CAPSTEAD MORTGAGE CORP
Form 10-Q
August 08, 2016

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: June 30, 2016

OR

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

For the transition period from ____________ to ______________

Commission File Number: 001-08896

CAPSTEAD MORTGAGE CORPORATION
(Exact name of Registrant as specified in its Charter)

Maryland	75-2027937
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

8401 North Central Expressway, Suite 800, Dallas, TX	75225-4404
(Address of principal executive offices)	(Zip Code)

(214) 874-2323
(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 website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

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

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock ($0.01 par value) 95,988,971 as of August 8, 2016

CAPSTEAD MORTGAGE CORPORATION
FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2016

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PART I. ¾ FINANCIAL INFORMATION

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ITEM 1. FINANCIAL STATEMENTS

PART I. ¾ FINANCIAL INFORMATION

CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED BALANCE SHEETS
(in thousands, except pledged and per share amounts)

	June 30, 2016 (unaudited)	December 31, 2015
Assets		
Residential mortgage investments ($13.48 and $13.54 billion pledged at June 30, 2016 and December 31, 2015, respectively)	$ 13,901,543	$ 14,154,737
Cash collateral receivable from interest rate swap counterparties	93,170	50,193
Interest rate swap agreements at fair value	24	7,720
Cash and cash equivalents	129,171	54,185
Receivables and other assets	179,449	179,531
	$ 14,303,357	$ 14,446,366
Liabilities		
Secured borrowings	$ 12,802,629	$ 12,958,394
Interest rate swap agreements at fair value	62,003	26,061
Unsecured borrowings	98,040	97,986
Common stock dividend payable	22,738	25,979
Accounts payable and accrued expenses	36,825	39,622
	13,022,235	13,148,042
Stockholders' equity		
Preferred stock - $0.10 par value; 100,000 shares authorized: 7.50% Cumulative Redeemable Preferred Stock, Series E, 8,204 and 8,156 shares issued and outstanding ($205,107 and $203,902 aggregate liquidation preferences) at June 30, 2016 and December 31, 2015, respectively	198,331	197,172
Common stock - $0.01 par value; 250,000 shares authorized: 95,947 and 95,825 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively	959	958
Paid-in capital	1,305,893	1,310,563
Accumulated deficit	(346,464)	(346,464)
Accumulated other comprehensive income	122,403	136,095
	1,281,122	1,298,324
	$ 14,303,357	$ 14,446,366

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)
(unaudited)

	Quarter Ended June 30		Six Months Ended June 30	
	2016	2015	2016	2015
Interest income:				
Residential mortgage investments	$53,309	$50,341	$112,809	$108,986
Other	128	99	320	193
	53,437	50,440	113,129	109,179
Interest expense:				
Secured borrowings	(27,014)	(20,098)	(53,596)	(39,312)
Unsecured borrowings	(1,976)	(2,122)	(3,953)	(4,245)
	(28,990)	(22,220)	(57,549)	(43,557)
	24,447	28,220	55,580	65,622
Other revenue (expense):				
Compensation-related expense	(2,042)	(2,160)	(5,266)	(4,509)
Other general and administrative expense	(1,157)	(1,170)	(2,326)	(2,319)
Miscellaneous other revenue	382	54	995	107
	(2,817)	(3,276)	(6,597)	(6,721)
Net income	$21,630	$24,944	$48,983	$58,901
Net income available to common stockholders:				
Net income	$21,630	$24,944	$48,983	$58,901
Less preferred stock dividends	(3,843)	(3,788)	(7,669)	(7,530)
	$17,787	$21,156	$41,314	$51,371
Net income per common share:				
Basic and diluted	$0.19	$0.22	$0.43	$0.54
Weighted average common shares outstanding:				
Basic	95,648	95,501	95,631	95,485
Diluted	95,786	95,689	95,766	95,682
Cash dividends declared per share:				
Common	$0.23	$0.31	$0.49	$0.62
Series E Preferred	0.47	0.47	0.94	0.94

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands, unaudited)

	Quarter Ended June 30		Six Months Ended June 30	
	2016	2015	2016	2015
Net income	$21,630	$24,944	$48,983	$58,901
Other comprehensive income (loss)				
Amounts related to available-for-sale securities:				
Change in net unrealized gains	16,917	(18,747)	29,400	(12,640)
Amounts related to cash flow hedges:				
Change in net unrealized losses	(22,145)	3,400	(54,272)	(14,991)
Reclassification adjustment for amounts included in net income	5,826	6,863	11,180	13,311
	598	(8,484)	(13,692)	(14,320)
Comprehensive income	$22,228	$16,460	$35,291	$44,581

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands, unaudited

	Six Months Ended June 30	
	2016	2015
Operating activities:		
Net income	$48,983	$58,901
Noncash items:		
Amortization of investment premiums	59,063	58,135
Amortization of equity-based awards	1,189	1,066
Other depreciation and amortization	66	66
Change in measureable hedge ineffectiveness related to interest rate swap agreements designated as cash flow hedges	546	26
Net change in receivables, other assets, accounts payable and accrued expenses	(781)	7,497
Net cash provided by operating activities	109,066	125,691
Investing activities:		
Purchases of residential mortgage investments	(1,512,737)	(1,936,354)
Interest receivable acquired with the purchase of residential mortgage investments	(1,977)	(3,027)
Principal collections on residential mortgage investments, including changes in mortgage securities principal remittance receivable	1,706,266	1,603,206
Redemption of Federal Home Loan Bank stock	30,000	–
Net cash provided by (used in) investing activities	221,552	(336,175)
Financing activities:		
Proceeds from repurchase arrangements and similar borrowings	60,553,581	58,392,825
Principal payments on repurchase arrangements and similar borrowings	(58,584,344)	(58,232,051)
Proceeds from other secured borrowings	1,175,000	–
Principal payments on other secured borrowings	(3,300,000)	–
Increase in cash collateral receivable from interest rate swap counterparties	(42,977)	(187)
Proceeds from issuance of preferred shares	1,167	11,531
Other capital stock transactions	(57)	(429)
Dividends paid	(58,002)	(70,131)
Net cash (used in) provided by financing activities	(255,632)	101,558
Net change in cash and cash equivalents	74,986	(108,926)
Cash and cash equivalents at beginning of period	54,185	307,526
Cash and cash equivalents at end of period	$129,171	$198,600

See accompanying notes to consolidated financial statements.

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CAPSTEAD MORTGAGE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2016
(unaudited)

NOTE 1 ¾ BUSINESS

Capstead Mortgage Corporation operates as a self-managed real estate investment trust for federal income tax purposes (a “REIT”) and is based in Dallas, Texas. Unless the context otherwise indicates, Capstead Mortgage Corporation, together with its subsidiaries, is referred to as “Capstead” or the “Company.” Capstead earns income from investing in a leveraged portfolio of residential mortgage pass-through securities consisting almost exclusively of adjustable-rate mortgage (“ARM”) securities issued and guaranteed by government-sponsored enterprises, either Fannie Mae, Freddie Mac, or by an agency of the federal government, Ginnie Mae. Residential mortgage pass-through securities guaranteed by Fannie Mae, Freddie Mac or Ginnie Mae are referred to as “Agency Securities” and are considered to have limited, if any, credit risk.

NOTE 2 ¾ BASIS OF PRESENTATION

Interim Financial Reporting

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the quarter and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the calendar year ending December 31, 2016. For further information refer to the audited consolidated financial statements and footnotes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2015.

Recent Accounting Pronouncements

In November 2014 the Financial Accounting Standards Board issued ASU 2014-16, Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity (“ASU 2014-16”). ASU 2014-16 provides guidance in evaluating whether the nature of the host contract is more debt-like or equity-like when determining whether derivative financial instruments embedded in the hybrid financial instrument, such as call rights and conversion features, should be bifurcated and accounted for separately. The Company adopted ASU 2014-16 on January 1, 2016. The provisions of this ASU had no effect on the Company’s results of operations, financial condition, or cash flows.

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NOTE 3 ¾ NET INCOME PER COMMON SHARE

Basic net income per common share is computed by dividing net income, after deducting dividends paid or accrued on preferred stock and allocating earnings to equity awards deemed to be participating securities pursuant to the two-class method, by the average number of shares of common stock outstanding, calculated excluding unvested stock awards. Participating securities include unvested equity awards that contain non-forfeitable rights to dividends prior to vesting.

Diluted net income per common share is computed by dividing the numerator used to compute basic net income per common share by the denominator used to compute basic net income per common share, further adjusted for the dilutive effect, if any, of equity awards and shares of preferred stock when and if convertible into shares of common stock. Shares of the Company's 7.50% Series E Cumulative Redeemable Preferred Stock are contingently convertible into shares of common stock only upon the occurrence of a change in control and therefore are not considered dilutive securities absent such an occurrence. Any unvested equity awards that are deemed participating securities are included in the calculation of diluted net income per common share, if dilutive, under either the two-class method or the treasury stock method, depending upon which method produces the more dilutive result. Components of the computation of basic and diluted net income per common share were as follows for the indicated periods (dollars in thousands, except per share amounts):

	Quarter Ended June 30		Six Months Ended June 30	
	2016	2015	2016	2015
Basic net income per common share				
Numerator for basic net income per common share:				
Net income	$21,630	$24,944	$48,983	$58,901
Preferred stock dividends	(3,843)	(3,788)	(7,669)	(7,530)
Earnings participation of unvested equity awards	(39)	(33)	(83)	(67)
	$17,748	$21,123	$41,231	$51,304
Denominator for basic net income per common share:				
Average number of shares of common stock outstanding	95,947	95,805	95,930	95,815
Average unvested stock awards outstanding	(299)	(304)	(299)	(330)
	95,648	95,501	95,631	95,485
	$0.19	$0.22	$0.43	$0.54
Diluted net income per common share				
Numerator for diluted net income per common share:				
Numerator for basic net income per common share	$17,748	$21,123	$41,231	$51,304
Denominator for diluted net income per common share:				
Denominator for basic net income per common share	95,648	95,501	95,631	95,485
Net effect of dilutive equity awards	138	188	135	197
	95,786	95,689	95,766	95,682
	$0.19	$0.22	$0.43	$0.54

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NOTE 4 ¾ RESIDENTIAL MORTGAGE INVESTMENTS

Residential mortgage investments classified by collateral type and interest rate characteristics as of the indicated dates were as follows (dollars in thousands):

	Unpaid Principal Balance	Investment Premiums	Amortized Cost Basis	Carrying Amount [(a)]	Net WAC [(b)]	Average Yield [(b)]
June 30, 2016						
Agency Securities:						
Fannie Mae/Freddie Mac:						
Fixed-rate	$448	$1	$449	$449	6.73 %	5.75 %
ARMs	10,068,818	319,152	10,387,970	10,555,529	2.65	1.63
Ginnie Mae ARMs	3,217,374	107,108	3,324,482	3,340,852	2.56	1.27
	13,286,640	426,261	13,712,901	13,896,830	2.63	1.54
Residential mortgage loans:						
Fixed-rate	824	1	825	825	6.76	4.09
ARMs	2,114	9	2,123	2,123	3.82	2.80
	2,938	10	2,948	2,948	4.64	3.16
Collateral for structured financings	1,736	29	1,765	1,765	8.12	7.67
	$13,291,314	$426,300	$13,717,614	$13,901,543	2.63	1.54
December 31, 2015						
Agency Securities:						
Fannie Mae/Freddie Mac:						
Fixed-rate	$796	$2	$798	$799	6.61 %	6.17 %
ARMs	10,014,401	317,545	10,331,946	10,487,785	2.55	1.68
Ginnie Mae ARMs	3,542,541	119,225	3,661,766	3,660,455	2.61	1.49
	13,557,738	436,772	13,994,510	14,149,039	2.57	1.63
Residential mortgage loans:						
Fixed-rate	1,155	1	1,156	1,156	6.76	5.02
ARMs	2,650	11	2,661	2,661	3.73	3.15
	3,805	12	3,817	3,817	4.65	3.71
Collateral for structured financings	1,850	31	1,881	1,881	8.12	7.82
	$13,563,393	$436,815	$14,000,208	$14,154,737	2.57	1.63

(a) Includes unrealized gains and losses for residential mortgage investments classified as available-for-sale.

(b) Net WAC, or weighted average coupon, is the weighted average interest rate of the mortgage loans underlying the indicated investments net of servicing and other fees as of the indicated balance sheet date. Net WAC is expressed as a percentage calculated on an annualized basis on the unpaid principal balances of the mortgage loans underlying these investments. Average yield is presented for the quarter then ended, and is based on the cash component of interest income expressed as a percentage calculated on an annualized basis on average amortized cost basis (the "cash yield") less the effects of amortizing investment premiums. Investment premium amortization is determined using the interest method and incorporates actual and anticipated future mortgage prepayments.

Agency Securities are considered to have limited, if any, credit risk because the timely payment of principal and interest is guaranteed by Fannie Mae and Freddie Mac, which are federally chartered corporations, or Ginnie Mae, which is an agency of the federal government. Residential mortgage loans held by Capstead were originated prior to 1995 when the Company operated a mortgage conduit and the related credit risk is borne by the Company. Collateral for structured financings consists of private residential mortgage securities that are backed by loans obtained through this mortgage conduit and are pledged to secure repayment of related structured financings. Credit risk for these securities is borne by the related bondholders. The maturity of Residential mortgage investments is directly affected by prepayments of principal on the underlying mortgage loans. Consequently, actual maturities will be significantly shorter than the portfolio's weighted average contractual maturity of 289 months.

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Fixed-rate investments consist of residential mortgage loans and Agency Securities backed by residential mortgage loans with fixed rates of interest. Adjustable-rate investments generally are ARM Agency Securities backed by residential mortgage loans that have coupon interest rates that adjust at least annually to more current interest rates or begin doing so after an initial fixed-rate period. After the initial fixed-rate period, if applicable, mortgage loans underlying ARM securities typically either (i) adjust annually based on specified margins over the one-year London interbank offered rate ("LIBOR") or the one-year Constant Maturity U.S. Treasury Note Rate ("CMT"), (ii) adjust semiannually based on specified margins over six-month LIBOR, or (iii) adjust monthly based on specified margins over indices such as one-month LIBOR, the Eleventh District Federal Reserve Bank Cost of Funds Index, or over a rolling twelve month average of the one-year CMT index, usually subject to periodic and lifetime limits, or caps, on the amount of such adjustments during any single interest rate adjustment period and over the contractual term of the underlying loans.

Capstead classifies its ARM investments based on average number of months until coupon reset ("months to roll"). Months to roll is an indicator of asset duration which is a measure of market price sensitivity to interest rate movements. A shorter duration generally indicates less interest rate risk. Current-reset ARM investments have months to roll of less than 18 months while longer-to-reset ARM investments have months to roll of 18 months or greater. As of June 30, 2016, the average months to roll for the Company's $7.84 billion (amortized cost basis) in current-reset ARM investments was 6.1 months while the average months to roll for the Company's $5.88 billion (amortized cost basis) in longer-to-reset ARM investments was 42.2 months.

NOTE 5 ¾ SECURED BORROWINGS

Capstead pledges its Residential mortgage investments as collateral for secured borrowings primarily in the form of repurchase arrangements with commercial banks and other financial institutions. In August 2015 the Company began supplementing its borrowings under repurchase arrangements with advances from the Federal Home Loan Bank ("FHLB") of Cincinnati (collectively referred to as "counterparties" or "lending counterparties"). Repurchase arrangements entered into by the Company involve the sale and a simultaneous agreement to repurchase the transferred assets at a future date and are accounted for as financings. The Company maintains the beneficial interest in the specific securities pledged during the term of each repurchase arrangement and receives the related principal and interest payments. FHLB advances differ from repurchase arrangements in that Capstead pledges collateral to the bank to secure each such advance rather than transferring ownership of the pledged collateral to the bank and simultaneously agreeing to repurchase the transferred assets at a future date. On January 12, 2016 the FHLB system regulator finalized rules originally proposed in 2014 that generally preclude captive insurers from remaining members beyond February 19, 2017 with transition rules that require outstanding advances to be repaid upon maturity or by that date. In response to this action, the Company has reduced outstanding FHLB advances to $750 million as of June 30, 2016 and anticipates migrating remaining balances away from the FHLB by November 2016. FHLB stock held by the Company in connection with advance activity was reduced by $30.0 million during the first quarter and the remaining $30.0 million held at June 30, 2016 is expected to be redeemed by December 31, 2016.

The terms and conditions of secured borrowings are negotiated on a transaction-by-transaction basis when each such borrowing is initiated or renewed. The amount borrowed is generally equal to the fair value of the securities pledged, as determined by the lending counterparty, less an agreed-upon discount, referred to as a "haircut." Interest rates are generally fixed based on prevailing rates corresponding to the terms of the borrowings. Interest may be paid monthly or at the termination of a borrowing at which time the Company may enter into a new borrowing at prevailing haircuts and rates with the same lending counterparty or repay that counterparty and negotiate financing with a different lending counterparty. None of the Company's lending counterparties are obligated to renew or otherwise enter into new borrowings at the conclusion of existing borrowings. In response to declines in fair value of pledged securities due to changes in market conditions or the publishing of monthly security pay-down factors, lending counterparties typically require the Company to post additional securities as collateral, pay down borrowings or fund cash margin accounts with the counterparties in order to re-establish the agreed-upon collateral requirements. These actions are referred to as margin calls. Conversely, in response to increases in fair value of pledged securities, the Company routinely margin calls its lending counterparties in order to have previously pledged collateral returned.

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Secured borrowings (and related pledged collateral, including accrued interest receivable), classified by collateral type and remaining maturities, and related weighted average borrowing rates as of the indicated dates were as follows (dollars in thousands):

Collateral Type	Collateral Carrying Amount	Accrued Interest Receivable	Borrowings Outstanding	Average Borrowing Rates	
June 30, 2016					
Borrowings under repurchase arrangements with maturities of 30 days or less:					
Agency Securities	$11,881,413	$ 25,232	$11,092,153	0.66	%
Borrowings under repurchase arrangements with maturities greater than 30 days:					
Agency Securities (31 to 90 days)	738,471	1,556	408,711	0.72	
Agency Securities (greater than 90 days)	82,555	377	550,000	0.82	
Similar borrowings:					
Collateral for structured financings	1,765	–	1,765	8.12	
	12,704,204	27,165	12,052,629		
FHLB advances	775,991	3,218	750,000	0.64	
	$13,480,195	$ 30,383	$12,802,629	0.67	
Quarter-end borrowing rates adjusted for effects of related derivative financial instruments (Derivatives) held as cash flow hedges				0.84	
December 31, 2015					
Borrowings under repurchase arrangements with maturities of 30 days or less:					
Agency Securities	$9,080,363	$ 18,504	$8,585,336	0.67	%
Borrowings under repurchase arrangements with maturities greater than 30 days:					
Agency Securities (31 to 90 days)	423,710	861	346,177	0.63	
Agency Securities (greater than 90 days)	1,073,254	2,519	1,150,000	0.75	
Similar borrowings:					
Collateral for structured financings	1,881	–	1,881	8.12	
	10,579,208	21,884	10,083,394		
FHLB advances	2,956,908	11,422	2,875,000	0.43	
	$13,536,116	$ 33,306	$12,958,394	0.62	
Year-end borrowing rates adjusted for effects of related Derivatives held as cash flow hedges				0.85	

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Average secured borrowings outstanding during the indicated periods differed from respective ending balances primarily due to changes in portfolio levels and differences in the timing of portfolio acquisitions relative to portfolio runoff as illustrated below (dollars in thousands):

	Quarter Ended			
	June 30, 2016		December 31, 2015	
	Average Borrowings	Average Rate	Average Borrowings	Average Rate
Average borrowings and rates adjusted for the effects of related Derivatives held as cash flow hedges for the indicated periods	$12,866,495	0.84 %	$13,160,703	0.73 %

NOTE 6 ¾ USE OF DERIVATIVES, OFFSETTING DISCLOSURES AND CHANGES IN OTHER COMPREHENSIVE INCOME BY COMPONENT

In addition to entering into longer-maturity secured borrowings when available at attractive rates and terms, Capstead attempts to mitigate exposure to higher interest rates by entering into currently-paying and forward-starting, one-month LIBOR-indexed, pay-fixed, receive-variable, interest rate swap agreements. These Derivatives are designated as cash flow hedges of the variability of the underlying benchmark interest rate of current and forecasted 30- to 90-day secured borrowings. This hedge relationship establishes a relatively stable fixed rate on related borrowings because the variable-rate payments received on the swap agreements offset a significant portion of the interest accruing on the designated borrowings, leaving the fixed-rate swap payments as the Company's effective borrowing rate, subject to certain adjustments. These adjustments include differences between variable-rate payments received on the swap agreements and related unhedged borrowing rates as well as the effects of measured hedge ineffectiveness. Additionally, changes in fair value of these Derivatives tend to partially offset opposing changes in fair value of the Company's residential mortgage investments that can occur in response to changes in market interest rates.

During the quarter and six months ended June 30, 2016 Capstead entered into swap agreements with notional amounts of $950 million and $2.45 billion requiring fixed-rate interest payments averaging 0.78% and 0.75% for two and three-year periods commencing on various dates between January 2016 and June 2016. Also during the quarter and six months ended June 30, 2016, $1.10 billion and $2.80 billion notional amount of swaps requiring fixed-rate interest payments averaging 0.47% and 0.50% matured. At June 30, 2016, the Company's portfolio financing-related swap positions had the following characteristics (dollars in thousands):

Period of Contract Expiration	Notional Amount	Average Fixed-Rate Payment Requirement
Third quarter 2016 (expired July 1, 2016)	$700,000	0.56 %
Fourth quarter 2016	800,000	0.66
First quarter 2017	1,000,000	0.72
Second quarter 2017	900,000	0.74
Third quarter 2017	400,000	0.74
Fourth quarter 2017	1,500,000	0.79
First quarter 2018	1,700,000	0.76
Second quarter 2018	600,000	0.79
Second quarter 2019	450,000	0.77
	$8,050,000	

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In 2010 the Company entered into forward-starting, three-month LIBOR-indexed, pay-fixed, receive-variable, interest rate swap agreements with notional amounts totaling $100 million and average fixed rates of 4.09% with 20-year payment terms coinciding with the floating-rate terms of the Company's Unsecured borrowings. These Derivatives are designated as cash flow hedges of the variability of the underlying benchmark interest rate associated with the floating-rate terms of these long-term borrowings.

Interest rate swap agreements are measured at fair value on a recurring basis primarily using Level Two Inputs in accordance with ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820). In determining fair value estimates for these Derivatives, Capstead utilizes the standard methodology of netting the discounted future fixed cash payments and the discounted future variable cash receipts which are based on expected future interest rates derived from observable market interest rate curves. The related net interest payable at the balance sheet date is recorded separately. The Company also incorporates both its own nonperformance risk and its counterparties' nonperformance risk in determining fair value. In considering the effect of nonperformance risk, the Company considered the impact of netting and credit enhancements, such as collateral postings and guarantees, and has concluded that counterparty risk is not significant to the overall valuation. The following tables include fair value and other related disclosures regarding all Derivatives held as of and for the indicated periods (in thousands):

	Balance Sheet Location	June 30 2016	December 31 2015
Balance sheet-related			
Swap agreements in a gain position (an asset) related to			
Secured borrowings	(a)	$24	$ 7,720
Swap agreements in a loss position (a liability) related to:			
Secured borrowings	(a)	(20,963)	(1,051)
Unsecured borrowings	(a)	(41,040)	(25,010)
Related net interest payable	(b)	(14,320)	(10,942)
		$(76,299)	$ (29,283)

(a) The fair value of Derivatives with unrealized gains are aggregated and recorded as an asset on the face of the Balance Sheets separately from the fair value of Derivatives with unrealized losses that are recorded as a liability. The amount of net unrealized losses scheduled to be recognized in the Statements of Income over the next twelve months primarily in the form of fixed-rate swap payments in excess of current market rates totaled $19.9 million at June 30, 2016.

(b) Included in "Accounts payable and accrued expenses" on the face of the Balance Sheets.

	Location of Gain or (Loss) Recognized in Net Income	Quarter Ended June 30 2016	Quarter Ended June 30 2015	Six Months Ended June 30 2016	Six Months Ended June 30 2015
Income statement-related					
Components of effect on interest expense:					
Amount of loss reclassified from Accumulated other comprehensive income related to the effective portion of active positions		$(5,826)	$(6,863)	$(11,180)	$(13,311)
Amount of gain (loss) recognized (ineffective portion)		(239)	3	(887)	(306)

Increase in interest expense and decrease in Net income as a result of the use of Derivatives	*	$(6,065)	$(6,860)	$(12,067)	$(13,617)
Other comprehensive income-related					
Amount of gain (loss) recognized in Other comprehensive income (loss) (effective portion)		$(22,145)	$3,400	$(54,272)	$(14,991)

*Included in "Interest expense: Secured borrowings" on the face of the Statements of Income.

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Capstead's swap agreements and borrowings under repurchase arrangements are subject to master netting arrangements in the event of default on, or termination of, any one contract. See NOTE 5 for more information on the Company's use of secured borrowings. The following tables provide disclosures concerning offsetting of financial liabilities and Derivatives as of the indicated dates (in thousands):

Offsetting of Derivative Assets

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet [(a)] Financial Instruments	Cash Collateral Received	Net Amount
June 30, 2016						
Counterparty 4	$–	$ 24	$ 24	$ (24)	$ –	$ –
December 31, 2015						
Counterparty 2	$–	$ 23	$ 23	$ (23)	$ –	$ –
Counterparty 4	4,758	2,939	7,697	(7,697)	–	–
	$4,758	$ 2,962	$ 7,720	$ (7,720)	$ –	$ –

Offsetting of Financial Liabilities and Derivative Liabilities

	Gross Amounts of Recognized Liabilities [(b)]	Gross Amounts Offset in the Balance Sheet	Net Amounts of Liabilities Presented in the Balance Sheet [(a)]	Gross Amounts Not Offset in the Balance Sheet [(c)] Financial Instruments	Cash Collateral Pledged	Net Amount
June 30, 2016						
Derivatives by counterparty:						
Counterparty 1	$41,307	$ –	$41,307	$–	$(41,307)	$ –
Counterparty 4	34,992	24	35,016	(24)	(34,992)	–
	76,299	24	76,323	(24)	(76,299)	–
Borrowings under repurchase arrangements	12,058,624	–	12,058,624	(12,058,624)	–	–
	$12,134,923	$ 24	$12,134,947	$(12,058,648)	$(76,299)	$ –
December 31, 2015						
Derivatives by counterparty:						
Counterparty 1	$26,311	$ –	$26,311	$–	$(26,311)	$ –
Counterparty 2	776	23	799	(23)	(776)	–
Counterparty 4	6,954	2,939	9,893	(7,697)	(2,196)	–
	34,041	2,962	37,003	(7,720)	(29,283)	–
Borrowings under repurchase arrangements	10,090,846	–	10,090,846	(10,090,846)	–	–
	$10,124,887	$ 2,962	$10,127,849	$(10,098,566)	$(29,283)	$ –

(a) Amounts presented are limited to recognized liabilities and cash collateral received associated with the indicated counterparty sufficient to reduce the related Net Amount to zero in accordance with ASU No. 2011-11, as amended by ASU No. 2013-01.

(b) Amounts include accrued interest of $14.3 million and $10.9 million on interest rate swap agreements and $7.8 million and $9.3 million on borrowings under repurchase arrangements, included in "Accounts payable and accrued expenses” on the face of the Balance Sheets as of June 30, 2016 and December 31, 2015, respectively.

(c) Amounts presented are limited to recognized assets and collateral pledged associated with the indicated counterparty sufficient to reduce the related Net Amount to zero in accordance with ASU No. 2011-11, as amended by ASU No. 2013-01.

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Changes in Accumulated other comprehensive income by component for the quarter and six months ended June 30, 2016 were as follows (in thousands):

	Gains and Losses on Cash Flow Hedges	Unrealized Gains and Losses on Available-for-Sale Securities	Total
Balance at March 31, 2016	$ (45,207)	$ 167,012	$121,805
Activity for the quarter ended June 30, 2016:			
Other comprehensive income (loss) before reclassifications	(22,145)	16,917	(5,228)
Amounts reclassified from accumulated other comprehensive income	5,826	–	5,826
Other comprehensive income (loss)	(16,319)	16,917	598
Balance at June 30, 2016	$ (61,526)	$ 183,929	$122,403
Balance at December 31, 2015	$ (18,434)	$ 154,529	$136,095
Activity for the six months ended June 30, 2016:			
Other comprehensive income (loss) before reclassifications	(54,272)	29,400	(24,872)
Amounts reclassified from accumulated other comprehensive income	11,180	–	11,180
Other comprehensive income (loss)	(43,092)	29,400	(13,692)
Balance at June 30, 2016	$ (61,526)	$ 183,929	$122,403

NOTE 7 ¾ UNSECURED BORROWINGS

Unsecured borrowings consist of 30-yea