AG Mortgage Investment Trust, Inc.
Form 10-Q
August 08, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2012

OR

o 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 001-35151

AG MORTGAGE INVESTMENT TRUST, INC.

Maryland 27-5254382

(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
245 Park Avenue, 26th Floor New York, New York (Address of Principal Executive Offices)	10167 (Zip Code)

(212) 692-2000

(Registrant's Telephone Number, Including Area Code)

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

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

Indicate by check mark whether the registrant is a large accelerated filed, 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 x 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 Exchange Act).
Yes ¨ No x

As of August 8, 2012, there were 15,807,258 outstanding shares of common stock of AG Mortgage Investment Trust, Inc.

AG MORTGAGE INVESTMENT TRUST, INC.

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PART I

ITEM 1. FINANCIAL STATEMENTS

AG Mortgage Investment Trust, Inc. and Subsidiaries

Consolidated Balance Sheets

(Unaudited)

	June 30, 2012	December 31, 2011
Assets		
Real estate securities, at fair value		
Agency - $2,138,181,777 and $1,186,149,842 pledged as collateral, respectively	$2,249,892,387	$ 1,263,214,099
Non-Agency - $122,992,984 and $47,227,005 pledged as collateral, respectively	149,897,715	58,787,051
ABS - $13,509,441 and $4,526,620 pledged as collateral, respectively	13,509,441	4,526,620
CMBS - $11,557,506 and $2,747,080 pledged as collateral, respectively	11,557,506	13,537,851
Linked transactions, net, at fair value	44,074,905	8,787,180
Cash and cash equivalents	17,457,490	35,851,249
Restricted cash	2,303,178	3,037,055
Interest receivable	8,341,685	4,219,640
Receivable on unsettled trades	141,814,687	-
Derivative assets, at fair value	-	1,428,595
Other assets	35,826	711,617
Due from affiliates	-	104,994
Total Assets	$2,638,884,820	$ 1,394,205,951
Liabilities		
Repurchase agreements	$2,133,730,466	$ 1,150,149,407
Payable on unsettled trades	123,670,601	18,759,200
Interest payable	752,036	613,803
Derivative liabilities, at fair value	23,413,215	9,569,643
Dividend payable	11,042,972	7,011,171
Due to affiliates	1,196,383	770,341
Accrued expenses	822,531	668,552
Due to broker	54,000	379,914
Total Liabilities	2,294,682,204	1,187,922,031
Stockholders' Equity		
	157,697	100,100

Common stock, par value $0.01 per share; 450,000,000 shares of common stock authorized and 15,769,674 and 10,009,958 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively		
Additional paid-in capital	302,304,109	198,228,694
Retained earnings	41,740,810	7,955,126
	344,202,616	206,283,920
Total Liabilities & Equity	$2,638,884,820	$ 1,394,205,951

The accompanying notes are an integral part of these consolidated financial statements.

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AG Mortgage Investment Trust, Inc. and Subsidiaries

Consolidated Statement of Operations

(Unaudited)

	Three Months Ended June 30, 2012	Period from March 7, 2011 to June 30, 2011	Six Months Ended June 30, 2012	Period from March 7, 2011 to June 30, 2011
Net Interest Income				
Interest income	$ 17,883,008	$ -	$ 31,879,636	$ -
Interest expense	2,450,017	-	4,277,431	-
	15,432,991	-	27,602,205	-
Other Income				
Net realized gain	7,552,780	-	9,981,800	-
Gain on linked transactions, net	3,364,972	-	6,804,157	-
Realized loss on periodic interest settlements of interest rate swaps, net	(2,132,414)	-	(3,590,364)	-
Unrealized loss on derivative instruments, net	(10,575,768)	-	(13,421,647)	-
Unrealized gain on real estate securities, net	33,593,211	-	32,837,659	-
	31,802,781	-	32,611,605	-
Expenses				
Management fee to affiliate	1,196,383	-	2,245,677	-
Other operating expenses	760,915	15,818	1,574,239	15,818
Equity based compensation to affiliate	104,771	-	192,100	-
Excise tax	255,925	-	333,578	-
	2,317,994	15,818	4,345,594	15,818
Net Income (Loss)	$ 44,917,778	$ (15,818)	$ 55,868,216	$ (15,818)
Earnings Per Share of Common Stock				
Basic	$ 2.85	NM	$ 3.73	NM
Diluted	$ 2.85	NM	$ 3.73	NM
Weighted Average Number of Shares of Common Stock Outstanding				
Basic	15,769,674	NM	14,974,655	NM
Diluted	15,772,853	NM	14,976,123	NM
Dividends Declared per Share of Common Stock	$ 0.70	$ -	$ 1.40	$ -

NM - not meaningful - See Note 2 for details

The accompanying notes are an integral part of these consolidated financial statements.

AG Mortgage Investment Trust, Inc. and Subsidiaries

Consolidated Statement of Stockholders' Equity

(Unaudited)

	Common Stock		Preferred Stock		Additional	Retained	
	Shares	Amount	Shares	Amount	Paid-in-Capital	Earnings	Total
Balance at March 7, 2011	-	$ -	-	$ -	$ -	$ -	$ -
Issuance of common stock	100	1	-	-	999	-	1,000
Net loss	-	-	-	-	-	(15,818)	(15,818)
Balance at June 30, 2011	100	$ 1	-	$ -	$ 999	$ (15,818)	$ (14,818)
Balance at January 1, 2012	10,009,958	$ 100,100	-	$ -	$ 198,228,694	$ 7,955,126	$ 206,283,920
Issuance of common stock	5,750,000	57,500	-	-	109,192,500	-	109,250,000
Offering costs			-	-	(5,344,481)	-	(5,344,481)
Grant of restricted stock and amortization of equity based compensation	9,716	97	-	-	227,396	-	227,493
Dividends declared	-	-	-	-		(22,082,532)	(22,082,532)
Net income	-	-	-	-	-	55,868,216	55,868,216
Balance at June 30, 2012	15,769,674	$ 157,697	-	$ -	$ 302,304,109	$ 41,740,810	$ 344,202,616

The accompanying notes are an integral part of these consolidated financial statements.

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AG Mortgage Investment Trust, Inc. and Subsidiaries

Consolidated Statement of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2012	Period from March 7, 2011 to June 30, 2011
Cash Flows from Operating Activities		
Net income (loss)	$ 55,868,216	$ (15,818)
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized gain	(9,981,800)	-
Net accretion of premium related to real estate securities	13,098,144	-
Unrealized gains on linked transactions, net	(2,859,986)	-
Unrealized losses on derivative instruments, net	13,421,647	-
Unrealized gains on real estate securities, net	(32,837,659)	-
Equity based compensation to affiliate	192,100	-
Equity based compensation expense	80,005	-
Change in operating assets/liabilities:		
Interest receivable	(4,122,045)	-
Prepaid expense	282,124	-
Other assets	393,667	-
Due from affiliates	104,994	-
Interest payable	1,977,035	-
Due to affiliates	426,042	-
Accrued expenses	153,979	15,605
Due to broker	(325,914)	-
Net cash provided by operating activities	35,870,549	(213)
Cash Flows from Investing Activities		
Purchase of real estate securities	(1,628,868,857)	-
Purchase of securities underlying linked transactions	(258,088,821)	-
Proceeds from sale of real estate securities	438,488,138	-
Proceeds from sale of securities underlying linked transactions	17,536,406	
Principal repayments on real estate securities	101,870,967	-
Principal repayments on securities underlying linked transactions	20,823,409	-
Net settlement of interest rate swaps	(267,115)	-
Net settlement of TBAs	1,717,266	-
Restricted cash provided by investment activities	2,208,001	-
Net cash used in investing activities	(1,304,580,606)	-
Cash Flows from Financing Activities		
Proceeds from issuance of common stock	109,250,000	1,000
Payment of offering costs	(5,344,481)	-

Borrowings under repurchase agreements	8,998,701,429	-
Borrowings under repurchase agreements underlying linked transactions	981,637,451	-
Repayments of repurchase agreements	(8,015,120,370)	-
Repayments of repurchase agreements underlying linked transactions	(799,282,876)	-
Collateral held by derivative counterparty	(340,000)	-
Collateral held by repurchase counterparty	(1,134,124)	-
Dividend paid	(18,050,731)	-
Net cash provided by financing activities	1,250,316,298	1,000
Net change in cash and cash equivalents	(18,393,759)	787
Cash and cash equivalents, Beginning of Period	35,851,249	-
Cash and cash equivalents, End of Period	$ 17,457,490	$ 787
Supplemental disclosure of cash flow information:		
Cash paid for interest on repurchase agreements	$ 3,960,904	$ -
Supplemental disclosure of non-cash financing activities:		
Common stock dividends declared but not paid	$ 11,042,972	$ -
Contributions received in advance	$ -	$ 63,150,227
Increase in deferred costs due to offering costs incurred	$ -	$ 1,825,395

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AG Mortgage Investment Trust Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

1. Organization

AG Mortgage Investment Trust, Inc. (the "Company") was organized in the state of Maryland on March 1, 2011. The Company is focused on investing in, acquiring and managing a diversified portfolio of residential mortgage-backed securities, or RMBS, issued or guaranteed by a government-sponsored enterprise such as Fannie Mae or Freddie Mac, or any agency of the U.S. Government such as Ginnie Mae (collectively, "Agency RMBS"), and other real estate-related securities and financial assets, including Non-Agency RMBS, ABS and CMBS.

Non-Agency RMBS represent fixed-and floating-rate residential non-Agency RMBS, including investment grade (AAA through BBB) and non-investment grade classes (BB and below). The mortgage loan collateral for residential Non-Agency RMBS consists of residential mortgage loans that do not generally conform to underwriting guidelines issued by U.S. government agencies or U.S. government-sponsored entities.

Asset Backed Securities ("ABS") investments are securitized investments similar to the aforementioned investments except the underlying assets are diverse, not only representing real estate related assets.

Commercial Mortgage Backed Securities ("CMBS") represent investments of fixed- and floating-rate CMBS, including investment grade (AAA through BBB) and non-investment grade classes (BB and below). CMBS will be secured by, or evidence ownership interest in, a single commercial mortgage loan or a pool of commercial mortgage loans.

Collectively, we refer to all asset types as real estate securities.

On March 7, 2011, AG Funds, L.P. ("AG Funds"), a Delaware limited liability company, entered into a subscription agreement with the Company and agreed to purchase 100 shares of common stock for $1,000. The subscription amount was received by the Company on April 1, 2011 making AG Funds the sole stockholder of the Company. The Company had no operations prior to the three months ended June 30, 2011. The Company subsequently completed an initial public offering on July 6, 2011 and concurrently repurchased the 100 shares from AG Funds at their issue price.

The Company is externally managed by AG REIT Management, LLC (the “Manager”), a newly formed subsidiary of Angelo, Gordon & Co., L.P. (“Angelo, Gordon”), a privately-held, SEC-registered investment adviser. Our Manager, pursuant to a delegation agreement dated as of June 29, 2011, has delegated to Angelo, Gordon the overall responsibility with respect to our Manager’s day-to-day duties and obligations arising under the management agreement.

The Company conducts its operations to qualify and be taxed as a real estate investment trust (a “REIT”) under the Internal Revenue Code commencing with its taxable period ended December 31, 2011.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, AG MIT, LLC and AG MIT II, LLC. All intercompany balances and transactions have been eliminated.

2. Summary of Significant Accounting Policies

The accompanying unaudited consolidated financial statements and related notes have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial reporting and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Certain prior period amounts have been reclassified to conform to the current period’s presentation. In the opinion of management, all adjustments considered necessary for a fair presentation for the interim period of the Company’s financial position, results of operations and cash flows have been included and are of a normal and recurring nature. The operating results presented for interim periods are not necessarily indicative of the results that may be expected for any other interim period or for the entire year.

AG Mortgage Investment Trust Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

Cash and cash equivalents

Cash is comprised of cash on deposit with financial institutions. We classify highly liquid investments with original maturities of three months or less from the date of purchase as cash equivalents. We place our cash and cash equivalents with high credit quality institutions to minimize credit risk exposure.

Restricted cash

Restricted cash includes cash pledged as collateral for clearing and executing trades, interest rate swaps and repurchase agreements. Restricted cash is carried at cost, which approximates fair value. Cash held by the Company as collateral is included in the due to broker line item on the consolidated balance sheet.

Offering and organization costs

The Company incurred offering and organization costs in connection with arranging the Company's initial public offering (the "IPO") and subsequent follow-on offering of its common stock. The offering and other organization costs were paid out of the proceeds of the respective offerings. Offering costs have been accounted for as a reduction of additional paid-in-capital. Costs incurred to organize the Company have been expensed as incurred. The Company's obligation to pay for organization and offering expenses incurred in connection with the IPO was capped at 1% of the total gross proceeds from the IPO and the concurrent private placement, and the Manager paid for such expenses incurred above the cap.

Use of estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results may differ from those estimates.

Earnings per share

In accordance with the provisions of Accounting Standards Codification ("ASC") 260, "Earnings per Share," the Company calculates basic income per share by dividing net income (loss) for the period by weighted-average shares of the Company's common stock outstanding for that period. Diluted income per share takes into account the effect of dilutive instruments, such as stock options, warrants and unvested restricted stock, but uses the average share price for the period in determining the number of incremental shares that are to be added to the weighted-average number of shares outstanding. For the period ended June 30, 2011, earnings per share is not presented. As the IPO and concurrent private placement had not yet closed as of June 30, 2011, the shares outstanding at June 30, 2011 represent the Company's nominal seed balance sheet shares. We therefore believe the presentation of earnings per share for June 30, 2011 is not a meaningful measure of the Company's performance.

Valuation of financial instruments

The fair value of the financial instruments that the Company records at fair value will be determined by the Manager, subject to oversight of the board of directors, and in accordance with ASC 820, "Fair Value Measurements and Disclosures." When possible, the Company determines fair value using independent data sources. ASC 820 establishes a hierarchy that prioritizes the inputs to valuation techniques giving the highest priority to readily available unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements) when market prices are not readily available or reliable. The three levels of the hierarchy under ASC 820 are described below:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Prices determined using other significant observable inputs. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.

AG Mortgage Investment Trust Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

- Level 3 – Prices determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used. Unobservable inputs reflect the Company's assumptions about the factors that market participants would use in pricing an asset or liability, and would be based on the best information available.

Transfers between levels are assumed to occur at the beginning of the reporting period.

Accounting for real estate securities

Investments in real estate securities are recorded in accordance with ASC 320. The Company has chosen to make a fair value election pursuant to ASC 825 for its real estate securities portfolio. The real estate securities are recorded at fair market value on the balance sheet and the period change in fair market value is recorded in current period earnings on the consolidated statement of operations as a component of "Unrealized gain on real estate securities, net."

These investments generally meet the requirements to be classified as available for sale under ASC 320-10-25, "Debt and Equity Securities," which requires the securities to be carried at fair value on the Consolidated Balance Sheet with changes in fair value charged to other comprehensive income, a component of Stockholders' Equity. Electing the fair value option allows the Company to record changes in fair value in the Statement of Operations, which, in management's view, more appropriately reflects the results of our operations for a particular reporting period as all securities activities will be recorded in a similar manner.

The cost of positions sold is calculated using a FIFO basis. Realized gains and losses on sales of real estate securities are recorded in earnings at the time of disposition.

Sales of securities

Sales of securities are driven by our Manager's portfolio management process. Our Manager seeks to mitigate risks including those associated with prepayments and will opportunistically rotate the portfolio into securities with more favorable attributes. Strategies may also be employed to manage net capital gains, which need to be distributed for tax purposes.

Realized gains or losses on sales of securities and derivatives, inclusive of securities classified as a component of linked transactions are included in the net realized gain line item on the consolidated statement of operations, and are recorded at the time of disposition. The cost of positions sold is calculated using a FIFO basis.

Investment consolidation

For each investment we make, we will evaluate the underlying entity that issued the securities we acquired or to which we make a loan to determine the appropriate accounting. A similar analysis will be performed for each entity with which we enter into an agreement for management, servicing or related services. In performing our analysis, we will refer to guidance in ASC 810-10, "Consolidation." In situations where we are the transferor of financial assets, we will refer to the guidance in ASC 860-10, "Transfers and Servicing."

In variable interest entities, or VIEs, an entity is subject to consolidation under ASC 810-10 if the equity investors either do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support, are unable to direct the entity's activities or are not exposed to the entity's losses or entitled to its residual returns. VIEs within the scope of ASC 810-10 are required to be consolidated by their primary beneficiary. The primary beneficiary of a VIE is determined to be the party that has both the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. This determination can sometimes involve complex and subjective analyses. Further, ASC 810-10 also requires ongoing assessments of whether an enterprise is the primary beneficiary of a VIE. In accordance with ASC 810-10, all transferees, including variable interest entities, must be evaluated for consolidation. If we were to treat securitizations as sales in the future, we will analyze the transactions under the guidelines of ASC 810-10 for consolidation.

AG Mortgage Investment Trust Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

We may periodically enter into transactions in which we sell assets. Upon a transfer of financial assets, we will sometimes retain or acquire senior or subordinated interests in the related assets. Pursuant to ASC 860-10, a determination must be made as to whether a transferor has surrendered control over transferred financial assets. That determination must consider the transferor's continuing involvement in the transferred financial asset, including all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer, even if they were not entered into at the time of the transfer. The financial components approach under ASC 860-10 limits the circumstances in which a financial asset, or portion of a financial asset, should be derecognized when the transferor has not transferred the entire original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented and/or when the transferor has continuing involvement with the transferred financial asset. It defines the term "participating interest" to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale.

Under ASC 860-10, after a transfer of financial assets that meets the criteria for treatment as a sale—legal isolation, ability of transferee to pledge or exchange the transferred assets without constraint and transferred control—an entity recognizes the financial and servicing assets it acquired or retained and the liabilities it has incurred, derecognizes financial assets it has sold and derecognizes liabilities when extinguished. The transferor would then determine the gain or loss on sale of mortgage loans by allocating the carrying value of the underlying mortgage between securities or loans sold and the interests retained based on their fair values. The gain or loss on sale is the difference between the cash proceeds from the sale and the amount allocated to the securities or loans sold. When a transfer of financial assets does not qualify for sale accounting, ASC 860-10 requires the transfer to be accounted for as a secured borrowing with a pledge of collateral.

From time to time, we may securitize mortgage loans we hold if such financing is available. These transactions will be recorded in accordance with ASC 860-10 and will be accounted for as either a "sale" and the loans will be removed from our balance sheet or as a "financing" and will be classified as "securitized loans" on our balance sheet, depending upon the structure of the securitization transaction. ASC 860-10 is a complex standard that may require us to exercise significant judgment in determining whether a transaction should be recorded as a "sale" or a "financing."

Interest income recognition

Interest income on our real estate securities portfolio is accrued based on the actual coupon rate and the outstanding principal balance of such securities. We have elected to record interest in accordance with ASC 835-30-35-2 using the effective interest method for all securities accounted for under the fair value option (ASC 825). As such, premiums and discounts are amortized or accreted into interest income over the lives of the securities in accordance with ASC 310-20, “Nonrefundable Fees and Other Costs”, ASC 320-10, “Investments—Debt and Equity Securities” or ASC 325-40, “Beneficial Interests in Securitized Financial Assets,” as applicable. Total interest income will flow though the interest income line item on the Consolidated Statement of Operations.

On at least a quarterly basis for securities accounted for under ASC 320-10 and ASC 310-20 (generally Agency RMBS), prepayments of the underlying collateral must be estimated, which directly affect the speed at which we amortize such securities. If actual and anticipated cash flows differ from previous estimates; we recognize a “catch-up” adjustment in the current period to the amortization of premiums for the impact of the cumulative change in the effective yield through the reporting date.

Similarly, we also reassess the cash flows on at least a quarterly basis for securities accounted for under ASC 325-40 (generally Non-Agency RMBS, ABS and CMBS). In estimating these cash flows, there are a number of assumptions that will be subject to uncertainties and contingencies. These include the rate and timing of principal and interest receipts, (including assumptions of prepayments, repurchases, defaults and liquidations), the pass-through or coupon rate and interest rate fluctuations. In addition, interest payment shortfalls due to delinquencies on the underlying mortgage loans have to be judgmentally estimated. Differences between previously estimated cash flows and current actual and anticipated cash flows are recognized prospectively through an adjustment of the yield over the remaining life of the security based on the current amortized cost of the investment as adjusted for credit impairment, if any.

AG Mortgage Investment Trust Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

For investments purchased with evidence of deterioration of credit quality for which it is probable, at acquisition, that we will be unable to collect all contractually required payments receivable, we will apply the provisions of ASC 310-30 "Loans and Debt Securities Acquired with Deteriorated Credit Quality." ASC 310-30 addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an investor's initial investment in loans or debt securities (loans) acquired in a transfer if those differences are attributable, at least in part, to credit quality. ASC 310-30 limits the yield that may be accreted (accretable yield) to the excess of the investor's estimate of undiscounted expected principal, interest and other cash flows (cash flows expected at acquisition to be collected) over the investor's initial investment in the loan. ASC 310-30 requires that the excess of contractual cash flows over cash flows expected to be collected (nonaccretable difference) not be recognized as an adjustment of yield, loss accrual or valuation allowance. Subsequent increases in cash flows expected to be collected generally should be recognized prospectively through adjustment of the loan's yield over its remaining life. Decreases in cash flows expected to be collected should be recognized as impairment.

Our accrual of interest, discount and premium for U.S. federal and other tax purposes is likely to differ from the financial accounting treatment of these items as described above.

Repurchase agreements

We finance the acquisition of certain assets within our portfolio through the use of repurchase agreements. Repurchase agreements are treated as collateralized financing transactions and are carried at primarily their contractual amounts, including accrued interest, as specified in the respective agreements.

We pledge certain of our securities as collateral under repurchase arrangements with financial institutions, the terms and conditions of which are negotiated on a transaction-by-transaction basis. The amounts available to be borrowed are dependent upon the fair value of the securities pledged as collateral, which fluctuates with changes in interest rates, type of security and liquidity conditions within the banking, mortgage finance and real estate industries. In response to declines in fair value of pledged securities, lenders may require us to post additional collateral or pay down borrowings to re-establish agreed upon collateral requirements, referred to as margin calls. As of June 30, 2012, we have met all margin call requirements.

In instances where we acquire assets through repurchase agreements with the same counterparty from whom the assets were purchased, we will evaluate such transactions in accordance with ASC 860-10. This standard requires the initial transfer of a financial asset and repurchase financing that are entered into contemporaneously with, or in contemplation of, one another to be considered linked unless all of the criteria found in ASC 860-10 are met at the inception of the transaction. If the transaction meets all of the conditions, the initial transfer shall be accounted for separately from the repurchase financing, and we will record the assets and the related financing on a gross basis on our balance sheet with the corresponding interest income and interest expense in our statements of operations. If the transaction is determined to be linked, we will record the initial transfer and repurchase financing on a net basis and record a forward commitment to purchase assets as a derivative instrument with changes in market value being recorded on the statement of operations. Such forward commitments are recorded at fair value with subsequent changes in fair value recognized in income. The Company refers to these transactions as Linked Transactions.

Accounting for derivative financial instruments

We may enter into derivative contracts, including interest rate swaps and interest rate caps, as a means of mitigating our interest rate risk. We primarily use interest rate derivative instruments to mitigate interest rate risk rather than to enhance returns. We account for derivative financial instruments in accordance with ASC 815-10, “Derivatives and Hedging.” ASC 815-10 requires an entity to recognize all derivatives as either assets or liabilities in the balance sheet and to measure those instruments at fair value. Additionally, the fair value adjustments will affect either other comprehensive income in stockholders’ equity until the hedged item is recognized in earnings or net income depending on whether the derivative instrument is designated and qualifies as a hedge for accounting purposes and, if so, the nature of the hedging activity. As of June 30, 2012 none of our interest rate derivatives have been designated as hedges. Such derivatives are recorded at fair value in accordance with ASC 820-10, with corresponding changes in value recognized in the statement of operations.

AG Mortgage Investment Trust Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

When derivative contracts are executed with the same counterparty, the value of the derivative contracts is reported on a net-by-counterparty basis on the balance sheet, where a legal right of off-set exists under an enforceable netting agreement. As a result, the net exposure to counterparties is reported as either an asset or liability on the balance sheet.

To-be-announced securities

A to-be-announced security (“TBA”) is a futures contract for the purchase or sale of Agency RMBS at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date. The specific Agency RMBS delivered into the contract upon the settlement date, published each month by the Securities Industry and Financial Markets Association, are not known at the time of the transaction. TBA securities are exempt from ASC 815 and are accounted for under ASC 320 if there is no other way to purchase or sell that security, if delivery of that security and settlement will occur within the shortest period possible for that type of security and if it is probable at inception and throughout the term of the individual contract that physical delivery of the security will occur (referred to as the “regular-way” exception). Unrealized gains and losses associated with TBA contracts not subject to the regular-way exception or not designated as hedging instruments are recognized in the Consolidated Statement of Operations in the line item “Unrealized loss on derivative instruments, net.”

Manager compensation

The management agreement provides for the payment to the Manager of a management fee. The management fee is accrued and expensed during the period for which it is calculated and earned. For a more detailed discussion on the fees payable under the management agreement, see Note 9.

Income taxes

The Company conducts its operations to qualify and be taxed as a REIT commencing with its taxable period ended December 31, 2011. Accordingly, the Company will generally not be subject to corporate U.S. federal or state income tax to the extent that the Company makes qualifying distributions to its stockholders, and provided that it satisfies on a continuing basis, through actual investment and operating results, the REIT requirements including certain asset, income, distribution and stock ownership tests. If the Company fails to qualify as a REIT, and do not qualify for certain statutory relief provisions, it will be subject to U.S. federal, state and local income taxes and may be precluded from qualifying as a REIT for the four taxable years following the year in which the Company lost its REIT qualification.

The dividends paid deduction of a REIT for qualifying dividends to its stockholders is computed using taxable income as opposed to net income reported under GAAP in the financial statements. Taxable income, generally, will differ from net income reported on the financial statements because the determination of taxable income is based on tax provisions and not financial accounting principles.

The Company has elected to treat certain of its subsidiaries, including AG MIT II, LLC, as taxable REIT subsidiaries, or TRSs. In general, a TRS of ours may hold assets and engage in activities that the Company cannot hold or engage in directly and generally may engage in any real estate or non-real estate-related business. A TRS is subject to U.S. federal, state and local corporate income taxes. As of June 30, 2012, there was no activity in the Company’s TRSs.

While a TRS will generate net income, a TRS can declare dividends to the Company which will be included in the Company’s taxable income and necessitate a distribution to stockholders. Conversely, if the Company retains earnings at a TRS level, no distribution is required and the Company can increase book equity of the consolidated entity.

The Company’s financial results are generally not expected to reflect provisions for current or deferred income taxes, except for any activities conducted through one or more taxable REIT subsidiaries, such as AG MIT II, LLC, that are subject to corporate income taxation. The Company believes it will operate in a manner that will allow the Company to qualify for taxation as a REIT. As a result of its expected REIT qualification, the Company does not generally expect to pay corporate U.S. federal or state income tax. Many of the REIT requirements, however, are highly technical and complex. If the Company were to fail to meet the REIT requirements, it would be subject to U.S. federal income taxes and applicable state and local taxes.

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As a REIT, if the Company fails to distribute in any calendar year at least the sum of (i) 85% of ordinary income for such year, (ii) 95% of capital gain net income for such year, and (iii) any undistributed taxable income from the prior year, the Company would be subject to a non-deductible 4% excise tax on the excess of such required distribution over the sum of (i) the amounts actually distributed and (ii) the amounts of income retained and on which the Company has paid corporate income tax.

The Company evaluates uncertain income tax positions, if any, in accordance with ASC Topic 740, Income Taxes (“ASC 740”). The Company classifies interest and penalties, if any, related to unrecognized tax benefits as a component of provision for income taxes. See Note 8 for further details.

Stock-based compensation

The Company applies the provisions of ASC 718, “Compensation—Stock Compensation” with regard to its equity incentive plans. ASC 718 covers a wide range of share-based compensation arrangements including stock options, restricted stock plans, performance-based awards, stock appreciation rights and employee stock purchase plans. ASC 718 requires that compensation cost relating to stock-based payment transactions be recognized in financial statements. The cost is measured based on the fair value of the equity or liability instruments issued.

Compensation cost related to restricted common shares issued to the Company’s directors is measured at its estimated fair value at the grant date, and is amortized and expensed over the vesting period on a straight-line basis. Compensation cost related to restricted common shares issued to the Manager is initially measured at estimated fair value at the grant date, and is remeasured on subsequent dates to the extent the awards are unvested. The Company has elected to use the straight-line method to amortize compensation expense for the restricted common shares granted to the Manager.

Recent accounting pronouncements

In December 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities (“ASU 2011-11”), which requires entities to provide enhanced disclosures about financial instruments and derivative instruments that are either presented on a net basis in the balance sheet or subject to an enforceable master netting arrangement or similar agreement including (i) a description of the rights of offset associated with relevant agreements and (ii) both net and gross information, including amounts of financial collateral, for relevant assets and liabilities. The purpose of the update is to enhance comparability between those companies that prepare their financial statements on the basis of U.S. GAAP and those that prepare their financial statements in accordance with IFRS and enables users of the financial statements to understand the effect or potential effect of the offsetting arrangements on the balance sheet. ASU 2011-11 is effective for fiscal years beginning on or after January 1, 2013, and for interim periods within those years. Disclosures are required retrospectively for all comparative periods presented in an entity's financial statements. We do not believe the adoption of ASU 2011-11 will have a material impact on our consolidated financial statements.

In April 2011, the FASB issued ASU 2011-03, Reconsideration of Effective Control for Repurchase Agreements, (“ASU 2011-03”), which changes the assessment of whether repurchase agreement transactions should be accounted for as sales or secured financings. In a typical repurchase agreement transaction, an entity transfers financial assets to the counterparty in exchange for cash with an agreement for the counterparty to return the same or equivalent financial assets for a fixed price in the future. Prior to this update, one of the factors in determining whether sale treatment could be used was whether the transferor maintained effective control of the transferred assets and in order to do so, the transferor must have the ability to repurchase such assets. This ASU changes the assessment of effective control by focusing on a transferor’s contractual rights and obligations with respect to transferred financial assets, rather than whether the transferor has the practical ability to perform in accordance with those rights or obligations. ASU 2011-03 was effective for the Company for the first interim or annual period beginning on or after December 15, 2011. With the exception of Linked Transactions, the Company records repurchase agreements as secured borrowings and not sales, and accordingly, the adoption of this update on January 1, 2012 did not have a material impact on the Company’s consolidated financial statements.

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3. Real Estate Securities

The following table presents the current principal balance, premium or discount, amortized cost, gross unrealized gain, gross unrealized loss, and fair market value of the Company's real estate securities portfolio at June 30, 2012. Real estate securities that are accounted for as components of linked transactions are not reflected in the tables set forth in this note. See Note 6 for further details. The Company's Agency RMBS are mortgage pass-through certificates or collateralized mortgage obligations representing interests in or obligations backed by pools of residential mortgage loans issued or guaranteed by Fannie Mae or Freddie Mac. The Non-Agency RMBS, ABS and CMBS portfolios are not issued or guaranteed by Fannie Mae, Freddie Mac or any agency of the U.S. Government and are therefore subject to credit risk. Agency RMBS securities have an explicit government guarantee.

		Premium		Gross Unrealized (1)			Weighted Ave	
	Current Face	(Discount)	Amortized Cost	Gains	Losses	Fair Value	Coupon	Yield
Agency RMBS:								
15 Year Fixed Rate	$718,433,236	$22,534,927	$740,968,163	$20,476,516	$-	$761,444,679	3.21%	2.43
20 Year Fixed Rate	267,032,664	9,993,509	277,026,173	6,280,230	(215,738)	283,090,665	3.60%	2.74
30 Year Fixed Rate	1,010,458,768	47,782,201	1,058,240,969	16,444,814	(76,255)	1,074,609,528	3.73%	3.00
ARM	39,356,792	1,672,664	41,029,456	25,043	-	41,054,499	2.96%	2.13
Interest Only	481,251,064	(391,876,102)	89,374,962	3,314,895	(2,996,841)	89,693,016	6.11%	8.57
Non-Agency RMBS	176,989,810	(27,215,940)	149,773,870	1,000,145	(876,300)	149,897,715	4.32%	6.56
ABS	13,500,000	(740)	13,499,260	10,181	-	13,509,441	6.59%	6.59
CMBS	12,490,589	(1,462,895)	11,027,694	529,812	-	11,557,506	5.17%	9.15
Total	$2,719,512,923	$(338,572,376)	$2,380,940,547	$48,081,636	$(4,165,134)	$2,424,857,049	4.05%	3.25

(1) We have chosen to make a fair value election pursuant to ASC 825 for our real estate securities portfolio. Unrealized gains and losses are recognized in current period earnings in the unrealized gain (loss) on real estate securities line item. The gross unrealized stated above represent inception to date unrealized gains (losses).

The following table details weighted average life by Agency RMBS, Agency Interest-Only ("IO") and Other Securities:

	Agency RMBS			Agency IO			Other Securities
Weighted Average Life (2)	Fair Value	Amortized Cost	Weighted Average Coupon	Fair Value	Amortized Cost	Weighted Average Coupon	Fair Value
Less than or equal to 1 year	$-	$-	-	$-	$-	-	$12,740,655
Greater than one year and less than or equal to three years	-	-	-	-	-	-	70,626,004
Greater than three years and less than or equal to five years	838,750,277	814,973,021	3.28%	77,044,913	76,985,875	6.09%	71,511,821
Greater than five years	1,321,449,094	1,302,291,740	3.66%	12,648,103	12,389,087	6.20%	20,086,182
Total	$2,160,199,371	$2,117,264,761	3.51%	$89,693,016	$89,374,962	6.11%	$174,964,662

(1) For purposes of this table, Other Securities represents Non-Agency RMBS, ABS and CMBS investments held as of June 30, 2012.

(2) Actual maturities of mortgage-backed securities are generally shorter than stated contractual maturities. Maturities are affected by the contractual lives of the underlying mortgages, periodic payments of principal and prepayments of principal.

During the quarter ended June 30, 2012, the Company sold nine securities for total proceeds of $214.9 million, with an additional $141.6 million of proceeds on four unsettled security sales as of quarter end, recording realized gains of $7.1 million and realized losses of $0.1 million. For the six months ended June 30, 2012, the Company sold fifteen securities for total proceeds of $438.5 million, with additional proceeds on four unsettled security sales as mentioned above as of June 30, 2012, recording realized gains of $9.3 million and realized losses of $1.7 million. See Note 6 for amounts realized on settlement of certain derivatives.

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4. Fair Value Measurements

As described in Note 2, the fair value of financial instruments that we record at fair value will be determined by the Manager, subject to oversight of the board of directors, and in accordance with ASC 820, “Fair Value Measurements and Disclosures.” When possible, the Company determines fair value using independent data sources. ASC 820 establishes a hierarchy that prioritizes the inputs to valuation techniques giving the highest priority to readily available unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements) when market prices are not readily available or reliable. The three levels of the hierarchy under ASC 820 are described below:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Prices determined using other significant observable inputs. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.
- Level 3 – Prices determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used. Unobservable inputs reflect the Company’s assumptions about the factors that market participants would use in pricing an asset or liability, and would be based on the best information available.

Values for the Company’s securities and derivatives portfolios are based upon prices obtained from third party pricing services, which are indicative of market activity. The evaluation methodology of the Company’s third-party pricing services incorporates commonly used market pricing methods, including a spread measurement to various indices such as the one-year constant maturity treasury and LIBOR, which are observable inputs. The evaluation also considers the underlying characteristics of each security, which are also observable inputs, including: coupon; maturity date; loan age; reset date; collateral type; periodic and life cap; geography; and prepayment speeds. The Company collects and considers current market intelligence on all major markets, including benchmark security evaluations and bid-lists from various sources, when available. As part of the risk management process, the Company reviews and analyzes all prices obtained by comparing prices to recently completed transactions involving the same or similar securities on or near the reporting date. If, in the opinion of the Manager, one or more securities prices reported to the Company are not reliable or unavailable, the Manager reviews the fair value based on characteristics of the security it receives from the issuer and available market information.

In valuing its derivatives, the Company considers the creditworthiness of both the Company and its counterparties, along with collateral provisions contained in each derivative agreement, from the perspective of both the Company and its counterparties. All of the Company's derivatives are subject to bilateral collateral arrangements. The Company also has netting arrangements in place with all derivative counterparties pursuant to standard documentation developed by the International Swap and Derivatives Association, or ISDA. Consequently, no credit valuation adjustment was made in determining the fair value of derivatives.

The securities underlying the Company's linked transactions are valued using similar techniques to those used for the Company's securities portfolio. The value of the underlying security is then netted against the carrying amount (which approximates fair value) of the repurchase agreement at the valuation date. Additionally, TBA instruments are similar in form to the Company's Agency RMBS portfolio, and the Company therefore estimates fair value based on similar methods.

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The following table presents the Company's financial instruments measured at fair value on a recurring basis as of June 30, 2012:

	Fair Value at June 30, 2012			
	Level 1	Level 2	Level 3	Total
Assets:				
Agency RMBS:				
15 Year Fixed Rate	$-	$761,444,679	$-	$761,444,679
20 Year Fixed Rate	-	283,090,665	-	283,090,665
30 Year Fixed Rate	-	1,074,609,528	-	1,074,609,528
ARM	-	41,054,499	-	41,054,499
Interest Only	-	89,693,016	-	89,693,016
Non-Agency RMBS	-	94,974,803	54,922,912	149,897,715
ABS	-	-	13,509,441	13,509,441
CMBS	-	4,048,231	7,509,275	11,557,506
Linked transactions	-	28,967,248	15,107,657	44,074,905
Total Assets Carried at Fair Value	$-	$2,377,882,669	$91,049,285	$2,468,931,954
Liabilities:				
Derivative liabilities	$-	$(23,413,215)	$-	$(23,413,215)
Total Liabilities Carried at Fair Value	$-	$(23,413,215)	$-	$(23,413,215)

The Company did not have any transfers of assets or liabilities between Levels 1 and 2 of the fair value hierarchy during the three and six months ended June 30, 2012.

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The following tables present additional information about the Company's investments which are measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs to determine fair value:

Three Months Ended

June 30, 2012

	Non-Agency RMBS	ABS	CMBS	Linked Transactions
Beginning balance	$34,165,419	$27,760,052	$-	$9,506,801
Transfers (1):				
Transfers into level 3	-	-	-	-
Transfers out of level 3	-	-	-	-
Purchases	26,904,731	-	9,725,625	48,959,782
Proceeds from sales				
Proceeds from settlement	(6,056,932)	(14,575,792)	(2,257,188)	(44,296,830)
Total net gains/ (losses) (2)				
Included in net income	(90,306)	325,181	40,838	937,904
Included in other comprehensive income (loss)	-	-	-	-
Ending Balance	$54,922,912	$13,509,441	$7,509,275	$15,107,657
Change in unrealized appreciation/depreciation for level 3 assets still held as of June 30, 2012 (3)	$(90,306)	$8,471	$40,838	$136,792

(1) Transfers are assumed to occur at the beginning of the period.
(2) Gains/(losses) are recorded in the following line items in the consolidated statement of operations:

Gain on linked transactions, net	$937,904
Unrealized gain on real estate securities, net	299,949
Interest income	(24,236