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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

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

**For the Quarterly Period Ended March 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 _____

ARMOUR RESIDENTIAL REIT, INC.
(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of incorporation or organization)

001-34766
(Commission File Number)

26-1908763
(I.R.S. Employer Identification No.)

3001 Ocean Drive, Suite 201, Vero Beach, FL 32963
(Address of principal executive offices)(zip code)

(772) 617-4340
(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 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

The number of outstanding shares of the Registrant's common stock as of April 29, 2016 was 36,692,694.

**ARMOUR Residential REIT, Inc. and Subsidiaries
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ARMOUR Residential REIT, Inc. and Subsidiaries
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except per share amounts)
(Unaudited)

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

	March 31, 2016	December 31, 2015
Assets		
Cash	\$ 243,294	\$ 289,925
Cash collateral posted to counterparties	306,104	263,799
Agency Securities, available for sale, at fair value (including pledged securities of \$10,208,822 at March 31, 2016 and \$12,109,868 at December 31, 2015)	10,474,010	12,461,556
Non-Agency Securities, trading, at fair value (including pledged securities of \$269,855 at March 31, 2016 and \$0 at December 31, 2015)	285,696	—
Derivatives, at fair value	1,665	999
Principal payments receivable	—	37
Accrued interest receivable	28,883	34,500
Prepaid and other	4,382	4,461
Total Assets	\$ 11,344,034	\$ 13,055,277
Liabilities and Stockholders' Equity		
Liabilities:		
Repurchase agreements	\$ 9,923,859	\$ 11,570,481
Payable for unsettled purchases	14,955	—
Derivatives, at fair value	298,685	233,301
Accrued interest payable- repurchase agreements	6,255	7,724
Accounts payable and other accrued expenses	4,645	18,605
Total Liabilities	\$ 10,248,399	\$ 11,830,111
Commitments and contingencies (Note 10)		
Stockholders' Equity:		
Preferred stock, \$0.001 par value, 50,000 shares authorized;		
8.250% Series A Cumulative Preferred Stock; 2,181 issued and outstanding (\$54,514 aggregate liquidation preference)	2	2
7.875% Series B Cumulative Preferred Stock; 5,650 issued and outstanding (\$141,250 aggregate liquidation preference)	6	6
Common stock, \$0.001 par value, 125,000 shares authorized, 36,692 and 36,682 shares issued and outstanding at March 31, 2016 and December 31, 2015	37	37
Additional paid-in capital	2,559,582	2,559,361
Accumulated deficit	(1,586,711)	(1,266,938)
Accumulated other comprehensive income (loss)	122,719	(67,302)
Total Stockholders' Equity	\$ 1,095,635	\$ 1,225,166
Total Liabilities and Stockholders' Equity	\$ 11,344,034	\$ 13,055,277

See notes to condensed consolidated financial statements.

ARMOUR Residential REIT, Inc. and Subsidiaries
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share amounts)
(Unaudited)

	For the Quarter Ended	
	March 31, 2016	March 31, 2015
Interest Income:		
Agency Securities, net of amortization of premium	\$ 78,133	\$ 99,550
Non-Agency Securities, including discount accretion	327	—
Total Interest Income	\$ 78,460	\$ 99,550
Interest expense- repurchase agreements	(19,148)	(14,192)
Net Interest Income	\$ 59,312	\$ 85,358
Other Income (Loss):		
Realized gain on sale of Agency Securities (reclassified from Other comprehensive income)	1,891	6,544
Gain on Non-Agency Securities	4,122	—
Subtotal	\$ 6,013	\$ 6,544
Realized gain (loss) on derivatives (1)	(246,105)	8,099
Unrealized loss on derivatives	(89,058)	(216,338)
Subtotal	\$ (335,163)	\$ (208,239)
Total Other Loss	\$ (329,150)	\$ (201,695)
Expenses:		
Management fee	6,508	6,877
Professional fees	2,173	793
Insurance	171	170
Compensation	518	613
Other	267	679
Total Expenses	\$ 9,637	\$ 9,132
Net Loss	\$ (279,475)	\$ (125,469)
Dividends declared on preferred stock	(3,905)	(3,905)
Net Loss related to common stockholders	\$ (283,380)	\$ (129,374)
Net loss per share related to common stockholders (Note 13):		
Basic	\$ (7.73)	\$ (2.96)
Diluted	\$ (7.73)	\$ (2.96)
Dividends declared per common share	\$ 0.99	\$ 0.96
Weighted average common shares outstanding:		
Basic	36,683	44,118
Diluted	36,683	44,118

(1) Interest expense related to our interest rate swap contracts is recorded as realized loss on derivatives on the condensed consolidated statements of operations. For additional information, see Note 9 to the condensed consolidated financial statements.

See notes to condensed consolidated financial statements.

ARMOUR Residential REIT, Inc. and Subsidiaries
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in thousands)
(Unaudited)

	For the Quarter Ended	
	March 31, 2016	March 31, 2015
Net Loss	\$ (279,475)	\$ (125,469)
Other comprehensive income (loss):		
Reclassification adjustment for realized gain on sale of available for sale Agency Securities	(1,891)	(6,544)
Net unrealized gain on available for sale Agency Securities	191,912	89,731
Other comprehensive income	\$ 190,021	\$ 83,187
Comprehensive Loss	\$ (89,454)	\$ (42,282)

See notes to the condensed consolidated financial statements.

ARMOUR Residential REIT, Inc. and Subsidiaries
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(in thousands, except per share amounts)
(Unaudited)

	Preferred Stock						Common Stock			Total Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
	8.250% Series A			7.875% Series B			Shares	Par Amount	Additional Paid-in Capital				
	Shares	Par Amount	Additional Paid-in Capital	Shares	Par Amount	Additional Paid-in Capital							
Balance, January 1, 2016	2,181	\$ 2	\$ 53,172	5,650	\$ 6	\$ 136,547	36,682	\$ 37	\$ 2,369,642	\$ 2,559,361	\$ (1,266,938)	\$ (67,302)	\$ 1,225,166
Series A Preferred dividends	—	—	—	—	—	—	—	—	—	—	(1,124)	—	(1,124)
Series B Preferred dividends	—	—	—	—	—	—	—	—	—	—	(2,781)	—	(2,781)
Common stock dividends	—	—	—	—	—	—	—	—	—	—	(36,393)	—	(36,393)
Stock based compensation, net of withholding requirements	—	—	—	—	—	—	10	—	221	221	—	—	221
Net loss	—	—	—	—	—	—	—	—	—	—	(279,475)	—	(279,475)
Other comprehensive income	—	—	—	—	—	—	—	—	—	—	—	190,021	190,021
Balance, March 31, 2016	2,181	\$ 2	\$ 53,172	5,650	\$ 6	\$ 136,547	36,692	\$ 37	\$ 2,369,863	\$ 2,559,582	\$ (1,586,711)	\$ 122,719	\$ 1,095,635

See notes to condensed consolidated financial statements.

ARMOUR Residential REIT, Inc. and Subsidiaries
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	For the Quarter Ended	
	March 31, 2016	March 31, 2015
Cash Flows From Operating Activities:		
Net loss	\$ (279,475)	\$ (125,469)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Net amortization of premium on Agency Securities	21,395	26,983
Accretion of net discount on Non-Agency Securities	181	—
Realized gain on sale of Agency Securities	(1,891)	(6,544)
Gain on Non-Agency Securities	(4,122)	—
Stock based compensation	221	255
Changes in operating assets and liabilities:		
Decrease in accrued interest receivable	5,617	240
Increase in prepaid and other assets	79	40
Decrease in derivatives, at fair value	64,718	194,956
Decrease in accrued interest payable- repurchase agreements	(1,469)	(1,514)
Decrease in accounts payable and other accrued expenses	(13,960)	(15,849)
Net cash provided by (used in) operating activities	<u>\$ (208,706)</u>	<u>\$ 73,098</u>
Cash Flows From Investing Activities:		
Purchases of Agency Securities	—	(1,982,478)
Purchases of Non-Agency Securities	(266,800)	—
Principal repayments of Agency Securities	368,885	481,387
Proceeds from sales of Agency Securities	1,789,215	1,626,904
Increase in cash collateral	(42,305)	(193,343)
Net cash provided by (used in) investing activities	<u>\$ 1,848,995</u>	<u>\$ (67,530)</u>
Cash Flows From Financing Activities:		
Issuance of common stock, net of expenses	—	43
Proceeds from repurchase agreements	40,339,908	20,966,843
Principal repayments on repurchase agreements	(41,986,530)	(20,943,994)
Series A Preferred stock dividends paid	(1,124)	(1,124)
Series B Preferred stock dividends paid	(2,781)	(2,781)
Common stock dividends paid	(36,393)	(42,486)
Common stock repurchased	—	(2,804)
Net cash used in financing activities	<u>\$ (1,686,920)</u>	<u>\$ (26,303)</u>
Net decrease in cash	<u>(46,631)</u>	<u>(20,735)</u>
Cash - beginning of period	289,925	494,561
Cash - end of period	<u>\$ 243,294</u>	<u>\$ 473,826</u>
Supplemental Disclosure:		
Cash paid during the period for interest	\$ 67,668	\$ 93,160
Non-Cash Investing and Financing Activities:		
Payable for unsettled purchases	\$ 14,955	\$ —
Net unrealized gain on available for sale Agency Securities	\$ 191,912	\$ 89,731

See notes to condensed consolidated financial statements

ARMOUR Residential REIT, Inc. and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except per share amounts)
(UNAUDITED)

Note 1 -Basis of Presentation

The accompanying condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X promulgated by the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Certain prior year amounts have been reclassified to conform to the current year's presentation. All per share amounts, common shares outstanding and stock-based compensation amounts for all periods presented reflect our one-for-eight reverse stock split (the "Reverse Stock Split"), which was effective July 31, 2015. Operating results for the quarter ended March 31, 2016 are not necessarily indicative of the results that may be expected for the calendar year ending December 31, 2016. These unaudited financial statements should be read in conjunction with the audited financial statements and notes thereto included in our annual report on Form 10-K for the year ended December 31, 2015.

The condensed consolidated financial statements include the accounts of ARMOUR Residential REIT, Inc. and its subsidiaries. All intercompany accounts and transactions have been eliminated. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates affecting the accompanying condensed consolidated financial statements include the valuation of MBS (as defined below), including an assessment of whether other-than-temporary impairment ("OTTI") exists, and derivative instruments.

Note 2 -Organization and Nature of Business Operations

References to "we," "us," "our," "ARMOUR" or the "Company" are to ARMOUR Residential REIT, Inc. References to "ACM" are to ARMOUR Capital Management LP, a Delaware limited partnership. In February 2016, the Company formed JMI Acquisition Corporation ("Acquisition"), a Maryland corporation and wholly-owned subsidiary of ours. Acquisition was formed for the purpose of acquiring all of the shares of common stock of JAVELIN Mortgage Investment Corp. ("JAVELIN"). See *Note 17 -Subsequent Events* for more information about the relationship between ARMOUR, JAVELIN and Acquisition.

We are an externally managed Maryland corporation incorporated in 2008, managed by ACM, an investment advisor registered with the SEC (see *Note 10 - Commitments and Contingencies* and *Note 15 -Related Party Transactions* for additional discussion). We invest in residential mortgage backed securities issued or guaranteed by a United States ("U.S.") Government-sponsored entity ("GSE"), such as the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac) or guaranteed by the Government National Mortgage Administration (Ginnie Mae) (collectively, "Agency Securities"). Other securities backed by residential mortgages in which we invest, for which the payment of principal and interest is not guaranteed by a GSE or government agency (collectively, "Non-Agency Securities" and together with Agency Securities, "MBS"), may benefit from credit enhancement derived from structural elements such as subordination, over collateralization or insurance. At March 31, 2016 and December 31, 2015, investments in Agency Securities accounted for 97.3% and 100.0% of our MBS portfolio, respectively. During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. At March 31, 2016, investments in Non-Agency Securities accounted for 2.7% of our MBS portfolio.

Our MBS portfolio consists primarily of Agency Securities backed by fixed rate home loans. From time to time, a portion of our assets may be invested in Agency Securities backed by hybrid adjustable rate and adjustable rate home loans as well as unsecured notes and bonds issued by GSEs, U.S. Treasuries and money market instruments, subject to certain income tests we must satisfy for our qualification as a real estate investment trust ("REIT"). Our charter permits us to invest in Agency Securities and Non-Agency Securities.

We have elected to be taxed as a REIT under the Internal Revenue Code, as amended ("the Code"). Our qualification as a REIT depends on our ability to meet, on a continuing basis, various complex requirements under the Code relating to, among other things, the sources of our gross income, the composition and values of our assets, our distribution levels and the concentration of ownership of our capital stock. We believe that we are organized in conformity with the requirements for qualification as a REIT under the Code and our manner of operations enables us to meet the requirements for taxation as a REIT for federal income tax purposes.

ARMOUR Residential REIT, Inc. and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except per share amounts)
(UNAUDITED)

As a REIT, we will generally not be subject to federal income tax on the REIT taxable income that we currently distribute to our stockholders. If we fail to qualify as a REIT in any taxable year and do not qualify for certain statutory relief provisions, we will be subject to federal income tax at regular corporate rates. Even if we qualify as a REIT for federal income tax purposes, we may still be subject to some federal, state and local taxes on our income.

Note 3 - Summary of Significant Accounting Policies

Cash

Cash includes cash on deposit with financial institutions. We may maintain deposits in federally insured financial institutions in excess of federally insured limits. However, management believes we are not exposed to significant credit risk due to the financial position and creditworthiness of the depository institutions in which those deposits are held.

Cash Collateral Posted To/By Counterparties

Cash collateral posted to/by counterparties represents cash posted by us to counterparties or posted by counterparties to us as collateral for our interest rate swap contracts (including swaptions and basis swap contracts), Eurodollar Futures Contracts ("Futures Contracts") and repurchase agreements on our MBS and our Agency Securities purchased or sold on a to-be-announced basis ("TBA Agency Securities").

MBS, at Fair Value

We generally intend to hold most of our MBS for extended periods of time. We may, from time to time, sell any of our MBS as part of the overall management of our MBS portfolio. Management determines the appropriate classifications of the securities at the time they are acquired and evaluates the appropriateness of such classifications at each balance sheet date. Purchases and sales of our MBS are recorded on the trade date.

Agency Securities, Available For Sale

At March 31, 2016 and December 31, 2015, all of our Agency Securities were classified as available for sale securities. Agency Securities classified as available for sale are reported at their estimated fair values with unrealized gains and losses excluded from earnings and reported as part of the condensed consolidated statements of comprehensive income (loss).

Non-Agency Securities, Trading

During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. At March 31, 2016, all of our Non-Agency Securities were classified as trading securities. Non-Agency Securities classified as trading are reported at their estimated fair values with unrealized gains and losses included in other income (loss) as a component of the consolidated statements of operations. We estimate future cash flows for each Non-Agency Security and then discount those cash flows based on our estimates of current market yield for each individual security. We then compare our calculated price with our pricing services and/or dealer marks. Our estimates for future cash flows and current market yields incorporate such factors as coupons, prepayment speeds, defaults, delinquencies and severities.

Receivables and Payables for Unsettled Sales and Purchases

We account for purchases and sales of securities on the trade date, including purchases and sales for forward settlement. Receivables and payables for unsettled trades represent the agreed trade price multiplied by the outstanding balance of the securities at the balance sheet date.

Accrued Interest Receivable and Payable

Accrued interest receivable includes interest accrued between payment dates on MBS. Accrued interest payable includes interest payable on our repurchase agreements and may, at certain times, contain interest payable on U.S. Treasury Securities sold short.

ARMOUR Residential REIT, Inc. and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except per share amounts)
(UNAUDITED)

Repurchase Agreements

We finance the acquisition of our MBS through the use of repurchase agreements. Our repurchase agreements are secured by our MBS and bear interest rates that have historically moved in close relationship to the Federal Funds Rate and the London Interbank Offered Rate (“LIBOR”). Under these repurchase agreements, we sell MBS to a lender and agree to repurchase the same MBS in the future for a price that is higher than the original sales price. The difference between the sales price that we receive and the repurchase price that we pay represents interest paid to the lender. A repurchase agreement operates as a financing arrangement under which we pledge our MBS as collateral to secure a loan which is equal in value to a specified percentage of the estimated fair value of the pledged collateral. We retain beneficial ownership of the pledged collateral. At the maturity of a repurchase agreement, we are required to repay the loan and concurrently receive back our pledged collateral from the lender or, with the consent of the lender, we may renew such agreement at the then prevailing interest rate. The repurchase agreements may require us to pledge additional assets to the lender in the event the estimated fair value of the existing pledged collateral declines.

In addition to the repurchase agreement financing discussed above, at certain times we have entered into reverse repurchase agreements with certain of our repurchase agreement counterparties. Under a typical reverse repurchase agreement, we purchase U.S. Treasury Securities from a borrower in exchange for cash and agree to sell the same securities in the future in exchange for a price that is higher than the original purchase price. The difference between the purchase price originally paid and the sale price represents interest received from the borrower. Reverse repurchase agreement receivables and repurchase agreement liabilities are presented net when they meet certain criteria, including being with the same counterparty, being governed by the same master repurchase agreement (“MRA”), settlement through the same brokerage or clearing account and maturing on the same day. We did not have any reverse repurchase agreements outstanding at March 31, 2016 and December 31, 2015.

Obligations to Return Securities Received as Collateral, at Fair Value

At certain times, we also sell to third parties the U.S. Treasury Securities received as collateral for reverse repurchase agreements and recognize the resulting obligation to return said U.S. Treasury Securities as a liability on our condensed consolidated balance sheets. Interest is recorded on the repurchase agreements, reverse repurchase agreements and U.S. Treasury Securities sold short on an accrual basis and presented as interest expense. Both parties to the transaction have the right to make daily margin calls based on changes in the fair value of the collateral received and/or pledged. We did not have any obligations to return securities received as collateral at March 31, 2016 and December 31, 2015.

Derivatives, at Fair Value

We recognize all derivatives as either assets or liabilities at fair value on our condensed consolidated balance sheets. All changes in the fair values of our derivatives are reflected in our condensed consolidated statements of operations. We designate derivatives as hedges for tax purposes and any unrealized derivative gains or losses would not affect our distributable net taxable income. These transactions include interest rate swap contracts, interest rate swaptions and basis swap contracts. We also may utilize forward contracts for the purchase or sale of TBA Agency Securities. We account for TBA Agency Securities as derivative instruments if it is reasonably possible that we will not take or make physical delivery of the Agency Security upon settlement of the contract. We account for TBA dollar roll transactions as a series of derivative transactions.

We may also purchase and sell TBA Agency Securities as a means of investing in and financing Agency Securities (thereby increasing our “at risk” leverage) or as a means of disposing of or reducing our exposure to Agency Securities (thereby reducing our “at risk” leverage). Pursuant to TBA Agency Securities, we agree to purchase or sell, for future delivery, Agency Securities with certain principal and interest terms and certain types of collateral, but the particular Agency Securities to be delivered are not identified until shortly before the TBA settlement date. We may also choose, prior to settlement, to move the settlement of these securities out to a later date by entering into an offsetting short or long position (referred to as a “pair off”), net settling the paired off positions for cash, and simultaneously purchasing or selling a similar TBA Agency Security for a later settlement date. This transaction is commonly referred to as a “dollar roll.” When it is reasonably possible that we will pair off a TBA Agency Security, we account for that contract as a derivative. We did not have any TBA Agency Securities outstanding at March 31, 2016 and December 31, 2015.

ARMOUR Residential REIT, Inc. and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except per share amounts)
(UNAUDITED)

Revenue Recognition

Interest income is earned and recognized on Agency Securities based on their unpaid principal amounts and their contractual terms. Recognition of interest income commences on the settlement date of the purchase transaction and continues through the settlement date of the sale transaction. Premiums and discounts associated with the purchase of Multi-Family MBS, which are generally not subject to prepayment, are amortized or accreted into interest income over the contractual lives of the securities using a level yield method. Premiums and discounts associated with the purchase of other Agency Securities are amortized or accreted into interest income over the actual lives of the securities, reflecting actual prepayments as they occur.

Fair Value of Agency Securities: We invest in Agency Securities representing interests in or obligations backed by pools of fixed rate, hybrid adjustable rate and adjustable rate mortgage loans. The authoritative literature requires us to classify our investments as either trading, available for sale or held to maturity securities. Management determines the appropriate classifications of the securities at the time they are acquired and evaluates the appropriateness of such classifications at each balance sheet date. We currently classify all of our Agency Securities as available for sale. Agency Securities classified as available for sale are reported at their estimated fair values with unrealized gains and losses excluded from earnings and reported as part of the statements of comprehensive income (loss).

Security purchase and sale transactions, including purchase of TBA Agency Securities, are recorded on the trade date to the extent it is probable that we will take or make timely physical delivery of the related securities. Gains or losses realized from the sale of securities are included in income and are determined using the specific identification method.

Impairment of Assets: We evaluate Agency Securities for other than temporary impairment at least on a quarterly basis and more frequently when economic or market concerns warrant such evaluation. We consider an impairment to be other than temporary if we (1) have the intent to sell the Agency Securities, (2) believe it is more likely than not that we will be required to sell the securities before recovery (for example, because of liquidity requirements or contractual obligations) or (3) a credit loss exists. Impairment losses recognized establish a new cost basis for the related Agency Securities.

Interest income on Non-Agency Securities is recognized using the effective yield method over the life of the securities based on the future cash flows expected to be received. Future cash flow projections and related effective yields are determined for each security and updated quarterly. Other than temporary impairments, which establish a new cost basis in the security for purposes of calculating effective yields, are recognized when the fair value of a security is less than its cost basis and there has been an adverse change in the future cash flows expected to be received. Other changes in future cash flows expected to be received are recognized prospectively over the remaining life of the security.

Comprehensive Income (Loss)

Comprehensive income (loss) refers to changes in equity during a period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period, except those resulting from investments by owners and distributions to owners.

Reclassification

All per share amounts, common shares outstanding and stock-based compensation amounts for all periods presented reflect the Reverse Stock Split, which was effective July 31, 2015. No other reclassifications have been made to previously reported amounts.

ARMOUR Residential REIT, Inc. and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except per share amounts)
(UNAUDITED)

Note 4 -Recent Accounting Pronouncements

In September 2015, the Financial Accounting Standards Board issued ASU 2015-16, *Business Combinations Simplifying the Accounting for Measurement-Period Adjustments (Topic 805)*. The amendment simplifies the accounting for measurement-period adjustments. An acquirer is required to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendment also requires acquirers to present separately on the face of the income statement or disclose in the notes, the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustments to the provisional amounts had been recognized as of the acquisition date. The amendment is effective for fiscal years beginning after December 15, 2015 and has not had a significant impact on the consolidated financial statements for the quarter.

In February 2016 the Financial Accounting Standards Board issued ASU 2016-02, *Leases (Topic 842)*. The standard introduces a new lessee model that will require most leases to be recorded on the balance sheet recognizing a right-of-use lease asset and a liability to make lease payments. The standard will be effective for annual periods beginning after December 15, 2018. The Company is in the process of assessing the impact of this standard but does not expect it to have a significant impact on the consolidated financial statements.

Note 5 -Fair Value of Financial Instruments

Our valuation techniques for financial instruments use observable and unobservable inputs. Observable inputs reflect readily obtainable data from third party sources, while unobservable inputs reflect management's market assumptions. The Accounting Standards Codification Topic No. 820, "*Fair Value Measurement*," classifies these inputs into the following hierarchy:

Level 1 Inputs - Quoted prices for identical instruments in active markets.

Level 2 Inputs - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs - Prices determined using significant unobservable inputs. Unobservable inputs may be used 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 reflect management'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.

The following describes the valuation methodologies used for our assets and liabilities measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy. Any transfers between levels are assumed to occur at the beginning of the reporting period.

Cash - Cash includes cash on deposit with financial institutions. The carrying amount of cash is deemed to be its fair value and is classified as Level 1. Cash balances posted by us to counterparties or posted by counterparties to us as collateral are classified as Level 2 because they are integrally related to the Company's repurchase financing and interest rate swap agreements, which are classified as Level 2.

Agency Securities, Available for Sale - Fair value for the Agency Securities in our MBS portfolio is based on obtaining a valuation for each Agency Security from third party pricing services and/or dealer quotes. The third party pricing services use common market pricing methods that may include pricing models that may incorporate such factors as coupons, prepayment speeds, spread to the Treasury curves and interest rate swap curves, duration, periodic and life caps and credit enhancement. If the fair value of an Agency Security is not available from the third party pricing services or such data appears unreliable, we obtain pricing indications from up to three dealers who make markets in similar Agency Securities. Management reviews pricing used to ensure that current market conditions are properly reflected. This review includes, but is not limited to, comparisons of similar market transactions or alternative third party pricing services, dealer pricing indications and comparisons to a third party pricing model. Fair values obtained from the third party pricing services for similar instruments are classified as Level 2 securities if the inputs to the pricing models used are consistent with the Level 2 definition. If quoted prices for a security are not reasonably available from the third party pricing service, but dealer pricing indications are, the security will be classified as a Level 2 security. If neither is available, management will determine the fair value based on characteristics of the security that we receive from the issuer and based on available market information and classify it as a Level 3 security. At March 31, 2016 and December 31, 2015,

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all of our Agency Security fair values are classified as Level 2 based on the inputs used by our third party pricing services and dealer quotes.

Non-Agency Securities Trading - The fair value for the Non-Agency Securities in our MBS portfolio is based on estimates prepared by our Portfolio Management group, which organizationally reports to our Chief Investment Officer. In preparing the estimates, our Portfolio Management group uses commercially available and proprietary models and data as well as market intelligence gained from discussions with, and transactions by, other market participants. We estimate the fair value of our Non-Agency Securities by estimating the future cash flows for each Non-Agency Security and then discounting those cash flows based on our estimates of current market yield for each individual security. Our estimates for future cash flows and current market yields incorporate such factors as collateral type, bond structure and priority of payments, coupons, prepayment speeds, defaults, delinquencies and severities. Quarterly, we compare our estimates of fair value of our Non-Agency Securities with pricing from third party pricing services, dealer marks received and recent purchase and financing transaction history to validate our assumptions of cash flow and market yield and calibrate our models. Fair values calculated in this manner are considered Level 3. During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. At March 31, 2016 all of our Non-Agency Security fair values are calculated in this manner and therefore were classified as Level 3.

Receivables and Payables for Unsettled Sales and Purchases - The carrying amount is generally deemed to be fair value because of the relatively short time to settlement. Such receivables and payables are classified as Level 2 because they are effectively secured by the related securities and could potentially be subject to counterparty credit considerations.

Repurchase Agreements - The fair value of repurchase agreements reflects the present value of the contractual cash flows discounted at the estimated LIBOR based market interest rates at the valuation date for repurchase agreements with a term equivalent to the remaining term to interest rate repricing, which may be at maturity, of our repurchase agreements. The fair value of the repurchase agreements approximates their carrying amount due to the short-term nature of these financial instruments. Our repurchase agreements are classified as Level 2.

Obligations to Return Securities Received as Collateral - The fair value of the obligations to return securities received as collateral are based upon the prices of the related U.S. Treasury Securities obtained from a third party pricing service. Such obligations are classified as Level 1.

Derivative Transactions - Our Futures Contracts are traded on the Chicago Mercantile Exchange ("CME") and are classified as Level 1. The fair values of our interest rate swap contracts, interest rate swaptions and basis swaps are valued using third party pricing services that incorporate common market pricing methods that may include current interest rate curves, forward interest rate curves and market spreads to interest rate curves. We estimate the fair value of TBA Agency Securities based on similar methods used to value our Agency Securities. Management compares pricing used to dealer quotes to ensure that the current market conditions are properly reflected. The fair values of our interest rate swap contracts, interest rate swaptions, basis swap contracts and TBA Agency Securities are classified as Level 2.

The following tables provide a summary of our assets and liabilities that are measured at fair value on a recurring basis at March 31, 2016 and December 31, 2015.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at March 31, 2016
Assets at Fair Value:				
Agency Securities, available for sale	\$ —	\$ 10,474,010	\$ —	\$ 10,474,010
Non-Agency Securities, trading	\$ —	\$ —	\$ 285,696	\$ 285,696
Derivatives	\$ —	\$ 1,665	\$ —	\$ 1,665
Liabilities at Fair Value:				
Derivatives	\$ —	\$ 298,685	\$ —	\$ 298,685

There were no transfers of assets or liabilities between the levels of the fair value hierarchy during the quarter ended March 31, 2016.

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	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2015
Assets at Fair Value:				
Agency Securities, available for sale	\$ —	\$ 12,461,556	\$ —	\$ 12,461,556
Derivatives	\$ —	\$ 999	\$ —	\$ 999
Liabilities at Fair Value:				
Derivatives	\$ —	\$ 233,301	\$ —	\$ 233,301

There were no transfers of assets or liabilities between the levels of the fair value hierarchy during the year ended December 31, 2015.

The following tables provide a summary of the carrying values and fair values of our financial assets and liabilities not carried at fair value but for which fair value is required to be disclosed at March 31, 2016 and December 31, 2015.

March 31, 2016

	Carrying Value	Fair Value	Fair Value Measurements using:		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:					
Cash	\$ 243,294	\$ 243,294	\$ 243,294	\$ —	\$ —
Cash collateral posted to counterparties	\$ 306,104	\$ 306,104	\$ —	\$ 306,104	\$ —
Accrued interest receivable	\$ 28,883	\$ 28,883	\$ —	\$ 28,883	\$ —
Financial Liabilities:					
Repurchase agreements	\$ 9,923,859	\$ 9,923,859	\$ —	\$ 9,923,859	\$ —
Payable for unsettled purchases	\$ 14,955	\$ 14,955	\$ —	\$ 14,955	\$ —
Accrued interest payable- repurchase agreements	\$ 6,255	\$ 6,255	\$ —	\$ 6,255	\$ —

December 31, 2015

	Carrying Value	Fair Value	Fair Value Measurements using:		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:					
Cash	\$ 289,925	\$ 289,925	\$ 289,925	\$ —	\$ —
Cash collateral posted to counterparties	\$ 263,799	\$ 263,799	\$ —	\$ 263,799	\$ —
Principal payments receivable	\$ 37	\$ 37	\$ —	\$ 37	\$ —
Accrued interest receivable	\$ 34,500	\$ 34,500	\$ —	\$ 34,500	\$ —
Financial Liabilities:					
Repurchase agreements	\$ 11,570,481	\$ 11,570,481	\$ —	\$ 11,570,481	\$ —
Accrued interest payable- repurchase agreements	\$ 7,724	\$ 7,724	\$ —	\$ 7,724	\$ —

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The following table provides a summary of the changes in Level 3 assets measured at fair value on a recurring basis at March 31, 2016. We did not have Level 3 assets at December 31, 2015.

	For the Quarter Ended	
	March 31, 2016	
Non-Agency Securities		
Balance, beginning of period	\$	—
Purchases of Non-Agency Securities, at cost		281,755
Gain on Non-Agency Securities		4,122
Discount accretion		(181)
Balance, end of period	\$	285,696
Gain on Non-Agency Securities	\$	4,122

The significant unobservable inputs used in the fair value measurement of our Level 3 Non-Agency Securities include assumptions for underlying loan collateral, cumulative default rates and loss severities in the event of default, as well as discount rates.

The following table presents the range of our estimates of cumulative default and loss severities, together with the discount rates implicit in our Level 3 Non-Agency Security fair values at March 31, 2016. We did not have Level 3 assets at December 31, 2015.

March 31, 2016

Unobservable Level 3 Input	Minimum	Weighted Average	Maximum
Cumulative default	0.00%	0.00%	0.00%
Loss severity (life)	0.00%	62.99%	100.00%
Discount rate	4.96%	5.62%	6.35%
Delinquency (life)	0.00%	0.87%	2.60%
Voluntary prepayments (life)	9.11%	14.73%	24.05%

The table above include the effects of the structural elements of our Non-Agency Securities, such as subordination and over collateralization or insurance. Significant increases or decreases in any of these inputs in isolation would result in a significantly lower or higher fair value measurement. Generally, a change in the assumption used for the probability of cumulative default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for voluntary prepayment rates for the life of the security. However, given the interrelationship between loss estimates and the discount rate, overall Non-Agency Security market conditions would likely have a more significant impact on our Level 3 fair values than changes in any one unobservable input.

Note 6 -Agency Securities, Available for Sale

All of our Agency Securities are classified as available for sale and, as such, are reported at their estimated fair value and changes in fair value reported as part of the statements of comprehensive income (loss). At March 31, 2016 and December 31, 2015, investments in Agency Securities accounted for 97.3% and 100.0% of our MBS portfolio.

We evaluated our Agency Securities with unrealized losses at March 31, 2016, March 31, 2015 and December 31, 2015, to determine whether there was an other than temporary impairment. All of our Agency Securities are issued and guaranteed by GSEs or Ginnie Mae. The GSEs have a long term credit rating of AA+. At those dates, we also considered whether we intended to sell Agency Securities and whether it was more likely than not that we could meet our liquidity requirements and contractual obligations without selling Agency Securities. As a result of this evaluation, no other than temporary impairment was recognized for the quarters ended March 31, 2016 and March 31, 2015 and for the year ended December 31, 2015, respectively, because we determined that we 1) did not have the intent to sell the Agency Securities in an unrealized loss position, 2) did not believe it more likely than not that we were required to sell the securities before recovery (for example, because of liquidity requirements or contractual obligations), and/or (3) determined that a credit loss did not exist.

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At March 31, 2016, we had the following Agency Securities in an unrealized gain or loss position as presented below. The components of the carrying value of our Agency Securities at March 31, 2016 are also presented below. Our Agency Securities had a weighted average coupon of 3.51% at March 31, 2016.

March 31, 2016	Amortized Cost	Gross Unrealized Loss	Gross Unrealized Gain	Fair Value	Percent of Total
Fannie Mae					
ARMs & Hybrids	\$ 43,992	\$ (103)	\$ 372	\$ 44,261	0.42%
Multi-Family MBS	1,501,472	—	57,340	1,558,812	14.88
10 Year Fixed	171,556	(164)	1,539	172,931	1.65
15 Year Fixed	3,478,018	(134)	40,669	3,518,553	33.59
20 Year Fixed	2,340,415	(3,460)	13,266	2,350,221	22.44
25 Year Fixed	17,798	(10)	28	17,816	0.17
30 Year Fixed	1,217,468	(45)	10,121	1,227,544	11.73
Total Fannie Mae	\$ 8,770,719	\$ (3,916)	\$ 123,335	\$ 8,890,138	84.88%
Freddie Mac					
10 Year Fixed	81,795	(60)	1,538	83,273	0.80
15 Year Fixed	87,086	(1)	1,254	88,339	0.84
20 Year Fixed	1,357,383	(5,398)	6,631	1,358,616	12.97
Total Freddie Mac	\$ 1,526,264	\$ (5,459)	\$ 9,423	\$ 1,530,228	14.61%
Ginnie Mae					
ARMs & Hybrids	54,000	(729)	43	53,314	0.51
10 Year Fixed	308	—	22	330	0.00
Total Ginnie Mae	\$ 54,308	\$ (729)	\$ 65	\$ 53,644	0.51%
Total Agency Securities	\$ 10,351,291	\$ (10,104)	\$ 132,823	\$ 10,474,010	100.00%

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At December 31, 2015, we had the following securities in an unrealized gain or loss position as presented below. The components of the carrying value of our Agency Securities at December 31, 2015 are also presented below. Our Agency Securities had a weighted average coupon of 3.47% at December 31, 2015.

December 31, 2015	Amortized Cost	Gross Unrealized Loss	Gross Unrealized Gain	Fair Value	Percent of Total
Fannie Mae					
ARMs&Hybrids	\$ 46,512	\$ (210)	\$ 486	\$ 46,788	0.38%
Multi-Family MBS	2,182,156	(30,879)	7,312	2,158,589	17.32
10 Year Fixed	91,752	(362)	605	91,995	0.74
15 Year Fixed	4,302,585	(10,462)	5,498	4,297,621	34.49
20 Year Fixed	2,692,310	(25,429)	5,289	2,672,170	21.44
25 Year Fixed	18,488	(128)	—	18,360	0.15
30 Year Fixed	1,447,835	(6,645)	492	1,441,682	11.56
Total Fannie Mae	<u>\$ 10,781,638</u>	<u>\$ (74,115)</u>	<u>\$ 19,682</u>	<u>\$ 10,727,205</u>	<u>86.08%</u>
Freddie Mac					
ARMs&Hybrids	12,738	(46)	197	12,889	0.10
10 Year Fixed	37,657	(92)	652	38,217	0.31
15 Year Fixed	192,982	(995)	310	192,297	1.54
20 Year Fixed	1,443,652	(16,380)	4,006	1,431,278	11.49
Total Freddie Mac	<u>\$ 1,687,029</u>	<u>\$ (17,513)</u>	<u>\$ 5,165</u>	<u>\$ 1,674,681</u>	<u>13.44%</u>
Ginnie Mae					
ARMs&Hybrids	59,877	(610)	69	59,336	0.48
15 Year Fixed	314	—	20	334	0.00
Total Ginnie Mae	<u>\$ 60,191</u>	<u>\$ (610)</u>	<u>\$ 89</u>	<u>\$ 59,670</u>	<u>0.48%</u>
Total Agency Securities	<u>\$ 12,528,858</u>	<u>\$ (92,238)</u>	<u>\$ 24,936</u>	<u>\$ 12,461,556</u>	<u>100.00%</u>

Recognition of interest income commences on the settlement date of the purchase transaction and continues through the settlement date of the sale transaction. At March 31, 2016 and December 31, 2015, we did not have any investment related receivables or payables with respect to unsettled sales and purchases of our Agency Securities.

Actual maturities of Agency Securities are generally shorter than stated contractual maturities because actual maturities of Agency Securities are affected by the contractual lives of the underlying mortgages, periodic payments of principal and prepayments of principal.

The following table summarizes the weighted average lives of our Agency Securities at March 31, 2016 and December 31, 2015.

Weighted Average Life of all Agency Securities	March 31, 2016		December 31, 2015	
	Fair Value	Amortized Cost	Fair Value	Amortized Cost
Less than one year	\$ 16	\$ 16	\$ 19	\$ 19
Greater than or equal to one year and less than three years	67,434	67,080	30,189	30,375
Greater than or equal to three years and less than five years	7,452,538	7,396,947	6,037,851	6,039,218
Greater than or equal to five years	2,954,022	2,887,248	6,393,497	6,459,246
Total Agency Securities	<u>\$ 10,474,010</u>	<u>\$ 10,351,291</u>	<u>\$ 12,461,556</u>	<u>\$ 12,528,858</u>

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We use a third party model to calculate the weighted average lives of our Agency Securities. Weighted average life is calculated based on expectations for estimated prepayments for the underlying mortgage loans of our Agency Securities. These estimated prepayments are based on assumptions such as interest rates, current and future home prices, housing policy and borrower incentives. The weighted average lives of our Agency Securities at March 31, 2016 and December 31, 2015 in the table above are based upon market factors, assumptions, models and estimates from the third party model and also incorporate management's judgment and experience. The actual weighted average lives of our Agency Securities could be longer or shorter than estimated.

The following table presents the unrealized losses and estimated fair value of our Agency Securities by length of time that such securities have been in a continuous unrealized loss position at March 31, 2016 and December 31, 2015.

	Unrealized Loss Position For:					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2016	\$ 575,246	\$ (1,068)	\$ 1,537,449	\$ (9,036)	\$ 2,112,695	\$ (10,104)
December 31, 2015	\$ 7,105,363	\$ (58,799)	\$ 1,861,211	\$ (33,439)	\$ 8,966,574	\$ (92,238)

During the quarters ended March 31, 2016 and March 31, 2015, we sold \$1,789,215 and \$1,372,538 of Agency Securities, which resulted in realized gains of \$1,891 and \$6,544, respectively. Sales of Agency Securities are done to reposition our MBS portfolio and to reach our target level of liquidity.

Note 7 -Non-Agency Securities, Trading

All of our Non-Agency Securities are classified as trading securities and reported at their estimated fair value. Fair value changes are reported in the condensed consolidated statements of operations in the period in which they occur. During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. At March 31, 2016, investments in Non-Agency Securities accounted for 2.7% of our MBS portfolio.

The components of the carrying value of our Non-Agency Securities at March 31, 2016 are presented in the table below.

	Non-Agency Securities			Weighted Average Coupon
	Fair Value	Amortized Cost	Principal Amount	
March 31, 2016				
Credit risk transfer	\$ 285,696	\$ 281,550	\$ 291,718	5.11%
Total Non-Agency Securities	\$ 285,696	\$ 281,550	\$ 291,718	

Included in the table above are unsettled purchases with an aggregate cost of \$14,936 and estimated fair value of \$14,955 at March 31, 2016.

The following table summarizes the weighted average lives of our Non-Agency Securities at March 31, 2016

Weighted Average Life of all Non-Agency Securities	March 31, 2016	
	Fair Value	Amortized Cost
Less than one year	\$ —	\$ —
Greater than or equal to one year and less than three years	12,909	12,745
Greater than or equal to three years and less than five years	56,427	55,399
Greater than or equal to five years	216,360	213,406
Total Non-Agency Securities	\$ 285,696	\$ 281,550

We use a third party model to calculate the weighted average lives of our Non-Agency Securities. Weighted average life is calculated based on expectations for estimated prepayments for the underlying mortgage loans of our Non-Agency Securities. These estimated prepayments are based on assumptions such as interest rates, current and future home prices, housing policy and

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borrower incentives. The weighted average lives of our Non-Agency Securities at March 31, 2016 in the table above are based upon market factors, assumptions, models and estimates from the third party model and also incorporate management's judgment and experience. The actual weighted average lives of our Non-Agency Securities could be longer or shorter than estimated.

The following table presents the unrealized losses and estimated fair value of our Non-Agency Securities by length of time that such securities have been in a continuous unrealized loss position at March 31, 2016.

As of	Unrealized Loss Position For:					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2016	\$ 103,211	\$ (430)	\$ —	\$ —	\$ 103,211	\$ (430)

Our Non-Agency Securities are subject to risk of loss with regard to principal and interest payments and at March 31, 2016, have generally either been assigned below investment grade ratings by rating agencies, or have not been rated. We evaluate each investment based on the characteristics of the underlying collateral and securitization structure, rather than relying on the ratings assigned by rating agencies.

Note 8 -Repurchase Agreements

At March 31, 2016, we had MRAs with 37 counterparties and had \$9,923,859 in outstanding borrowings with 26 of those counterparties. At December 31, 2015, we had MRAs with 38 counterparties and had \$11,570,481 in outstanding borrowings with 26 of those counterparties.

The following table represents the contractual repricing regarding our repurchase agreements to finance our MBS purchases at March 31, 2016 and December 31, 2015. No amounts below are subject to offsetting.

March 31, 2016	Repurchase Agreements	Weighted Average Contractual Rate	Weighted Average Maturity in days	Haircut for Repurchase Agreements (1)
Agency Securities	\$ 9,722,888	0.69%	32	4.80%
Non-Agency Securities	200,971	2.15%	31	24.83%
Total or Weighted Average	\$ 9,923,859	0.72%	32	5.21%

(1) The Haircut represents the weighted average margin requirement, or the percentage amount by which the collateral value must exceed the loan amount.

December 31, 2015	Repurchase Agreements	Weighted Average Contractual Rate	Weighted Average Maturity in days	Haircut for Repurchase Agreements (1)
Agency Securities	\$ 11,570,481	0.57%	38	4.79%
Total or Weighted Average	\$ 11,570,481	0.57%	38	4.79%

(1) The Haircut represents the weighted average margin requirement, or the percentage amount by which the collateral value must exceed the loan amount.

Our repurchase agreements require that we maintain adequate pledged collateral. A decline in the value of the Agency Securities pledged as collateral for borrowings under repurchase agreements could result in the counterparties demanding additional collateral pledges or liquidation of some of the existing collateral to reduce borrowing levels. We manage this risk by maintaining an adequate balance of available cash and unpledged securities. An event of default or termination event under the standard MRA would give our counterparty the option to terminate all repurchase transactions existing with us and require any amount due to be payable immediately. In addition, certain of our MRAs contain a restriction that prohibits our leverage from exceeding twelve times our stockholders' equity as well as termination events in the case of significant reductions in equity capital. We also may receive cash or securities as collateral from our derivative counterparties which we may use as additional collateral for repurchase agreements. Certain interest rate swap contracts provide for cross collateralization and cross default with repurchase agreements and other contracts with the same counterparty.

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	March 31, 2016		December 31, 2015	
	Repurchase Agreements	Weighted Average Contractual Rate	Repurchase Agreements	Weighted Average Contractual Rate
Maturing or Repricing				
Within 30 days	\$ 7,366,962	0.71%	\$ 8,089,403	0.55%
31 days to 60 days	1,794,880	0.70%	2,487,174	0.57%
61 days to 90 days	112,017	1.01%	343,904	0.71%
Greater than 90 days	650,000	0.81%	650,000	0.67%
Total or Weighted Average	\$ 9,923,859	0.72%	\$ 11,570,481	0.57%

At March 31, 2016, 5 repurchase agreement counterparties individually accounted for between 5% and 10% of our aggregate borrowings and 1 counterparty that individually accounted for 10.5% of our aggregate borrowings. In total, these counterparties accounted for approximately 43.5% of our repurchase agreement borrowings outstanding at March 31, 2016. At December 31, 2015, we had 8 repurchase agreement counterparties that individually accounted for between 5% and 10% of our aggregate borrowings. In total, these counterparties accounted for 53.48% of our repurchase agreement borrowings at December 31, 2015. At March 31, 2016 and December 31, 2015, we did not have any repurchase counterparties that individually account for 5% or greater of our stockholders' equity.

Note 9 - Derivatives

We enter into derivative transactions to manage our interest rate risk exposure. These transactions include entering into interest rate swap contracts and interest rate swaptions as well as purchasing or selling Futures Contracts. These transactions are designed to lock in funding costs for repurchase agreements associated with our assets in such a way to help assure the realization of net interest margins. Such transactions are based on assumptions about prepayments which, if not realized, will cause transaction results to differ from expectations. Basis swap contracts allow us to exchange one floating interest rate basis for another, for example, 3 month LIBOR and Fed Funds Rates, thereby allowing us to diversify our floating rate basis exposures. We also utilize forward contracts for the purchase or sale of TBA Agency Securities.

We have agreements with our derivative counterparties that provide for the posting of collateral based on the fair values of our interest rate swap contracts, swaptions, basis swap contracts and TBA Agency Securities. Through this margin process, either we or our swap counterparty may be required to pledge cash or Agency Securities as collateral. Collateral requirements vary by counterparty and change over time based on the fair value, notional amount and remaining term of the contracts. Certain interest rate swap contracts provide for cross collateralization and cross default with repurchase agreements and other contracts with the same counterparty.

Interest rate swaptions generally provide us the option to enter into an interest rate swap agreement at a certain point of time in the future with a predetermined notional amount, stated term and stated rate of interest in the fixed leg and interest rate index on the floating leg.

Our Futures Contracts are traded on the CME which requires the use of daily mark-to-market collateral and the CME provides substantial credit support. The collateral requirements of the CME require us to pledge assets under a bi-lateral margin arrangement, including either cash or Agency Securities and these requirements may vary and change over time based on the market value, notional amount and remaining term of the Futures Contracts. In the event we are unable to meet a margin call under one of our Futures Contracts, the counterparty to such agreement may have the option to terminate or close-out all of the outstanding Futures Contracts with us. In addition, any close-out amount due to the counterparty upon termination of the counterparty's transactions would be immediately payable by us pursuant to the applicable agreement.

TBA Agency Securities are forward contracts for the purchase ("long position") or sale ("short position") of Agency Securities at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date. The specific Agency Securities 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. We may enter into TBA Agency Securities as a means of hedging against short-term changes in interest rates. We may also enter into TBA Agency Securities as a means of acquiring or disposing of Agency Securities and we may from time to time utilize TBA dollar roll transactions to finance Agency Security purchases. We estimate the fair value of TBA Agency Securities based on similar methods used to value our Agency Securities.

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We did not have any TBA Agency Securities outstanding at March 31, 2016 and December 31, 2015.

The following tables present information about our derivatives at March 31, 2016 and December 31, 2015.

March 31, 2016

Derivative Type	Remaining / Underlying Term	Weighted Average Remaining Swap / Option Term (Months)	Weighted Average Rate	Notional Amount (3)	Asset Fair Value (1)	Liability Fair Value (1)
Interest rate swap contracts	13-24 Months	19	0.80%	\$ 650,000	\$ —	\$ (2,532)
Interest rate swap contracts	25-36 Months	25	1.29%	400,000	—	(5,666)
Interest rate swap contracts	37-48 Months	44	1.47%	2,350,000	—	(71,913)
Interest rate swap contracts	61-72 Months	70	2.04%	275,000	—	(18,190)
Interest rate swap contracts	73-84 Months	80	2.10%	1,900,000	—	(101,528)
Interest rate swap contracts	109-120 Months	119	2.27%	750,000	—	(70,939)
Interest rate swap contracts	121-132 Months	123	2.50%	250,000	—	(27,917)
Basis swap contracts (2)	0-60 Months	19	0.22%	2,000,000	1,665	—
Total or Weighted Average				\$ 8,575,000	\$ 1,665	\$ (298,685)

(1) See Note 5, "Fair Value of Financial Instruments" for additional discussion.

(2) Weighted average rate is the spread over the pay index.

(3) Notional amount includes \$1,175,000 of forward starting interest rate swap contracts which become effective within 3 months.

December 31, 2015

Derivative Type	Remaining / Underlying Term	Weighted Average Remaining Swap / Option Term (Months)	Weighted Average Rate	Notional Amount	Asset Fair Value (1)	Liability Fair Value (1)
Interest rate swap contracts	13-24 Months	19	0.63%	350,000	265	(87)
Interest rate swap contracts	25-36 Months	27	1.16%	700,000	192	(1,633)
Interest rate swap contracts	37-48 Months	47	1.46%	2,000,000	—	(18,120)
Interest rate swap contracts	49-60 Months	49	1.53%	350,000	—	(3,085)
Interest rate swap contracts	73-84 Months	75	2.05%	1,025,000	—	(26,047)
Interest rate swap contracts	85-96 Months	86	2.11%	1,375,000	—	(23,543)
Interest rate swap contracts	109-120 Months	108	2.66%	1,000,000	—	(92,927)
Interest rate swap contracts	121-132 Months	123	2.30%	2,000,000	—	(67,858)
Basis swap contracts (2)	0-60 Months	22	0.22%	2,000,000	542	(1)
Total or Weighted Average				\$ 10,800,000	\$ 999	\$ (233,301)

(1) See Note 5, "Fair Value of Financial Instruments" for additional discussion.

We have netting arrangements in place with all derivative counterparties pursuant to standard documentation developed by the International Swap and Derivatives Association. We are also required to post or hold cash collateral based upon the net underlying market value of our open positions with the counterparty.

The following tables present information about interest rate swap contracts and basis swap contracts and the potential effects of netting if we were to offset the assets and liabilities of these financial instruments on the accompanying condensed

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consolidated balance sheets. Currently, we present these financial instruments at their gross amounts and they are included in derivatives, at fair value on the accompanying condensed consolidated balance sheet at March 31, 2016.

March 31, 2016	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheet			
Assets	Gross and Net Amounts of Assets Presented in the Condensed Consolidated Balance Sheet	Financial Instruments	Cash Collateral	Net Amount
Interest rate swap contracts	\$ —	\$ (298,685)	\$ 304,396	\$ 5,711
Basis swap contracts	1,665	—	—	1,665
Totals	\$ 1,665	\$ (298,685)	\$ 304,396	\$ 7,376

March 31, 2016	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheet			
Liabilities	Gross and Net Amounts of Liabilities Presented in the Condensed Consolidated Balance Sheet	Financial Instruments	Cash Collateral	Net Amount
Interest rate swap contracts	\$ (298,685)	\$ 298,685	\$ —	\$ —
Totals	\$ (298,685)	\$ 298,685	\$ —	\$ —

The following tables present information about interest rate swap contracts and Futures Contracts and the potential effects of netting if we were to offset the assets and liabilities of these financial instruments on the accompanying condensed consolidated balance sheets. Currently, we present these financial instruments at their gross amounts and they are included in derivatives, at fair value on the accompanying condensed consolidated balance sheet at December 31, 2015.

December 31, 2015	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheet			
Assets	Gross and Net Amounts of Assets Presented in the Condensed Consolidated Balance Sheet	Financial Instruments	Cash Collateral	Net Amount
Interest rate swap contracts	\$ 457	\$ (233,301)	\$ 241,604	\$ 8,760
Basis swap contracts	542	—	—	542
Totals	\$ 999	\$ (233,301)	\$ 241,604	\$ 9,302

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December 31, 2015	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheet			
Liabilities	Gross and Net Amounts of Liabilities Presented in the Condensed Consolidated Balance Sheet	Financial Instruments	Cash Collateral	Net Amount
Interest rate swap contracts	\$ (233,301)	\$ 233,301	\$ —	\$ —
Totals	\$ (233,301)	\$ 233,301	\$ —	\$ —

The following table represents the location and information regarding our derivatives which are included in Other Income (Loss) in the accompanying condensed consolidated statements of operations for the quarters ended March 31, 2016 and March 31, 2015.

Derivatives	Location on condensed consolidated statements of operations	Income (Loss) Recognized For the Quarter Ended	
		March 31, 2016	March 31, 2015
Interest rate swap contracts:			
Realized gain (loss)	Realized loss on derivatives	\$ (226,754)	\$ 48,931
Interest income	Realized loss on derivatives	7,449	4,178
Interest expense	Realized loss on derivatives	(26,991)	(44,919)
Changes in fair value	Unrealized gain (loss) on derivatives	(89,989)	(216,426)
		<u>\$ (336,285)</u>	<u>\$ (208,236)</u>
Futures Contracts:			
Realized loss	Realized loss on derivatives	—	(91)
Changes in fair value	Unrealized gain (loss) on derivatives	—	88
		<u>\$ —</u>	<u>\$ (3)</u>
Basis swap contracts:			
Interest income	Realized loss on derivatives	472	—
Interest expense	Realized loss on derivatives	(281)	—
Changes in fair value	Unrealized gain (loss) on derivatives	931	—
		<u>\$ 1,122</u>	<u>\$ —</u>
Totals		<u>\$ (335,163)</u>	<u>\$ (208,239)</u>

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Note 10 -Commitments and Contingencies*Management Agreement with ACM*

We are externally managed by ACM pursuant to a management agreement (the "Management Agreement") see also Note 15, "*Related Party Transactions*". The Management Agreement entitles ACM to receive a management fee payable monthly in arrears. Currently, the monthly management fee is 1/12th of the sum of (a) 1.5% of gross equity raised up to \$1.0 billion plus (b) 0.75% of gross equity raised in excess of \$1.0 billion. The cost of repurchased stock and any dividend representing a return of capital for tax purposes will reduce the amount of gross equity raised used to calculate the monthly management fee. At March 31, 2016 and March 31, 2015, the effective management fee was 1.05%, and 1.03% based on gross equity raised of \$2,469,368 and \$2,663,917, respectively. The ACM monthly management fee is not calculated based on the performance of our assets. Accordingly, the payment of our monthly management fee may not decline in the event of a decline in our earnings and may cause us to incur losses. We are also responsible for any costs and expenses that ACM incurred solely on behalf of ARMOUR other than the various overhead expenses specified in the terms of the Management Agreement. ACM is further entitled to receive a termination fee from us under certain circumstances.

Indemnifications and Litigation

We enter into certain contracts that contain a variety of indemnifications, principally with ACM and underwriters, against third party claims for errors and omissions in connection with their services to us. We have not incurred any costs to defend lawsuits or settle claims related to these indemnification agreements. As a result, the estimated fair value of these agreements, as well as the maximum amount attributable to past events, is not material. Accordingly, we have no liabilities recorded for these agreements at March 31, 2016 and December 31, 2015.

Nine putative class action lawsuits have been filed in connection with the Tender Offer and Merger for JAVELIN (see *Note 17 -Subsequent Events* for more information about the Tender Offer and Merger). The Tender Offer and Merger are collectively defined herein as the "Transactions." All nine suits name ARMOUR, the previous members of JAVELIN's board of directors prior to the Merger (of which eight are current members of ARMOUR's board of directors) (the "Individual Defendants") and Acquisition as defendants. Certain cases also name ACM and JAVELIN as additional defendants. The lawsuits were brought by purported holders of JAVELIN's common stock, both individually and on behalf of a putative class of JAVELIN's stockholders, alleging that the Individual Defendants breached their fiduciary duties owed to the plaintiffs and the putative class of JAVELIN stockholders, including claims that the Individual Defendants failed to properly value JAVELIN; failed to take steps to maximize the value of JAVELIN to its stockholders; ignored or failed to protect against conflicts of interest; failed to disclose material information about the Transactions; took steps to avoid competitive bidding and to give ARMOUR an unfair advantage by failing to adequately solicit other potential acquirors or alternative transactions; and erected unreasonable barriers to other third-party bidders. The suits also allege that ARMOUR, JAVELIN, ACM and Acquisition aided and abetted the alleged breaches of fiduciary duties by the Individual Defendants. The lawsuits seek equitable relief, including, among other relief, to enjoin consummation of the Transactions, or rescind or unwind the Transactions if already consummated, and award costs and disbursements, including reasonable attorneys' fees and expenses. On April 25, 2016, the court issued an order consolidating eight Maryland cases into one action, captioned *In re JAVELIN Mortgage Investment Corp. Shareholder Litigation* (Case No. 24-C-16-001542), and designated counsel for one of the Maryland cases as interim lead co-counsel.

Each of ARMOUR, JAVELIN, ACM and the Individual Defendants believes that the claims made in these lawsuits are without merit and intends to defend such claims vigorously; however, there can be no assurance that any of ARMOUR, JAVELIN, ACM or the Individual Defendants will prevail in its defense of any of these lawsuits to which it is a party. An unfavorable resolution of any such litigation surrounding the Transactions may result in monetary damages being awarded to the plaintiffs and the putative class of former stockholders of JAVELIN and the cost of defending the litigation, even if resolved favorably, could be substantial. Due to the preliminary nature of all nine suits, ARMOUR is not able at this time to estimate their outcome.

Note 11 -Stock Based Compensation

We adopted the 2009 Stock Incentive Plan as amended, (the "Plan") to attract, retain and reward directors and other persons who provide services to us in the course of operations. The Plan authorizes the Board to grant awards including common stock, restricted shares of common stock ("RSUs"), stock options, performance shares, performance units, stock appreciation rights and other equity and cash-based awards (collectively "Awards"), subject to terms as provided in the Plan.

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On May 8, 2014, our stockholders approved an amendment to the Plan to increase the number of shares issuable thereunder from 2,000 to 15,000 shares and the Plan was amended accordingly. In connection with the Reverse Stock Split, the number of shares of common stock issuable under the Plan was properly adjusted to 1,875 shares to reflect the Reverse Stock Split.

Transactions related to awards for the quarter ended March 31, 2016 are summarized below:

	March 31, 2016	
Number of Awards	\$	Weighted Average Grant Date Fair Value per Award
Unvested RSU Awards Outstanding beginning of period	78	\$ 48.85
Vested	(12)	\$ 56.33
Unvested RSU Awards Outstanding end of period	66	\$ 47.76

At March 31, 2016, there was approximately \$1,433 of unvested stock based compensation related to the Awards (based on the March 31, 2016 stock price of \$21.53 per share), that we expect to recognize as an expense over the remaining average service period of 0.6 years. We also pay our non-executive Board quarterly fees of \$33, which is payable in cash, common stock, or a combination of common stock and cash at the option of the director.

Note 12 -Stockholders' Equity

Preferred Stock

At March 31, 2016 and December 31, 2015, we were authorized to issue up to 50,000 shares of preferred stock, par value \$0.001 per share, with such designations, voting and other rights and preferences as may be determined from time to time by our Board of Directors ("Board") or a committee thereof. We have designated 9,610 shares as 8.250% Series A Preferred Stock and 6,210 shares as 7.875% Series B Preferred Stock. At March 31, 2016, a total of 34,180 shares of our authorized preferred stock remain available for designation as future series.

Series A Cumulative Preferred Shares ("Series A Preferred Stock")

At March 31, 2016 and December 31, 2015, we had 2,181 shares of Series A Preferred Stock issued and outstanding with a par value of \$0.001 per share and a liquidation preference of \$25.00 per share, or \$54,514 in the aggregate. Shares designated as Series A Preferred Stock but unissued totaled 7,429 at March 31, 2016. At March 31, 2016 and December 31, 2015, there were no accrued or unpaid dividends on the Series A Preferred Stock. The Series A Preferred Stock is entitled to a dividend at a rate of 8.250% per year based on the \$25.00 per share liquidation preference before the common stock is entitled to receive any dividends. The Series A Preferred Stock is redeemable at \$25.00 per share plus accrued and unpaid dividends exclusively at our option commencing on June 7, 2017 (subject to our right under limited circumstances to redeem the Series A Preferred Stock earlier in order to preserve our qualification as a REIT). The Series A Preferred Stock is senior to our common stock and therefore in the event of liquidation, dissolution or winding up, the Series A Preferred Stock will receive a liquidation preference of \$25.00 per share plus accumulated and unpaid dividends before distributions are paid to holders of our common stock, with no right or claim to any of our remaining assets thereafter. The Series A Preferred Stock generally does not have voting rights, except if we fail to pay dividends on the Series A Preferred Stock for eighteen months, whether or not consecutive. Under such circumstances, the Series A Preferred Stock will be entitled to vote to elect two additional directors to the Board, until all unpaid dividends have been paid or declared and set aside for payment. The Series A Preferred Stock has no stated maturity, is not subject to any sinking fund or mandatory redemption and will remain outstanding indefinitely unless repurchased or redeemed by us or converted into our common stock in connection with a change of control by the holders of Series A Preferred Stock.

Series B Cumulative Preferred Shares ("Series B Preferred Stock")

At March 31, 2016 and December 31, 2015, we had 5,650 shares of Series B Preferred Stock issued and outstanding with a par value of \$0.001 per share and a liquidation preference of \$25.00 per share, or \$141,250 in the aggregate. Shares designated as Series B Preferred Stock but unissued totaled 560 at March 31, 2016. At March 31, 2016 and December 31, 2015, there were no accrued or unpaid dividends on the Series B Preferred Stock. The Series B Preferred Stock is entitled to a dividend at a rate of 7.875% per year based on the \$25.00 per share liquidation preference before the common stock is entitled to receive any dividends.

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The Series B Preferred Stock is redeemable at \$25.00 per share plus accrued and unpaid dividends exclusively at our option commencing on February 12, 2018 (subject to our right under limited circumstances to redeem the Series A Preferred Stock earlier in order to preserve our qualification as a REIT). The Series B Preferred Stock is senior to our common stock and rank on parity with the Series A Preferred Stock. In the event of liquidation, dissolution or winding up, the Series B Preferred Stock will receive a liquidation preference of \$25.00 per share plus accumulated and unpaid dividends before distributions are paid to holders of our common stock, with no right or claim to any of our remaining assets thereafter. The Series B Preferred Stock generally does not have voting rights, except if we fail to pay dividends on the Series B Preferred Stock for eighteen months, whether or not consecutive. Under such circumstances, the Series B Preferred Stock will be entitled to vote to elect two additional directors to the Board, until all unpaid dividends have been paid or declared and set aside for payment. The Series B Preferred Stock has no stated maturity, is not subject to any sinking fund or mandatory redemption and will remain outstanding indefinitely unless repurchased or redeemed by us or converted into our common stock in connection with a change of control by the holders of Series B Preferred Stock.

Common Stock

Common Stock

On June 18, 2015, we announced that our Board of Directors had approved a Reverse Stock Split. The Reverse Stock Split took effect at approximately 5:00 p.m. Eastern Time on July 31, 2015 (the "Effective Time"). At the Effective Time, every eight issued and outstanding shares of common stock was converted into one share of common stock, and as a result, the number of outstanding shares of common stock was reduced from approximately 350,000 to approximately 43,750. At the Effective Time, the number of authorized shares of common stock was also reduced, on a one-for-eight basis, from 1,000,000 to 125,000. The par value of each share of common stock remained unchanged. No fractional shares were issued in connection with the Reverse Stock Split.

At March 31, 2016 and December 31, 2015, we were authorized to issue up to 125,000 shares of common stock, par value \$0.001 per share, with such designations, voting and other rights and preferences as may be determined from time to time by our Board. We had 36,692 shares of common stock issued and outstanding at March 31, 2016 and 36,682 shares of common stock issued and outstanding at December 31, 2015.

Common Stock Repurchased

On March 5, 2014, our Board increased the authorization under our common stock repurchase program (the "Repurchase Program") to 50,000 shares of our common stock outstanding (on a pre-reverse stock split basis). On July 28, 2015, our Board of Directors increased the number of shares of common stock authorized for repurchase under our Repurchase Program to an aggregate of 9,000 shares on a post-reverse stock split basis, effective August 3, 2015. Under the Repurchase Program, shares may be purchased in the open market, including block trades, through privately negotiated transactions, or pursuant to a trading plan separately adopted in the future. The timing, manner, price and amount of any repurchases will be at our discretion, subject to the requirements of the Securities Exchange Act of 1934, as amended, and related rules. We are not required to repurchase any shares under the Repurchase Program and it may be modified, suspended or terminated at any time for any reason. We do not intend to purchase shares from our Board or other affiliates. Under Maryland law, such repurchased shares are treated as authorized but unissued. At March 31, 2016, there were 1,874 authorized shares remaining under the Repurchase Program. During the quarter ended March 31, 2016, we did not repurchase any common shares under the Repurchase Program.

Dividends

The following tables present our common stock dividend transactions for the quarter ended March 31, 2016.

Record Date	Payment Date	Rate per common share	Aggregate amount paid to holders of record
January 15, 2016	January 27, 2016	\$ 0.33	\$ 12,131.0
February 13, 2016	February 27, 2016	\$ 0.33	12,131.0
March 13, 2016	March 27, 2016	\$ 0.33	12,131.0
Total dividends paid			<u>\$ 36,393.0</u>

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The following tables present our Series A Preferred Stock dividend transactions for the quarter ended March 31, 2016.

Record Date	Payment Date	Rate per Series A Preferred Share	Aggregate amount paid to holders of record
January 15, 2016	January 27, 2016	\$ 0.17	\$ 374.8
February 15, 2016	February 26, 2016	\$ 0.17	374.8
March 15, 2016	March 28, 2016	\$ 0.17	374.8
Total dividends paid			<u>\$ 1,124.4</u>

The following tables present our Series B Preferred Stock dividend transactions for the quarter ended March 31, 2016.

Record Date	Payment Date	Rate per Series B Preferred Share	Aggregate amount paid to holders of record
January 15, 2016	January 27, 2016	\$ 0.16	\$ 927.0
February 15, 2016	February 26, 2016	\$ 0.16	927.0
March 15, 2016	March 28, 2016	\$ 0.16	927.0
Total dividends paid			<u>\$ 2,781.0</u>

Note 13 -Net Loss per Common Share

The following table presents a reconciliation of net loss and the shares used in calculating weighted average basic and diluted earnings per common share for the quarters ended March 31, 2016, and March 31, 2015.

	For the Quarter Ended	
	March 31, 2016	March 31, 2015
Net Loss	\$ (279,475)	\$ (125,469)
Less: Preferred dividends	(3,905)	(3,905)
Net loss related to common stockholders	<u>\$ (283,380)</u>	<u>\$ (129,374)</u>
Weighted average common shares outstanding – basic	36,683	44,118
Add: Effect of dilutive non-vested awards, assumed vested	—	—
Weighted average common shares outstanding – diluted	<u>36,683</u>	<u>44,118</u>

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Note 14 -Income Taxes

The following table reconciles our GAAP net income to estimated REIT taxable income for the quarters ended March 31, 2016, March 31, 2015.

	For the Quarter Ended	
	March 31, 2016	March 31, 2015
GAAP net loss	\$ (279,475)	\$ (125,469)
Book to tax differences:		
Net book to tax differences on Non-Agency Securities	(4,125)	—
Changes in interest rate contracts	315,811	167,407
Gains on Security Sales	(1,891)	(6,544)
Amortization of deferred hedging costs	(9,232)	(1,877)
Other	3	4
Estimated REIT taxable income	<u>\$ 21,091</u>	<u>\$ 33,521</u>

Interest rate contracts are treated as hedging transactions for tax purposes. Unrealized gains and losses on open interest rate contracts are not included in the determination of taxable income. Realized gains and losses on interest rate contracts terminated before their maturity are deferred and amortized over the remainder of the original term of the contract.

Net capital losses realized in 2013, 2014 and 2015 totaling \$(579,322), \$(341,850) and \$(5,175) will be available to offset future capital gains realized through 2018, 2019 and 2020, respectively.

The aggregate tax basis of our assets and liabilities was greater than our total Stockholders' Equity at March 31, 2016 by approximately \$333,763, or approximately \$9.10 per common share (based on the 36,692 common shares then outstanding).

We are required and intend to timely distribute substantially all of our REIT taxable income in order to maintain our REIT status under the Code. Total dividend payments to stockholders were \$40,298 and \$46,391 for the quarters ended March 31, 2016 and March 31, 2015, respectively. Our estimated REIT taxable income available to pay dividends was \$21,091 and \$33,521 for the quarters ended March 31, 2016 and March 31, 2015, respectively. Our taxable REIT income and dividend requirements to maintain our REIT status are determined on an annual basis. Dividends paid in excess of taxable REIT income for the year (including amounts carried forward from prior years) will generally not be taxable to common stockholders.

Our management is responsible for determining whether tax positions taken by us are more likely than not to be sustained on their merits. We have no material unrecognized tax benefits or material uncertain tax positions.

Note 15 -Related Party Transactions

We are externally managed by ACM pursuant to the Management Agreement. All of our executive officers are also employees of ACM. ACM manages our day-to-day operations, subject to the direction and oversight of the Board. The Management Agreement runs through June 18, 2022 and is thereafter automatically renewed for successive five-year terms unless terminated under certain circumstances. Either party must provide 180 days prior written notice of any such termination.

Under the terms of the Management Agreement, ACM is responsible for costs incident to the performance of its duties, such as compensation of its employees and various overhead expenses. ACM is responsible for the following primary roles:

- Advising us with respect to, arranging for and managing the acquisition, financing, management and disposition of, elements of our investment portfolio;
- Evaluating the duration risk and prepayment risk within the investment portfolio and arranging borrowing and hedging strategies;
- Coordinating capital raising activities;

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- Advising us on the formulation and implementation of operating strategies and policies, arranging for the acquisition of assets, monitoring the performance of those assets and providing administrative and managerial services in connection with our day-to-day operations; and
- Providing executive and administrative personnel, office space and other appropriate services required in rendering management services to us.

In accordance with the Management Agreement, we incurred \$6,508 and \$6,877 in management fees for the quarters ended March 31, 2016 and March 31, 2015, respectively.

We are required to take actions as may be reasonably required to permit and enable ACM to carry out its duties and obligations. We are also responsible for any costs and expenses that ACM incurred solely on our behalf other than the various overhead expenses specified in the terms of the Management Agreement. For the quarters ended March 31, 2016 and March 31, 2015, we reimbursed ACM \$467 and \$382, respectively for other expenses incurred on our behalf. In consideration of our 2012 results, in 2013, we also elected to make a restricted stock award to our executive officers and other ACM employees through ACM. No new awards have been granted since 2013. The award vests through 2017 and resulted in our recognizing stock based compensation expense of \$118 and \$179 for the quarters ended March 31, 2016 and March 31, 2015.

Note 16 -Interest Rate Risk

Our primary market risk is interest rate risk. Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. Changes in the general level of interest rates can affect net interest income, which is the difference between the interest income earned and the interest expense incurred in connection with the liabilities, by affecting the spread between the interest-earning assets and interest-bearing liabilities. Changes in the level of interest rates also can affect the value of MBS and our ability to realize gains from the sale of these assets. A decline in the value of the MBS pledged as collateral for borrowings under repurchase agreements could result in the counterparties demanding additional collateral pledges or liquidation of some of the existing collateral to reduce borrowing levels.

Note 17 -Subsequent Events

Acquisition of JAVELIN Mortgage Investment Corp.

On April 6, 2016 we completed our acquisition of all of the outstanding common stock of JAVELIN pursuant the Transactions, for cash consideration of \$85.2 million. Subsequently JAVELIN became a wholly-owned subsidiary of ARMOUR. The acquisition expands and diversifies our investment portfolio. JAVELIN's complementary assets provide us with investment opportunities in Non-Agency MBS.

We recognized JAVELIN's assets and liabilities (including JAVELIN's liability under JAVELIN's management agreement with ACM) at their fair values on the date of the Merger. None of the bargain purchase price is expected to be included in income for income tax purposes.

The following table summarizes the consideration paid for JAVELIN and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date, as well as the fair value at the acquisition date. The following amounts are preliminary and subject to change (amounts in millions):

Consideration:		
Cash	\$	85.2
Fair value of consideration transferred	\$	85.2
Acquisition related costs (included in professional fees for the quarter ended March 31, 2016)	\$	1.5
Recognized amounts of identifiable assets acquired and liabilities assumed		
Cash and cash collateral	\$	36.6
Agency Securities		440.7
Non-Agency Securities		223.2
Accrued interest receivable		1.4
Prepaid and other assets		5.4
Repurchase agreements		(589.6)
Derivatives		(17.5)
Accrued interest payable		(0.9)
Accounts payable and other accrued expenses		(7.6)
Total identifiable net assets	\$	91.7
Goodwill/(Bargain purchase price)		(6.5)
Total	\$	85.2

Included in accounts payable and other accrued expenses is a liability of \$3.4 million which has been recognized as the fair value of the Second Amended and Restated Management Agreement between JAVELIN and ACM.

We expect to recognize a gain of \$6.5 million as a result of the Transactions which will be included in other income in our condensed consolidated income statement for the period ending June 30, 2016.

Dividends

On April 27, 2016, a cash dividend of \$0.17 per outstanding share of Series A Preferred Stock, or \$375 in the aggregate, and \$0.16 per outstanding share of Series B Preferred Stock, or \$927 in the aggregate, was paid to holders of record on April 15, 2016. We have also declared cash dividends of \$0.17 and \$0.16 per outstanding share of Series A Preferred Stock and Series B Preferred Stock, respectively, payable May 27, 2016 to holders of record on May 15, 2016 and payable June 27, 2016 to holders of record on June 15, 2016.

On April 27, 2016, a cash dividend of \$0.27 per outstanding common share, or \$9,907 in the aggregate, was paid to holders of record on April 15, 2016. We have also declared cash dividends of \$0.22 per outstanding common share payable May 27, 2016 to holders of record on May 16, 2016 and payable June 29, 2016 to holders of record on June 15, 2016.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this report.

References to "we," "us," "our," "ARMOUR" or the "Company" are to ARMOUR Residential REIT, Inc. References to "ACM" are to ARMOUR Capital Management LP, a Delaware limited partnership. In February 2016, the Company formed JMI Acquisition Corporation ("Acquisition"), a Maryland corporation and wholly-owned subsidiary of ours which merged with and into JAVELIN Mortgage Investment Corp. ("JAVELIN") on April 6, 2016. Acquisition was formed for the purpose of acquiring all of the shares of common stock of JAVELIN. See below for more information about the relationship between ARMOUR, JAVELIN and Acquisition. Refer to the Glossary of Terms for definitions of capitalized terms and abbreviations used in this report. All per share amounts, common shares outstanding and stock-based compensation amounts for all periods presented reflect our Reverse Stock Split, which was effective July 31, 2015.

U.S. dollar amounts are presented in thousands, except per share amounts or as otherwise noted.

Overview

We are a Maryland corporation formed to invest in and manage a leveraged portfolio of MBS and mortgage loans. We invest in residential mortgage backed securities issued or guaranteed by a U.S. GSE, such as Fannie Mae, Freddie Mac or Ginnie Mae (collectively, Agency Securities). Other securities backed by residential mortgages in which we invest, for which the payment of principal and interest is not guaranteed by a GSE or government agency (collectively, Non-Agency Securities and together with Agency Securities, MBS), may benefit from credit enhancement derived from structural elements such as subordination, over collateralization or insurance.

At March 31, 2016 and December 31, 2015, investments in Agency Securities accounted for 97.3% and 100% of our MBS portfolio, respectively. During the quarter ended March 31, 2016 we began to invest in Non-Agency Securities. At March 31, 2016, investments in Non-Agency Securities accounted for 2.7% of our MBS portfolio. Our MBS portfolio consists primarily of Agency Securities backed by fixed rate home loans. From time to time, a portion of our assets may be invested in Agency Securities backed by hybrid adjustable rate and adjustable rate home loans as well as unsecured notes and bonds issued by GSEs, U.S. Treasuries and money market instruments, subject to certain income tests we must satisfy for our qualification as a REIT. Our charter permits us to invest in Agency Securities and Non-Agency Securities.

We are externally managed by ACM, pursuant to the Management Agreement, which was most recently amended on February 23, 2015. ACM is an investment advisor registered with the SEC. ACM is also the external manager of JAVELIN. Certain of our executive officers also serve as the executive officers of JAVELIN.

We seek attractive long-term investment returns by investing our equity capital and borrowed funds in our targeted asset class of MBS. We earn returns on the spread between the yield on our assets and our costs, including the interest cost of the funds we borrow, after giving effect to our hedges. We identify and acquire MBS, finance our acquisitions with borrowings under a series of short-term repurchase agreements at the most competitive interest rates available to us and then cost-effectively hedge our interest rate and other risks based on our entire portfolio of assets, liabilities and derivatives and our management's view of the market. Successful implementation of this approach requires us to address interest rate risk, maintain adequate liquidity and effectively hedge interest rate risks. We believe that the residential mortgage market will undergo significant changes in the coming years as the role of GSEs, such as Fannie Mae and Freddie Mac, is diminished, which we expect will create attractive investment opportunities for us. We execute our business plan in a manner consistent with our intention of qualifying as a REIT under the Code and avoiding regulation as an investment company under the 1940 Act.

We have elected to be taxed as a REIT under the Code. We will generally not be subject to federal income tax to the extent that we distribute our taxable income to our stockholders and as long as we satisfy the ongoing REIT requirements under the Code including meeting certain asset, income and stock ownership tests.

Recent Developments

Acquisition of JAVELIN Mortgage Investment Corp.

On March 1, 2016, we entered into an Agreement and Plan of Merger (the "Merger Agreement") with JAVELIN and Acquisition. Pursuant to the Merger Agreement, Acquisition commenced a tender offer (the "Tender Offer") to purchase all of the outstanding common stock of JAVELIN for cash at a price of \$7.18 (the "Tender Offer Price"), without interest and less any

applicable withholding taxes. The Tender Offer was subject to the condition that greater than 50% of the total outstanding shares of common stock which were not owned immediately before the expiration of the Tender Offer by us, any of our subsidiaries, including Acquisition, or any of our officers or directors, or JAVELIN, would be validly tendered and not withdrawn (the "Minimum Condition"). Upon completion of the Tender Offer, Acquisition would be merged with and into JAVELIN (the "Merger"). Pursuant to the Merger Agreement, any remaining untendered shares of JAVELIN common stock were converted into the right to receive cash equal to the Tender Offer Price. On April 1, 2016, the Tender Offer expired with the Minimum Condition having been successfully met. On April 6, 2016, we completed the cash acquisition of JAVELIN for an aggregate of approximately \$85.2 million in cash, in which the Merger was effected pursuant to Section 3-106.1 of the MGCL. The MGCL did not require that the Merger be approved by our stockholders. Upon consummation of the Merger, JAVELIN became a wholly-owned, qualified REIT subsidiary of ours and continues to be managed by ACM pursuant to the pre-existing management agreement between JAVELIN and ACM (the "JAVELIN Management Agreement"). We recognized JAVELIN's assets and liabilities (including JAVELIN's liability under the JAVELIN Management Agreement) at their fair values on the date of the Merger. JAVELIN continues to invest in a leveraged portfolio of Agency Securities, Non-Agency Securities and other mortgage-related investments. Our Co-CEOs and directors, Scott J. Ulm and Jeffrey J. Zimmer, our CFO, James R. Mountain, and our Chief Operating Officer, Mark Gruber served as the executive officers of JAVELIN prior to the Merger. Upon effectiveness of the Merger, Messrs. Ulm, Zimmer and Mountain began to serve as the only executive officers and directors of JAVELIN. Also, eight of our nine directors, which are Marc Bell, Thomas Guba, Robert Hain, John Hollihan, Stewart Paperin and Daniel Staton, and Messrs. Ulm and Zimmer, also served as the directors of JAVELIN prior to the Merger. As a result of the completion of the Merger, shares of JAVELIN common stock ceased trading on the NYSE before the open of market on April 7, 2016.

Factors that Affect our Results of Operations and Financial Condition

Our results of operations and financial condition are affected by various factors, many of which are beyond our control, including, among other things, our net interest income, the market value of our assets and the supply of and demand for such assets. We invest in financial assets and markets. Recent events, such as those discussed below, can affect our business in ways that are difficult to predict and may produce results outside of typical operating variances. Our net interest income varies primarily as a result of changes in interest rates, borrowing costs and prepayment speeds, the behavior of which involves various risks and uncertainties. We invest across the spectrum of mortgage investments, from Agency Securities, for which the principal and interest payments are guaranteed by a GSE, to Non-Agency Securities, non-prime mortgage loans and unrated equity tranches of CMBS. As such, we expect our investments to be subject to risks arising from delinquencies and foreclosures, thereby exposing our investment portfolio to potential losses. We are exposed to changing credit spreads, which could result in declines in the fair value of our investments. We believe ACM's in-depth investment expertise across multiple sectors of the mortgage market, prudent asset selection and our hedging strategy enable us to minimize our credit losses, our market value losses and financing costs. Prepayment rates, as reflected by the rate of principal pay downs and interest rates vary according to the type of investment, conditions in financial markets, government actions, competition and other factors, none of which can be predicted with any certainty. In general, as prepayment rates on our assets that are purchased at a premium increase, related purchase premium amortization increases, thereby reducing the net yield on such assets. Because changes in interest rates may significantly affect our activities, our operating results depend, in large part, upon our ability to manage interest rate risks and prepayment risks effectively while maintaining our status as a REIT.

For any period during which changes in the interest rates earned on our assets do not coincide with interest rate changes on our borrowings, such assets will tend to reprice more slowly than the corresponding liabilities. Consequently, changes in interest rates, particularly short-term interest rates, may significantly influence our net interest income. With the maturities of our assets generally of a longer term than those of our liabilities, interest rate increases will tend to decrease our net interest income and the market value of our assets (and therefore our book value). Such rate increases could possibly result in operating losses or adversely affect our ability to make distributions to our stockholders.

Prepayments on MBS and the underlying mortgage loans may be influenced by changes in market interest rates and a variety of economic and geographic factors, policy decisions by regulators, as well as other factors beyond our control. To the extent we hold MBS acquired at a premium or discount to par, or face value, changes in prepayment rates may impact our anticipated yield. In periods of declining interest rates, prepayments on our MBS will likely increase. If we are unable to reinvest the proceeds of such prepayments at comparable yields, our net interest income may decline. The recent climate of government intervention in the mortgage markets significantly increases the risk associated with prepayments.

While we use strategies to economically hedge some of our interest rate risk, we do not hedge all of our exposure to changes in interest rates and prepayment rates, as there are practical limitations on our ability to insulate our MBS portfolio from all potential negative consequences associated with changes in short-term interest rates in a manner that will allow us to seek attractive net spreads on our MBS portfolio. Also, since we have not elected to use cash flow hedge accounting, earnings reported in accordance with GAAP will fluctuate even in situations where our derivatives are operating as intended. As a result of this

mark-to-market accounting treatment, our results of operations are likely to fluctuate far more than if we were to designate our derivative activities as cash flow hedges. Comparisons with companies that use cash flow hedge accounting for all or part of their derivative activities may not be meaningful. For these and other reasons more fully described under the section captioned "Derivative Instruments" below, no assurance can be given that our derivatives will have the desired beneficial impact on our results of operations or financial condition.

In addition to the use of derivatives to hedge interest rate risk, a variety of other factors relating to our business may also impact our financial condition and operating performance; these factors include

- our degree of leverage;
- our access to funding and borrowing capacity;
- the REIT requirements under the Code; and
- the requirements to qualify for an exemption under the 1940 Act and other regulatory and accounting policies related to our business.

Our Manager

See Note 10 and Note 15 to the condensed consolidated financial statements.

Market and Interest Rate Trends and the Effect on our MBS portfolio

Developments at Fannie Mae and Freddie Mac

The payments we receive on the Agency Securities in which we invest depend upon a steady stream of payments by borrowers on the underlying mortgages and the fulfillment of guarantees by GSEs. There can be no assurance that the U.S. Government's intervention in Fannie Mae and Freddie Mac will continue to be adequate for the longer-term viability of these GSEs. These uncertainties may lead to concerns about the availability of and trading market for Agency Securities in the long term. Accordingly, if the GSEs defaulted on their guaranteed obligations, suffered losses or ceased to exist, the value of our Agency Securities and our business, operations and financial condition could be materially and adversely affected.

The passage of any new federal legislation affecting Fannie Mae and Freddie Mac may create market uncertainty and reduce the actual or perceived credit quality of securities issued or guaranteed by them. If Fannie Mae and Freddie Mac were reformed or wound down, it is unclear what effect, if any, this would have on the value of the existing Fannie Mae and Freddie Mac Agency Securities. The foregoing could materially adversely affect the pricing, supply, liquidity and value of the Agency Securities in which we invest and otherwise materially adversely affect our business, operations and financial condition.

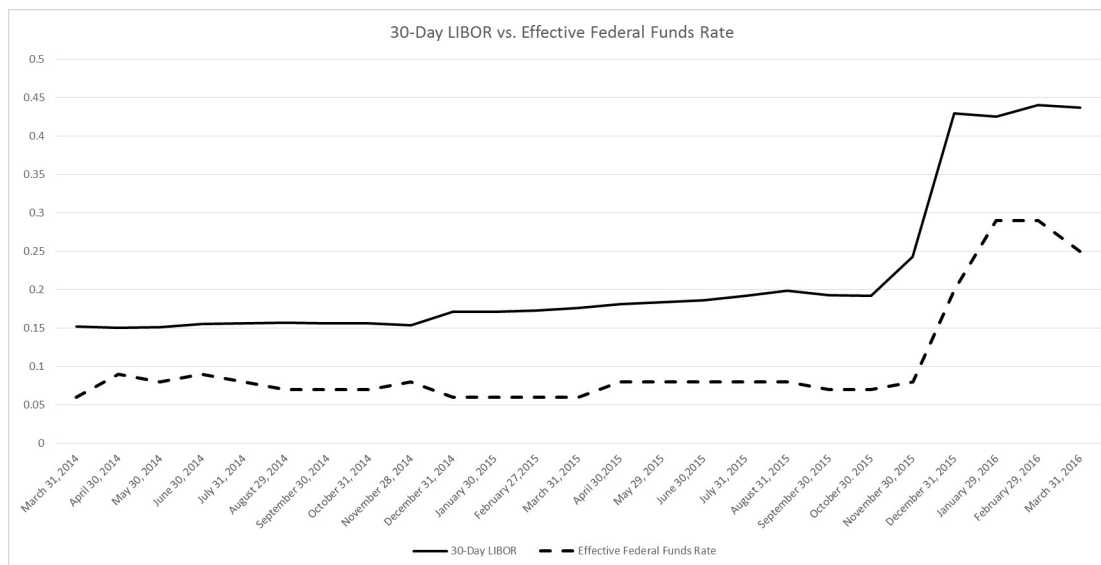
Short-term Interest Rates and Funding Costs

On December 16, 2015, the Fed raised its target range for the Federal Funds Rate to between 0.25% and 0.50%. At the January 27, 2016 and the March 16, 2016 Fed meetings, the Fed announced their decision to hold the same target range. Changes in Fed policy affect our financial results, since our cost of funds is largely dependent on short-term rates. An increase in our cost of funds without a corresponding increase in interest income earned on our Agency Securities would cause our net income to decline.

Historically, 30-day LIBOR has closely tracked movements in the Federal Funds Rate and the Effective Federal Funds Rate. The Effective Federal Funds Rate can differ from the Federal Funds Rate in that the Effective Federal Funds Rate represents the volume weighted average of interest rates at which depository institutions lend balances at the Fed to other depository institutions overnight (actual transactions, rather than target rate).

Our borrowings in the repurchase market have also historically closely tracked the Federal Funds Rate and LIBOR. Traditionally, a lower Federal Funds Rate has indicated a time of increased net interest margin and higher asset values. The difference between 30-day LIBOR and the Effective Federal Funds Rate can be quite volatile, with the spread alternately returning to more normal levels and then widening out again. Volatility in these rates and divergence from the historical relationship among these rates could negatively impact our ability to manage our MBS portfolio. If rates were to increase as a result, our net interest margin and the value of our MBS portfolio might suffer as a result.

The following graph shows 30-day LIBOR as compared to the Effective Federal Funds Rate on a monthly basis from March 31, 2014 to March 31, 2016.



Long-term Interest Rates and Mortgage Spreads

Our Agency Securities are valued at an interest rate spread versus long-term interest rates (mortgage spread). This mortgage spread varies over time and can be above or below long-term averages, depending upon market participants' current desire to own Agency Securities over other investment alternatives. When the mortgage spread gets smaller (or negative) versus long-term interest rates, our book value will be positively affected. When this spread gets larger (or positive), our book value will be negatively affected.

Mortgage spreads can vary due to movements in MBS valuations, movements in long-term interest rates or a combination of both. During 2015, interest rate swap rates declined more than U.S. Treasury interest rates, causing the interest rate swap spread to be negative to U.S. Treasury interest rates for certain longer tenors, an inversion of longstanding market norms. The market conditions continued during the quarter ended March 31, 2016. We mainly use interest rate swap contracts (including swaptions) to hedge against changes in the valuation of our MBS. As of March 31, 2016 and December 31, 2015, we have not entered into any contract or purchased any asset specifically designed to offset the impact of mortgage spreads on our book value.

Results of Operations**Net Income (Loss) Summary**

The following is a summary of our condensed consolidated results of operations:

	For the Quarter Ended		Change vs. Prior
	March 31, 2016	March 31, 2015	Year 2016
Net Interest Income	\$ 59,312	\$ 85,358	(30.51)%
Total Other Loss	(329,150)	(201,695)	(63.19)%
Total Expenses	9,637	9,132	5.53%
Net Loss	\$ (279,475)	\$ (125,469)	(122.74)%
Dividends declared on preferred stock	\$ (3,905)	\$ (3,905)	—%
Net Loss related to common stockholders	\$ (283,380)	\$ (129,374)	(119.04)%
Net loss per share related to common stockholders, basic	\$ (7.73)	\$ (2.96)	(161.15)%
Net loss per share related to common stockholders, diluted	\$ (7.73)	\$ (2.96)	(161.15)%

Our net losses on derivatives in 2016 paired with the decrease in our MBS portfolio, which lead to a decline in net interest income, were the main factors for the change in net loss for the quarter ended March 31, 2016, as compared to the quarter ended March 31, 2015.

Net Interest Income (Loss)

	For the Quarter Ended		Change vs. Prior
	March 31, 2016	March 31, 2015	Year 2016
Agency Securities, net of amortization of premium	\$ 78,133	\$ 99,550	(21.51)%
Non-Agency Securities, including discount accretion	327	—	100.00%
Interest expense- repurchase agreements	(19,148)	(14,192)	(34.92)%
Net Interest Income	\$ 59,312	\$ 85,358	(30.51)%

Net interest income is a function of both our MBS portfolio size, asset yield and repurchase agreements expense and net interest rate spread.

2016 vs. 2015

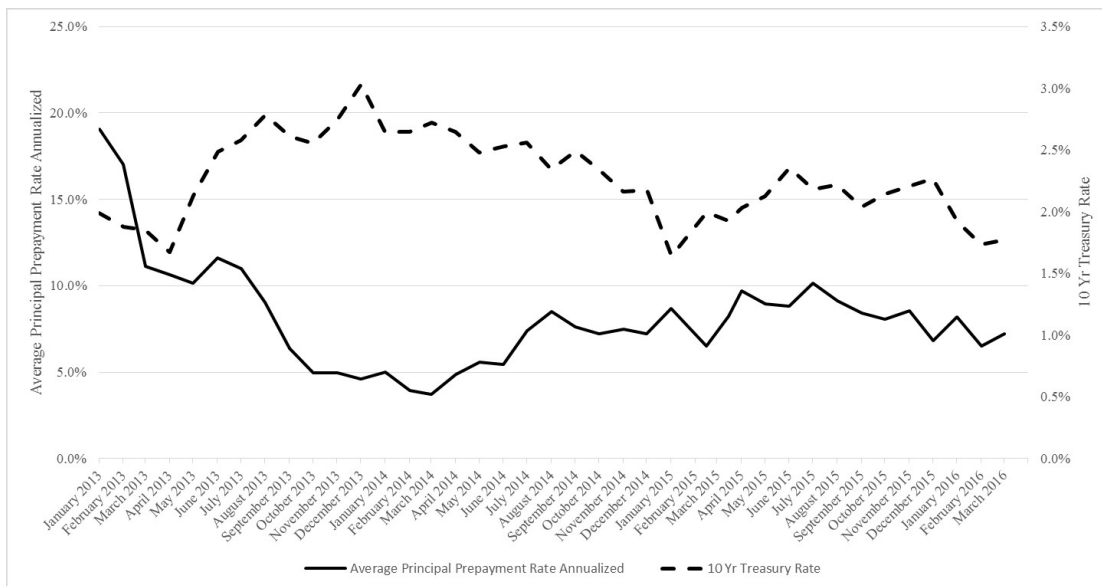
- Our average MBS portfolio decreased 16.7% from \$14,634,391 at March 31, 2015 to \$11,455,691 at March 31, 2016.
- Our asset yields increased 0.01% and our interest expense on our repurchase agreements increased by 0.28% for the quarter ended March 31, 2016, compared to the quarter ended March 31, 2015.
- Our net interest rate spread increased 0.17% from 1.20% at March 31, 2015 to 1.37% at March 31, 2016. The increase in the interest rate spread from 2015 to 2016, combined with the decrease in our MBS portfolio, resulted in decreased net interest income.

At March 31, 2016 and December 31, 2015, our Agency Securities in our MBS portfolio were carried at a net premium to par value with a weighted average amortized cost of 106.3% and 104.9%, respectively, due to the average interest rates on these securities being higher than prevailing market rates.

The following table presents the components of the yield earned on our MBS portfolio for the quarterly periods presented.

MBS	Asset Yield	Cost of Funds	Net Interest Margin	Interest Expense on Repurchase Agreements
Agency Securities:				
March 31, 2016	2.73%	1.36%	1.37%	0.67%
September 30, 2015	2.56%	1.12%	1.44%	0.44%
June 30, 2015	2.60%	1.24%	1.36%	0.40%
March 31, 2015	2.72%	1.52%	1.20%	0.39%
Non-Agency Securities:				
March 31, 2016	5.74%	2.26%	3.48%	2.26%
Total portfolio:				
March 31, 2016	2.73%	1.36%	1.37%	0.68%
September 30, 2015	2.56%	1.12%	1.44%	0.44%
June 30, 2015	2.60%	1.24%	1.36%	0.40%
March 31, 2015	2.72%	1.52%	1.20%	0.39%

The yield on our assets is most significantly affected by the rate of repayments on our Agency Securities. The following graph shows the annualized CPR on a monthly basis.



Other Income (Loss)

	For the Quarter Ended		Change vs. Prior
	March 31, 2016	March 31, 2015	Year 2016
Realized gain on sale of Agency Securities (reclassified from Other comprehensive income)	\$ 1,891	\$ 6,544	(71.10)%
Gain on Non-Agency Securities	4,122	—	100.00%
Subtotal	\$ 6,013	\$ 6,544	(8.11)%
Realized gain (loss) on derivatives	(246,105)	8,099	(3,138.71)%
Unrealized loss on derivatives	(89,058)	(216,338)	58.83%
Subtotal	\$ (335,163)	\$ (208,239)	(60.95)%
Total Other Loss	\$ (329,150)	\$ (201,695)	(63.19)%

2016 vs. 2015

- Gains on Agency Securities resulted from the sales of Agency Securities during the quarter ended March 31, 2016 of \$1,789,215 compared to \$1,372,538 during the quarter ended March 31, 2015. At March 31, 2016 and March 31, 2015, we also considered whether we intended to sell Agency Securities and whether it was more likely than not that we could meet our liquidity requirements and contractual obligations without selling Agency Securities. As a result of this evaluation, no other than temporary impairment was recognized for the quarters ended March 31, 2016 and March 31, 2015, respectively, because we determined that we 1) did not have the intent to sell the Agency Securities in an unrealized loss position, 2) did not believe it more likely than not that we were required to sell the securities before recovery (for example, because of liquidity requirements or contractual obligations), and/or (3) determined that a credit loss did not exist.
- During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. Gain on Non-Agency Securities resulted from purchases of \$285,696, fair value of Non-Agency Securities during the quarter ended March 31, 2016.
- Gains (losses) on Derivatives resulted from a combination of the following: We decreased our total interest rate swap contracts aggregate notional balance from \$12,025,000 at March 31, 2015 to \$6,575,000 at March 31, 2016, respectively. Our total Futures Contracts notional amount decreased from \$10,000 at March 31, 2015 to \$0 at March 31, 2016, respectively, due to the maturity of contracts. Our total basis swap contracts aggregate notional balance was \$2,000,000 at March 31, 2016. We did not have basis swap contracts at March 31, 2015.

Expenses

	For the Quarter Ended		Change vs. Prior
	March 31, 2016	March 31, 2015	Year 2016
Management fee	\$ 6,508	\$ 6,877	(5.37)%
Professional fees	2,173	793	174.02 %
Insurance	171	170	0.59 %
Compensation	518	613	(15.50)%
Other	267	679	(60.68)%
Total Expenses	\$ 9,637	\$ 9,132	5.53 %

Management fees are determined based on gross equity raised. Therefore, our management fee increases when we raise capital and declines when we repurchase previously issued stock or pay dividends in excess of taxable income. However, because the management fee rate decreased to 0.75% per annum for gross equity raised in excess of \$1.0 billion pursuant to the Management Agreement, the effective average management fee rate declines as equity is raised. Gross equity raised was \$2,469,368 at March 31, 2016, compared to \$2,663,917 at March 31, 2015.

Professional fees include securities clearing, legal, audit and consulting costs and are generally driven by the size and complexity of our MBS portfolio, the volume of transactions we execute and the extent of research and due diligence activities we undertake on potential transactions. The increase in professional fees for the quarter ended March 31, 2016, was due to the \$1,525 of costs recognized in connection with the acquisition of JAVELIN.

Insurance includes premiums for both general business and directors and officers liability coverage.

Compensation includes both non-executive director compensation as well as the restricted stock awarded to our executive officers and other ACM employees through ACM. The decline in 2016 is primarily the result of lower stock based compensation due to a decline in our stock price and award vesting to our executive officers and other ACM employees. No new awards have been granted since 2013.

Other expenses include fees for market and pricing data, analytics and risk management systems and portfolio related data processing costs as well as stock exchange listing fees and similar shareholder related expenses.

Taxable Income

As a REIT we are generally not subject to taxation. See Note 14 to the condensed consolidated financial statements.

Other Comprehensive Income (Loss)

Comprehensive income (loss) includes all changes in equity during a period, except those resulting from investments by owners and distributions to owners. For the quarters ended March 31, 2016 and March 31, 2015, other comprehensive income (loss) totaled \$190,021, and \$83,187, respectively, reflecting net unrealized gains or losses on available for sale Agency Securities net of amounts reclassified upon sale.

Financial Condition

Agency Securities and TBA Agency Securities

Security purchase and sale transactions, including purchases and sales for forward settlement, are recorded on the trade date to the extent it is probable that we will take or make timely physical delivery of the related securities. Gains or losses realized from the sale of securities are included in income and are determined using the specific identification method. We typically purchase Agency Securities at premium prices. The premium price paid over par value on those assets is expensed as the underlying mortgages experience repayment or prepayment. The lower the constant prepayment rate, the lower the amount of amortization expense for a particular period. Accordingly, the yield on an asset and earnings, are higher. If prepayment rates increase, the amount of amortization expense for a particular period will go up. These increased prepayment rates would act to decrease the yield on an asset and would decrease earnings.

We account for TBA Agency Securities as derivative instruments if it is reasonably possible that we will not take or make physical delivery of the Agency Security upon settlement of the contract. TBA Agency Securities are forward contracts for the purchase ("long position") or sale ("short position") of Agency Securities at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date. The specific Agency Securities 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. We estimate the fair value of TBA Agency Securities based on similar methods used to value our Agency Securities. TBA Agency Securities are included in the table below on a gross basis as they can be used to establish and finance portfolio positions in Agency Securities. We did not have any TBA Agency Securities outstanding at March 31, 2016 and December 31, 2015.

The tables below summarize certain characteristics of our Agency Securities at March 31, 2016 and December 31, 2015.

March 31, 2016

<u>Asset Type</u>	<u>Principal Amount</u>	<u>Fair Value</u>	<u>Weighted Average Coupon</u>	<u>CPR (1)</u>	<u>Weighted Average Month to Reset or Maturity</u>	<u>% of Total Agency Securities</u>
ARMs & Hybrids	\$ 93,632	\$ 97,577	2.50%	11.29%	14	0.95%
Multi-Family MBS	1,466,048	1,558,812	3.19%	0.00%	99	14.88
10 Year Fixed	241,797	256,533	3.79%	9.10%	123	2.45
15 Year Fixed	3,404,404	3,606,892	3.36%	8.13%	155	34.54
20 Year Fixed	3,484,706	3,708,836	3.67%	10.09%	198	35.36
25 Year Fixed	16,327	17,816	4.50%	10.45%	286	0.17
30 Year Fixed	1,148,547	1,227,544	3.87%	6.09%	346	11.65
Total or Weighted Average	\$ 9,855,461	\$ 10,474,010	3.51%	7.43%	182	100.00%

(1) Weighted average for all prepayments during the quarter ended March 31, 2016, including prepayments related to Agency Securities purchased during the quarter.

December 31, 2015

<u>Asset Type</u>	<u>Principal Amount</u>	<u>Fair Value</u>	<u>Weighted Average Coupon</u>	<u>CPR (1)</u>	<u>Weighted Average Month to Reset or Maturity</u>	<u>% of Total Agency Securities</u>
ARMs & Hybrids	\$ 114,000	\$ 119,013	2.53%	11.51%	12	0.95%
Multi-Family MBS	2,126,155	2,158,589	3.09%	0.00%	105	17.80
10 Year Fixed	124,035	130,546	3.88%	14.25%	116	1.04
15 Year Fixed	4,295,880	4,489,918	3.33%	8.92%	150	35.97
20 Year Fixed	3,900,738	4,103,449	3.64%	11.70%	193	32.66
25 Year Fixed	16,960	18,359	4.50%	14.15%	279	0.14
30 Year Fixed	1,366,748	1,441,682	3.86%	5.89%	347	11.44
Total or Weighted Average	\$ 11,944,516	\$ 12,461,556	3.45%	7.98%	178	100.00%

(1) Weighted average for all prepayments during the year ended December 31, 2015, including prepayments related to Agency Securities purchased or sold during the year.

Recognition of interest income commences on the settlement date of the purchase transaction and continues through the settlement date of the sale transaction. At March 31, 2016 and December 31, 2015, we did not have any investment related receivables or payables with respect to unsettled sales and purchases of our Agency Securities.

Our net interest income is primarily a function of the difference between the yield on our assets and the financing cost of owning those assets. Since we tend to purchase Agency Securities at a premium to par, the main item that can affect the yield on our Agency Securities after they are purchased is the rate at which the mortgage borrowers repay the loan. While the scheduled repayments, which are the principal portion of the homeowners' regular monthly payments, are fairly predictable, the unscheduled repayments, which are generally refinancing of the mortgage but can also result from repurchases of delinquent, defaulted, or modified loans, are less so. Being able to accurately estimate and manage these repayment rates is a critical portion of the management of our MBS portfolio, not only for estimating current yield but also for considering the rate of reinvestment of those proceeds into new securities, the yields which those new securities may add to our MBS portfolio and our hedging strategy.

At March 31, 2016 and December 31, 2015, the adjustable and hybrid adjustable rate mortgage loans underlying our Agency Securities have fixed-interest rates for an average period of approximately 14 months and 7 months, respectively, after which time the interest rates reset and become adjustable. After a reset date, interest rates on our adjustable and hybrid adjustable Agency Securities float based on spreads over various indices, typically LIBOR or the one-year constant maturity treasury rate.

These interest rates are subject to caps that limit the amount the applicable interest rate can increase during any year, known as an annual cap and through the maturity of the security, known as a lifetime cap.

Non-Agency Securities

During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. We purchase Non-Agency Securities at prices which incorporate our expectations for prepayment speeds, defaults, delinquencies and severities. These expectations determine the yields we receive on our assets. If actual prepayment speeds, defaults, delinquencies and severities are different from our expectations, our actual yields could be higher or lower.

The tables below summarize certain characteristics of our Non-Agency Securities at March 31, 2016.

March 31, 2016

<u>Asset Type</u>	<u>Principal Amount</u>	<u>Fair Value</u>	<u>Weighted Average Coupon</u>	<u>Weighted Average Month to Maturity</u>	<u>% of Total Non-Agency Securities</u>
Credit risk transfer	\$ 291,718	\$ 285,696	5.11%	123	100.00%
Total or Weighted Average	\$ 291,718	\$ 285,696			100.00%

During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. At March 31, 2016, investments in Non-Agency Securities accounted for 2.7% of our MBS portfolio.

Recognition of interest income commences on the settlement date of the purchase transaction and continues through the settlement date of the sale transaction. At March 31, 2016, we had investment related payables of \$14,955 with respect to unsettled purchases of Non-Agency Securities. At December 31, 2015, we did not have any investment related receivables or payables.

Repurchase Agreements

We have entered into repurchase agreements to finance most of our Agency Securities. Our repurchase agreements are secured by our Agency Securities and bear interest at rates that have historically moved in close relationship to the Federal Funds Rate and LIBOR. We have established borrowing relationships with numerous investment banking firms and other lenders, 26 of which had open repurchase agreements with us at March 31, 2016 and 26 of which had open repurchases agreements with us at December 31, 2015. We had outstanding balances under our repurchase agreements at March 31, 2016 and December 31, 2015 of \$9,923,859 and \$11,570,481, respectively, consistent with the decrease in our Agency Securities in our MBS portfolio.

Our repurchase agreements require excess collateral, known as a "hair cut." At March 31, 2016, the average haircut percentage was 5.21% compared to 4.79% at December 31, 2015. No counterparty held collateral in excess of 5% of our total stockholders' equity at March 31, 2016 or at December 31, 2015.

In January 2016, the Federal Housing Financing Authority issued a Final Rule revising its regulations governing FHLB bank membership. The Final Rule changes the definition of "insurance company" to exclude captives, thereby making them ineligible for membership. The Final Rule contains a transition provision to give captives admitted to membership on or after the date of the publication of the proposed rule, which includes SABRE, until February 2017 to terminate its membership in the FHLB Des Moines.

Under the Final Rule, SABRE is prohibited from taking new advances or renewing its existing \$100,000 advance, which matures in December 2016. JAVELIN's captive insurance company is subject to the same FHLB rules. See Recent Developments section above and *Note 17 -Subsequent Events* for more information about the relationship between ARMOUR and JAVELIN and the Tender Offer and Merger. The Final Rule does not directly affect ARMOUR's or JAVELIN's MRA agreements or related repurchase financing with another FHLB.

Derivative Instruments

We use various interest rate contracts to manage our interest rate risk as we deem prudent in light of market conditions and the associated costs with counterparties that have a high quality credit rating and with futures exchanges. We generally pay a fixed rate and receive a floating rate with the objective of fixing a portion of our borrowing costs and hedging the change in our book value to some degree. The floating rate we receive is generally the Federal Funds Rate or LIBOR. While our policies do not contain specific requirements as to the percentages or amount of interest rate risk that we are required to hedge, we maintain an overall target of hedging at least 40% of our non-adjustable rate mortgages. At March 31, 2016 and December 31, 2015, the notional value of our derivatives was 82.6% and 87.5%, respectively, of the fair market value of our non-adjustable rate mortgages. For interest rate risk mitigation purposes, we consider Agency Securities to be ARMs if their interest rate is either currently subject to adjustment according to prevailing rates or if they are within 18 months of the period where such adjustments will occur. No assurance can be given that our derivatives will have the desired beneficial impact on our results of operations or financial condition. We have not elected cash flow hedge accounting treatment as allowed by GAAP. Since we do not designate our derivative activities as cash flow hedges, realized as well as unrealized gains/losses from these transactions will impact our GAAP earnings.

Use of derivative instruments may fail to protect or could adversely affect us because, among other things:

- available derivatives may not correspond directly with the interest rate risk for which protection is sought (e.g., the difference in interest rate movements for long-term U.S. Treasury Securities compared to Agency Securities);
- the duration of the derivatives may not match the duration of the related liability;
- the counterparty to a derivative agreement with us may default on its obligation to pay or not perform under the terms of the agreement and the collateral posted may not be sufficient to protect against any consequent loss;
- we may lose collateral we have pledged to secure our obligations under a derivative agreement if the associated counterparty becomes insolvent or files for bankruptcy;
- we may experience a termination event under one or more of our derivative agreements related to our REIT status, equity levels and performance, which could result in a payout to the associated counterparty and a taxable loss to us;
- the credit-quality of the party owing money on the derivatives may be downgraded to such an extent that it impairs our ability to sell or assign our side of the hedging transaction; and
- the value of derivatives may be adjusted from time to time in accordance with GAAP to reflect changes in fair value; downward adjustments, or “mark-to-market losses,” would reduce our net income or increase any net loss.

At March 31, 2016 and December 31, 2015, we had derivatives with a net fair value of \$(297,020) and (232,302), respectively. At March 31, 2016 and December 31, 2015, we had interest rate swap contracts with an aggregate notional balance of \$6,575,000 and \$8,800,000, respectively. At December 31, 2015, all of our Futures Contracts had expired. Futures Contracts are traded on the CME. Counterparty risk of interest rate swap contracts, interest rate swaptions and Futures Contracts are limited to some degree because of daily mark-to-market and collateral requirements. In addition, substantial credit support for the Futures Contracts is provided by the CME. These derivative transactions are designed to lock in a portion of funding costs for financing activities associated with our assets in such a way as to help assure the realization of attractive net interest margins and to vary inversely in value with our Agency Securities. Such contracts are based on assumptions about prepayments which, if not realized, will cause results to differ from expectations. Our basis swap contracts aggregate notional balance was \$2,000,000 at March 31, 2016, remaining unchanged from December 31, 2015.

Although we attempt to structure our derivatives to offset the changes in asset prices, the complexity of the actual and expected pre-payment characteristics of the underlying mortgages as well as the volatility in mortgage interest rates relative to U.S. Treasury and interest rate swap contract rates makes achieving high levels of off-set difficult. We recognized net losses of \$(335,163) and \$(208,239), respectively, for the quarters ended March 31, 2016 and March 31, 2015, respectively, related to our derivatives. For the quarters ended March 31, 2016 and March 31, 2015, the net unrealized gain of our Agency Securities increased by \$191,912 and \$89,731, respectively. The net unrealized gain on Agency Securities is due to market price fluctuations.

As required by the Dodd-Frank Act, the Commodity Futures Trading Commission has adopted rules requiring certain interest rate swap contracts to be cleared through a derivatives clearing organization. We are required to clear certain new interest rate swap contracts. Cleared interest rate swaps may have higher margin requirements than un-cleared interest rate swaps we previously had. We have established an account with a futures commission merchant for this purpose. To date, we have not entered into any cleared interest rate swap contracts.

We are required to account for our TBA Agency Securities as derivatives when it is reasonably possible that we will not take or make timely physical delivery of the related securities. However, from time to time, we use TBA Agency Securities primarily

to effectively establish and finance portfolio positions. See the section, Financial Condition-Agency Securities and TBA Agency Securities above.

Contractual Obligations and Commitments

We had the following contractual obligations at March 31, 2016:

Obligations	Payments Due By Period				
	Total	Less Than 1 Year	2-3 Years	4-5 Years	Greater Than 5 Years
Repurchase agreements	\$ 9,923,859	\$ 9,923,859	\$ —	\$ —	\$ —
Interest expense on repurchase agreements	10,814	10,814	—	—	—
Related Party Fees (1)	182,143	26,020	52,041	52,041	52,041
Board of Directors fees (2)	7,553	1,079	2,158	2,158	2,158
Total	\$ 10,124,369	\$ 9,961,772	\$ 54,199	\$ 54,199	\$ 54,199

(1) Represents fees to be paid to ACM under the terms of the Management Agreement (Refer to Note 10 and Note 15 to the condensed consolidated financial statements).

(2) Represents fees to be paid to the Board.

We had contractual commitments under derivatives at March 31, 2016. We had interest rate swap contracts with an aggregate notional balance of \$6,575,000, a weighted average swap rate of 1.73% and a weighted average term of 63 months at March 31, 2016. Our total Basis swaps notional amount at March 31, 2016 was \$2,000,000, with a weighted average swap rate of 0.22% and weighted average term of 19 months.

Liquidity and Capital Resources

Cash provided by (used in) operating activities was \$(208,706) and \$73,098, respectively, for the quarters ended March 31, 2016 and March 31, 2015. The decline in cash related to operating activities is primarily related to the overall decline in the size of our MBS portfolio, which caused a decrease in interest income. The losses on our derivatives was also a factor. Our average MBS portfolio was \$11,455,691 and \$14,634,391, respectively, for the quarters ended March 31, 2016 and March 31, 2015, respectively.

At March 31, 2016, we financed our MBS portfolio with \$9,923,859 of borrowings under repurchase agreements. Our leverage ratio at March 31, 2016, was 9.06 to 1. At March 31, 2016, our liquidity totaled \$509,387, consisting of \$243,294 of cash plus \$266,093 of unpledged Agency Securities (including securities received as collateral). Our primary sources of funds are borrowings under repurchase arrangements, monthly principal and interest payments on our Agency Securities and cash generated from our operating results. Other sources of funds may include proceeds from equity and debt offerings and asset sales. We generally maintain liquidity to pay down borrowings under repurchase arrangements to reduce borrowing costs and otherwise efficiently manage our long-term investment capital. Because the level of our borrowings can be adjusted on a daily basis, the level of cash carried on our condensed consolidated balance sheet is significantly less important than our potential liquidity available under our borrowing arrangements.

In addition to the repurchase agreement financing discussed above, from time to time we have entered into reverse repurchase agreements with certain of our repurchase agreement counterparties. Under a typical reverse repurchase agreement, we purchase U.S. Treasury Securities from a borrower in exchange for cash and agree to sell the same securities back in the future. We then sell such U.S. Treasury Securities to third parties and recognize a liability to return the securities to the original borrower. Reverse repurchase agreement receivables and repurchase agreement liabilities are presented net when they meet certain criteria, including being with the same counterparty, being governed by the same MRA, settlement through the same brokerage or clearing account and maturing on the same day. The practical effect of these transactions is to replace a portion of our repurchase agreement financing of our Agency Securities in our MBS portfolio with short positions in U.S. Treasury Securities. We believe that this helps to reduce interest rate risk, and therefore counterparty credit and liquidity risk. We did not have any reverse repurchase agreements outstanding at March 31, 2016 and December 31, 2015.

Both parties to the repurchase and reverse repurchase transactions have the right to make daily margin calls based on changes in the value of the collateral obtained and/or pledged.

We currently believe that we have sufficient liquidity and capital resources available for the acquisition of additional investments, repayments on repurchase borrowings, reacquisition of securities to be returned to borrowers and the payment of cash dividends as required for continued qualification as a REIT.

Our primary uses of cash are to purchase Agency Securities, pay interest and principal on our borrowings, fund our operations and pay dividends. From time to time, we purchase or sell assets for forward settlement up to 90 days in the future to lock in purchase prices or sales proceeds.

During the quarter ended March 31, 2016, we purchased \$281,755 of Non-Agency Securities using proceeds from repurchase agreements and principal repayments. During the quarter ended March 31, 2016, we received cash of \$368,885 from prepayments and scheduled principal payments on our Agency Securities. We had a net cash increase from our repurchase agreements of \$1,646,622 for the quarter ended March 31, 2016 and made cash interest payments of approximately \$67,668 on our liabilities for the quarter ended March 31, 2016. Part of funding our operations includes providing margin cash to offset liability balances on our derivatives. We recovered \$42,305 of cash collateral posted to counterparties at March 31, 2016.

During the quarter ended March 31, 2015, we purchased \$1,982,478 of Agency Securities using proceeds from repurchase agreements and principal repayments. During the quarter ended March 31, 2015, we received cash of \$481,387 from prepayments and scheduled principal payments on our Agency Securities. We received net proceeds of \$43 from common equity issuances under our common stock DRIP and we repurchased 875 shares of our outstanding common stock under our Repurchase Program for an aggregate cost of \$2,804. We had a net cash increase from our repurchase agreements of \$22,849 for the quarter ended March 31, 2015 and made cash interest payments of approximately \$93,160 on our liabilities. Part of funding our operations includes providing margin cash to offset liability balances on our derivatives. We recovered \$183,443 of cash collateral posted to counterparties and decreased our liability by \$9,900 for cash collateral posted by counterparties at March 31, 2015.

We have continued to pursue additional lending counterparties in order to help increase our financial flexibility and ability to withstand periods of contracting liquidity in the credit markets.

Repurchase Agreements

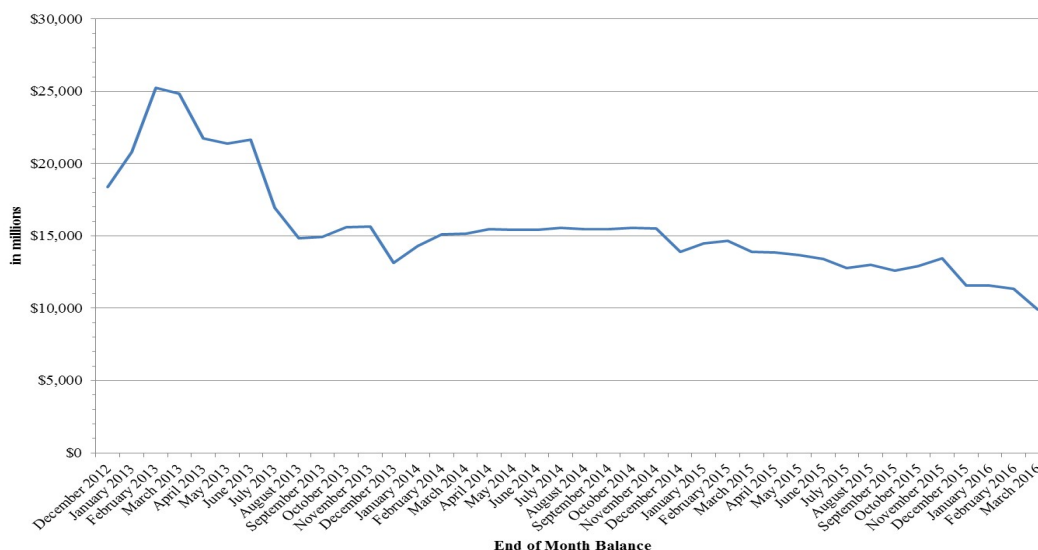
Declines in the value of our Agency MBS portfolio can trigger margin calls by our lenders under our repurchase agreements. An event of default or termination event under the standard MRA would give our counterparty the option to terminate all repurchase transactions existing with us and require any amount due to be payable immediately.

Changing capital or other financial market regulatory requirements may cause our lenders to exit the repurchase market, increase financing rates, tighten lending standards or increase the amount of required equity capital or haircut we post, any of which could make it more difficult or costly for us to obtain financing.

Financial sector volatility can also lead to increased demand and prices for high quality debt securities, including Agency Securities. While increased prices may increase the value of our Agency Securities, higher values may also reduce the return on reinvestment of capital, thereby lowering our future profitability.

The following graph represents the month-end outstanding balances of our repurchase agreements (before the effect of netting reverse repurchase agreements), which finance most of our Agency Securities. Our repurchase agreements balance will fluctuate based on our change in capital, leverage targets and the market prices of our assets. The balance of repurchase agreements outstanding will fluctuate within any given month based on changes in the market value of the particular Agency Security pledged as collateral (including the effects of principal paydowns) and the level and timing of investment and reinvestment activity.

Repurchase Agreements



See Note 8 to the condensed consolidated financial statements for more information.

Effects of Margin Requirements, Leverage and Credit Spreads

Our MBS have values that fluctuate according to market conditions and, as discussed above, the market value of our MBS will decrease as prevailing interest rates or credit spreads increase. When the value of the securities pledged to secure a repurchase agreement decreases to the point where the positive difference between the collateral value and the loan amount is less than the haircut, our lenders may issue a margin call, which means that the lender will require us to pay the margin call in cash or pledge additional collateral to meet that margin call. Under our repurchase facilities, our lenders have full discretion to determine the value of the MBS we pledge to them. Most of our lenders will value securities based on recent trades in the market. Lenders also issue margin calls as the published current principal balance factors change on the pool of mortgages underlying the securities pledged as collateral when scheduled and unscheduled principal repayments are announced monthly.

We experience margin calls in the ordinary course of our business and under certain conditions, such as during a period of declining market value for MBS and we may experience margin calls as frequently as daily. In seeking to effectively manage the margin requirements established by our lenders, we maintain a position of cash and unpledged securities. We refer to this position as our liquidity. The level of liquidity we have available to meet margin calls is directly affected by our leverage levels, our haircuts and the price changes on our securities. If interest rates increase as a result of a yield curve shift or for another reason or if credit spreads widen, the prices of our collateral (and our unpledged assets that constitute our liquidity) will decline and we may experience margin calls. We will use our liquidity to meet such margin calls. There can be no assurance that we will maintain sufficient levels of liquidity to meet any margin calls. If our haircuts increase, our liquidity will proportionately decrease. If we increase our borrowings, our liquidity will decrease by the amount of additional haircut on the increased level of indebtedness. In addition, certain of our MRAs contain a restriction that prohibits our leverage from exceeding twelve times our stockholders' equity as well as termination events in the case of significant reductions in equity capital.

We intend to maintain a level of liquidity in relation to our assets that enables us to meet reasonably anticipated margin calls but that also allows us to be substantially invested in MBS. We may misjudge the appropriate amount of our liquidity by maintaining excessive liquidity, which would lower our investment returns, or by maintaining insufficient liquidity, which would force us to involuntarily liquidate assets into unfavorable market conditions and harm our results of operations and financial condition.

We generally seek to borrow (on a recourse basis) between six and ten times the amount of our total stockholders' equity. At March 31, 2016 and December 31, 2015, our total borrowings were \$9,923,859 and \$11,570,481 (excluding accrued interest), respectively. At March 31, 2016 and December 31, 2015, we had a leverage ratio of approximately 9.06:1 and 9.44:1, respectively.

Forward-Looking Statements Regarding Liquidity

Based on our current portfolio, leverage rate and available borrowing arrangements, we believe that our cash flow from operations and our ability to make timely portfolio adjustments, will be sufficient to enable us to meet anticipated short-term (one year or less) liquidity requirements such as to fund our investment activities, meet our financing obligations, pay fees under the Management Agreement and fund our distributions to stockholders and pay general corporate expenses.

We may increase our capital resources by obtaining long-term credit facilities or making public or private offerings of equity or debt securities, including classes of preferred stock, common stock and senior or subordinated notes to meet our long-term (greater than one year) liquidity. Such financing will depend on market conditions for capital raises and for the investment of any proceeds and there can be no assurances that we will successfully obtain any such financing.

Stockholders' Equity

See Note 12 to the condensed consolidated financial statements.

Off-Balance Sheet Arrangements

At March 31, 2016 and December 31, 2015, we had not maintained any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance, or special purpose or variable interest entities, established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Furthermore, at March 31, 2016 and December 31, 2015, we had not guaranteed any obligations of any unconsolidated entities or entered into any commitment or intent to provide funding to any such entities.

Critical Accounting Policies

See Note 3 to the condensed consolidated financial statements for our significant accounting policies.

Valuation of MBS and Derivatives

We carry our MBS and derivatives at fair value. Our Agency Securities are classified as available for sale, and therefore unrealized changes in fair value are reflected directly in total stockholders' equity as accumulated other comprehensive income or loss. Our Non-Agency Securities are classified as trading securities, and therefore changes in fair value are reported in the condensed consolidated statements of operations as income or loss. We do not use hedge accounting for our derivatives for financial reporting purposes and therefore changes in fair value are reflected in net income as other gain or loss. To the extent that fair value changes on derivatives offset fair value changes in our MBS, the fluctuation in our stockholders' equity will be lower. For example, rising interest rates may tend to result in an overall increase in our reported net income even while our total stockholders' equity declines.

Fair value for the Agency Securities in our MBS portfolio is based on obtaining a valuation for each Agency Security from third party pricing services and/or dealer quotes. The third party pricing services use common market pricing methods that may include pricing models that may incorporate such factors as coupons, prepayment speeds, spread to the Treasury curves and interest rate swap curves, duration, periodic and life caps and credit enhancement. If the fair value of an Agency Security is not available from the third party pricing services or such data appears unreliable, we obtain pricing indications from up to three dealers who make markets in similar Agency Securities. Management reviews pricing used to ensure that current market conditions are properly reflected. This review includes, but is not limited to, comparisons of similar market transactions or alternative third party pricing services, dealer pricing indications and comparisons to a third party pricing model.

The fair values of our derivatives are valued using information provided by third party pricing services that incorporate common market pricing methods that may include current interest rate curves, forward interest rate curves and market spreads to interest rate curves. Management compares pricing information received to dealer quotes to ensure that the current market conditions are properly reflected.

Fair value for the Non-Agency Securities in our MBS portfolio is based on estimates prepared by our Portfolio Management

group, which organizationally reports to our Chief Investment Officer. In preparing the estimates, our Portfolio Management group uses commercially available and proprietary models and data as well as market intelligence gained from discussions with, and transactions by, other market participants. We estimate the fair value of our Non-Agency Securities by estimating the future cash flows for each Non-Agency Security and then discounting those cash flows based on our estimates of current market yield for each individual security. Our estimates for future cash flows and current market yields incorporate such factors as collateral type, bond structure and priority of payments, coupons, prepayment speeds, defaults, delinquencies and severities. Quarterly, we compare our estimates of fair value of our Non-Agency Securities with pricing from third party pricing services, dealer marks received and recent purchase and financing transaction history to validate our assumptions of cash flow and market yield and calibrate our models.

Realized Gains and Losses on Agency Securities

Security purchase and sale transactions, including purchases and sales for forward settlement, are recorded on the trade date to the extent it is probable that we will take or make timely physical delivery of the related securities. Gains or losses realized from the sale of securities are included in income and are determined using the specific identification method. We realize gains and losses on our Agency Securities upon their sale. At that time, previously unrealized amounts included in accumulated other comprehensive income are reclassified and reported in net income as other gain or loss. To the extent that we sell Agency Securities in later periods after changes in the fair value of those Agency Securities have occurred, we may report significant net income or net loss without a corresponding change in our total stockholders' equity.

Declines in the fair values of our Agency Securities that represent other than temporary impairments are also treated as realized losses and reported in net income as other loss. We evaluate Agency Securities for other than temporary impairment at least on a quarterly basis and more frequently when economic or market concerns warrant such evaluation. We consider an impairment to be other than temporary if we (1) have the intent to sell the Agency Securities, (2) believe it is more likely than not that we will be required to sell the securities before recovery (for example, because of liquidity requirements or contractual obligations), or (3) a credit loss exists. Impairment losses recognized establish a new cost basis for the related Agency Securities. Gains or losses on subsequent sales are determined by reference to such new cost basis.

Gains and Losses on Non-Agency Securities

We carry our Non-Agency Securities at fair value and reflect changes in those fair values in net income as other gains and losses.

Inflation

Virtually all of our assets and liabilities are interest rate-sensitive in nature. As a result, interest rates and other factors influence our performance far more than inflation. Changes in interest rates do not necessarily correlate with inflation rates or changes in inflation rates. Our financial statements are prepared in accordance with GAAP and any distributions we may make will be determined by our Board based in part on our REIT taxable income as calculated according to the requirements of the Code; in each case, our activities and balance sheet are measured with reference to fair value without considering inflation.

Subsequent Events

See Note 17 to the condensed consolidated financial statements.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains various "forward-looking statements." Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. In some cases, you can identify forward-looking statements by the use of forward-looking terminology such as "believes," "expects," "may," "will," "would," "could," "should," "seeks," "approximately," "intends," "plans," "projects," "estimates" or "anticipates" or the negative of these words and phrases or similar words or phrases. All forward-looking statements may be impacted by a number of risks and uncertainties, including statements regarding the following subjects:

- our business and investment strategy;
- our anticipated results of operations;
- statements about future dividends;
- our ability to obtain financing arrangements;
- our understanding of our competition and ability to compete effectively;

- market, industry and economic trends; and
- interest rates.

The forward-looking statements in this report are based on our beliefs, assumptions and expectations of our future performance, taking into account all information currently available to us. These beliefs, assumptions and expectations are subject to risks and uncertainties and can change as a result of many possible events or factors, not all of which are known to us. If a change occurs, our business, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. You should carefully consider these risks before you make an investment decision with respect to our stock, along with the following factors that could cause actual results to vary from our forward-looking statements:

- the impact of the federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the federal government and the Fed system;
- the possible material adverse effect on our business if the U.S. Congress passed legislation reforming or winding down Fannie Mae or Freddie Mac;
- mortgage loan modification programs and future legislative action;
- actions by the Fed which could cause a flattening of the yield curve, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders;
- the impact of the delay or failure of the U.S. Government in reaching an agreement on the national debt ceiling;
- availability, terms and deployment of capital;
- changes in economic conditions generally;
- changes in interest rates, interest rate spreads and the yield curve or prepayment rates;
- general volatility of the financial markets, including markets for mortgage securities;
- the downgrade of the U.S. Government's or certain European countries' credit ratings and future downgrades of the U.S. Government's or certain European countries' credit ratings may materially adversely affect our business, financial condition and results of operations.;
- inflation or deflation;
- availability of suitable investment opportunities;
- the degree and nature of our competition, including competition for MBS;
- changes in our business and investment strategy;
- our failure to maintain an exemption from being regulated as a commodity pool operator;
- our dependence on ACM and ability to find a suitable replacement if ACM was to terminate its management relationship with us;
- the existence of conflicts of interest in our relationship with ACM, certain of our directors and our officers, which could result in decisions that are not in the best interest of our stockholders;
- our management's competing duties to other affiliated entities, which could result in decisions that are not in the best interest of our stockholders.
- changes in personnel at ACM or the availability of qualified personnel at ACM;
- limitations imposed on our business by our status as a REIT under the Code;
- the potential burdens on our business of maintaining our exclusion from the 19440 Act and possible consequences of losing that exemption;
- changes in GAAP, including interpretations thereof; and
- changes in applicable laws and regulations.

We cannot guarantee future results, levels of activity, performance or achievements. You should not place undue reliance on forward-looking statements, which apply only as of the date of this report. We do not intend and disclaim any duty or obligation to update or revise any industry information or forward-looking statements set forth in this report to reflect new information, future events or otherwise, except as required under the U.S. Federal securities laws.

GLOSSARY OF TERMS

“Agency Securities” means securities issued or guaranteed by Fannie Mae, Freddie Mac and Ginnie Mae; interests in or obligations backed by pools of fixed rate, hybrid adjustable rate and adjustable rate mortgage loans.

“ARMs” means Adjustable Rate Mortgage backed securities.

“AVM” means AVM L.P, a securities broker dealer, which we contract with for administering clearing and settlement services for our securities and derivative transactions, as well as assistance with financing transaction services such as repurchase financing.

“Basis swap contracts” means derivative contracts that allow us to exchange one floating interest rate basis for another, for example, 3 month LIBOR and Fed Funds Rates, thereby allowing us to diversify our floating rate basis exposures.

“Board” means ARMOUR’s Board of Directors.

“CFO” means Chief Financial Officer, James Mountain.

“CFTC” means the U.S. Commodity Futures Trading Commission.

“Co-CEOs” means our Co-Chief Executive Officers, Jeffrey Zimmer and Scott Ulm.

“Common Stock DRIP” means the Company's dividend reinvestment and stock purchase plan.

“CPOs” means commodity pool operators.

“CMBS” means commercial mortgage backed securities.

“CME” means the Chicago Mercantile Exchange.

“CMOs” means collateralized mortgage obligations.

“Code” means the Internal Revenue Code of 1986.

“CPR” means constant prepayment rate.

“Dodd-Frank Act” means the Dodd-Frank Wall Street Reform and Consumer Protection Act.

“ERISA” means Employee Retirement Income Security Act.

“Exchange Act” means the Securities Exchange Act of 1934.

“Fannie Mae” means the Federal National Mortgage Association.

“Fed” means the U.S. Federal Reserve.

“FHFA” means the Federal Housing Finance Agency.

“FHLB” means Federal Home Loan Bank.

“Freddie Mac” means the Federal Home Loan Mortgage Corporation.

“Futures Contracts” means Eurodollar Futures Contracts.

“GAAP” means accounting principles generally accepted in the United States of America.

“GDP” means gross domestic product.

“Ginnie Mae” means the Government National Mortgage Administration.

“GSE” means U.S. Government Sponsored Entity. Obligations of agencies originally established or chartered by the U.S. government to serve public purposes as specified by the U.S. Congress; these obligations are not explicitly guaranteed as to the timely payment of principal and interest by the full faith and credit of the U.S. government.

“Haircut” means the weighted average margin requirement, or the percentage amount by which the collateral value must exceed the loan amount. Among other things, it is a measure of our unsecured credit risk to our lenders.

“Hybrid” means a mortgage that has a fixed rate for an initial term after which the rate becomes adjustable according to a specific schedule.

GLOSSARY OF TERMS

“IRS” means Internal Revenue Service.

“JAVELIN” means JAVELIN Mortgage Investment Corp., formerly a publicly-traded REIT. Upon consummation of the Merger on April 6, 2016, JAVELIN became a wholly-owned, qualified REIT subsidiary of ARMOUR and continues to be managed by ACM pursuant to the pre-existing management agreement between JAVELIN and ACM.

“LIBOR” means the London Interbank Offered Rate.

“Management Agreement” means the management agreement between ARMOUR and ACM whereby ACM performs certain services for ARR in exchange for a specified fee.

“MBS” means mortgage backed securities, a security representing a direct interest in a pool of mortgage loans. The pass-through issuer or servicer collects the payments on the loans in the pool and “passes through” the principal and interest to the security holders on a pro rata basis.

“MGCL” means Maryland General Corporation Law.

“MRA” means master repurchase agreement. A document that outlines standard terms between the Company and counterparties for repurchase agreement transactions.

“Multi-Family MBS” means MBS issued under Fannie Mae's Delegated Underwriting System (DUS) program.

“NFA” means National Futures Association.

“Non-Agency Securities” means securities backed by residential mortgages in which we may invest, for which the payment of principal and interest is not guaranteed by a GSE or government agency.

“NYSE” means New York Stock Exchange.

“REIT” means Real Estate Investment Trust. A special purpose investment vehicle that provides investors with the ability to participate directly in the ownership or financing of real-estate related assets by pooling their capital to purchase and manage mortgage loans and/or income property.

“Repurchase Program” means the Company's common stock repurchase program authorized by our Board.

“Reverse Stock Split” means the one-for-eight reverse stock split, which was effective July 31, 2015.

“RMBS” means residential mortgage backed securities.

“SABRE” means SABRE Business Insurance LLC, a wholly owned subsidiary of ARMOUR and a captive insurance company.

“Sarbanes-Oxley Act” means a U.S. federal law that set new or enhanced standards for all U.S. public company boards, management and public accounting firms. Section 302 requires senior management to certify the accuracy of the financial statements. Section 404 requires that management and auditors establish internal controls and reporting methods on the adequacy of those controls.

“SEC” means the Securities and Exchange Commission.

“S&P 500” means Standard and Poor's 500 Stock Index

“TBA Agency Securities” means forward contracts for the purchase (“long position”) or sale (“short position”) of Agency Securities at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date.

“TRS” means taxable REIT subsidiary.

“U.S.” means United States.

“1940 Act” means the Investment Company Act of 1940.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We seek to manage our risks related to the credit-quality of our assets, interest rates, liquidity, prepayment speeds and market value while, at the same time, seeking to provide an opportunity to stockholders to realize attractive risk adjusted returns through ownership of our capital stock. While we do not seek to avoid risk completely, we believe the risk can be quantified from historical experience and seek to actively manage that risk, to earn sufficient compensation to justify taking those risks and to maintain capital levels consistent with the risks we undertake.

Interest Rate, Cap and Mismatch Risk

A portion of our MBS portfolio consists of hybrid adjustable rate and adjustable rate MBS. Hybrid mortgages are ARMs that have a fixed-interest rate for an initial period of time (typically three years or greater) and then convert to an adjustable rate for the remaining loan term. Our debt obligations are generally repurchase agreements of limited duration that are periodically refinanced at current market rates.

ARMs are typically subject to periodic and lifetime interest rate caps that limit the amount the interest rate can change during any given period. ARMs are also typically subject to a minimum interest rate payable. Our borrowings are not subject to similar restrictions. Hence, in a period of increasing interest rates, interest rates on our borrowings could increase without limitation, while the interest rates on our mortgage related assets could be limited. This exposure would be magnified to the extent we acquire fixed rate MBS or ARMs that are not fully indexed. Furthermore, some ARMs may be subject to periodic payment caps that result in some portion of the interest being deferred and added to the principal outstanding. These factors could lower our net interest income or cause a net loss during periods of rising interest rates, which would negatively impact our liquidity, net income and our ability to make distributions to stockholders.

We fund the purchase of a substantial portion of our ARMs with borrowings that have interest rates based on indices and repricing terms similar to, but of shorter maturities than, the interest rate indices and repricing terms of our mortgage assets. Thus, we anticipate that in most cases the interest rate indices and repricing terms of our mortgage assets and our funding sources will not be identical, thereby creating an interest rate mismatch between assets and liabilities. During periods of changing interest rates, such interest rate mismatches could negatively impact our net interest income, dividend yield and the market price of our stock. Most of our adjustable rate assets are based on the one-year constant maturity treasury rate and the one-year LIBOR rate and our debt obligations are generally based on LIBOR. These indices generally move in the same direction, but there can be no assurance that this will continue to occur.

Our ARMs and borrowings reset at various different dates for the specific asset or obligation. In general, the repricing of our debt obligations occurs more quickly than on our assets. Therefore, on average, our cost of funds may rise or fall more quickly than our earnings rate on our assets.

Furthermore, our net income may vary somewhat as the spread between one-month interest rates, the typical term for our repurchase agreements and six-month and twelve-month interest rates, the typical reset term of ARMs, varies.

Prepayment Risk

As we receive repayments of principal on our Agency Securities from prepayments and scheduled payments, premiums paid on such securities are amortized against interest income and discounts are accreted to interest income as realized. Premiums arise when we acquire Agency Securities at prices in excess of the principal balance of the mortgage loans underlying such Agency Securities. Conversely, discounts arise when we acquire Agency Securities at prices below the principal balance of the mortgage loans underlying such Agency Securities. Volatility in actual prepayment speeds will create volatility in the amount of premium amortization we recognize. Higher speeds will reduce our interest income and lower speeds will increase our interest income. At March 31, 2016 and December 31, 2015, substantially all of our Agency Securities were purchased at a premium to par. During the quarter ended March 31, 2016, we began to invest in Non-Agency Securities. At March 31, 2016, all of our Non-Agency Securities were purchased at or below par.

Credit Risk for Non-Agency Securities

We purchase Non-Agency Securities at prices which incorporate our expectations for prepayment speeds, defaults, delinquencies and severities. These expectations determine the yields we receive on our assets. If actual prepayment speeds, defaults, delinquencies and severities are different from our expectations, our actual yields could be higher or lower.

Interest Rate Risk and Effect on Market Value Risk

Another component of interest rate risk is the effect changes in interest rates will have on the market value of our MBS. We face the risk that the market value of our MBS will increase or decrease at different rates than that of our liabilities, including our derivative instruments and obligations to return securities received as collateral.

We primarily assess our interest rate risk by estimating the effective duration of our assets and the effective duration of our liabilities and by estimating the time difference between the interest rate adjustment of our assets and the interest rate adjustment of our liabilities. Effective duration essentially measures the market price volatility of financial instruments as interest rates change. We generally estimate effective duration using various financial models and empirical data. Different models and methodologies can produce different effective duration estimates for the same securities.

The sensitivity analysis tables presented below reflect the estimated impact of an instantaneous parallel shift in the yield curve, up and down 50 and 100 basis points, on the market value of our interest rate-sensitive investments and net interest income, at March 31, 2016 and December 31, 2015. It assumes that the spread between the interest rates on Agency Securities and long term U.S. Treasury Securities remains constant. Actual interest rate movements over time will likely be different, and such differences may be material. When evaluating the impact of changes in interest rates, prepayment assumptions and principal reinvestment rates are adjusted based on ACM's expectations. The analysis presented utilized assumptions, models and estimates of ACM based on ACM's judgment and experience.

March 31, 2016

Change in Interest Rates	Percentage Change in Projected Net Interest Income	Percentage Change in Projected Portfolio Value Including Derivatives
1.00%	(14.56)%	(0.49)%
0.50%	(7.10)%	(0.02)%
(0.50)%	16.37%	0.34%
(1.00)%	23.95%	0.05%

December 31, 2015

Change in Interest Rates	Percentage Change in Projected Net Interest Income	Percentage Change in Projected Portfolio Value Including Derivatives
1.00%	(16.79)%	(0.08)%
0.50%	(8.22)%	0.16%
(0.50)%	15.27%	0.27%
(1.00)%	16.46%	(0.03)%

While the tables above reflect the estimated immediate impact of interest rate increases and decreases on a static MBS portfolio, we rebalance our MBS portfolio from time to time either to seek to take advantage of or reduce the impact of changes in interest rates. It is important to note that the impact of changing interest rates on market value and net interest income can change significantly when interest rates change beyond 100 basis points from current levels. Therefore, the volatility in the market value of our assets could increase significantly when interest rates change beyond amounts shown in the tables above. In addition, other factors impact the market value of and net interest income from our interest rate-sensitive investments and derivative instruments, such as the shape of the yield curve, market expectations as to future interest rate changes and other market conditions. Accordingly, interest income would likely differ from that shown above and such difference might be material and adverse to our stockholders.

The above tables quantify the potential changes in net interest income and MBS portfolio value, which includes the value of our derivatives, should interest rates immediately change. Given the low level of interest rates at March 31, 2016 and December 31, 2015, we applied a floor of 0% for all anticipated interest rates included in our assumptions. Due to the presence of this floor, it is anticipated that any hypothetical interest rate decrease would have a limited positive impact on our funding costs beyond a certain level; however, because prepayments speeds are unaffected by this floor, it is expected that any increase in our prepayment speeds (occurring as a result of any interest rate decrease or otherwise) could result in an acceleration of our premium amortization and the reinvestment of such prepaid principal in lower yielding assets. As a result, the presence of this floor limits

the positive impact of any interest rate decrease on our funding costs. Therefore, at some point, hypothetical interest rate decreases could cause the fair value of our financial instruments and our net interest income to decline.

Market Value Risk

All of our Agency Securities are classified as available for sale securities. As such, they are reflected at fair value with the periodic adjustment to fair value (that is not considered to be an other than temporary impairment) reported as part of the separate consolidated statement of comprehensive income (loss).

All of our Non-Agency Securities are classified as trading securities. As such, they are reflected at fair value with the periodic adjustment to fair value reflected as part of "Other Income (Loss)" reported as part of the condensed consolidated statements of operations.

The market value of our MBS can fluctuate due to changes in interest rates and other factors. Weakness in the mortgage market may adversely affect the performance and market value of our investments. This could negatively impact our book value. Furthermore, if our lenders are unwilling or unable to provide additional financing, we could be forced to sell our MBS at an inopportune time when prices are depressed. The principal and interest payments on our Agency Securities may be guaranteed by Fannie Mae, Freddie Mac, or Ginnie Mae.

Credit Risk

We have limited our exposure to credit losses on our MBS portfolio of Agency Securities. The payment of principal and interest on the Freddie Mac and Fannie Mae Agency Securities are guaranteed by those respective agencies and the payment of principal and interest on the Agency Securities guaranteed by Ginnie Mae are backed by the full faith and credit of the U.S. Government.

Fannie Mae and Freddie Mac remain in conservatorship of the U.S. Government. There can be no assurances as to how or when the U.S. Government will end these conservatorships or how the future profitability of Fannie Mae and Freddie Mac and any future credit rating actions may impact the credit risk associated with Agency Securities and, therefore, the value of the Agency Securities in our MBS portfolio.

We purchase Non-Agency Securities at prices which incorporate our expectations for prepayment speeds, defaults, delinquencies and severities. These expectations determine the yields we receive on our assets. If actual prepayment speeds, defaults, delinquencies and severities are different from our expectations, our actual yields could be higher or lower.

Liquidity Risk

Our primary liquidity risk arises from financing long-maturity MBS with short-term debt. The interest rates on our borrowings generally adjust more frequently than the interest rates on our ARMs. Accordingly, in a period of rising interest rates, our borrowing costs will usually increase faster than our interest earnings from MBS.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our Co-Chief Executive Officers ("Co-CEOs") and Chief Financial Officer ("CFO") participated in an evaluation by our management of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of our fiscal quarter that ended on March 31, 2016. Based on their participation in that evaluation, our Co-CEOs and CFO concluded that our disclosure controls and procedures were effective as of March 31, 2016 to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and to ensure that information required to be disclosed in our reports filed or furnished under the Exchange Act, is accumulated and communicated to our management, including our Co-CEOs and CFO, as appropriate, to allow timely decisions regarding required disclosures.

Internal Control Over Financial Reporting

Our Co-CEOs and CFO also participated in an evaluation by our management of any changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the quarter ended March 31, 2016. That evaluation did not identify any changes that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Nine putative class action lawsuits have been filed in connection with the Tender Offer and Merger (collectively, the “Transactions”): (1) Stourbridge Investments Ltd. v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001542), filed March 8, 2016 in the Circuit Court for Baltimore City, Maryland; (2) Timothy Lenell v. ARMOUR Residential REIT, Inc., et al., (Case No. 2016 CA 000164), filed March 8, 2016 in the Circuit Court for the Nineteenth Judicial Circuit for Indian River County, Florida; (3) Alexander Vartanov v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001593), filed March 10, 2016, in the Circuit Court for Baltimore City, Maryland; (4) Robert Curley v. ARMOUR Residential REIT, Inc. et al. (Case No. 24-C-16-001659, filed March 14, 2016 in the Circuit Court for Baltimore City, Maryland; (5) Antonio Rado and Craig and Amanda Hosler v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001684), filed March 15, 2016 in the Circuit Court for Baltimore City, Maryland; (6) Curtis Heid v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001706), filed March 16, 2016 in the Circuit Court for Baltimore City, Maryland; (7) Robert Aivasian v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001808), filed March 22, 2016 in the Circuit Court for Baltimore City, Maryland; (8) Neil Harmon v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001812), filed March 22, 2016 in the Circuit Court for Baltimore City, Maryland; and (9) Benjamin C. Washington, et al. v. ARMOUR Residential REIT, Inc., et al. (Case No. 24-C-16-001829), filed March 23, 2016 in the Circuit Court for Baltimore City, Maryland.

All nine suits name ARMOUR, the previous members of JAVELIN’s board of directors prior to the Merger (of which eight are current members of ARMOUR’s board of directors) (the “Individual Defendants”) and Acquisition as defendants. The Lenell, Curley, Heid and Harmon suits also name ACM as an additional defendant. All suits except for the Harmon suit also name JAVELIN as an additional defendant. The lawsuits were brought by purported holders of JAVELIN’s common stock, both individually and on behalf of a putative class of JAVELIN’s stockholders, alleging that the Individual Defendants breached their fiduciary duties owed to the plaintiffs and the putative class of JAVELIN stockholders, including claims that the Individual Defendants failed to properly value JAVELIN; failed to take steps to maximize the value of JAVELIN to its stockholders; ignored or failed to protect against conflicts of interest; failed to disclose material information about the Transactions; took steps to avoid competitive bidding and to give ARMOUR an unfair advantage by failing to adequately solicit other potential acquirors or alternative transactions; and erected unreasonable barriers to other third-party bidders. The suits also allege that ARMOUR, JAVELIN, ACM and Acquisition aided and abetted the alleged breaches of fiduciary duties by the Individual Defendants. The lawsuits seek equitable relief, including, among other relief, to enjoin consummation of the Transactions, or rescind or unwind the Transactions if already consummated, and award costs and disbursements, including reasonable attorneys’ fees and expenses. On April 25, 2016, the court issued an order consolidating eight Maryland cases into one action, captioned In re JAVELIN Mortgage Investment Corp. Shareholder Litigation (Case No. 24-C-16-001542), and designating counsel for one of the Maryland cases as interim lead co-counsel.

Each of ARMOUR, JAVELIN, ACM and the Individual Defendants believes that the claims made in these lawsuits are without merit and intends to defend such claims vigorously; however, there can be no assurance that any of ARMOUR, JAVELIN, ACM or the Individual Defendants will prevail in its defense of any of these lawsuits to which it is a party. An unfavorable resolution of any such litigation surrounding the Transactions may result in monetary damages being awarded to the plaintiffs and the putative class of former stockholders of JAVELIN, and the cost of defending the litigation, even if resolved favorably, could be substantial. Such litigation could also substantially divert the attention of the Individual Defendants and ARMOUR’s, JAVELIN’s and ACM’s management and their resources in general. Due to the preliminary nature of all nine suits, ARMOUR is not able at this time to estimate their outcome.

Item 1A. Risk Factors

There have been no material changes to the risk factors disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC on February 18, 2016, except for the following risk factors:

The risk factors referenced in JAVELIN's Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC on March 3, 2016, as amended on April 20, 2016, are incorporated by reference herein, to the extent applicable, and attached to this Quarterly Report on Form 10-Q as Exhibit 99.1.

Several lawsuits have been filed against ARMOUR, the previous members of JAVELIN's board of directors prior to the Merger (of which eight are current members of ARMOUR's board of directors), and in some suits, ACM and JAVELIN, challenging the Tender Offer and Merger, and an adverse judgment in any such lawsuit may result in rescinding and unwinding the Tender Offer and Merger and monetary damages, among other and further relief, being awarded to the plaintiffs and the putative class of former stockholders of JAVELIN.

Nine putative class action lawsuits have been filed in connection with the Tender Offer and Merger for JAVELIN (see *Note 17 -Subsequent Events* for more information about the Tender Offer and Merger). The Tender Offer and Merger are collectively defined herein as the "Transactions". All nine suits name ARMOUR, the previous members of JAVELIN's board of directors prior to the Merger (of which eight are current members of ARMOUR's board of directors) (the "Individual Defendants") and Acquisition as defendants. Certain cases also name ACM and JAVELIN as additional defendants. The lawsuits were brought by purported holders of JAVELIN's common stock, both individually and on behalf of a putative class of JAVELIN's stockholders, alleging that the Individual Defendants breached their fiduciary duties owed to the plaintiffs and the putative class of JAVELIN stockholders, including claims that the Individual Defendants failed to properly value JAVELIN; failed to take steps to maximize the value of JAVELIN to its stockholders; ignored or failed to protect against conflicts of interest; failed to disclose material information about the Transactions; took steps to avoid competitive bidding and to give ARMOUR an unfair advantage by failing to adequately solicit other potential acquirors or alternative transactions; and erected unreasonable barriers to other third-party bidders. The suits also allege that ARMOUR, JAVELIN, ACM and Acquisition aided and abetted the alleged breaches of fiduciary duties by the Individual Defendants. The lawsuits seek equitable relief, including, among other relief, to enjoin consummation of the Transactions, or rescind or unwind the Transactions if already consummated, and award costs and disbursements, including reasonable attorneys' fees and expenses. On April 25, 2016, the court issued an order consolidating eight Maryland cases into one action, captioned *In re JAVELIN Mortgage Investment Corp. Shareholder Litigation* (Case No. 24-C-16-001542), and designating counsel for one of the Maryland cases as interim lead co-counsel.

Each of ARMOUR, JAVELIN, ACM and the Individual Defendants believes that the claims made in these lawsuits are without merit and intends to defend such claims vigorously; however, there can be no assurance that any of ARMOUR, JAVELIN, ACM or the Individual Defendants will prevail in its defense of any of these lawsuits to which it is a party. An unfavorable resolution of any such litigation surrounding the Transactions may result in monetary damages being awarded to the plaintiffs and the putative class of former stockholders of JAVELIN and the cost of defending the litigation, even if resolved favorably, could be substantial. Due to the preliminary nature of all nine suits, ARMOUR is not able at this time to estimate their outcome.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

See Exhibit Index.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

/s/ James R. Mountain

James R. Mountain

Chief Financial Officer, Duly Authorized Officer and Principal
Financial and Accounting Officer

EXHIBIT INDEX

Exhibit Number	Description
31.1	Certification of Chief Executive Officer Pursuant to SEC Rule 13a-14(a)/15d-14(a) (1)
31.2	Certification of Chief Executive Officer Pursuant to SEC Rule 13a-14(a)/15d-14(a) (1)
31.3	Certification of Chief Financial Officer Pursuant to SEC Rule 13a14(a)/15d-14(a) (1)
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. §1350 (2)
32.2	Certification of Chief Executive Officer Pursuant to 18 U.S.C. §1350 (2)
32.3	Certification of Chief Financial Officer Pursuant to 18 U.S.C. §1350 (2)
99.1	Risk Factors relating to JAVELIN Mortgage Investment Corp.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
(1)	Filed herewith.
(2)	Furnished herewith.

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Section 2: EX-31.1 (EXHIBIT 31.1)

EXHIBIT 31.1

Certification Pursuant to 18 U.S.C Section 1350, Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Scott J. Ulm of ARMOUR Residential REIT, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended March 31, 2016 of ARMOUR Residential REIT, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely

to adversely affect the registrant's ability to record, process, summarize and report financial information; and

- (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting

Date: May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

By: /s/ Scott J. Ulm
 Scott J. Ulm
 Co-Chief Executive Officer

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Section 3: EX-31.2 (EXHIBIT 31.2)

EXHIBIT 31.2

Certification Pursuant to 18 U.S.C Section 1350, Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Jeffrey J. Zimmer of ARMOUR Residential REIT, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended March 31, 2016 of ARMOUR Residential REIT, Inc. (the "registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting

Date: May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

By: /s/ Jeffrey J. Zimmer
 Jeffrey J. Zimmer
 Co-Chief Executive Officer

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Section 4: EX-31.3 (EXHIBIT 31.3)

EXHIBIT 31.3

Certification Pursuant to 18 U.S.C Section 1350, Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, James R. Mountain of ARMOUR Residential REIT, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended March 31, 2016 of ARMOUR Residential REIT, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting

Date: May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

By: /s/ James R. Mountain
 James R. Mountain
 Chief Financial Officer

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Section 5: EX-32.1 (EXHIBIT 32.1)

EXHIBIT 32.1

**Certification Pursuant To
 18 U.S.C. Section 1350,
 as Adopted Pursuant to
 Section 906 of The Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report of ARMOUR Residential REIT, Inc. (the "Company") on Form 10-Q for the period ended March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Scott J. Ulm, Co-Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

By: /s/ Scott J. Ulm
 Scott J. Ulm
 Co-Chief Executive Officer

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Section 6: EX-32.2 (EXHIBIT 32.2)

EXHIBIT 32.2

**Certification Pursuant To
 18 U.S.C. Section 1350,
 as Adopted Pursuant to
 Section 906 of The Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report of ARMOUR Residential REIT, Inc. (the "Company") on Form 10-Q for the period ended March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jeffrey J. Zimmer, Co-Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

By: /s/ Jeffrey J. Zimmer
 Jeffrey J. Zimmer
 Co-Chief Executive Officer

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Section 7: EX-32.3 (EXHIBIT 32.3)

EXHIBIT 32.3

**Certification Pursuant To
 18 U.S.C. Section 1350,
 as Adopted Pursuant to
 Section 906 of The Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report of ARMOUR Residential REIT, Inc. (the "Company") on Form 10-Q for the period ended March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, James R. Mountain, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 2, 2016

ARMOUR RESIDENTIAL REIT, INC.

By: /s/ James R. Mountain
James R. Mountain
Chief Financial Officer

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Section 8: EX-99.1 (EXHIBIT 99.1)

EXHIBIT 99.1

RISK FACTORS RELATING TO JAVELIN MORTGAGE INVESTMENT CORP.

Risks Related to Our Business

Our lenders may insist on financing terms that could result in reducing availability and/or increasing the cost of our financing or may terminate our financing.

In order to achieve a competitive return to our investors, we use financial leverage to hold a portfolio of MBS that is several times larger than our total stockholders' equity. Our borrowings are predominantly in the form of repurchase agreements where we nominally sell MBS to counterparties with an agreement to repurchase them at a later date. The sale and purchase prices are set several percentage points below the current fair value of the MBS. This "haircut" percentage provides the counterparty with excess collateral to secure their loan and provides us with an incentive to complete the repurchase transaction on schedule.

There is a risk that our counterparties might be unwilling to continue to extend repurchase financing to us. Changes in regulation, market conditions or the financial position or business strategy of our counterparties could cause them to reduce or terminate our repurchase financing facilities. There is also a risk that counterparties insist on higher haircut percentages, interest rates or other terms that have the practical effect of reducing availability and/or increasing the cost of our financing. If we are unable to maintain adequate levels of funding, we would be required to reduce the size of our MBS portfolio and our net interest income would decline.

We attempt to mitigate our funding risk by maintaining repurchase funding relationships with a variety of counterparties that are diversified as to size, character and primary regulatory jurisdiction. We also monitor our borrowing levels with each counterparty, attempt to establish appropriate additional business relationships beyond our borrowing and regularly communicate with their credit and business officers responsible for our relationship. From time to time, we explore new funding structures and opportunities, but there can be no assurance that any such additional funding will become available on attractive terms.

Our ability to buy or sell our securities and derivatives may be severely limited or not profitable and we may be required to post additional collateral in connection with our financing and derivatives.

Our MBS are traded in the over-the-counter market. Therefore, we must buy and sell our securities in privately negotiated transactions with banks, brokers, dealers, or principal counter parties such as originators, the GSEs and other investors. Without the benefit of a securities exchange, there may be times when the supply of or demand for the MBS and derivatives we wish to buy or sell is severely limited. Our hedging derivatives, depending on their characteristics, are traded on either the over-the-counter market or on derivatives exchanges. The bid-ask spread between the prices at which we can purchase and sell MBS and derivatives may also become temporarily wide relative to historical levels. This could exacerbate our losses or limit our opportunities to profit during times of market stress or dislocation. We attempt to mitigate this risk by concentrating our investments in MBS that have more widespread trading interest resulting in deeper and more liquid trading.

All of our repurchase financing and our hedging derivatives have daily collateral maintenance requirements and a substantial portion of our MBS are pledged as collateral. These collateral requirements are monitored by our counterparties and we may be required to post additional collateral when the value of our posted collateral declines and/or the fair value of our net liability under a derivative increases. We attempt to mitigate this risk by moderating the amount of our financial leverage, monitoring collateral maintenance requirements and timely calling for collateral (or a return of collateral) from our counterparties on financing positions and derivatives, and maintaining reserve liquidity in the form of cash or unpledged Agency Securities that are widely acceptable as collateral. By concentrating our Agency Security investments in more liquid positions, we also seek to be able to quickly sell positions and reduce our financial leverage if necessary.

The daily collateral maintenance required for our repurchase financing and our hedging derivatives, generally move in opposite directions as market interest rates change. However, because market yields on our Agency Securities are not perfectly correlated with interest rate swap market yields, it is likely that our daily requirements to post collateral to our counterparties will not equal the collateral our counterparties are required to post to us. In times of higher market volatility, those differences can become more significant.

Changes in interest rates may impact our level of net interest income and stockholders' equity and we may not be able to successfully mitigate such interest rate risks.

We invest predominately in MBS backed by loans with fixed interest rates, and to a lesser extent from time to time, in MBS backed by loans with interest rates that adjust no more frequently than annually. The interest rates on our repurchase financing generally adjust quarterly or more frequently. This mismatch in the interest rate terms between our assets and our liabilities is the primary source of our ability to generate positive net income because long-term interest rates tend to be higher than short-term rates.

Short-term and long-term interest rates do not always move together. Changes in short-term rates will most significantly impact our level of net interest income, with rising rates likely to reduce our net interest income. Changes in long-term rates will initially impact the fair value of our MBS, with rising interest rates reducing their fair value. Changes in the fair values of our Agency Securities are generally not reflected in our net income or our earnings per share, but rather are reflected directly in our stockholders' equity. Changes in the values of our Non-Agency Securities are reflected in our income as other gain or loss with rising rates likely to generate losses. Over longer periods of time, rising long-term interest rates will provide us the opportunity to reinvest principal receipts and otherwise acquire additional MBS with higher yields.

We attempt to mitigate interest rate risk by moderating the amount of our financial leverage, diversifying our portfolio of MBS across both maturities and interest rate coupons, and economic hedging with derivatives. For example, we enter into interest rate swaps that require us to pay fixed rates and receive variable rates. These swaps are designed to offset the fluctuations in the interest costs of our repurchase financing due to movements in short-term interest rates. We record our derivatives and our Non-Agency Securities at fair value and periodic changes in fair value are reflected in other income (loss) in our consolidated statements of operations. To the extent that fair value changes on derivatives offset fair value changes in our MBS, the fluctuation in our stockholders' equity will be lower. However, our income statement volatility will not be reduced, because the fair value changes in our Agency Securities are reflected directly in stockholders' equity. Rising interest rates may tend to result in an overall increase in our reported net income even while our total stockholders' equity declines.

Factors beyond our control may increase the prepayment speeds on our Agency Securities, thereby reducing our interest income.

At December 31, 2015 and December 31, 2014, approximately 78.49% and 78.27% of our single family Agency Securities were backed by loans where the underlying borrowers may prepay their loans without premium or penalty. Also, when borrowers default on their loans, the GSE that issued or guaranteed our Agency Securities (including Agency Securities backed by multi-family loans) pay off the remaining loan balance. Those prepayments are passed through to us, reducing the balance of the Agency Security. We generally purchase Agency Securities at premium prices, and the premium amortization associated with prepayments reduces our interest income.

We experience prepayments on our Agency Securities every month and the speed of prepayments can vary widely from month to month and across individual Agency securities. Factors driving prepayment speeds include the rate of new and existing home sales, the level of borrower refinancing activities and the frequency of borrower defaults. Such factors are themselves influenced by government monetary, fiscal and regulatory policies and general economic conditions such as the level of and trends in interest rates, GDP, employment and consumer confidence. Prepayment expectations are an integral part of pricing Agency Securities in the marketplace. Volatility in actual prepayment speeds will create volatility in the amount of premium amortization we recognize. Higher speeds will reduce our interest income and lower speeds will increase our interest income.

We consider our expectations of future prepayments when evaluating the prices at which we purchase and sell Agency Securities. We attempt to mitigate the risk of unexpected prepayments by identifying characteristics of the underlying loans, such as the loan size, coupon rate, loan age and maturity, geographic location, borrower credit scores and originator/servicer that might predict relatively faster or slower prepayment speed tendencies for a particular Agency Security. Agency Securities with characteristics expected to be favorable often command marginally higher prices, or "pay ups." We seek to purchase Agency Securities with favorable prepayment characteristics when the required pay ups are relatively lower and may sell our Agency Securities when their pay ups are relatively higher.

The structural characteristics of our Non-Agency Securities make them less sensitive to variations in prepayment speeds of the underlying mortgage loans.

Volatility in the relationships between the market prices and yields for our securities and certain benchmark prices and interest rates can adversely affect our net income, earnings per share and stockholders' equity.

The market prices and yields for MBS and interest rate derivatives like those we hold are generally correlated over time to each other and to certain benchmark prices and interest rates, such as those for U.S. Treasury Securities. Those correlations are never perfect, and can vary widely on occasion, particularly in times of market stress. This variation in the "spread" relationship among the market yields, and therefore prices, of different instruments can result in our hedging positions being not as effective in protecting book value than normally would be expected, exposing us to the risk of unexpected volatility in our net income, earnings per share, and total stockholders' equity.

Spread risk is difficult and expensive to hedge effectively. Avoiding holding Agency Securities with interest rate spread risk would severely limit our opportunity to generate net interest income because low spread risk investments, such as U.S. Treasury Securities, usually have substantially lower yields. Our efforts to mitigate spread risk are limited to attempting to identify characteristics that might cause particular MBS to have relatively higher or lower spread risk under potential future market conditions. Such characteristics include characteristics of the underlying loans and current market premium levels. All other things being equal, we attempt to overweight our MBS portfolio with Agency Securities that have marginally lower spread risk. However, other investment considerations, such as prepayment risk, tend to overshadow spread risk in our selection of Agency Securities. Spread risk tends to be a relatively less significant factor in the price volatility in Non-Agency Securities because other factors such as liquidity and credit risk tend to be more important.

We may not be able to minimize potential credit risks that could arise in the event of bankruptcy of one or more of our counterparties.

Substantially all of our Agency Securities are issued or guaranteed by GSEs, which we consider the functional equivalent of the full faith and credit of the U.S. Government. Our primary credit risk relates to our exposure to our counterparties for the amount of the excess collateral they hold to secure our repurchase financing and derivative obligations. We would typically become a general unsecured creditor for that amount in the event of the bankruptcy of a counterparty.

We mitigate our credit risk by evaluating the credit quality of our counterparties on an ongoing basis, reducing or closing positions with counterparties where we have credit concerns, monitoring our collateral positions to minimize excess collateral balances and diversifying our repurchase financing and derivatives positions among numerous counterparties. See Note 9 to the consolidated financial statements for a list of counterparties that the amount at risk, or aggregate haircut, accounts for 5% or greater of our total stockholders' equity.

We are also exposed to the credit risk of borrowers on mortgage loans underlying our Non-Agency Securities. We mitigate our credit risk by conducting our own pre-purchase evaluation and analysis of our Non-Agency Securities. Our analysis includes structural elements of the security, such as the credit enhancement benefit of one or more of over-collateralization, subordination or insurance, as well as estimation of expected losses based on borrower characteristics.

Changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government may adversely affect our business.

The payments we receive on the Agency Securities in which we invest depend upon a steady stream of payments by borrowers on the underlying mortgages and the fulfillment of guarantees by GSEs. There can be no assurance that the U.S. Government's intervention in Fannie Mae and Freddie Mac will continue to be adequate for the longer-term viability of these GSEs. These uncertainties may lead to concerns about the availability of and trading market for Agency Securities in the long term. Accordingly, if the GSEs defaulted on their guaranteed obligations, suffered losses or ceased to exist, the value of our Agency Securities and our business, operations and financial condition could be materially and adversely affected.

The passage of any new federal legislation affecting Fannie Mae and Freddie Mac may create market uncertainty and reduce the actual or perceived credit quality of securities issued or guaranteed by them. If Fannie Mae and Freddie Mac were reformed or wound down, it is unclear what effect, if any, this would have on the value of the existing Fannie Mae and Freddie Mac Agency Securities. The foregoing could materially adversely affect the pricing, supply, liquidity and value of the Agency Securities in which we invest and otherwise materially adversely affect our business, operations and financial condition.

The adoption of derivatives legislation by Congress could have an adverse impact on our ability to hedge risks associated with our business.

The Dodd-Frank Act regulates derivative transactions, which include certain instruments used in our risk management activities. Under the Dodd-Frank Act, most swaps will eventually be required to clear through a registered clearing facility and traded on a designated exchange or swap execution facility. There are some exceptions to these requirements for entities that use swaps to hedge or mitigate commercial risk. However, we do not currently anticipate qualifying for an exception. Among the other provisions of the Dodd-Frank Act that may affect derivative transactions are those relating to establishment of capital and margin requirements for certain derivative participants, establishment of business conduct standards, record keeping and reporting requirements, and imposition of position limits. Although the Dodd-Frank Act includes significant new provisions regarding the regulation of derivatives, the impact of those requirements will not be known definitively until regulations have been adopted by the SEC and the CFTC. The new legislation and any new regulations could increase the operational and transactional cost of derivatives contracts and affect the number and/or creditworthiness of available hedge counterparties to us. We have established an account with a futures commission merchant for this purpose. To date, we have not entered into any cleared interest rate swap contracts.

We cannot predict the impact of future Fed monetary policy on the prices and liquidity of Agency Securities or other securities in which we invest, although Fed action could increase the prices of our target assets and reduce the spread on our investments, or decrease our book value.

Since 2008, the Fed has conducted various quantitative easing programs of buying Agency and U.S. Treasury Securities intended to expedite an economic recovery, stabilize prices, reduce unemployment and improve business and household spending. The Fed's most recent round of this quantitative easing ended in September 2014. On December 16, 2015, the Fed raised its target range for the Federal Funds Rate to between 0.25% and 0.50%. On January 27, 2016, the Fed announced their decision to hold the same target range. Changes in Fed policy affect our financial results, since our cost of funds is largely dependent on short-term rates. An increase in our cost of funds without a corresponding increase in interest income earned on our MBS would cause our net income to decline. We cannot predict the impact of any future actions by the Fed on the prices and liquidity of Agency Securities or other securities in which we invest, although future Fed action could increase the prices of our target assets and reduce the spread on our investments or decrease our book value. Future securities purchase programs or other monetary policy enacted by the Fed could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Our business could be negatively affected as a result of shareholder activism, which could cause us to incur significant expense, hinder execution of our business strategy and impact the trading value of our stock.

Shareholder activism, which can take many forms or arise in a variety of situations, has been increasing in publicly traded companies in recent years and we are subject to the risks associated with such activism. On December 15, 2015, we received a formal notice from an activist shareholder of its nomination of six non-Company director candidates. In connection with this notice, the activist shareholder filed a Schedule 13D and Soliciting Material under Rule 14a-12, on December 14, 2015 and December 15, 2015, respectively. Upon completion of the tender offer and Merger described above, we will become a private, wholly-owned subsidiary of ARMOUR and managed by ACM. The Merger is subject to customary closing conditions and is expected to close in the second quarter of 2016. We expect to terminate the listing of our common stock on the NYSE and the registration of our common stock under the Exchange Act. As such, we do not expect to hold an annual meeting in 2016 to nominate our own slate of directors in the normal course of business in accordance with past practice. Shareholder activism, including potential proxy contests, requires significant time and attention by management and the Board, potentially interfering with our ability to execute our strategic plan. Additionally, such shareholder activism could give rise to perceived uncertainties as to our future direction, adversely affect our relationships with key business partners and make it more difficult to attract and retain qualified personnel. Also, we may be required to incur significant legal fees and other expenses related to activist shareholder matters. Any of these impacts could materially and adversely affect our business and operating results. Further, the market price of our common stock could be subject to significant fluctuation or otherwise be adversely affected by the events, risks and uncertainties described above.

Risks Related to Our Corporate Structure***Maintenance of our exclusion from the 1940 Act will impose limits on our business.***

We conduct our business so as not to become regulated as an investment company under the 1940 Act. If we were to fall within the definition of investment company, we would be unable to conduct our business as described in this Annual Report on Form 10-K. Section 3(a)(1)(A) of the 1940 Act defines an investment company as any issuer that is or holds itself out as being

engaged primarily in the business of investing, reinvesting or trading in securities. Section 3(a)(1)(C) of the 1940 Act also defines an investment company as any issuer that is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of the issuer's total assets (exclusive of U.S. Government securities and cash items) on an unconsolidated basis. Excluded from the term "investment securities," among other things, in Section 3(a)(1)(C) of the 1940 Act, as defined above, are U.S. Government securities and securities issued by majority-owned subsidiaries that are not themselves investment companies and are not relying on the exclusion from the definition of investment company set forth in Section 3(c)(1) or Section 3(c)(7) of the 1940 Act.

We rely on the exclusion from the definition of "investment company" provided by Section 3(c)(5)(C) of the 1940 Act. To qualify for the exclusion, we make investments so that at least 55% of the assets we own consist of "qualifying assets" and so that at least 80% of the assets we own consist of qualifying assets and other real estate related assets. We generally expect that our investments in our target assets will be treated as either qualifying assets or real estate related assets under Section 3(c)(5)(C) of the 1940 Act in a manner consistent with SEC staff no-action letters. Qualifying assets for this purpose include mortgage loans and other assets, such as whole pool Agency Securities that are considered the functional equivalent of mortgage loans for purposes of the 1940 Act. The SEC staff has not issued guidance with respect to whole pool Non-Agency Securities. Accordingly, based on our own judgment and analysis of the SEC's pronouncements with respect to agency whole pool certificates, we may also treat Non-Agency Securities issued with respect to an underlying pool of mortgage loans in which we hold all of the certificates issued by the pool as qualifying assets. We invest at least 55% of our assets in whole pool Agency and Non-Agency Securities that constitute qualifying assets in accordance with SEC staff guidance and at least 80% of our assets in qualifying assets plus other real estate related assets. Other real estate related assets would consist primarily of Agency and Non-Agency Securities that are not whole pools, such as CMOs and CMBS. As a result of the foregoing restrictions, we are limited in our ability to make or dispose of certain investments. To the extent that the SEC staff publishes new or different guidance with respect to these matters, we may be required to adjust our strategy accordingly. These restrictions could also result in our holding assets we might wish to sell or selling assets we might wish to hold. Although we monitor our portfolio for compliance with the Section 3(c)(5)(C) exclusion periodically and prior to each acquisition and disposition, there can be no assurance that we will be able to maintain this exclusion.

To the extent that we elect in the future to conduct our operations through majority-owned subsidiaries, such business will be conducted in such a manner as to ensure that we do not meet the definition of investment company under either Section 3(a)(1)(A) or Section 3(a)(1)(C) of the 1940 Act, because less than 40% of the value of our total assets on an unconsolidated basis would consist of investment securities. We intend to monitor our portfolio periodically to insure compliance with the 40% test. In such case, we would be a holding company which conducts business exclusively through majority-owned subsidiaries and we would be engaged in the non-investment company business of our subsidiaries.

Loss of the 1940 Act exclusion would adversely affect us, the market price of shares of our stock and our ability to distribute dividends.

As described above, we conduct our operations so as not to become required to register as an investment company under the 1940 Act based on current laws, regulations and guidance. Although we monitor our portfolio, we may not be able to maintain this exclusion under the 1940 Act. If we were to fail to qualify for this exclusion in the future, we could be required to restructure our activities or the activities of our subsidiaries, if any, including effecting sales of assets in a manner that, or at a time when we would not otherwise choose, which could negatively affect the value of our stock, the sustainability of our business model and our ability to make distributions. The sale could occur during adverse market conditions and we could be forced to accept a price below that which we believe is appropriate.

There can be no assurance that the laws and regulations governing the 1940 Act status of REITs, including guidance and interpretations from the SEC and its staff regarding the Section 3(c)(5)(C) exclusion, will not change in a manner that adversely affects our operations or business. The SEC or its staff may issue new interpretations of the Section 3(c)(5)(C) exclusion causing us to change the way we conduct our business, including changes that may adversely affect our ability to achieve our investment objective. We may be required at times to adopt less efficient methods of financing certain of our mortgage related investments and we may be precluded from acquiring certain types of higher yielding securities. The net effect of these factors would be to lower our net interest income. If we fail to qualify for an exclusion from registration as an investment company or an exclusion from the definition of an investment company, our ability to use leverage would be substantially reduced. Our business will be materially and adversely affected if we fail to qualify for an exclusion from regulation under the 1940 Act.

Failure to maintain an exemption from being regulated as a CPO could subject us to additional regulation and compliance requirements and may result in fines and other penalties which could materially adversely affect our business and financial condition.

Rules adopted under the Dodd-Frank Act establish a comprehensive new regulatory framework for derivative contracts commonly referred to as swaps. Under these rules, any investment fund that trades in swaps may be considered a “commodity pool,” which would cause its directors to be regulated as CPOs. Under the rules, which became effective on October 12, 2012 for those who became CPOs solely because of their use of swaps, CPOs must register with the NFA, which requires compliance with NFA’s rules, and are subject to regulation by the CFTC including with respect to disclosure, reporting, record keeping and business conduct.

On December 7, 2012, the CFTC staff issued a no-action letter (CFTC Staff Letter 12-44) to provide exemptive relief to mortgage REITs that claim such relief. On December 11, 2012, we submitted our claim and our directors do not intend to register as CPOs with the NFA. To comply with CFTC Staff Letter 12-44, we are restricted to operating within certain parameters discussed in the no-action letter. For example, the exemptive relief limits our ability to enter into interest rate hedging transactions such that the initial margin and premiums for such hedges will not exceed five percent of the fair market value of our total assets.

Our hedging strategies are designed to reduce the impact on our earnings caused by the potential adverse effects of changes in interest rates on our target assets and liabilities. Subject to complying with REIT requirements, we use hedging techniques to limit the risk of adverse changes in interest rates on the value of our target assets as well as the differences between the interest rate adjustments on our target assets and borrowings. These techniques primarily consist of entering into interest rate swap contracts and may also include entering into interest rate cap or floor agreements, purchasing put and call options on securities or entering into forward rate agreements. Although we are not legally limited to our use of hedging, we limit our use of derivative instruments to only those techniques described above and enter into derivative transactions only with counterparties that we believe have a strong credit rating to help limit the risk of counterparty default or insolvency. These transactions are not entered into for speculative purposes. We do not use these instruments for the purpose of trading in commodity interests, and we do not consider our company or its operations to be a commodity pool as to which CPO regulation or compliance is required.

The CFTC has substantial enforcement power with respect to violations of the laws over which it has jurisdiction, including their anti-fraud and anti-manipulation provisions. Among other things, the CFTC may suspend or revoke the registration of a person who fails to comply, prohibit such a person from trading or doing business with registered entities, impose civil money penalties, require restitution and seek fines or imprisonment for criminal violations. Additionally, a private right of action exists against those who violate the laws over which the CFTC has jurisdiction or who willfully aid, abet, counsel, induce or procure a violation of those laws. In the event we fail to maintain exemptive relief from the CFTC on this matter and our directors fail to comply with the regulatory requirements of these new rules, we may be subject to significant fines, penalties and other civil or governmental actions or proceedings, any of which could have a materially adverse effect on our business, financial condition and results of operations.

We are highly dependent on information and communications systems. System failures, security breaches or cyber-attacks of networks or systems could significantly disrupt our business and negatively affect the market price of our common stock and our ability to distribute dividends.

Our business is highly dependent on communications and information systems that allow us to monitor, value, buy, sell, finance and hedge our investments. These systems are primarily operated by third parties and, as a result, we have limited ability to ensure their continued operation. In the event of systems failure or interruption, we will have limited ability to affect the timing and success of systems restoration. Any failure or interruption of our systems could cause delays or other problems in our securities trading activities, including Agency RMBS trading activities, 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.

We rely on sophisticated information technology systems, networks and infrastructure in managing our day-to-day operations. Despite cyber-security measures already in place, our information technology systems, networks and infrastructure may be vulnerable to deliberate attacks or unintentional events that could interrupt or interfere with their functionality or the confidentiality of our information. Our inability to effectively utilize our information technology systems, networks and infrastructure, and protect our information could adversely affect our business.

We have not established a minimum dividend payment level and there are no guarantees of our ability to pay dividends in the future.

We expect to continue to make regular cash distributions to our stockholders in amounts such that all or substantially all of our taxable income in each year, subject to certain adjustments, is distributed. This, along with other factors, should enable us to qualify for the tax benefits accorded to a REIT under the Code. However, we have not established a minimum dividend payment level and our ability to pay dividends may be adversely affected by the risk factors described in this report. Future distributions are made at the discretion of our Board and will depend on our earnings, our financial condition, maintenance of our REIT status, restrictions on making distributions under the MGCL, and such other factors as our Board may deem relevant from time to time. There are no guarantees of our ability to pay dividends in the future. In addition, some of our distributions may include a return of capital.

Although we have no intention to do so, we may use proceeds from equity and debt offerings and other financings to fund distributions, which will decrease the amount of capital available for purchasing our target assets.

We presently have no intention of using the proceeds of any offering of our equity or debt or other financings to fund distributions to stockholders. However, there are no restrictions in our charter or in any agreement to which we are a party that prohibits us from doing so. In the event that we elect to fund any distribution to our stockholders from sources other than our earnings, the amount of capital available to us to purchase our target assets would decrease, which could have an adverse effect on our overall financial results and performance.

We have, and may continue to, return capital to shareholders by repurchasing shares and/or paying dividends in excess of our taxable income.

Share repurchases and dividends paid in excess of our taxable income will reduce our capital base and our ability to invest in MBS without increasing financial leverage. Reducing our capital base will increase our expense ratio and could potentially reduce the availability of our repurchase financing and interest rate swap hedges. We will be more likely to consider future returns of capital to shareholders when the market trading price for our common stock represents a significant discount to our book value. For the year ended December 31, 2015, we returned capital to shareholders of \$1,009 through stock repurchases and \$2,677 through dividends in excess of taxable income. For the year ended December 31, 2014, we returned capital to shareholders of \$591 through stock repurchases and \$3,463 through dividends in excess of taxable income. For the year ended December 31, 2013, we returned capital to shareholders of \$19,201 through stock repurchases and \$1,128 through dividends in excess of taxable income. At December 31, 2015, there were 1,936 authorized shares remaining under our Repurchase Program.

We are subject to financial reporting and other requirements for which our accounting, internal audit and other management systems and resources may not be adequately prepared.

We are subject to reporting and other obligations under the Securities Act and the Exchange Act, including the requirements of Section 404 of the Sarbanes-Oxley Act. These reporting and other obligations, may place significant demands on our management, administrative, operational, internal audit and accounting resources and cause us to incur significant expenses. We may need to upgrade our systems or create new systems; implement additional financial and management controls, reporting systems and procedures; expand or outsource our internal audit function; and hire additional accounting, internal audit and finance staff. If we are unable to accomplish these objectives in a timely and effective fashion, our ability to comply with the financial reporting requirements and other rules that apply to reporting companies could be impaired. Any failure to maintain effective internal controls could have a material adverse effect on our business, operating results and stock price.

Future issuances or sales of stock could cause our stock price to decline.

Sales of substantial amounts of our stock in the public market, or the perception that such sales might occur, could adversely affect the market price of our stock. In addition, the sale of these shares could impair our ability to raise capital through a sale of additional equity securities.

Other issuances of our stock could have an adverse effect on the market price of our stock. In addition, future issuances of our stock may be dilutive to existing stockholders.

Provisions of Maryland law and other provisions of our organizational documents may limit the ability of a third party to acquire control of the company.

Certain provisions of the MGCL may have the effect of delaying, deferring or preventing a transaction or a change in control of the company that might involve a premium price for holders of our common stock or otherwise be in their best interests. Additionally, our charter and bylaws contain other provisions that may delay or prevent a change of control of the company.

If we have a class of equity securities registered under the Securities Exchange Act and meet certain other requirements, Title 3, Subtitle 8 of the MGCL permits us without stockholder approval and regardless of what is currently provided in our charter or bylaws, to elect to be subject to statutory provisions that may have the effect of delaying, deferring or preventing a transaction or a change in control of the company that might involve a premium price for holders of our common stock or otherwise be in their best interest. Pursuant to Title 3, Subtitle 8 of the MGCL, once we meet the applicable requirements, our charter provides that our Board will have the exclusive power to fill vacancies on our Board. As a result, unless all of the directorships are vacant, our stockholders will not be able to fill vacancies with nominees of their own choosing. We may elect to opt in to additional provisions of Title 3, Subtitle 8 of the MGCL without stockholder approval at any time that we have a class of equity securities registered under the Securities Exchange Act and satisfy certain other requirements.

We have very broad investment guidelines and our Board will not approve each investment and financing decision made by ACM.

We are authorized to invest in Agency Securities and Non-Agency Securities backed by fixed rate, hybrid adjustable rate and adjustable rate home loans as well as unsecured notes and bonds issued by GSEs, U.S. Treasuries and money market instruments, subject to certain income tests we must satisfy for our qualification as a REIT. ACM is authorized to invest and obtain financing on our behalf within these guidelines. Our Board periodically reviews our investment guidelines and our investment portfolio but does not, and is not required to, review all of our investments on an individual basis or in advance. In conducting periodic reviews, our Board relies primarily on information provided to it by ACM. Furthermore, ACM may use complex strategies and transactions that may be costly, difficult or impossible to unwind if our Board determines that they are not consistent with our investment guidelines. In addition, because ACM has a certain amount of discretion in investment, financing and hedging decisions, ACM's decisions could result in investment returns that are substantially below expectations or that result in losses, which would materially and adversely affect our business, financial condition and results of operations.

We may change our target assets, financing and investment strategy and other operational policies without stockholder consent, which may adversely affect the market price of our common stock and our ability to make distributions to stockholders.

Within our overall investment guidelines, we may change our target assets financing strategy, and investment guidelines at any time without the consent of our stockholders, which could result in our making investments that are different from, and possibly riskier than, the investments described in this Annual Report on Form 10-K. Our Board also determines our other operational policies and may amend or revise such policies, including our policies with respect to our REIT qualification, acquisitions, dispositions, operations, indebtedness and distributions, or may approve transactions that deviate from these policies, without a vote of, or notice to, our stockholders. A change in our targeted investments, financing strategy, investment guidelines and other operational policies may increase our exposure to interest rate risk, default risk and real estate market fluctuations, all of which could adversely affect the market price of our common stock and our ability to make distributions to our stockholders.

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

We operate in a highly competitive market for investment opportunities and borrowing facilities. Our profitability depends, in large part, on our ability to acquire our target assets at attractive prices and finance them economically. In acquiring and financing our target assets, we will compete with a variety of institutional investors, including other REITs, specialty finance companies, public and private funds, government entities, commercial and investment banks, 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 may have investment objectives that overlap with ours, which may create additional competition for investment opportunities and financing. 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. or foreign governments. 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 us. 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 provide assurance 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 take advantage of attractive investment opportunities from time to time, as we can provide no assurance that we will be able to identify, finance and make investments that are consistent with our investment objectives.

Risks Related to Our Management and Conflicts of Interest

We depend on ACM and particularly key personnel. The loss of those key personnel could severely and detrimentally affect our operations.

As an externally managed company, we depend on the diligence, experience and skill of ACM for the selection, acquisition, structuring, hedging and monitoring of our MBS and associated borrowings. We depend on the efforts and expertise of our operating officers to manage our day-to-day operations and strategic business direction. If any of our key personnel were to leave the Company, locating individuals with specialized industry knowledge and skills similar to that of our key personnel may not be possible or could take months. Because we have no employees, the loss of ACM could harm our business, financial condition, cash flow and results of operations.

We have a contract with AVM to administer clearing and settlement services for our securities and derivative transactions. We have also entered into a second contract with AVM to assist us with financing transaction services such as repurchase financings and managing the margin arrangement between us and our lenders for each of our repurchase agreements. We use the services of AVM for these aspects of our business so our executive officers can focus on our daily operations and strategic direction. Further, as our business expands, reliance on AVM to provide us with timely, effective services will increase. In the future, as we expand our staff, we may absorb internally some or all of the services provided by AVM. Until we elect to move those services in-house, we will continue to use AVM or other third parties that provide similar services. If we are unable to maintain a relationship with AVM or are unable to establish a successful relationship with other third parties providing similar services at comparable pricing, we may have to reduce or delay our operations and/or increase our expenditures and undertake the repurchase agreement and trading and administrative activities on our own, which could have a material adverse effect on our business operations and financial condition. However, we believe that the breadth and scope of ACM's experience will enable them to fill any needs created by discontinuing a relationship with AVM.

There are conflicts of interest in our relationship with ACM and its affiliates, 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 ACM and its affiliates. Each of our executive officers and our non-independent directors are also affiliated with ARMOUR and such officers and directors will not be exclusively dedicated to our business. Entities affiliated with Mr. Ulm and Mr. Zimmer are the general partners of ACM and each of Mr. Ulm, Mr. Zimmer, Mr. Staton and Mr. Bell is a limited partner in ACM and a stockholder of ARMOUR.

The Management Agreement with ACM may create a conflict of interest and its terms, including fees payable to ACM, may not be as favorable to us as if they had been negotiated with an unaffiliated third-party. In addition, we may choose not to enforce, or to enforce less vigorously, our rights under the Management Agreement because of our desire to maintain our ongoing relationship with ACM. ACM maintains a contractual and fiduciary relationship with us. The Management Agreement with ACM does not prevent ACM and its affiliates from engaging in additional management or investment opportunities some of which will compete with us. ACM and its affiliates may engage in additional management or investment opportunities that have overlapping objectives with ours and may thus face conflicts in the allocation of investment opportunities to these other investments. Such allocation is at the discretion of ACM and there is no guarantee that this allocation would be made in the best interest of our stockholders. We are not entitled to receive preferential treatment as compared with the treatment given by ACM or its affiliates to any investment company, fund or advisory account other than any fund or advisory account which contains only funds invested by ACM (and not of any of its clients or customers) or its officers and directors. Additionally, the ability of ACM and its respective officers and employees to engage in other business activities, including their activities related to ARMOUR, may reduce the time spent managing our activities.

We compete with current and future investment entities affiliated with ACM.

There are conflicts of interest in allocating investment opportunities among us and other funds, investment vehicles and ventures managed by ACM. There is a significant overlap in the assets and investment strategies of us and ARMOUR. Although ACM may dedicate certain trading and investment personnel to serve us only, in most cases the same trading and investment personnel may provide services to both entities. ACM and its affiliates may in the future form additional funds or sponsor additional

investment vehicles and ventures that have overlapping objectives with us and therefore may compete with us for investment opportunities and ACM resources. ACM has an allocation policy that addresses the manner in which investment opportunities are allocated among the various entities and strategies for which they provide investment management services. However, we cannot assure you that ACM will always allocate every investment opportunity in a manner that is advantageous for us; indeed, we may expect that the allocation of investment opportunities will at times result in our receiving only a portion of, or none of, certain investment opportunities.

Resolution of potential conflicts of interest in allocation of investment opportunities.

In allocating investment opportunities among us and any other funds or accounts managed by them, ACM's personnel are guided by the principles that they will treat all entities fairly and equitably, they will not arbitrarily distinguish among entities and they will not favor one entity over another.

In allocating a specific investment opportunity among us and ARMOUR, ACM will make a determination, exercising their judgment in good faith, as to whether the opportunity is appropriate for each entity. Factors in making such a determination may include an evaluation of each entity's liquidity, overall investment strategy and objectives, the composition of the existing portfolio, the size or amount of the available opportunity, the characteristics of the securities involved, the liquidity of the markets in which the securities trade, the risks involved, and other factors relating to the entity and the investment opportunity. ACM is not required to provide every opportunity to each entity.

If ACM determines that an investment opportunity is appropriate for both us and ARMOUR, then ACM will allocate that opportunity in a manner that they determine, exercising their judgment in good faith, to be fair and equitable, taking into consideration all allocations among us and ARMOUR taken as a whole. ACM has broad discretion in making that determination, and in amending that determination over time.

In the future, ACM may adopt additional conflicts of interest resolution policies and procedures designed to support the equitable allocation and to prevent the preferential allocation of investment opportunities among entities with overlapping investment objectives.

If ACM ceases to be our investment manager, financial institutions providing any financing arrangements to us may not provide future financing to us.

Financial institutions that finance our investments may require that ACM continue to act in such capacity. If ACM ceases to be 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, it is likely that we would be materially and adversely affected.

ACM's failure to make investments on favorable terms that satisfy our investment strategy and otherwise generate attractive risk adjusted returns initially and consistently from time to time in the future would materially and adversely affect us.

Our ability to achieve our investment objective depends on ACM's personnel and their ability to make investments on favorable terms that satisfy our investment strategy and otherwise generate attractive risk adjusted returns initially and consistently from time to time in the future. Accomplishing this result is also a function of ACM's ability to execute our financing strategy on favorable terms.

The manner of determining the management fee may not provide sufficient incentive to ACM to maximize risk adjusted returns on our investment portfolio since it is based on our gross equity raised and not on our performance.

ACM is entitled to receive a monthly management fee that is based on the total of all gross equity raised (see Note 11 and Note 16 to the consolidated financial statements), as measured as of the date of determination (i.e., each month), regardless of our performance. Accordingly, the possibility exists that significant management fees could be payable to ACM for a given month despite the fact that we could experience a net loss during that month. ACM's entitlement to such significant nonperformance-based compensation may not provide sufficient incentive to ACM to devote its time and effort to source and maximize risk adjusted returns on our investment portfolio, which could, in turn, adversely affect our ability to pay dividends to our stockholders and the market price of our common stock. Further, the management fee structure gives ACM the incentive to maximize gross equity raised by the issuance of new equity securities or the retention of existing equity, regardless of the effect of these actions on existing stockholders. In other words, the management fee structure will reward ACM primarily based on the size of our equity raised and not on our financial returns to stockholders.

The termination of the Management Agreement may be difficult and costly, which may adversely affect our inclination to end our relationship with ACM.

Termination of the Management Agreement with ACM without cause may be difficult and costly. The term “cause” is limited to those circumstances described in the Management Agreement with ACM. We may not terminate the Management Agreement during the Initial Term, as defined therein, except for cause or in connection with a Corporate Event, as defined therein. Upon a termination by us without cause, which shall include a Corporate Event, the Management Agreement provides that we will pay ACM a termination payment equal to the greater of (a) the base management fee as calculated immediately prior to the effective date of the termination of the Management Agreement pursuant to Section 10.2 of the Management Agreement for the remainder of the then current term, or (b) three times the base management fee paid to ACM in the preceding twelve-month period before such termination, calculated as of the effective date of the termination. This provision increases the effective cost to us of electing to terminate the Management Agreement, thereby adversely affecting our inclination to end our relationship with ACM, even if we believe ACM’s performance is not satisfactory.

ACM may terminate the Management Agreement at any time and for any reason 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 execute our business plan.

Additionally, following the Initial Term, the Management Agreement will automatically renew for successive one-year renewal terms unless either we or ACM give advance notice to the other of our intent not to renew the agreement prior to the expiration of the Initial Term or any renewal term. However, our right to give such a notice of non-renewal is limited and requires our independent directors to agree that certain conditions are met.

ACM’s liability is limited under the Management Agreement and we have agreed to indemnify ACM and its affiliates against certain liabilities. As a result, we could experience poor performance or losses for which ACM would not be liable.

The Management Agreement limits the liability of ACM and any directors and officers of ACM for money damages, except for liability resulting from actual receipt of an improper benefit or profit in money, property or services, or a final judgment based upon a finding of active and deliberate dishonesty by the director or officer that was material to the cause of action adjudicated.

Pursuant to the Management Agreement, ACM will not assume any responsibility other than to render the services called for thereunder and will not be responsible for any action of our Board in following or declining to follow its advice or recommendations. ACM and its affiliates, directors, officers, stockholders, equity holders, employees, representatives and agents and any affiliates thereof, will not be liable to us, our stockholders, any subsidiary of ours, the stockholders of any subsidiary of ours, our Board, any issuer of mortgage securities, any credit-party, any counterparty under any agreement, or any other person for any acts or omissions, errors of judgment or mistakes of law by ACM or its affiliates, directors, officers, stockholders, equity holders, employees, representatives or agents, or any affiliates thereof, under or in connection with the Management Agreement, except if ACM was grossly negligent, acted with reckless disregard or engaged in willful misconduct or fraud while discharging its duties under the Management Agreement. We have agreed to indemnify ACM and its affiliates, directors, officers, stockholders, equity holders, employees, representatives and agents and any affiliates thereof, with respect to all expenses, losses, costs, damages, liabilities, demands, charges and claims of any nature, actual or threatened (including reasonable attorneys’ fees), arising from or in respect of any acts or omissions, errors of judgment or mistakes of law (or any alleged acts or omissions, errors of judgment or mistakes of law) performed or made while acting in any capacity contemplated under the Management Agreement or pursuant to any underwriting or similar agreement to which ACM is a party that is related to our activities, unless ACM was grossly negligent, acted with reckless disregard or engaged in willful misconduct or fraud while discharging its duties under the Management Agreement. As a result, we could experience poor performance or losses for which ACM would not be liable.

In addition, our articles of incorporation provide that no director or officer of ours shall be personally liable to us or our stockholders for money damages. Furthermore, our articles of incorporation permit and our by-laws require, us to indemnify, pay or reimburse any present or former director or officer of ours who is made or threatened to be made a party to a proceeding by reason of his or her service to us in such capacity. Officers and directors of ours who are also officers and board members of ACM will therefore benefit from the exculpation and indemnification provisions of our articles of incorporation and by-laws and accordingly may not be liable to us in such circumstances.

The Management Agreement was not negotiated on an arm's-length basis and the terms, including fees payable, may not be as favorable to us as if they were negotiated with an unaffiliated third party.

The Management Agreement that we entered into with ACM was negotiated between related parties, and we did not have the benefit of arm's-length negotiations of the type normally conducted with an unaffiliated third party. The terms of the Management Agreement, including fees payable, may not reflect the terms that we may have received if it were negotiated with an unrelated third party. In addition, we may choose not to enforce, or to enforce less vigorously, our rights under the Management Agreement because of our desire to maintain our ongoing relationship with ACM.

Members of our management team have competing duties to other entities, which could result in decisions that are not in the best interests of our stockholders.

Our executive officers and the employees of ACM do not spend all of their time managing our activities and our investment portfolio. Our executive officers and the employees of ACM allocate some, or a material portion, of their time to other businesses and activities. For example, each of our executive officers is also an officer of ARMOUR and an employee of ACM. None of these individuals is required to devote a specific amount of time to our affairs. As a result of these overlapping responsibilities, there may be conflicts of interest among and reduced time commitments from our officers and the officers of ARMOUR or employees of ACM that we will face in making investment decisions on our behalf. Accordingly, we will compete with ARMOUR and ACM, and their existing activities, other ventures and possibly other entities in the future for the time and attention of these officers.

In the future, we may enter, or ACM may cause us to enter, into additional transactions with ACM or its affiliates. In particular, we may purchase, or ACM may cause us to purchase, assets from ACM or its affiliates or make co-purchases alongside ACM or its affiliates. These transactions may not be the result of arm's length negotiations and may involve conflicts between our interests and the interests of ACM and/or its affiliates in obtaining favorable terms and conditions.

Federal Income Tax Risks

Rapid changes in the values of our target assets may make it more difficult for us to maintain our qualification as a REIT or our exemption from the 1940 Act.

If the market value or income potential of our MBS declines as a result of increased interest rates, prepayment rates, general market conditions, government actions or other factors, we may need to increase certain types of our assets and income or liquidate our non-qualifying assets to maintain our REIT qualifications or our exemption from the 1940 Act. If the decline in real estate asset values or income occurs quickly, this may be especially difficult to accomplish. We may have to make decisions that we otherwise would not make absent the REIT and the 1940 Act considerations.

Our qualification as a REIT subjects us to a broad array of financial and operating parameters that may influence our business and investment decisions and limit our flexibility in reacting to market developments.

In order to qualify and maintain our qualification as a REIT, we must, among other things, ensure:

- that at least 75% of our gross income each year is derived from certain real estate related sources;
- that at least 75% of the value of our assets consists of cash, cash items, government securities and qualified REIT real estate assets at the end of each calendar quarter;
- that the remainder of our investment in securities generally cannot include more than 10% of the outstanding voting securities of any one issuer, or more than 10% of the total value of the outstanding securities of any one issuer; and
- that no more than 5% of the value of our assets can consist of securities of any one issuer.

If we fail to comply with these requirements, we must dispose of a portion of our assets within 30 days after the end of the calendar quarter in order to avoid losing our REIT status and suffering adverse tax consequences. If we fail to qualify as a REIT, we will be subject to federal income tax as a regular corporation and may face substantial tax liability.

Qualification as a REIT involves the satisfaction of numerous requirements (some on an annual or quarterly basis) established under highly technical and complex provisions of the Code for which only a limited number of judicial or administrative interpretations exist. We believe we currently satisfy all the requirements of a REIT. However, the determination that we satisfy all REIT requirements requires an analysis of various factual matters and circumstances that may not be totally within our control. We have not requested and do not intend to request, a ruling from the IRS that we qualify as a REIT. Accordingly, we are not certain we will be able to qualify and remain qualified as a REIT for federal income tax purposes. Even a technical or inadvertent

mistake could jeopardize our REIT status. Furthermore, the U.S. Congress or the IRS might change tax laws or regulations and the courts might issue new rulings, in each case potentially having retroactive effect, which could make it more difficult or impossible for us to qualify as a REIT.

If we fail to qualify as a REIT in any tax year, then:

- we would be taxed as a regular domestic corporation, which, among other things, means that we would be unable to deduct distributions to stockholders in computing taxable income and would be subject to federal income tax on our taxable income at regular corporate rates;
- any resulting tax liability could be substantial and would reduce the amount of cash available for distribution to stockholders and could force us to liquidate assets at inopportune times, causing lower income or higher losses than would result if these assets were not liquidated; and
- any resulting tax liability could be substantial and would reduce the amount of cash available for distribution to stockholders and could force us to liquidate assets at inopportune times, causing lower income or higher losses than would result if these assets were not liquidated; and
- unless we were entitled to relief under applicable statutory provisions, we would be disqualified from treatment as a REIT for the subsequent four taxable years following the year during which we lost our qualification and thus, our cash available for distribution to our stockholders would be reduced for each of the years during which we do not qualify as a REIT.

Even if we qualify and remain qualified as a REIT, we may face other tax liabilities that reduce our cash flow.

Even if we qualify and remain qualified for taxation as a REIT, we may be subject to certain federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, excise taxes, state or local income, property and transfer taxes, such as mortgage recording taxes, and other taxes. In addition, in order to meet the REIT qualification requirements, prevent the recognition of certain types of non-cash income, or to avert the imposition of a 100% tax that applies to certain gains derived by a REIT from dealer property or inventory, we may hold some of our assets through a TRS or other subsidiary corporations that will be subject to corporate level income tax at regular rates. In addition, if we lend money to a TRS, the TRS may be unable to deduct all or a portion of the interest paid to us, which could result in an even higher corporate level tax liability. Any of these taxes would decrease cash available for distribution to our stockholders.

REIT distribution requirements could adversely affect our ability to execute our business plan.

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 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 non-deductible 4% excise tax if the actual amount that we pay out to our stockholders in a calendar year is less than 85% of our taxable income. We intend to make distributions to our stockholders to comply with the REIT requirements of the Code.

From time to time, we may generate taxable income greater than our income for financial reporting purposes prepared in accordance with GAAP, or differences in timing between the recognition of taxable income and the actual receipt of cash may occur. For example, we may be required to accrue income from MBS and other types of debt securities or interests in debt securities before we receive any payments of interest or principal on such assets. We may also acquire discounted debt investments that are subsequently modified by agreement with the borrower. If such arrangements constitute "significant modifications" of such debt under the applicable Treasury regulations, the modified debt may be considered to have been reissued to us in a debt-for-debt exchange with the borrower, with gain recognized by us to the extent that the principal amount of the modified debt exceeds our cost of purchasing it prior to modification.

As a result, we may find it difficult or impossible to meet distribution requirements in certain circumstances. In particular, where we experience differences in timing between the recognition of taxable income and the actual receipt of cash, the requirement to distribute a substantial portion of our taxable income could cause us to: (i) sell assets in adverse market conditions, (ii) borrow on unfavorable terms, (iii) distribute amounts that would otherwise be invested in future acquisitions, capital expenditures or repayment of debt, in order to comply with REIT requirements, or (iv) make taxable distributions of our capital stock or debt securities. These alternatives could increase our costs or reduce our equity. Thus, compliance with the REIT requirements may hinder our ability to grow, which could adversely affect the value of our common stock.

Complying with REIT requirements may cause us to forgo otherwise attractive opportunities.

To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts that we distribute to our stockholders and the ownership of our stock. We may be required to make distributions to stockholders at disadvantageous times or when we do not have funds readily available for distribution, and may be unable to pursue investments that would be otherwise advantageous to us in order to satisfy the source-of-income or asset-diversification requirements for qualifying as a REIT. In addition, in certain cases, the modification of a debt instrument or, potentially, an increase in the value of a debt instrument that we acquired at a significant discount, could result in the conversion of the instrument from a qualifying real estate asset to a wholly or partially non-qualifying asset that must be contributed to a TRS or disposed of in order for us to qualify or maintain our qualification as a REIT. Thus, compliance with the REIT requirements may hinder our ability to make and, in certain cases, to maintain ownership of, certain attractive investments.

Complying with REIT requirements may force us to liquidate otherwise attractive investments.

To qualify as a REIT, we must ensure that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified REIT real estate assets, including certain mortgage loans and certain kinds of MBS. The remainder of our investment in securities (other than government securities, TRSs and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities, TRSs and qualified real estate assets) can consist of the securities of any one issuer, and no more than 25% (20% for taxable years beginning after December 31, 2017) of the value of our total securities can be represented by securities of one or more TRSs. If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate from our investment portfolio otherwise attractive investments. For example, in certain cases, the modification of a debt instrument or, potentially, an increase in the value of a debt instrument that we acquired at a significant discount, could result in the conversion of the instrument from a qualifying real estate asset to a wholly or partially non-qualifying asset that must be liquidated in order for us to qualify or maintain our qualification as a REIT. These actions could have the effect of reducing our income and amounts available for distribution to our stockholders.

The failure of assets subject to repurchase agreements to qualify as real estate assets could adversely affect our ability to qualify as a REIT.

In order to finance some of our assets that we hold or acquire, we may enter into repurchase agreements, including with persons who sell us those assets. Under a repurchase agreement, we will nominally sell certain of our assets to a counterparty and simultaneously enter into an agreement to repurchase those sold assets. Although the tax treatment of repurchase transactions is unclear, we take the position that we are treated for U.S. federal income tax purposes as the owner of those assets that are the subject of any such repurchase agreement notwithstanding that we may transfer record ownership of those assets to the counterparty during the term of any such agreement. Because we enter into repurchase agreements the tax treatment of which is unclear, the IRS could assert, particularly in respect of our repurchase agreements with persons who sell us the assets that we wish to finance by way of repurchase agreements, that we did not own those assets during the term of the repurchase agreements, in which case we could fail to qualify as a REIT.

Our capital loss carry forward for tax purposes may expire before we can fully use it to offset otherwise taxable income or gains.

Capital losses may be carried forward for five taxable years and generally used to offset taxable net capital gains realized during the carry forward period. Net capital losses realized in 2013 and 2014 totaled \$(80,509) and \$(33,335) respectively, will be available to offset future capital gains realized through 2018 and 2019, respectively. For the year ended December 31, 2015, we had capital gains of \$6,419 offset by these amounts. Any capital loss carry forward that we have not used to offset otherwise taxable net capital gains will expire after the end of such five-year period, and will no longer be available to us. Our capital loss carry forward may expire before we can fully use it because, for example, we do not generate enough taxable net capital gains during that period. In the absence of offsetting net capital loss carry forward amounts, we will be required to make timely distributions of future net capital gains realized, or alternatively, pay U.S. federal income tax on such realized net capital gains not distributed.

We may be required to report taxable income for certain investments in excess of the economic income we ultimately realize from them.

We may acquire debt instruments in the secondary market for less than their face amount. The discount at which such debt instruments are acquired may reflect doubts about their ultimate collectability rather than current market interest rates. The amount of such discount will nevertheless generally be treated as “market discount” for federal income tax purposes. Accrued market discount is reported as income when, and to the extent that, any payment of principal of the debt instrument is made. If we collect less on the debt instrument than our purchase price plus the market discount we had previously reported as income, we may not be able to benefit from any offsetting loss deductions. Some of the debt instruments that we acquire may have been issued with original issue discount. We are required to report such original issue discount based on a constant yield method and will be taxed based on the assumption that all future projected payments due on such debt instruments will be made. If such debt instruments or MBS turn out not to be fully collectible, an offsetting loss deduction will become available only in the later year that uncollectability is provable.

In addition, we may acquire debt instruments that are subsequently modified by agreement with the borrower. If the amendments to the outstanding instrument are “significant modifications” under the applicable Treasury regulations, the modified instrument is considered to have been reissued to us in a debt-for-debt exchange with the borrower. In that event, we may be required to recognize taxable gain to the extent the principal amount of the modified instrument exceeds our adjusted tax basis in the unmodified instrument, even if the value of the instrument or the payment expectations have not changed. Following such a taxable modification, we would hold the modified loan with a cost basis equal to its principal amount for federal tax purposes.

Finally, in the event that any debt instruments acquired by us are delinquent as to mandatory principal and interest payments, or in the event payments with respect to a particular instrument are not made when due, we may nonetheless be required to continue to recognize the unpaid interest as taxable income as it accrues, despite doubt as to its ultimate collectability. Similarly, we may be required to accrue interest income with respect to debt instruments at its stated rate regardless of whether corresponding cash payments are received or are ultimately collectible. In each case, while we would in general ultimately have an offsetting loss deduction available to us when such interest was determined to be uncollectible, the utility of that deduction could depend on our having taxable income in that later year or thereafter.

Distributions to tax-exempt investors may be classified as unrelated business taxable income.

Neither ordinary nor capital gain distributions with respect to our common stock nor gain from the sale of common stock should generally constitute unrelated business taxable income to a tax-exempt investor. However, there are certain exceptions to this rule, including: (i) part of the income and gain recognized by certain qualified employee pension trusts with respect to our common stock may be treated as unrelated business taxable income if shares of our common stock are predominantly held by qualified employee pension trusts, and we are required to rely on a special look-through rule for purposes of meeting one of the REIT ownership tests, and we are not operated in a manner to avoid treatment of such income or gain as unrelated business taxable income; (ii) part of the income and gain recognized by a tax-exempt investor with respect to our common stock would constitute unrelated business taxable income if the investor incurs debt in order to acquire the common stock; (iii) part or all of the income or gain recognized with respect to our common stock by social clubs, voluntary employee benefit associations, supplemental unemployment benefit trusts and qualified group legal services plans which are exempt from federal income taxation under the Code may be treated as unrelated business taxable income; and (iv) to the extent that we are (or a part of us, or a disregarded subsidiary of ours, is) a “taxable mortgage pool,” or if we hold residual interests in a REMIC, a portion of the distributions paid to a tax-exempt stockholder that is allocable to excess inclusion income may be treated as unrelated business taxable income.

The “taxable mortgage pool” rules may increase the taxes that we or our stockholders may incur, and may limit the manner in which we effect future securitizations.

Securitizations could result in the creation of taxable mortgage pools for federal income tax purposes. As a REIT, so long as we own 100% of the equity interests in a taxable mortgage pool, we generally would not be adversely affected by the characterization of the securitization as a taxable mortgage pool. Certain categories of stockholders, however, such as foreign stockholders eligible for treaty or other benefits, stockholders with net operating losses and certain tax-exempt stockholders that are subject to unrelated business income tax, could be subject to increased taxes on a portion of their distribution income from us that is attributable to the taxable mortgage pool. In addition, to the extent that our stock is owned by tax-exempt “disqualified organizations,” such as certain government-related entities and charitable remainder trusts that are not subject to tax on unrelated business income, we may incur a corporate level tax on a portion of our income from the taxable mortgage pool. In that case, we will reduce the amount of our distributions to any disqualified organization whose stock ownership gave rise to the tax. Moreover, we would be precluded from selling equity interests in these securitizations to outside investors, or selling any debt securities

issued in connection with these securitizations that might be considered to be equity interests for tax purposes. These limitations may prevent us from using certain techniques to maximize our returns from securitization transactions.

We may incur excess inclusion income that would increase the tax liability of our stockholders or the Company.

In general, dividend income that a tax-exempt entity receives from us should not constitute unrelated business taxable income as defined in Section 512 of the Code. If we realize excess inclusion income and allocate it to stockholders, however, then this income would be fully taxable as unrelated business taxable income under Section 512 of the Code. If the stockholder is foreign, it would generally be subject to U.S. federal income tax withholding on this income without reduction pursuant to any otherwise applicable income tax treaty. U.S. stockholders would not be able to offset such income with their operating losses. If our stock is held in record name by “disqualified organizations” (generally government entities and certain tax-exempt investors, such as certain state pension plans and charitable remainder trusts, that are not subject to the tax on unrelated business taxable income), the Company must pay tax at the highest corporate rate on any excess inclusion income attributable to such disqualified organization investors. That tax would reduce our taxable REIT income.

We generally structure our borrowing arrangements in a manner designed to avoid generating significant amounts of excess inclusion income. However, excess inclusion income could result if we held a residual interest in a REMIC. Excess inclusion income also may be generated if we were to issue debt obligations with two or more maturities and the terms of the payments on these obligations bore a relationship to the payments that we received on our mortgage loans or MBS securing those debt obligations. For example, we may engage in non-REMIC CMO securitizations. We also enter into various repurchase agreements that have differing maturity dates and afford the lender the right to sell any pledged mortgage securities if we default on our obligations. These transactions may give rise to excess inclusion income that requires allocation among our stockholders. We may invest in equity securities of other REITs and it is possible that we might receive excess inclusion income from those investments. Some types of entities, including, without limitation, voluntarily employee benefit associations and entities that have borrowed funds to acquire their shares of our stock, may be required to treat a portion of or all of the dividends they receive from us as unrelated business taxable income.

To the extent we invest in construction loans, we may fail to qualify as a REIT if the IRS successfully challenges our estimates of the fair market value of land improvements that will secure those loans.

We may invest in construction loans, the interest from which will be qualifying income for purposes of the REIT income tests, provided that the loan value of the real property securing the construction loan is equal to or greater than the highest outstanding principal amount of the construction loan during any taxable year. For purposes of construction loans, the loan value of the real property is the fair market value of the land plus the reasonably estimated cost of the improvements or developments (other than personal property), which will secure the loan and which are to be constructed from the proceeds of the loan. There can be no assurance that the IRS would not successfully challenge our estimate of the loan value of the real property and our treatment of the construction loans for purposes of the REIT income and assets tests, which may cause us to fail to qualify as a REIT.

Liquidation of assets may jeopardize our REIT qualification or create additional tax liability for us.

To qualify as a REIT, we must comply with requirements regarding the composition of our assets and our sources of income. If we are compelled to liquidate our investments to repay obligations to our lenders, we may be unable to comply with these requirements, ultimately jeopardizing our qualification as a REIT, or we may be subject to a 100% tax on any resultant gain if we sell assets that are treated as dealer property or inventory.

The tax on prohibited transactions limits our ability to engage in transactions, including certain methods of securitizing mortgage loans, which would be treated as prohibited transactions for federal income tax purposes.

Net income that we derive from a prohibited transaction is subject to a 100% tax. The term “prohibited transaction” generally includes a sale or other disposition of property (including mortgage loans, but other than foreclosure property, as discussed below) that is held primarily for sale to customers in the ordinary course of a trade or business by us or by a borrower that has issued a shared appreciation mortgage or similar debt instrument to us. We might be subject to this tax if we were to dispose of or securitize loans in a manner that was treated as a prohibited transaction for federal income tax purposes.

We conduct our operations so that no asset that we own (or are treated as owning) will be treated as, or as having been, held for sale to customers, and that a sale of any such asset will not be treated as having been in the ordinary course of our business. As a result, we may choose not to engage in certain sales of loans at the REIT level, and may limit the structures we utilize for our securitization transactions, even though the sales or structures might otherwise be beneficial to us. In addition, whether property is held “primarily for sale to customers in the ordinary course of a trade or business” depends on the particular facts and

circumstances. No assurance can be given that any property that we sell will not be treated as property held for sale to customers, or that we can comply with certain safe-harbor provisions of the Code that would prevent such treatment. The 100% tax does not apply to gains from the sale of property that is held through a TRS or other taxable corporation, although such income will be subject to tax in the hands of the corporation at regular corporate rates. We structure our activities to avoid prohibited transaction characterization.

Complying with REIT requirements may force us to borrow to make distributions to our stockholders.

As a REIT, we must distribute at least 90% of our annual REIT taxable income (excluding net capital gains) to our stockholders. From time to time, we may generate taxable income greater than our net income for financial reporting purposes from, among other things, the non-taxable unrealized changes in the value of our derivatives, or our taxable income may be greater than our cash flow available for distribution to our stockholders. If we do not have other funds available in these situations, we may be unable to distribute 90% of our taxable income as required by the REIT rules. Thus, we could be required to borrow funds, sell a portion of our assets at disadvantageous prices or find another alternative source of funds. These alternatives could increase our costs or reduce our equity and reduce amounts available to invest in MBS.

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