


# PennyMac Mortgage Investment Trust

## Second Quarter 2022 Earnings Transcript

August 2, 2022

**Introduction**

Good afternoon, and welcome to the second quarter earnings discussion for PennyMac Mortgage Investment Trust. The slides that accompany this discussion are available on PennyMac Mortgage Investment Trust's website at www.pennymac-reit.com. Before we begin, let me remind you that our discussion contains forward-looking statements that are subject to the risks identified on Slide 2 that could cause our actual results to differ materially.

Now I'd like to introduce David Spector, PMT's Chairman and Chief Executive Officer, who will discuss the Company's second quarter 2022 results.

**Speaker:**

*David Spector – Chairman and Chief Executive Officer*

Thank you, Isaac.

PMT reported a net loss of 81.2 million dollars, or 88 cents per common share for the second quarter, as fair value declines in its credit sensitive strategies due to continued spread widening more than offset strong performance from its strategies excluding the impacts of market-driven fair value changes. Additionally, PMT recorded a tax expense related to fair value gains on its MSR assets in its taxable REIT subsidiary, which also impacted results.

PMT paid a common dividend of 47 cents per share. Book value per share decreased to 16 dollars and 59 cents from 17 dollars and 87 cents at the end of the prior quarter.

Dan Perotti, Senior Managing Director and Chief Financial Officer, will review additional details of PMT's financial performance later on in this discussion.

During the quarter, we repurchased 1.9 million shares of PMT's common stock for 28 million dollars at an average price of 14 dollars and 72 cents, significantly below current book value per share; and in July we repurchased an additional 510 thousand shares, for an approximate cost of 7.3 million dollars at 14 dollars and 30 cents per share.

One of PMT's greatest strengths is its ability to organically generate investments through our high-quality loan production sourced from correspondent sellers across the country. This quarter, 10.3 billion dollars in UPB of conventional correspondent production led to the creation of 171 million dollars in high-quality mortgage servicing rights.

Although current forecasts for 2022 total originations range from 2.4 to 2.8 trillion dollars primarily due to activity in the first half of the year, mortgage application indices point to further declines in the second half as the market reacts to the rapid increase in mortgage rates.

While we believe there is potential for these forecasts to decrease further, we believe PMT's leadership as the largest correspondent aggregator and

one of the largest producers of purchase-money loans in the country positions us well to execute over the long-term.

Now I'd like to turn the call over to Vandy Fartaj, Senior Managing Director and Chief Investment Officer, who will talk about potential investment opportunities, drivers of PMT's outlook and second quarter investment performance.

**Speaker:**

*Vandy Fartaj – Senior Managing Director and Chief Investment Officer*

Thank you, David.

The rapid shift in market interest rates and credit spreads created opportunities for PMT to make investments in addition to those normally created from its correspondent production activities. Although our ability to organically produce investments distinguishes PMT from most other public mortgage REITs, we also have the strong balance sheet and risk management capabilities necessary to deploy capital in investments from third parties when attractive opportunities arise.

Year to date, we have invested nearly 170 million dollars in these investments and continue to monitor the market for opportunities to deploy capital at attractive returns. We remain prudent and selectively deploying capital, given the currently volatile and uncertain mortgage landscape.

Turning to lender-based CRT, PMT is a leader in lender risk share transactions, with nearly 120 billion dollars in UPB of loans sold to Fannie

Mae from 2015 to 2020. While we are not currently delivering loans into CRT transactions, we are actively engaged in discussions with the GSEs regarding the potential resumption of lender risk share investments. We believe we are well-positioned to lead broadly on this effort given our history, platform and expertise. Because of the greater capital relief CRT provides the GSEs under the amended Enterprise Regulatory Capital Framework, and the additional private capital CRT provides to the housing ecosystem, we remain optimistic for the future of lender risk share. Most importantly, the alignment of interest as acquirer and servicer of the loans should be compelling for the GSEs, given we can work directly with our borrowers in times of hardship. While our ongoing discussions with the GSEs are encouraging, we have no further update on the potential resumption of our lender risk share transactions.

Let's now take a look at our potential returns across the investment portfolio. On slide 6 of our second quarter earnings presentation, we illustrate the run-rate return potential from PMT's investment strategies, which represents the average annualized return and quarterly earnings potential that PMT expects over the next four quarters. In total, we expect the quarterly run-rate return for PMT's strategies to average 40 cents per share or a 9.6 percent annualized return on common equity.

This run-rate potential reflects performance expectations in the highly-competitive, transitioning mortgage market. In our credit sensitive strategies, the potential return from PMT's organically created CRT

investments increased from last quarter, reflecting credit spreads that continued to widen.

In the interest rate sensitive strategies, we expect more consistent returns given slower prepayment speeds.

In correspondent production, the projected returns reflect our expectation for high levels of competition with low volumes and tight margins.

This analysis excludes potential contributions from additional opportunistic investments and opportunities under exploration, such as new investments in PMT's organically-created GSE CRT.

Our forecast for PMT's taxable income and liquidity continues to support the common dividend at its current level of 47 cents per share through the remainder of 2022; thereafter, the dividend level will be driven primarily by projections of PMT's earnings potential.

Now let's discuss the drivers of second quarter results in our Correspondent Production segment.

Total correspondent loan acquisition volume was 21 billion dollars in the second quarter. 49 percent, or 10.3 billion dollars were conventional loans and 51 percent, or 10.6 billion dollars were government loans.

Purchase volume was 82 percent of total acquisitions, up from 69 percent last quarter, demonstrating PMT's ability to quickly adapt in a transitioning mortgage environment.

Conventional lock volume in the second quarter was 11.1 billion dollars, up from the prior quarter as correspondents seek high-quality aggregators to sell loans servicing-released in the current environment. Our reputation in the industry and consistent commitment in the channel has provided our partners the stability and support they need to navigate the current environment.

PMT's correspondent production segment pretax income as a percentage of interest rate lock commitments was 9 basis points, up from 4 basis points in the prior quarter and the weighted average fulfillment fee rate in the second quarter was 20 basis points, up from 17 basis points in the prior quarter.

Acquisition volumes in July were 7 billion dollars, and locks were 6.8 billion dollars.

PMT's Interest Rate Sensitive strategies consist of our investments in MSRs sourced from our correspondent production, and investments in Agency MBS, non-Agency senior MBS and interest rate derivatives with offsetting interest rate exposure.

The fair value of PMT's MSR investments at the end of the second quarter was 3.7 billion dollars, up from 3.4 billion dollars at the end of the prior quarter. The increase reflects both newly originated MSRs resulting from conventional production volumes and fair value gains. The UPB of loans underlying PMT's MSR investments also continued to grow as new production more than offset runoff from prepayments.

Now I would like to discuss PMT's Credit Sensitive Strategies, which primarily consist of investments in organically-created CRT from PMT's production, investments in non-Agency subordinate bonds from private-label securitizations of PMT's production, and opportunistic investments in GSE CRT.

The total UPB of loans underlying PMT's organically-created CRT investments as of June 30th was 26.3 billion dollars, down 7 percent quarter-over-quarter. The fair value of our organically-created CRT investments at the end of the quarter was 1.3 billion dollars, down from 1.4 billion dollars at March 31st due to fair value decreases that resulted from market credit spread widening and prepayments.

The outlook for our current investments in organically-created CRT remains favorable, with a current weighted average loan-to-value ratio of 63 percent at June 30th, benefiting from the home price appreciation experienced in recent years. The 60-plus day delinquency rate underlying these organically-created GSE CRT investments continued to improve and declined to 1.31 percent at June 30th from 1.85 percent at March 31st.

PMT also purchased 39 million dollars in floating-rate CRT bonds issued by Fannie Mae and Freddie Mac during the quarter at attractive risk-adjusted returns.

We will continue to evaluate investments across the mortgage landscape and be prudent in the deployment of capital given the widening of market credit spreads and increased volatility.

Now I would like to turn the call over to Dan who will review our quarterly financial results.

**Speaker:**

*Daniel Perotti – Senior Managing Director and Chief Financial Officer*

Thank you Vandy.

PMT reports results through four segments: Credit Sensitive Strategies, which contributed 63.7 million dollars in pretax loss; Interest Rate Sensitive Strategies, which contributed 29.4 million dollars in pretax income; Correspondent Production, which contributed 9.8 million dollars in pretax income; and the Corporate segment, which had a pretax loss of 15.3 million dollars.

The losses on PMT's organically-created CRT investments this quarter totaled 49.8 million dollars. This amount included 67 million dollars in market-driven fair value losses, reflecting the impact of wider credit spreads. Losses on PMT's organically-created CRT investments also included 20.2 million dollars in realized gains and carry, 4.5 million dollars in net recoveries of previously-realized losses, primarily related to L Street Securities 2017-PM1, 2.4 million dollars in interest income on cash deposits, 9.7 million dollars of financing expenses, and 100 thousand dollars of expenses to assist certain borrowers in mitigating loan delinquencies they incurred as a result of dislocations arising from the COVID-19 pandemic.

PMT's interest rate sensitive strategies contributed income of 29.4 million dollars in the quarter. MSR fair value increased 220 million dollars during the quarter driven by higher mortgage rates, resulting in expectations for lower prepayment activity in the future. These fair values gains held in PMT's taxable REIT subsidiary resulted in a provision for tax expense of 31 million dollars.

The fair value of Agency MBS and interest rate hedges declined by 234 million dollars primarily driven by higher interest rates.

PMT's Correspondent Production segment contributed 9.8 million dollars of pretax income for the quarter.

PMT's Corporate segment includes interest income from cash and short-term investments, management fees and corporate expenses. The segment's contribution for the quarter was a pretax loss of 15.3 million dollars.

Excluding market-driven value changes, and the related tax impact, PMT reported 55.8 million dollars of net income across its strategies.

Successfully navigating a challenging mortgage environment requires a strong balance sheet, expertise in the capital markets and strong investment management and capital planning disciplines – areas we have been focused on for years. Our financing arrangements are critical to our business and we have worked diligently throughout our history to ensure that PMT has a solid capital structure and remains in a strong liquidity position.

PMT has 555 million dollars outstanding of exchangeable senior notes. With more than two years left until the first maturity of these notes, this financing provides low fixed coupons and depth to our capital structure.

This quarter we issued 305 million dollars in new 5-year term notes secured by Fannie Mae MSRs at favorable terms, bringing the total to 1.1 billion dollars. In addition to the secured term notes, PMT maintains substantial revolving bank financing structures which provide increased flexibility to support financing for fluctuating MSR and advance balances.

Similar to our MSR financing, we have maintained strong financing structures related to our CRT investments. Our first three CRT transactions, representing 7 percent of the total fair value, are currently financed by securities repurchase agreements, while the remainder, or 93 percent of the total fair value, is currently financed by secured term notes. Importantly, these term notes collateralized by our CRT transactions do not contain mark-to-market, or margin call provisions. This has served us extraordinarily well, as we are not obligated to post collateral for the majority of our CRT investments if fair values decline.

Looking towards upcoming maturities, although we expect to refinance the 450 million dollars of MSR term notes that mature next year, PMT has the ability to extend the maturity for an additional two years in the event of market dislocation. Similarly, with respect to upcoming maturities of CRT term notes, we expect to refinance these notes utilizing securities repurchase agreements or new term notes depending upon the market environment at the time. Again, in the event of market dislocation PMT also

has the ability to extend the maturity of many of its CRT term notes for two years as well.

As you can see, our risk governance emphasis provides a strong foundation to navigate the transitioning mortgage landscape with a diverse capital structure, low overall leverage, and 890 million dollars of available liquidity at June 30th.

And with that, I'll turn the discussion back over to David for some closing remarks.

**Speaker:**

*David Spector – Chairman and Chief Executive Officer*

Thank you, Dan.

The recent increase in spreads has improved our projected return potential for PMT's investment portfolio going forward and presents opportunities to prudently invest additional capital at attractive risk-adjusted returns. With our deep management team that has years of experience executing through mortgage cycles, a strong balance sheet, sophisticated financing structures and hedging strategies that mitigate volatility in book value and preserve a strong liquidity position, PMT is well-positioned to deliver attractive returns to its shareholders in the long term.

We encourage investors with any questions to reach out to our Investor Relations team by email or phone. Thank you.

**Operator:**

This concludes PennyMac Mortgage Investment Trust's second quarter earnings discussion. For any questions, please visit our website at www.pennymac-reit.com, or call our Investor Relations department at 818-224-7028. Thank you.