CAPSTEAD MORTGAGE CORP
Form 10-Q
May 01, 2019

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, 2019

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 every Interactive Data File required to be submitted 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 such files). YES NO

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

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

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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) 85,580,126 as of May 1, 2019

CAPSTEAD MORTGAGE CORPORATION

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2019

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ITEM 1. FINANCIAL STATEMENTS

PART I. — FINANCIAL INFORMATION

CAPSTEAD MORTGAGE CORPORATION

CONSOLIDATED BALANCE SHEETS

(in thousands, except pledged and per share amounts)

	March 31, 2019 (unaudited)	December 31, 2018
Assets		
Residential mortgage investments ($11.82 and $11.57 billion pledged at March 31, 2019 and December 31, 2018, respectively)	$12,228,422	$11,965,381
Cash collateral receivable from interest rate swap counterparties	58,191	31,797
Derivative instruments at fair value	7,037	–
Cash and cash equivalents	32,433	60,289
Receivables and other assets	115,691	129,058
	$12,441,774	$12,186,525
Liabilities		
Secured borrowings	$11,222,451	$10,979,362
Derivative instruments at fair value	21,903	17,834
Unsecured borrowings	98,317	98,292
Common stock dividend payable	7,110	7,132
Accounts payable and accrued expenses	27,115	24,842
	11,376,896	11,127,462
Stockholders' equity		
Preferred stock - $0.10 par value; 100,000 shares authorized:		
7.50% Cumulative Redeemable Preferred Stock, Series E, 10,329 shares issued and outstanding ($258,226 aggregate liquidation preference) at March 31, 2019 and December 31, 2018	250,946	250,946
Common stock - $0.01 par value; 250,000 shares authorized:		
85,580 and 85,277 shares issued and outstanding at March 31, 2019 and December 31, 2018, respectively	856	853
Paid-in capital	1,175,878	1,174,880
Accumulated deficit	(366,110)	(346,570)
Accumulated other comprehensive income (loss)	3,308	(21,046)
	1,064,878	1,059,063
	$12,441,774	$12,186,525

See accompanying notes to consolidated financial statements.

CAPSTEAD MORTGAGE CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(unaudited)

	Quarter Ended March 31	
	2019	2018
Interest income:		
Residential mortgage investments	$83,807	$69,138
Other	422	408
	84,229	69,546
Interest expense:		
Secured borrowings	(63,779)	(45,021)
Unsecured borrowings	(1,891)	(1,891)
	(65,670)	(46,912)
	18,559	22,634
Other (expense) income:		
Loss on derivative instruments (net)	(21,657)	–
Compensation-related expense	(3,609)	(2,048)
Other general and administrative expense	(1,128)	(1,237)
Miscellaneous other revenue	89	71
	(26,305)	(3,214)
Net (loss) income	(7,746)	19,420
Less preferred stock dividends	(4,842)	(4,842)
Net (loss) income to common stockholders	$(12,588)	$14,578
Net (loss) income per common share:		
Basic and diluted	$(0.15)	$0.16
Weighted average common shares outstanding:		
Basic	84,894	93,425
Diluted	84,894	93,506
Cash dividends declared per share:		
Common	$0.08	$0.16
Series E preferred	0.47	0.47

See accompanying notes to consolidated financial statements.

CAPSTEAD MORTGAGE CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands, unaudited)

	Quarter Ended March 31	
	2019	2018
Net (loss) income	$(7,746)	$19,420
Other comprehensive income (loss)		
Amounts related to available-for-sale securities:		
Change in net unrealized gains (losses)	43,476	(44,053)
Amounts related to derivative instruments held as cash flow hedges:		
Change in net unrealized (losses) gains	(8,551)	30,933
Reclassification adjustment for amounts included in net (loss) income	(10,571)	(4,644)
	24,354	(17,764)
Comprehensive income	$16,608	$1,656

See accompanying notes to consolidated financial statements.

CAPSTEAD MORTGAGE CORPORATION

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands, unaudited)

	Preferred Stock	Common Stock	Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance at December 31, 2018	$250,946	$ 853	$1,174,880	$ (346,570)	$ (21,046)	$ 1,059,063
Net loss	–	–	–	(7,746)	–	(7,746)
Change in unrealized gain on mortgage securities, net	–	–	–	–	43,476	43,476
Amounts related to cash flow hedges, net	–	–	–	–	(19,122)	(19,122)
Cash dividends:						
Common – $0.08 per share	–	–	–	(6,952)	–	(6,952)
Preferred	–	–	–	(4,842)	–	(4,842)
Other additions to capital	–	3	998	–	–	1,001
Balance at March 31, 2019	$250,946	$ 856	$1,175,878	$ (366,110)	$ 3,308	$ 1,064,878
Balance at December 31, 2017	$250,946	$ 957	$1,271,425	$ (346,570)	$ 62,118	$ 1,238,876
Net income	–	–	–	19,420	–	19,420
Change in unrealized gain on mortgage securities, net	–	–	–	–	(44,053)	(44,053)
Amounts related to cash flow hedges, net	–	–	–	–	26,289	26,289
Cash dividends:						
Common – $0.16 per share	–	–	(164)	(14,578)	–	(14,742)
Preferred	–	–	–	(4,842)	–	(4,842)
Common stock repurchases	–	(34)	(29,028)	–	–	(29,062)
Other additions to capital	–	2	340	–	–	342
Balance at March 31, 2018	$250,946	$ 925	$1,242,573	$ (346,570)	$ 44,354	$ 1,192,228

See accompanying notes to consolidated financial statements.

CAPSTEAD MORTGAGE CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands, unaudited)

	Quarter Ended March 31	
	2019	2018
Operating activities:		
Net (loss) income	$(7,746)	$19,420
Noncash items:		
Amortization of investment premiums	18,253	25,620
Amortization of equity-based awards	1,109	415
Amortization of unrealized gain on de-designated hedges	(3,020)	–
Unrealized loss on derivative instruments (net)	26,237	–
Other depreciation and amortization	27	26
Net change in receivables, other assets, accounts payable and accrued expenses	12,635	1,290
Net cash provided by operating activities	47,495	46,771
Investing activities:		
Purchases of residential mortgage investments	(994,371)	(461,381)
Interest receivable acquired with the purchase of residential mortgage investments	(2,190)	(798)
Principal collections on residential mortgage investments, including changes in mortgage securities principal remittance receivable	768,168	812,524
Repayment of lending counterparty investment	5,000	–
Net cash (used in) provided by investing activities	(223,393)	350,345
Financing activities:		
Proceeds from repurchase arrangements and similar borrowings	31,034,056	48,138,234
Principal payments on repurchase arrangements and similar borrowings	(30,790,967)	(48,524,450)
(Decrease) increase in cash collateral receivable from interest rate swap counterparties	(26,394)	5,920
Net (payments on) proceeds from interest rate swap settlements	(56,731)	21,324
Common stock repurchases	–	(29,062)
Other capital stock transactions	(106)	(72)
Dividends paid	(11,816)	(23,002)
Net cash provided by (used in) financing activities	148,042	(411,108)

Net change in cash and cash equivalents	(27,856)	(13,992)
Cash and cash equivalents at beginning of period	60,289	103,907
Cash and cash equivalents at end of period	$32,433	$89,915

See accompanying notes to consolidated financial statements.

CAPSTEAD MORTGAGE CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2019

(unaudited)

NOTE 1 — 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 — 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 ended March 31, 2019 are not necessarily indicative of the results that may be expected for the calendar year ending December 31, 2019. 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, 2018.

Change in Use of Hedge Accounting

On March 1, 2019 the Company discontinued its use of hedge accounting on its interest rate swaps related to Secured borrowings, while retaining hedge accounting for swaps related to Unsecured borrowings. See NOTE 6 for additional information regarding these changes in the Company's use of derivative instruments ("Derivatives") and its related risk management policies.

Recent Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2016-02, Leases ("ASU 2016-02") which requires entities who are lessees to recognize a right-of-use asset and a lease liability arising from those leases on the balance sheet. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. The Company adopted ASU 2016-02 on January 1, 2019, which had no material effect on the Company's results of operations, financial condition and cash flows.

NOTE 3 — NET INCOME (LOSS) PER COMMON SHARE

Basic net income (loss) 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 (loss) per common share is computed by dividing the numerator used to compute basic net income (loss) per common share by the denominator used to compute basic net income (loss) 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 (loss) 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 (loss) per common share were as follows for the indicated periods (dollars in thousands, except per share amounts):

	Quarter Ended March 31	
	2019	2018
Basic net income (loss) per common share		
Numerator for basic net income (loss) per common share:		
Net (loss) income	$(7,746)	$19,420
Preferred stock dividends	(4,842)	(4,842)
Earnings participation of unvested equity awards	(19)	(32)
	$(12,607)	$14,546
Denominator for basic net income (loss) per common share:		
Average number of shares of common stock outstanding	85,549	93,867
Average unvested stock awards outstanding	(655)	(442)
	84,894	93,425
	$(0.15)	$0.16
Diluted net income (loss) per common share		
Numerator for diluted net income (loss) per common share	$(12,607)	$14,546
Denominator for diluted net income (loss) per common share:		
Denominator for basic net income (loss) per common share	84,894	93,425
Net effect of dilutive equity awards	–	81
	84,894	93,506
	$(0.15)	$0.16

Securities that could be potentially dilutive in the future that were not included in the computation of diluted net income (loss) per common share include 1.2 million anti-dilutive equity awards excludable under the treasury stock method for the quarter ended March 31, 2019. There were no potentially dilutive securities excluded from the computation of diluted net income (loss) per common share for the quarter ended March 31, 2018.

NOTE 4 — 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 [(c)]
March 31, 2019						
Agency Securities:						
Fannie Mae/Freddie Mac:						
Fixed-rate	$113	$–	$113	$113	6.50 %	5.25 %
ARMs	8,844,800	260,507	9,105,307	9,118,646	3.58	2.69
Ginnie Mae ARMs	3,026,085	78,649	3,104,734	3,107,625	3.43	2.93
	11,870,998	339,156	12,210,154	12,226,384	3.54	2.75
Residential mortgage loans:						
Fixed-rate	241	1	242	242	7.12	2.68
ARMs	806	4	810	810	3.90	4.44
	1,047	5	1,052	1,052	4.64	3.80
Collateral for structured financings	970	16	986	986	8.25	7.57
	$11,873,015	$339,177	$12,212,192	$12,228,422	3.54	2.75
December 31, 2018						
Agency Securities:						
Fannie Mae/Freddie Mac:						
Fixed-rate	$126	$–	$126	$126	6.50 %	6.23 %
ARMs	8,691,794	257,999	8,949,793	8,931,558	3.42	2.28
Ginnie Mae ARMs	2,964,531	75,744	3,040,275	3,031,264	3.30	2.54
	11,656,451	333,743	11,990,194	11,962,948	3.39	2.34
Residential mortgage loans:						
Fixed-rate	552	1	553	553	6.80	2.44
ARMs	868	4	872	872	3.91	3.24
	1,420	5	1,425	1,425	5.03	2.95
Collateral for structured financings	991	17	1,008	1,008	7.99	7.43
	$11,658,862	$333,765	$11,992,627	$11,965,381	3.39	2.34

(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.

(c) 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 287 months.

Fixed-rate investments consist of residential mortgage loans and Agency Securities backed by residential mortgage loans with fixed rates of interest. ARMs are adjustable-rate 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 March 31, 2019, the average months to roll for the Company's $6.10 billion (amortized cost basis) in current-reset ARM investments was approximately six months while the average months to roll for the Company's $6.11 billion (amortized cost basis) in longer-to-reset ARM investments was approximately 43 months.

NOTE 5 — 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 (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.

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.

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	
March 31, 2019					
Borrowings under repurchase arrangements with maturities of 30 days or less:					
Agency Securities	$10,703,199	$ 31,632	$10,154,691	2.73	%
Borrowings under repurchase arrangements with maturities greater than 30 days:					
Agency Securities (31 to 90 days)	1,119,381	3,513	1,066,774	2.69	
Similar borrowings:					
Collateral for structured financings	986	–	986	8.25	
	$11,823,566	$ 35,145	$11,222,451	2.73	
Quarter-end borrowing rates adjusted for effects of related Derivatives				2.34	
December 31, 2018					
Borrowings under repurchase arrangements with maturities of 30 days or less:					
Agency Securities	$4,424,311	$ 12,287	$4,204,988	2.73	%
Borrowings under repurchase arrangements with maturities greater than 30 days:					
Agency Securities (31 to 90 days)	7,143,129	19,621	6,773,366	2.68	
Similar borrowings:					
Collateral for structured financings	1,008	–	1,008	7.99	
	$11,568,448	$ 31,908	$10,979,362	2.70	
Year-end borrowing rates adjusted for effects of related Derivatives				2.26	

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

	March 31, 2019		December 31, 2018	
	Average Borrowings	Average Rate	Average Borrowings	Average Rate
Average borrowings and rates adjusted for the effects of related Derivatives	$11,156,608	2.12 %	$11,439,646	2.07 %

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

Capstead attempts to mitigate exposure to higher interest rates by entering into one- and three-month LIBOR-indexed, pay-fixed, receive-variable, interest rate swap agreements for terms of two and three years. These Derivatives hedge the variability of the underlying benchmark interest rate of current and forecasted 30- to 90-day secured borrowings. From an economic perspective, 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 borrowings, leaving the fixed-rate swap payments as the Company's effective borrowing rate, subject to certain adjustments. 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.

Historically, the Company designated its interest rate swaps related to secured borrowings as hedges for accounting purposes, whereby changes in the swaps' fair values were recorded in Accumulated other comprehensive income (loss). The Company discontinued hedge accounting on March 1, 2019 for these swaps and, for GAAP purposes, related changes in the fair value are recorded in the Company's consolidated statement of operations beginning on that date. Also, for GAAP purposes, related net unrealized gains recorded in Accumulated other comprehensive income (loss) through February 28, 2019 are being recognized as a component of interest expense in the Company's consolidated statement of operations over the remaining lives of these swaps.

During the quarter ended March 31, 2019, Capstead entered into swap agreements with notional amounts of $2.6 billion requiring fixed-rate interest payments averaging 2.55%. During the quarter ended March 31, 2019, $950 million notional amount of swaps requiring fixed-rate interest payments averaging 1.58% matured. At March 31, 2019 the Company's swap positions related to secured borrowings had the following characteristics (dollars in thousands):

Period of Contract Expiration	Notional Amount	Average Fixed-Rate Payment Requirement	
Second quarter 2019	$1,650,000	1.33	%
Third quarter 2019	550,000	1.40	
Fourth quarter 2019	700,000	1.72	
First quarter 2020	600,000	2.07	
Second quarter 2020	600,000	2.68	
Third quarter 2020	200,000	1.64	
Fourth quarter 2020	200,000	2.04	
First quarter 2021	100,000	2.67	
Second quarter 2021	200,000	2.87	
Fourth quarter 2021	800,000	2.85	
First quarter 2022	2,600,000	2.55	
	$8,200,000		

The Company has 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 remain designated as cash flow hedges for accounting purposes of the variability of the underlying contractual rate associated with the floating-rate terms of these long-term borrowings which began on various dates between October 2015 and September 2016.

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). Fair value estimates for these Derivatives are calculated using the net 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 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 fair value of exchange-traded swap agreements hedging Secured borrowings is calculated including accrued interest and net of variation margin amounts received or paid through the exchange, resulting in separately presenting on the balance sheet a significantly reduced fair value amount representing the unsettled fair value of these Derivatives. Non-exchange traded swap agreements held as cash flow hedges of Unsecured borrowings are reported at fair value calculated excluding accrued interest. At March 31, 2019, Cash collateral receivable from interest rate swap counterparties includes initial margin for all swap agreements and variation margin for non-exchange traded swap agreements. Accrued interest for non-exchange traded swap agreements is included in Accounts payable and accrued expenses.

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	March 31 2019	December 31 2018
Balance sheet-related			
Swap agreements in a gain position (an asset) related to			
secured borrowings	(a)	$7,037	$ –
Swap agreements in a loss position (a liability) related to unsecured borrowings	(a)	(21,903)	(17,834)
Related net interest payable	(b)	(871)	(372)
		$(15,737)	$ (18,206)

(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 unrealized gains, net of unrealized losses, included in Accumulated other comprehensive income (loss) and scheduled to be recognized in the Statements of Operations over the next twelve months primarily in the form of amortization of net unrealized gains on de-designated interest rate swaps and fixed-rate swap payments in excess of current market rates on swaps related to unsecured borrowings totaled $13.3 million at March 31, 2019.

(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 March 31 2019	2018
Income statement-related			
Components of Secured borrowings-related effects on interest expense:			
Amount of gain reclassified from Accumulated other comprehensive income (loss)		$7,891	$5,247
Amortization of unrealized gain, net of unrealized losses on de-designated Derivatives		3,020	–
	(a)	10,911	5,247
Component of Unsecured borrowings-related effects on interest expense:			
Amount of loss reclassified from Accumulated other comprehensive income (loss)	(b)	(340)	(603)
Decrease in interest expense and increase in Net (loss) income as a result of the use of Derivatives		$10,571	$4,644
Realized and unrealized loss on non-designated Derivatives (net)	(c)	$(21,657)	$–
Other comprehensive income-related			
Amount of (loss) gain recognized in Other comprehensive income		$(8,551)	$30,933

(a) Included in “Interest expense: Secured borrowings” on the face of the Statements of Operations.
(b) Included in “Interest expense: Unsecured borrowings” on the face of the Statements of Operations.
(c) Included in “Loss on derivative instruments (net)” on the face of the Statement of Operations.

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 [(a)]	Gross Amounts Offset in the Balance Sheet [(a)]	Net Amounts of Assets Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet [(b)]		
				Financial Instruments	Cash Collateral Received	Net Amount
March 31, 2019						
Counterparty 4	$10,913	$(3,877)	$7,037	$ –	$ –	$7,037
December 31, 2018						
Counterparty 4	$26,787	$(26,787)	$ –	$ –	$ –	$ –

(a) Included in gross amounts of recognized assets at March 31, 2019 is the fair value of exchange-traded swap agreements, calculated including accrued interest. Included in gross amounts offset in the balance sheet are variation margin amounts associated with these swaps at March 31, 2019.

(b) 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.

Offsetting of Financial Liabilities and Derivative Liabilities

	Gross Amounts of Recognized Liabilities [a]	Gross Amounts Offset in the Balance Sheet [a]	Net Amounts of Liabilities Presented in the Balance Sheet [b]	Gross Amounts Not Offset in the Balance Sheet [c] Financial Instruments	Cash Collateral Pledged	Net Amount
March 31, 2019						
Derivatives by counterparty:						
Counterparty 1	$22,774	$ –	$22,774	$–	$(22,774)	$ –
Counterparty 4	41,548	(41,548)	–	–	–	–
	64,322	(41,548)	22,774	–	(22,774)	–
Borrowings under repurchase arrangements [d]	11,233,090	–	11,233,090	(11,233,090)	–	–
	$11,297,412	$ (41,548)	$11,255,864	$(11,233,090)	$(22,774)	$ –
December 31, 2018						
Derivatives by counterparty:						
Counterparty 1	$18,205	$ –	$18,205	$–	$(18,205)	$ –
Counterparty 4	9,718	(9,718)	–	–	–	–