commercial property owner to generate net income from operating the property as well as the risks of delinquency and foreclosure.

Commercial mortgage loans are secured by multifamily or commercial property and are subject to risks of delinquency and foreclosure, and risks of loss that may be greater than similar risks associated with loans made on the security of single family residential property. The ability of a borrower to repay a loan secured by an income producing property typically is dependent primarily upon the successful operation of such property rather than upon the existence of independent income or assets of the borrower. If the net operating income of the property is reduced, the borrower's ability to repay the loan may be impaired. Net operating income of an income producing property can be adversely affected by, among other things,

- tenant mix;
- success of tenant businesses;
- property management decisions;
- property location, condition and design;
- competition from comparable types of properties;
- changes in laws that increase operating expenses or limit rents that may be charged;
- changes in national, regional or local economic conditions and/or specific industry segments, including the credit and securitization markets;
- declines in regional or local real estate values;
- declines in regional or local rental or occupancy rates;
- increases in interest rates, real estate tax rates and other operating expenses;
- costs of remediation and liabilities associated with environmental conditions;
- the potential for uninsured or underinsured property losses;
- changes in governmental laws and regulations, including fiscal policies, zoning ordinances and environmental legislation and the related costs of compliance; and
- acts of God, terrorist attacks, social unrest and civil disturbances.

In the event of any default under a mortgage loan held directly by us, we will bear a risk of loss of principal to the extent of any deficiency between the value of the collateral and the principal and accrued interest of the mortgage loan, which could have a material adverse effect on our cash flow from operations and limit amounts available for distribution to our stockholders. In the event of the bankruptcy of a mortgage loan borrower, the mortgage loan to such borrower will be deemed to be secured only to the extent of the value of the underlying collateral at the time of bankruptcy (as determined by the bankruptcy court), and the lien securing the mortgage loan will be subject to the avoidance powers of the bankruptcy trustee or debtor in possession to the extent the lien is unenforceable under state

law. Foreclosure of a mortgage loan can be an expensive and lengthy process, which could have a substantial negative effect on our anticipated return on the foreclosed mortgage loan.

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Our investments in CMBS are generally subject to losses.

Our investments in CMBS are subject to losses. In general, losses on a mortgaged property securing a mortgage loan included in a securitization will be borne first by the equity holder of the property, then by a cash reserve fund or letter of credit, if any, then by the holder of a mezzanine loan or B Note, if any, then by the “first loss” subordinated security holder (generally, the “B Piece” buyer) and then by the holder of a higher rated security. In the event of default and the exhaustion of any equity support, reserve fund, letter of credit, mezzanine loans or B Notes, and any classes of securities junior to those in which we invest, we will not be able to recover all of our investment in the securities we purchase. In addition, if the underlying mortgage portfolio has been overvalued by the originator, or if the values subsequently decline and, as a result, less collateral is available to satisfy interest and principal payments due on the related CMBS, there would be an increased risk of loss. The prices of lower credit quality securities are generally less sensitive to interest rate changes than more highly rated investments, but more sensitive to adverse economic downturns or individual issuer developments.

Dislocations, illiquidity and volatility in the market for commercial real estate as well as the broader financial markets could adversely affect the performance and value of commercial mortgage loans, the demand for CMBS and the value of CMBS investments.

In recent years, the real estate and securitization markets, including the market for CMBS, as well as global financial markets and the economy generally, experienced significant dislocations, illiquidity and volatility. We cannot assure you that dislocations in the commercial mortgage loan market will not occur in the future.

Challenging economic conditions have affected the financial strength of many commercial, multi family and other tenants and have resulted in increased rent delinquencies and decreased occupancy. Economic challenges may lead to decreased occupancy, decreased rents or other declines in income from, or the value of, commercial, multi family and manufactured housing community real estate.

In past years, declining commercial real estate values, coupled with tighter underwriting standards for commercial real estate loans, prevented many commercial borrowers from refinancing their mortgages, which resulted in increased delinquencies and defaults on commercial, multi family and other mortgage loans. Past declines in commercial real estate values also resulted in reduced borrower equity, further hindering borrowers’ ability to refinance in an environment of increasingly restrictive lending standards and giving them less incentive to cure delinquencies and avoid foreclosure. The lack of refinancing opportunities in past years has impacted and could impact in the future, in particular, mortgage loans that do not fully amortize and on which there is a substantial balloon payment due at maturity, because borrowers generally expect to refinance these types of loans on or prior to their maturity date. There are substantial amounts of U.S. mortgage loans with balloon payment obligations in excess of their respective current property values that are scheduled to mature over the next 18 months. Finally, declining commercial real estate values and the associated increases in loan to value ratios would result in lower recoveries on foreclosure and an increase in losses above those that would have been realized had commercial property values remained the same or increased. Continuing defaults, delinquencies and losses would further decrease property values, thereby resulting in additional defaults by commercial mortgage borrowers, further credit constraints and further declines in property values.

If our Manager overestimates the yields or incorrectly prices the risks of our investments, we may experience losses.

Our Manager values our potential investments based on yields and risks, taking into account estimated future losses on the mortgage loans and the underlying collateral included in the securitization’s pools, and the estimated impact of these losses on expected future cash flows and returns. Our Manager’s loss estimates may not prove accurate, as actual results may vary from estimates. In the event that our Manager underestimates the asset level losses relative to the price we pay for a particular investment, we may experience losses with respect to such investment.



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Real estate valuation is inherently subjective and uncertain.

The valuation of real estate and therefore the valuation of any underlying security relating to loans made by us is inherently subjective due to, among other factors, the individual nature of each property, its location, the expected future rental revenues from that particular property and the valuation methodology adopted. In addition, where we invest in construction loans, initial valuations will assume completion of the project. As a result, the valuations of the real estate assets against which we will make loans are subject to a degree of uncertainty and are made on the basis of assumptions and methodologies that may not prove to be accurate, particularly in periods of volatility, low transaction flow or restricted debt availability in the commercial or residential real estate markets.

Any investments in corporate bank debt and debt securities of commercial real estate operating or finance companies are subject to the specific risks relating to the particular companies and to the general risks of investing in real estate related loans and securities, which may result in significant losses.

We may invest in corporate bank debt and in debt securities of commercial real estate operating or finance companies. These investments involve special risks relating to the particular company, including its financial condition, liquidity, results of operations, business and prospects. In particular, the debt securities are often non collateralized and may also be subordinated to its other obligations. We also invest in debt securities of companies that are not rated or are rated non investment grade by one or more rating agencies. Investments that are not rated or are rated non investment grade have a higher risk of default than investment grade rated assets and therefore may result in losses to us. We have not adopted any limit on such investments.

These investments also subject us to the risks inherent with real estate related investments, including:

- risks of delinquency and foreclosure, and risks of loss in the event thereof;
- the dependence upon the successful operation of, and net income from, real property;
- risks generally incident to interests in real property; and
- risks specific to the type and use of a particular property.

These risks may adversely affect the value of our investments in commercial real estate operating and finance companies and the ability of the issuers thereof to make principal and interest payments in a timely manner, or at all, and could result in significant losses.

Investments in non conforming and non investment grade rated loans or securities involve increased risk of loss.

Many of our investments do not conform to conventional loan standards applied by traditional lenders and either are not rated or rated as non investment grade by the rating agencies. The non investment grade credit ratings for these assets typically result from the overall leverage of the loans, the lack of a strong operating history for the properties underlying the loans, the borrowers' credit history, the properties' underlying cash flow or other factors. As a result, these investments have a higher risk of default and loss than investment grade rated assets. Any loss we incur may be significant and may reduce distributions to our stockholders and adversely affect the market value of our common stock. There are no limits on the percentage of unrated or non investment grade rated assets we may hold in our investment portfolio.

Any credit ratings assigned to our investments are subject to ongoing evaluations and revisions and we cannot assure you that those ratings will not be downgraded.

Some of our investments are rated by Moody's Investors Service, Inc., Fitch Ratings, Inc., Standard & Poor's Ratings Services, DBRS, Inc., Kroll Bond Rating Agency, Inc. or Morningstar Credit Ratings, LLC. Any credit ratings on our investments are subject to ongoing evaluation by credit rating agencies, and we cannot assure you that any such ratings will not be changed or withdrawn by a rating agency in the future if, in its judgment, circumstances warrant. If

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rating agencies assign a lower than expected rating or reduce or withdraw, or indicate that they may reduce or withdraw, their ratings of our investments in the future, the value of these investments could significantly decline, which would adversely affect the value of our investment portfolio and could result in losses upon disposition or the failure of borrowers to satisfy their debt service obligations to us.

The B Notes that we acquire may be subject to additional risks related to the privately negotiated structure and terms of the transaction, which may result in losses to us.

We invest in B Notes. A B Note is a mortgage loan typically (i) secured by a first mortgage on a single large commercial property or group of related properties and (ii) subordinated to an A Note secured by the same first mortgage on the same collateral. As a result, if a borrower defaults, there may not be sufficient funds remaining for a B Note holder after payment to the A Note holder. However, because each transaction is privately negotiated, B Notes can vary in their structural characteristics and risks. For example, the rights of holders of B Notes to control the process following a borrower default may vary from transaction to transaction. Further, B Notes typically are secured by a single property and so reflect the risks associated with significant concentration. Significant losses related to our B Notes would result in operating losses for us and may limit our ability to make distributions to our stockholders.

Our mezzanine loans involve greater risks of loss than senior loans secured by income producing properties.

We invest in mezzanine loans, which sometimes take the form of subordinated loans secured by second mortgages on the underlying property or more commonly take the form of loans secured by a pledge of the ownership interests of either the entity owning the property or a pledge of the ownership interests of the entity that owns the interest in the entity owning the property. These types of assets involve a higher degree of risk than long term senior mortgage lending secured by income producing real property because the loan may become unsecured as a result of foreclosure by the senior lender. In the event of a bankruptcy of the entity providing the pledge of its ownership interests as security, we may not have full recourse to the assets of such entity, or the assets of the entity may not be sufficient to satisfy our mezzanine loan. If a borrower defaults on our mezzanine loan or debt senior to our loan, or in the event of a borrower bankruptcy, our mezzanine loan will be satisfied only after the senior debt. As a result, we may not recover some or all of our investment. In addition, mezzanine loans may have higher loan to value ratios than conventional mortgage loans, resulting in less equity in the property and increasing the risk of loss of principal. Significant losses related to our mezzanine loans would result in operating losses for us and may limit our ability to make distributions to our stockholders.

Bridge loans involve a greater risk of loss than traditional investment grade mortgage loans with fully insured borrowers.

We may acquire bridge loans secured by first lien mortgages on a property to borrowers who are typically seeking short term capital to be used in an acquisition, construction or rehabilitation of a property, or other short term liquidity needs. The typical borrower under a bridge loan has usually identified an undervalued asset that has been under managed and/or is located in a recovering market. If the market in which the asset is located fails to recover according to the borrower's projections, or if the borrower fails to improve the quality of the asset's management and/or the value of the asset, the borrower may not receive a sufficient return on the asset to satisfy the bridge loan, and we bear the risk that we may not recover some or all of our initial expenditure.

In addition, borrowers usually use the proceeds of a conventional mortgage to repay a bridge loan. A bridge loan therefore is subject to the risk of a borrower's inability to obtain permanent financing to repay the bridge loan. Bridge loans are also subject to risks of borrower defaults, bankruptcies, fraud, losses and special hazard losses that are not covered by standard hazard insurance. In the event of any default under bridge loans held by us, we bear the risk of loss of principal and non payment of interest and fees to the extent of any deficiency between the value of the

mortgage collateral and the principal amount and unpaid interest of the bridge loan. To the extent we suffer such losses with respect to our bridge loans, the value of our company and the price of our shares of common stock may be adversely affected.

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We purchase securities backed by subprime or alternative documentation residential mortgage loans, which are subject to increased risks.

We own non agency RMBS backed by collateral pools of mortgage loans that have been originated using underwriting standards that are less restrictive than those used in underwriting “prime” mortgage loans. These lower standards include mortgage loans made to borrowers having imperfect or impaired credit histories, mortgage loans where the amount of the loan at origination is 80% or more of the value of the mortgaged property, mortgage loans made to borrowers with low credit scores, mortgage loans made to borrowers who have other debt that represents a large portion of their income and mortgage loans made to borrowers whose income is not required to be disclosed or verified. Due to economic conditions, including increased interest rates and lower home prices, as well as aggressive lending practices, subprime mortgage loans have in recent periods experienced increased rates of delinquency, foreclosure, bankruptcy and loss, and they are likely to continue to experience delinquency, foreclosure, bankruptcy and loss rates that are higher, and that may be substantially higher, than those experienced by mortgage loans underwritten in a more traditional manner. Thus, because of the higher delinquency rates and losses associated with subprime mortgage loans and alternative documentation (“Alt-A”) mortgage loans, the performance of non agency RMBS backed by subprime mortgage loans and Alt-A mortgage loans that we acquire could be correspondingly adversely affected, which could adversely impact our results of operations, financial condition and business.

We may acquire and sell from time to time residential mortgage loans, including “non-QM” loans, which may subject us to legal, regulatory and other risks, which could adversely impact our business and financial results.

We may from time to time acquire residential mortgage loans, including residential mortgage loans sometimes referred to as “non-qualified mortgages” or “non-QMs” that will not have the benefit of enhanced legal protections otherwise available in connection with the origination of residential mortgage loans to a more restrictive credit standard than just determining a borrower’s ability to repay, as further described below.

The ownership of residential mortgage loans, including non-QMs, will subject us to legal, regulatory and other risks, including those arising under federal consumer protection laws and regulations designed to regulate residential mortgage loan underwriting and originators’ lending processes, standards, and disclosures to borrowers. These laws and regulations include the Consumer Financial Protection Bureau’s (“CFPB”) TILA-RESPA Integrated Disclosure rule (also referred to as “TRID”), the “ability-to-repay” rules (“ATR Rules”) under the Truth-in-Lending Act and “qualified mortgage” regulations, in addition to various federal, state and local laws and regulations intended to discourage predatory lending practices by residential mortgage loan originators. The ATR Rules specify the characteristics of a “qualified mortgage” and two levels of presumption of compliance with the ATR Rules: a safe harbor and a rebuttable presumption for higher priced loans. The “safe harbor” under the ATR Rules applies to a covered transaction that meets the definition of “qualified mortgage” and is not a “higher-priced covered transaction.” For any covered transaction that meets the definition of a “qualified mortgage” and is not a “higher-priced covered transaction,” the creditor or assignee will be deemed to have complied with the ability-to-repay requirement and, accordingly, will be conclusively presumed to have made a good faith and reasonable determination of the consumer’s ability to repay. Creditors or assignees will have the benefit of a rebuttable presumption of compliance with the applicable ATR Rules if they have complied with the qualified mortgage characteristics of the ATR Rules other than the residential mortgage loan being higher-priced in excess of certain thresholds. Non-QMs, such as residential mortgage loans with a debt-to-income ratio exceeding 43%, are among the loan products that we may acquire that do not constitute qualified mortgages and, accordingly, do not have the benefit of either a safe harbor from liability under the ATR Rules or a rebuttable presumption of compliance with the ATR Rules. Application of certain standards set forth in the ATR Rules is highly subjective and subject to interpretive uncertainties. As a result, a court may determine that a residential mortgage loan did not meet the standard or test even if the originator reasonably believed such standard or test had been satisfied. Failure of residential mortgage loan originators or servicers to comply with these laws and regulations could subject us, as an assignee or purchaser of these loans (or as an investor in securities backed by these loans), to monetary

penalties assessed by the CFPB through its administrative enforcement authority and by mortgagors through a private right of action against lenders or as a defense to foreclosure, including by recoupment or setoff of finance charges and fees collected, and could result in rescission of the affected residential mortgage loans, which could adversely impact our business and financial results. Such risks may be higher in connection with the acquisition of non-QMs. Borrowers under Non-QMs may be more likely to challenge the analysis conducted under the ATR Rules by lenders. Even if a borrower does not succeed in the challenge, additional costs may be incurred in connection with challenging and defending such claims, which may be more costly in judicial foreclosure jurisdictions than in non-judicial foreclosure jurisdictions, and there may be more of a

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likelihood such claims are made since the borrower is already exposed to the judicial system to process the foreclosure.

In addition, when certain of our wholly-owned subsidiaries sell, finance or sponsor securitizations of residential mortgage loans, such subsidiaries may make representations and warranties to the purchaser, the financing provider or to other third parties regarding, among other things, certain characteristics of those assets, including characteristics sought to be verified through underwriting and due diligence efforts. In the event of breaches of representations and warranties with respect to any asset, such subsidiaries may be obligated to repurchase that asset or pay damages or remove that asset from the borrowing base, as applicable, which may result in a loss. Even if representations and warranties are made by counterparties from whom we acquired the loans, they may not parallel the representations and warranties our subsidiaries make or may otherwise not protect us from losses, including, for example, due to the fact that the counterparty may be insolvent or otherwise unable to make a payment at the time of a claim against such counterparty for damages for a breach of representation or warranty.

The residential mortgage loans that we may acquire, and that underlie the RMBS we acquire, are subject to risks particular to investments secured by mortgage loans on residential property. These risks are heightened because we may purchase non-performing loans.

Residential mortgage loans are secured by single family residential property and are subject to risks of delinquency and foreclosure and risks of loss. The ability of a borrower to repay a loan secured by a residential property typically is dependent upon the income and/or assets of the borrower. A number of factors may impair borrowers' abilities to repay their loans, including:

- changes in the borrowers' income or assets;
- acts of God, which may result in uninsured losses;
- acts of war or terrorism, including the consequences of such events;
- adverse changes in national and local economic and market conditions;
- changes in governmental laws and regulations, including fiscal policies, zoning ordinances and environmental legislation and the related costs of compliance;
- costs of remediation and liabilities associated with environmental conditions; and
- the potential for uninsured or under insured property losses.

In the event of any default under a residential mortgage loan held directly by us, we will bear a risk of loss of principal to the extent of any deficiency between the value of the collateral and the price we paid for the loan and any accrued interest of the mortgage loan plus advances made, which could have a material adverse effect on our cash flow from operations. In the event of the bankruptcy of a mortgage loan borrower, the mortgage loan to such borrower will be deemed to be secured only to the extent of the value of the underlying collateral at the time of bankruptcy (as determined by the bankruptcy court), and the lien securing the mortgage loan will be subject to the avoidance powers of the bankruptcy trustee or debtor in possession to the extent the lien is unenforceable under state law. Additionally, foreclosure on a mortgage loan could subject us to greater concentration of the risks of the residential real estate markets and risks related to the ownership and management of real property.

We may acquire non-agency RMBS, which are backed by residential property but, in contrast to agency RMBS, their principal and interest are not guaranteed by federally chartered entities such as the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation and, in the case of the Government National Mortgage Association, the U.S. government. Our investments in RMBS are subject to the risks of defaults, foreclosure timeline extension, fraud, home price depreciation and unfavorable modification of loan principal amount, interest rate and amortization of principal accompanying the underlying residential mortgage loans. To the extent that assets underlying our investments are concentrated geographically, by property type or in certain other respects, we may be subject to

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certain of the foregoing risks to a greater extent. In the event of defaults on the residential mortgage loans that underlie our investments in agency RMBS and the exhaustion of any underlying or any additional credit support, we may not realize our anticipated return on our investments and we may incur a loss on these investments.

Our inability to promptly foreclose upon defaulted residential mortgage loans could increase our cost of doing business and/or diminish our expected return on investments.

Our ability to promptly foreclose upon defaulted residential mortgage loans and liquidate the underlying real property plays a critical role in our valuation of, and expected return on, those investments. There are a variety of factors that may inhibit our ability to foreclose upon a residential mortgage loan and liquidate the real property within the time frames we model as part of our valuation process. These factors include, without limitation: federal, state or local legislative action or initiatives designed to provide homeowners with assistance in avoiding residential mortgage loan foreclosures and that serve to delay the foreclosure process; Home Affordable Modification Program and other programs that require specific procedures to be followed to explore the refinancing of a mortgage loan prior to the commencement of a foreclosure proceeding; and continued declines in real estate values and sustained high levels of unemployment that increase the number of foreclosures and place additional pressure on the already overburdened judicial and administrative systems.

Prepayment rates may adversely affect the value of our investment portfolio.

The value of our investment portfolio is affected by prepayment rates on our mortgage assets. In many cases, borrowers are not prohibited from making prepayments on their mortgage loans. Prepayment rates are influenced by changes in interest rates and a variety of economic, geographic and other factors beyond our control, including, without limitation, housing and financial markets and relative interest rates on fixed rate mortgage loans, and adjustable rate mortgage loans (“ARMs”) and consequently prepayment rates cannot be predicted.

We generally receive payments from principal payments that are made on our mortgage assets, including residential mortgage loans underlying the agency RMBS or the non agency RMBS that we acquire. When borrowers prepay their mortgage loans faster than expected, it results in prepayments that are faster than expected. Faster than expected prepayments could adversely affect our profitability and our ability to recoup our cost of certain investments purchased at a premium over par value, including in the following ways:

- We may purchase RMBS that have a higher interest rate than the prevailing market interest rate at the time. In exchange for this higher interest rate, we may pay a premium over the par value to acquire our mortgage asset. In accordance with GAAP, we may amortize this premium over the estimated term of our mortgage asset. If our mortgage asset is prepaid in whole or in part prior to its maturity date, however, we may be required to expense the allocable portion of the premium at the time of the prepayment.
- Prepayment rates generally increase when interest rates fall and decrease when interest rates rise, making it unlikely that we would be able to reinvest the proceeds of any prepayment in mortgage assets of similar quality and terms (including yield). If we are unable to invest in similar mortgage assets, we would be adversely affected.

While we seek to minimize prepayment risk to the extent practical, in selecting investments we must balance prepayment risk against other risks and the potential returns of each investment. No strategy can completely insulate us from prepayment risk.

Interest rate mismatches between our agency RMBS backed by ARMs and our borrowings used to fund our purchases of these assets may reduce our net interest income and cause us to suffer a loss during periods of rising interest rates.

To the extent that we invest in agency RMBS backed by ARMs, we may finance these investments with borrowings that have interest rates that adjust more frequently than the interest rates of those agency RMBS or the ARMs that back those RMBS. Accordingly, if short term interest rates increase, our borrowing costs may increase faster

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than the interest rates on agency RMBS backed by ARMs adjust. As a result, in a period of rising interest rates, we could experience a decrease in net income or a net loss. In most cases, the interest rates on our agency RMBS and on our borrowings will not be identical, thereby potentially creating an interest rate mismatch between our investments and our borrowings. While the historical spread between relevant short term interest rate indices has been relatively stable, there have been periods when the spread between these indices was volatile. During periods of changing interest rates, these interest rate index mismatches could reduce our net income or produce a net loss, and adversely affect our ability to make distributions and the market price of our common stock.

In addition, agency RMBS backed by ARMs are typically subject to lifetime interest rate caps which limit the amount that interest rates can increase through the maturity of the agency RMBS. However, our borrowings under repurchase agreements typically are not subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, the interest rates paid on our borrowings could increase without limitation while caps could limit the interest rates on these types of agency RMBS. This problem is magnified for agency RMBS backed by ARMs that are not fully indexed. Further, some agency RMBS backed by ARMs may be subject to periodic payment caps that result in a portion of the interest being deferred and added to the principal outstanding. As a result, we may receive less cash income on these types of agency RMBS than we need to pay interest on our related borrowings. These factors could reduce our net interest income and cause us to suffer a loss during periods of rising interest rates.

Risks of cost overruns and noncompletion of renovation of the properties underlying rehabilitation loans may result in significant losses.

The renovation, refurbishment or expansion by a borrower under a mortgaged property involves risks of cost overruns and noncompletion. Estimates of the costs of improvements to bring an acquired property up to standards established for the market position intended for that property may prove inaccurate. Other risks may include rehabilitation costs exceeding original estimates, possibly making a project uneconomical, environmental risks and rehabilitation and subsequent leasing of the property not being completed on schedule. If such renovation is not completed in a timely manner, or if it costs more than expected, the borrower may experience a prolonged impairment of net operating income and may not be able to make payments on our investment, which could result in significant losses.

Interest rate fluctuations could reduce our ability to generate income on our investments and may cause losses.

Changes in interest rates affect our net interest income, which is the difference between the interest income we earn on our interest earning investments and the interest expense we incur in financing these investments. Changes in the level of interest rates also may affect our ability to originate and acquire assets, the value of our assets and our ability to realize gains from the disposition of assets. Changes in interest rates may also affect borrower default rates. In a period of rising interest rates, our interest expense could increase, while the interest we earn on our fixed rate debt investments would not change, adversely affecting our profitability. Our operating results depend in large part on differences between the income from our assets, net of credit losses, and our financing costs. We anticipate that for any period during which our assets are not match funded, the income from such assets will respond more slowly to interest rate fluctuations than the cost of our borrowings. Consequently, changes in interest rates may significantly influence our net income. Interest rate fluctuations resulting in our interest expense exceeding interest income would result in operating losses for us.

We may invest in distressed and non-performing commercial loans which could subject us to increased risks relative to performing loans, which may result in losses to us.

We may invest in distressed and non-performing commercial mortgage loans, which are subject to increased risks of loss. Such loans may be or become non-performing for a variety of reasons, including, without limitation, because the underlying property is too highly leveraged or the borrower falls upon financial distress, in either case, resulting in the

borrower being unable to meet its debt service obligations. Such loans may require a substantial amount of workout negotiations and/or restructuring, which may divert the attention of our Manager from other activities and may entail, among other things, a substantial reduction in the interest rate and a substantial write-down of the principal of the loan. Moreover, the ability to implement a successful restructuring entails a high degree of uncertainty, and there can be no assurance that our Manager would be able to implement any such restructuring on favorable terms or at all.

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The financial or operating difficulties relating to the distressed or non-performing loan may never be overcome and may cause the borrower to become subject to bankruptcy or other similar administrative proceedings. In connection with any such proceeding, we may incur substantial or total losses on our investments and may become subject to certain additional potential liabilities that may exceed the value of our original investment therein. For example, under certain circumstances, a lender that has inappropriately exercised control over the management and policies of a debtor may have its claims subordinated or disallowed or may be found liable for damages suffered by parties as a result of such actions. In addition, under certain circumstances, payments to us may be reclaimed if any such payment is later determined to have been a fraudulent conveyance, preferential payment, or similar transaction under applicable bankruptcy and insolvency laws.

Alternatively, we may find it necessary or desirable to foreclose on one of these loans, and the foreclosure process may be lengthy and expensive. Borrowers or junior lenders may resist mortgage foreclosure actions by asserting numerous claims, counterclaims and defenses against us. Any costs or delays involved in the effectuation of a foreclosure of the loan or a liquidation of the underlying property, or defending challenges brought after the completion of a foreclosure, will further reduce the proceeds and thus increase our loss.

We may experience a decline in the fair value of our assets.

A decline in the fair value of our assets may require us to recognize an “other than temporary” impairment against such assets under GAAP if we were to determine that, with respect to any assets in unrealized loss positions, we do not have the ability and intent to hold such assets to maturity or for a period of time sufficient to allow for recovery to the amortized cost of such assets. If such a determination were to be made, we would recognize unrealized losses through earnings and write down the amortized cost of such assets to a new cost basis, based on the fair value of such assets on the date they are considered to be other than temporarily impaired. Such impairment charges reflect non-cash losses at the time of recognition; subsequent disposition or sale of such assets could further affect our future losses or gains, as they are based on the difference between the sale price received and adjusted amortized cost of such assets at the time of sale.

Some of our portfolio investments are recorded at fair value and, as a result, there is uncertainty as to the value of these investments.

Some of our portfolio investments are in the form of positions or securities that are not publicly traded. The fair value of securities and other investments that are not publicly traded may not be readily determinable. We value these investments quarterly at fair value, as determined in accordance with GAAP, which include consideration of unobservable inputs. Because such valuations are subjective, the fair value of certain of our assets may fluctuate over short periods of time and our determinations of fair value may differ materially from the values that would have been used if a ready market for these securities existed. The value of our common stock could be adversely affected if our determinations regarding the fair value of these investments were materially higher than the values that we ultimately realize upon their disposal.

Liability relating to environmental matters may impact the value of properties that we may purchase or acquire.

We may be subject to environmental liabilities arising from properties we own. Under various U.S. federal, state and local laws, an owner or operator of real property may become liable for the costs of removal of certain hazardous