



PennyMac Mortgage Investment Trust

Fourth Quarter and Full-Year 2022 Earnings Transcript

February 2, 2023

Introduction

Good afternoon, and welcome to the fourth quarter and full year earnings discussion for PennyMac Mortgage Investment Trust. The slides that accompany this discussion are available on PennyMac Mortgage Investment Trust's website at pmt.pennymac.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 fourth quarter and full year 2022 results.

Speaker:

David Spector – Chairman and Chief Executive Officer

Thank you, Isaac.

For the fourth quarter 2022, PMT reported a net loss attributable to common shareholders of 5.8 million dollars, or 7 cents per common share, as solid income excluding the impacts of market-driven fair value changes was more than offset by fair value declines in PMT's interest rate and credit sensitive strategies.

PMT paid a common dividend of 40 cents per share. Book value per share decreased to 15 dollars and 78 cents from 16 dollars and 18 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, PMT repurchased 1.2 million shares of common stock for 14 million dollars at an average price of 11 dollars and 80 cents, significantly below current book value per share; and through January 31st PMT repurchased an additional 22 thousand shares, for an approximate cost of 278 thousand dollars at 12 dollars and 63 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, 6.8 billion dollars in UPB of PMT conventional correspondent production led to the creation of 127 million dollars in high-quality mortgage servicing rights.

With mortgage interest rates currently still above 6 percent, the most recent third-party forecasts for 2023 originations range from 1.6 to 1.9 trillion dollars, down meaningfully from 2022. While many industry participants have taken the appropriate steps to reduce capacity, it has been happening slowly and we believe overcapacity still remains. It is our expectation that mortgage REITs with diversified investment portfolios, efficient cost structures and strong risk management practices such as PMT are best-

positioned to manage through the volatility presented by the current market environment.

Although returns in PMT's credit sensitive strategies were impacted by wider market credit spreads in 2022, we have seen a material improvement in early 2023 which has driven improvements in structured product markets and which may generate additional attractive investment opportunities over time. The underlying fundamentals of our lender risk share investments remains strong, consisting of seasoned loans with a weighted average current loan to value of 53 percent, benefiting from the strong home price appreciation we have seen in recent years. With delinquency rates at pre-COVID levels and current strong employment data, recent realized losses on our CRT investments have been limited.

In our interest rate sensitive strategies, the fair value of PMT's MSRs increased as interest rates increased and prepayment speeds have fallen significantly. With increased visibility with respect to the Federal Reserve's projected terminal rate, we expect reduced volatility going forward for the segment. Additionally, higher short-term rates are expected to continue contributing to earnings from custodial balances and deposits in the coming quarters. Over the long-term, we believe the underlying performance of PMT's MSR portfolio will be strong, supported by PFSI's industry-leading servicing capabilities, workflows and proprietary technology.

Turning to correspondent production, though we expect volumes to remain constrained in the near term given the reduced forecasts for originations,

our customers are increasingly selling loans to stable capital partners like Pennymac as they seek to manage profitability and enhance liquidity. And with the exit of Wells Fargo from the channel, we expect to see additional opportunities for market share growth, largely driven by the smaller bank and community credit union sector of the market where Wells Fargo previously had a strong presence. With a strong capital base and consistent commitment to the channel, we believe PMT is well-positioned to continue leading as we provide our partners the stability and support they need to successfully navigate the current challenging mortgage market. We stand ready and able to absorb the volumes left by Wells Fargo's exit and remain committed to being a strong capital partner for independent mortgage companies throughout the country.

Now I'd like to turn the call over to Vandy Fartaj, Senior Managing Director and Chief Investment Officer, who will talk about the outlook for PMT and its fourth quarter investment performance.

Speaker:

Vandy Fartaj – Senior Managing Director and Chief Investment Officer

Thank you, David.

Let's now take a look at our potential returns across the investment portfolio. On slide 7 of our fourth 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 10 percent annualized return on common equity.

This run-rate potential reflects performance expectations in the current 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 fourth quarter.

In the interest rate sensitive strategies, we expect increased returns on MSRs due to low levels of expected prepayment speeds, offset by increased financing costs and decreasing MBS returns.

In correspondent production, our expectations are similar to the prior quarter due to the competitive production environment.

This analysis excludes potential contributions from additional opportunistic investments and opportunities under exploration, such as new credit sensitive investments or the introduction of new products.

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

Total correspondent loan acquisition volume was 20.8 billion dollars in the fourth quarter. 51 percent, or 10.7 billion dollars were conventional loans and 49 percent, or 10.1 billion dollars were government loans. As we mentioned last quarter, PMT began selling certain of its conventional

correspondent loan production to PFSI, which totaled 3.9 billion dollars in UPB.

Purchase volume was 93 percent of total acquisitions, up from 90 percent last quarter.

Conventional lock volume in the fourth quarter was 12.3 billion dollars, up 15 percent from the prior quarter. 4.8 billion dollars of these locks were for PFSI's account. In the first quarter, PMT will continue selling certain of its conventional correspondent loans to PFSI at cost plus a sourcing fee of one to two basis points.

PMT's correspondent production segment pretax income as a percentage of interest rate lock commitments was 9 basis points, up from 6 basis points in the prior quarter and the weighted average fulfillment fee rate was 18 basis points, unchanged from the prior quarter.

Acquisition volumes in January are estimated to be 6.8 billion dollars, and locks are estimated to be 6.1 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 fourth quarter was 4 billion dollars, up slightly from 3.9 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.

While delinquency rates for borrowers underlying PMT's MSR portfolio increased marginally from the prior quarter, they remain consistent with seasonal trends and our expectations for a conventional loan portfolio. Servicing advances outstanding for PMT's MSR portfolio increased to 178 million dollars at year end from 61 million dollars at September 30th due to seasonal property tax payments. No principal and interest advances are currently outstanding, as prepayment activity continues to sufficiently cover remittance obligations.

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 fair value of PMT's organically-created CRT investments as of December 31st was 1.1 billion dollars, down slightly from 1.2 billion dollars at September 30th primarily due to prepayments.

The outlook for our current investments in organically-created CRT remains favorable as David mentioned, with a current weighted average loan-to-value ratio of 53 percent. The 60-plus day delinquency rate underlying these

organically-created GSE CRT investments increased slightly to 1.25 percent at December 31st from 1.14 percent at September 30th.

We will continue to evaluate investments across the mortgage landscape and be prudent in the deployment of capital given current market conditions.

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 10.8 million dollars in pretax income; Interest Rate Sensitive Strategies, which contributed 9.3 million dollars in pretax loss; Correspondent Production, which contributed 7.1 million dollars in pretax income; and the Corporate segment, which had a pretax loss of 14.1 million dollars.

Income from PMT's organically-created CRT investments this quarter totaled 4.7 million dollars. This amount included 8.1 million dollars in market-driven fair value losses, reflecting the impact of wider credit spreads in the fourth quarter. Gains on PMT's organically-created CRT investments also included 17.8 million dollars in realized gains and carry, 1.2 million dollars of net realized losses recognized during the period, 11.7

million dollars in interest income on cash deposits, and 15.5 million dollars of financing expenses.

PMT's interest rate sensitive strategies contributed a loss of 9.3 million dollars in the quarter. MSR fair value increased 44 million dollars as prepayment speeds were lower than expected during the quarter and due to expectations for lower prepayment activity in the future. These fair value gains were more than offset by net interest rate hedge fair value declines, which drove a tax benefit of 10 million dollars.

The net fair value of Agency MBS, interest rate hedges and related tax impacts declined by 74 million dollars.

PMT's Correspondent Production segment contributed 7.1 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 14.1 million dollars.

Excluding market-driven value changes, and the related tax impact, PMT reported 39 million dollars of net income across its strategies.

We have maintained strong financing structures related to our MSR and CRT investments. With respect to PMT's 450 million dollars of MSR term notes maturing in April 2023, PMT has the option to extend the maturity for

2-years at its own discretion and is likely to do so given current market conditions.

Our first three CRT transactions, representing 7 percent of the total fair value, are currently financed by securities repurchase agreements. As we discussed last quarter, the CRT term notes financing a portion of our sixth CRT transaction that originally matured in December 2022 were settled and the underlying investment has also been financed by securities repurchase agreements with multiple banks. For our CRT investments financed by repurchase agreements, PMT holds an appropriate level of associated reserves for potential margin calls. Additionally, the maturity for the CRT term notes originally due in March of this year has been extended two years. The remainder of PMT's CRT investments are financed with term notes that 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. All CRT term notes contain the option to extend the maturity for 2 years at PMT's discretion, except 54 million dollars of term notes due in October 2024.

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

Speaker:

David Spector – Chairman and Chief Executive Officer

Thanks, Dan. While performance in recent periods has not met our expectations, relative performance over the long-term remains strong as

PMT's shareholder returns remain well-above comparable indices and its peer group. Additionally, we have seen a material improvement in credit markets in early 2023 as well as increased interest rate stability. With PMT's current portfolio of seasoned investments in credit risk transfer and hedged mortgage servicing rights, we remain confident in its ability to deliver attractive returns to its shareholders over 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 fourth quarter earnings discussion. For any questions, please visit our website at pmt.pennymac.com, or call our Investor Relations department at (818) 224-7028. Thank you.