



Analyst Day - February 2015

# Disclaimers

## FORWARD-LOOKING INFORMATION

This presentation contains forward-looking statements and information. Statements that are not historical facts, including statements about our beliefs and expectations, are forward-looking statements. Forward-looking statements include statements preceded by, followed by or that include the words “may,” “could,” “would,” “should,” “believe,” “expect,” “anticipate,” “plan,” “estimate,” “target,” “project,” “intend” and similar expressions. These statements include, among others, statements regarding our expected performance, anticipated returns and our investment, financing, and hedging strategies and means to implement the strategy.

Forward-looking statements are only predictions and are not guarantees of performance. These statements are based on our management’s beliefs and assumptions, which in turn are based on currently available information. These assumptions could prove inaccurate. Forward-looking statements also involve known and unknown risks and uncertainties, which could cause actual results that differ materially from those contained in any forward-looking statement. Many of these factors are beyond our ability to control or predict.

All forward-looking statements speak only as of the date of this presentation. Except as required by applicable law, we are under no obligation to publicly update or revise any forward-looking statements, whether as a result of any new information, future events or otherwise. Potential investors should not place undue reliance on our forward-looking statements. Before you invest in our common stock, you should be aware that the occurrence of the events described in “Risk Factors” section and elsewhere in our Form 10-K for the year ended December 31, 2013 and other document filed with the Securities and Exchange Commission could harm our business, financial condition and results of operations and our ability to pay distributions to our stockholders.



# Business Model and Background

# Overview

## Topic Point

## Slide

- Management Experience 5
- Independent Directors 6
- Challenges of the Traditional Model 7
- Orchid Business Model 8
- Capital Allocation Process 9
- Security Selection and Considerations 10 - 15
- Risk Mitigation 16

# Experienced Management

## Robert E. Cauley

*Chief Executive Officer, President and Chairman of the Board*

**Co-Founded Bimini**  
**21 years of industry experience**

- **Position at Orchid:** Chairman, President and CEO since August 2010
- **2008 - Present:** CEO and Chairman of the Board of Bimini
- **2003 - 2008:** Vice-Chairman, CFO and CIO of Bimini
- **1996 - 2003:** Vice-President and portfolio manager; Federated Investors
- **1994 - 1996:** ABS/MBS structuring desk; Lehman Brothers
- **1992 - 1994:** Credit Analyst; Barclays Bank, PLC

## G. Hunter Haas, IV

*Chief Financial Officer, Secretary, Chief Investment Officer and Director*

**14 years of industry experience**

- **Position at Orchid:** CFO and CIO and Secretary since August 2010
- **2008 - Present:** President, Chief Investment Officer and Chief Financial Officer of Bimini
- **2004 - 2008:** Senior Vice-President and head of Mortgage Research of Bimini
- **2002 - 2004:** Vice President, Servicing Asset Risk Management; National City
- **2001 - 2002:** Assistant Vice President, Capital Markets Finance Group; HomeSide Lending

## Jerry Sintes

*Vice President, Controller and Treasurer*

**27 years of industry accounting and audit experience**

- **Position at Orchid:** Vice President and Treasurer since August 2010
- **2007 - Present:** Vice President and Controller of Bimini
- **2006 - 2007:** Vice President and Assistant Controller: Riverside National Bank
- **2003 - 2005:** Chief Financial Officer: Guaranty Savings Homestead Association and GS Financial Corp
- **1992 - 2003:** Audit manager; Bain, Freibaum, Sagona & Co., LLP
- **1988 – 1992** Audit Senior; Whitney National Bank
- Certified Public Accountant, Member AICPA

# Independent Directors

## John B. Van Heuvelen

**Position at Orchid:** Director; audit committee chair and financial expert, member of compensation committee.

**Board Memberships:**

2009 – Present: Hallador Energy Company (Nasdaq: HNRG): audit committee chair.

2002 – Present: MasTec, Inc (NYSE: MTZ): Currently the lead outside director and member of audit committee; past chairman of the audit committee and financial expert from 2004-2009.

2005 – 2007: LifeVantage, Inc. (OTC: LFDV)

**Experience:**

President of Morgan Stanley Dean Witter Trust Company from 1993 - 1999

## W. Coleman Bitting

**Position at Orchid:** Independent director, compensation committee chair and member of nominating and governance committee.

**Experience:**

23 Years Industry Experience

2007 - Present: Maintains a private consulting practice focused on REITs

2000 - 2007: Founding Partner and Head of Corporate Finance; Flagstone Securities

Prior to Flagstone: Senior equity research position; Stifel, Nicolaus & Co. Inc. and Kidder, Peabody & Co., Inc.

## Frank P. Filippis

**Position at Orchid:** Independent Director, member of audit, compensation, and nominating and governance committees.

**Board Memberships:**

1995 – Present: Impac Mortgage Holdings, Inc. (Amex: IMH): chair of audit committee

2002 – Present Primus Guaranty, Ltd (NYSE: PRS): chair of compensation committee from 2002-2006 and chair of the nominating and governance committee from 2007 – 2011.

2010 – Present: Fortegra Financial Corp. (NYSE: FRF); chairman of the nominating and governance committee from 2010 – 2011, member of audit committee since 2010 and chair of the compensation committee since 2012.

**Experience:**

2005 – 2008 Chair and CEO of Clayton Holdings (Nasdaq: Clay)

1992 – 2005 Chairman and CEO Radian Group, Inc.

1975 – 1992 Various executive positions at AIG including founder, president and CEO of AIG Capital Corp.

## Ava L. Parker

**Position at Orchid:** Independent Director, nominating and governance committee chair, and member of audit committee.

**Board Memberships:**

2006 - Present: Jacksonville Transportation Authority Board; Past chairman

2010 – 2012: Immediate Prior Chairman of the State of Florida Board of Governors of the State University System; Reappointed by Governor Rick Scott in Jan. 2012

**Experience:**

Lawrence & Parker PA: Partner

Linking Solutions, Inc.: President

# Challenges of the Traditional Model

## The traditional REIT investment model: Repo-funded pass-through securities

### Price Risk

- Holders of premium priced Agency RMBS are vulnerable to losses if prepayments rise unexpectedly
- Limited further price appreciation with premium Agency RMBS, but risk of accelerated price declines remain as rates rise

### Reinvestment Risk

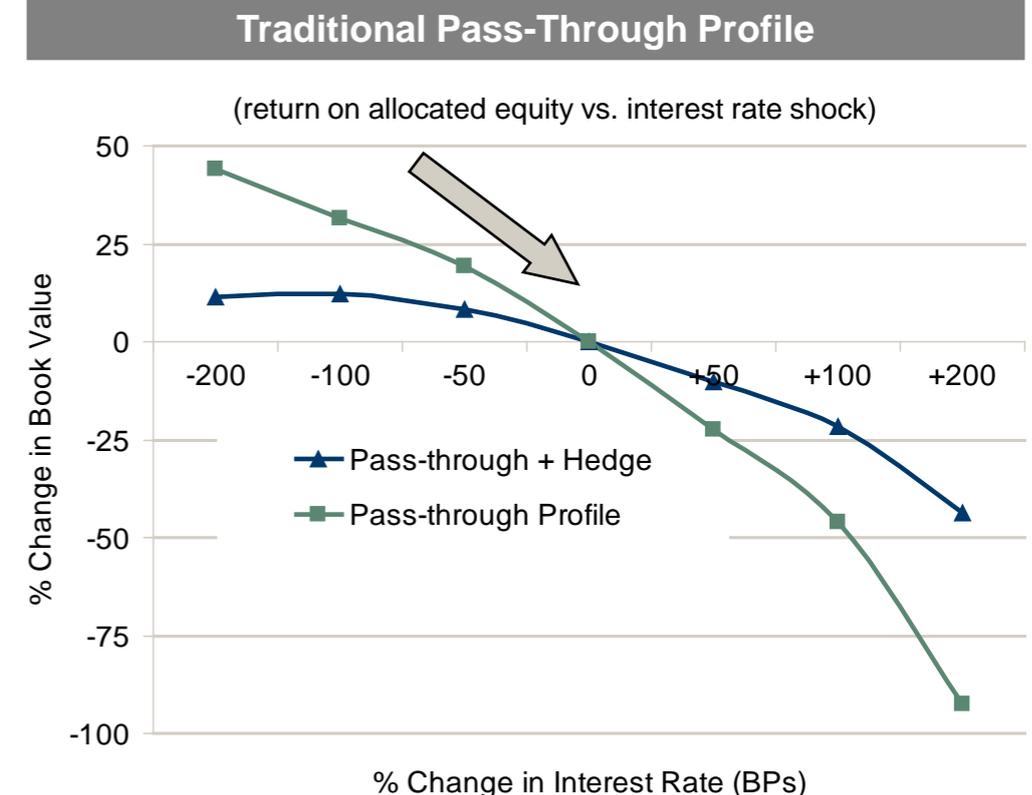
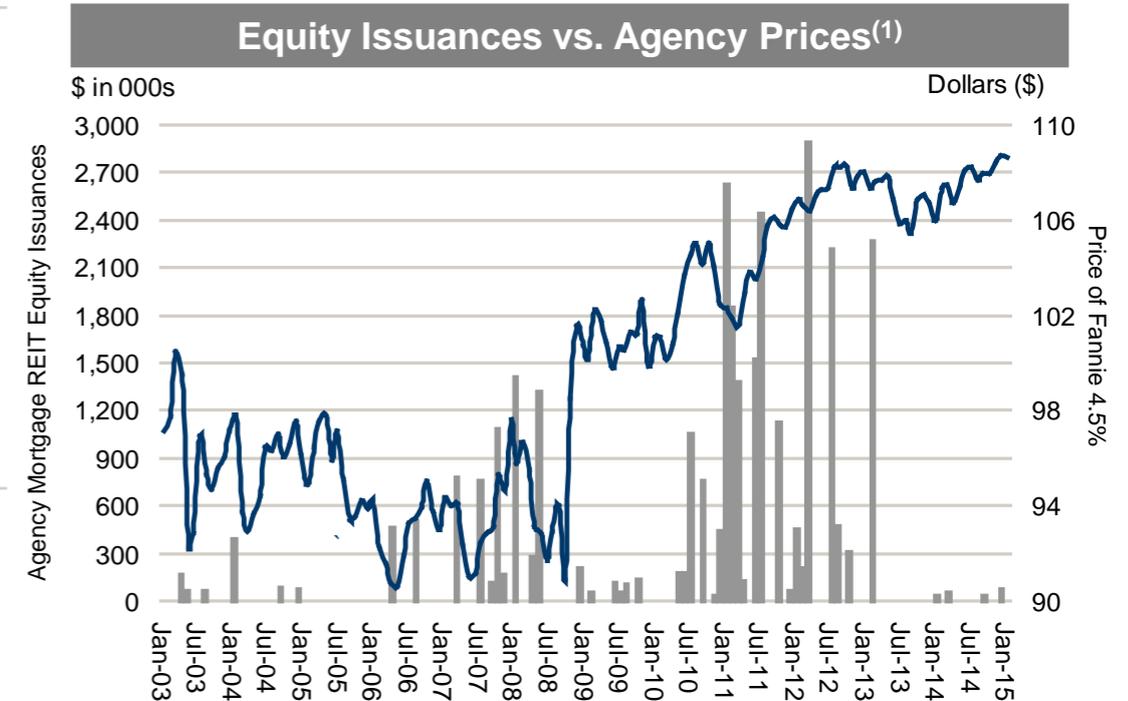
- Agency RMBS prepay faster in low rate environments
  - But capital has to be deployed in a less attractive investment environment due to higher RMBS prices

### Maturity Risk

- Short term repo funding comes due before the assets pay off creating funding risk
- Traditional REIT model assumes the ability to continuously roll-over maturing liabilities

### Counterparty Risk

- Deteriorating counterparty financial condition can result in funding instability
  - Risk that all funding counterparties pull back simultaneously



(1) Source: Bloomberg

# The Orchid Island Business Model

## Model Overview

- Capital allocated to two sub-portfolios
  - ① A levered pass-through portfolio utilizing funding hedges
  - ② A structured securities portfolio
- The two sub-portfolios act as hedges for one another – enhancing book value stability

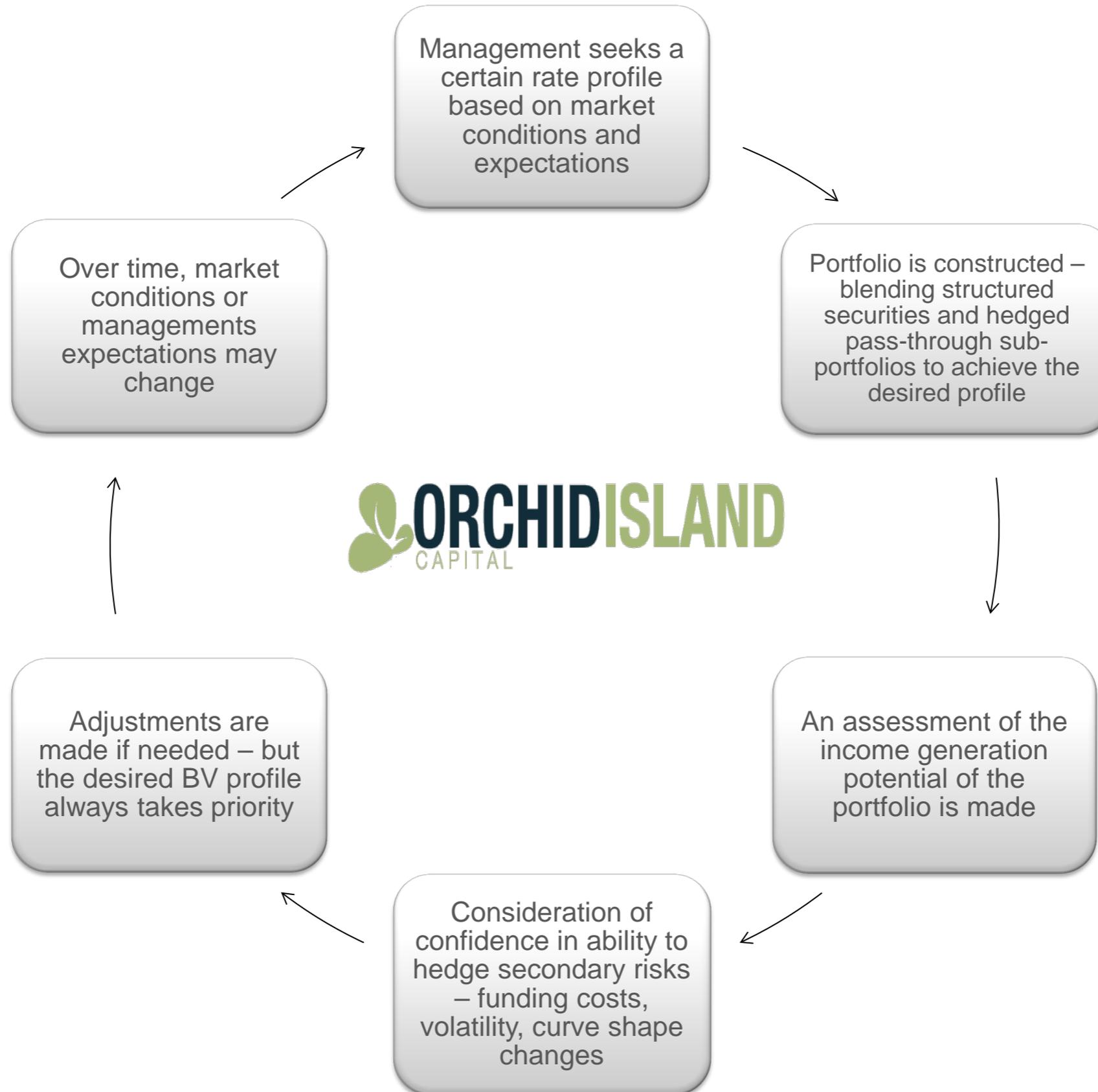
## Model Benefits

- Same expected returns as traditional levered pass-through strategies employed by peers
- Greater book value stability – leading to a higher Sharpe Ratio
- Less reliance on funding since not all of our capital is levered

## Model Implementation

- Capital allocation process
- Security selection process
- Funding hedge design and execution
- Risk monitoring process

# Capital Allocation Process



# Creating the Desired Rate Profile

## Asset Selection

- Structured Agency RMBS typically exhibit different sensitivity to interest rate movements – often inversely correlated with PT's

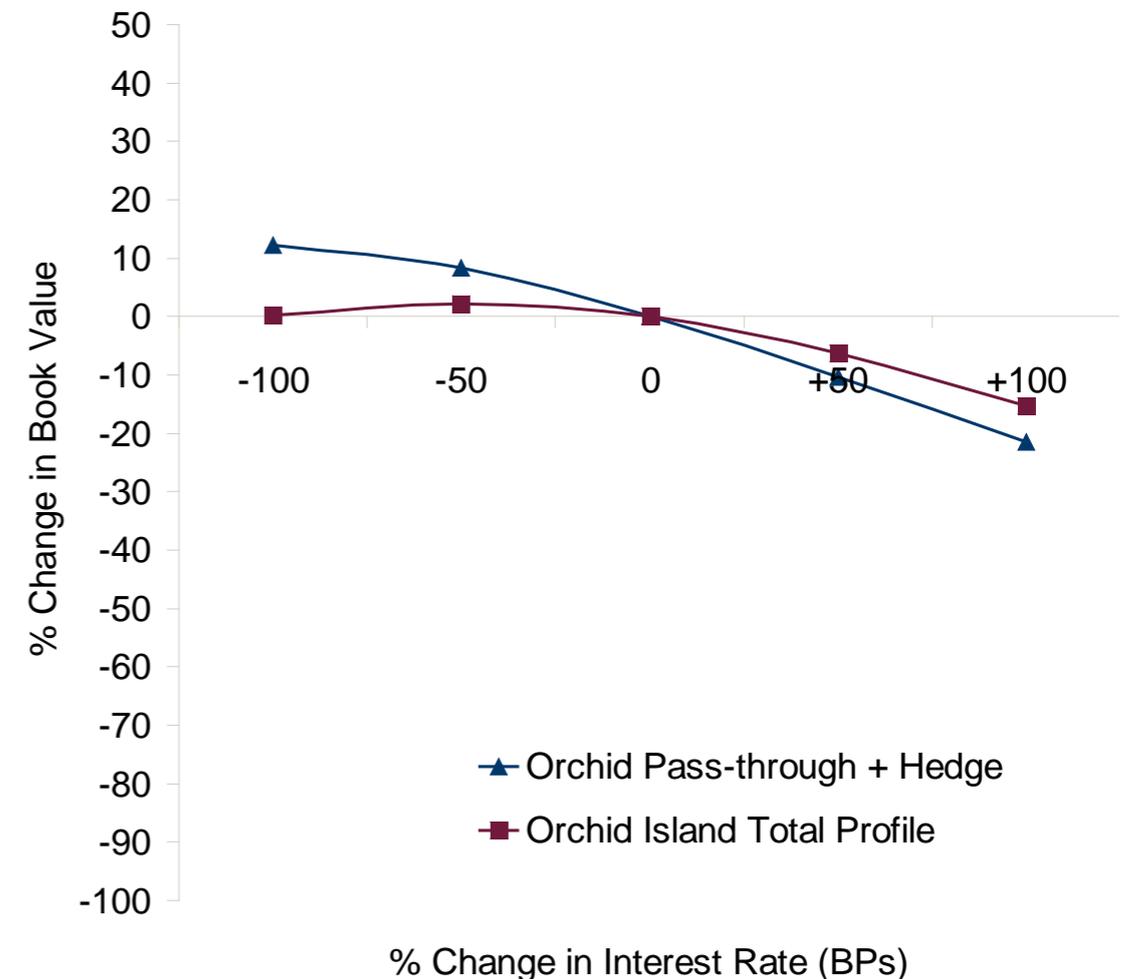
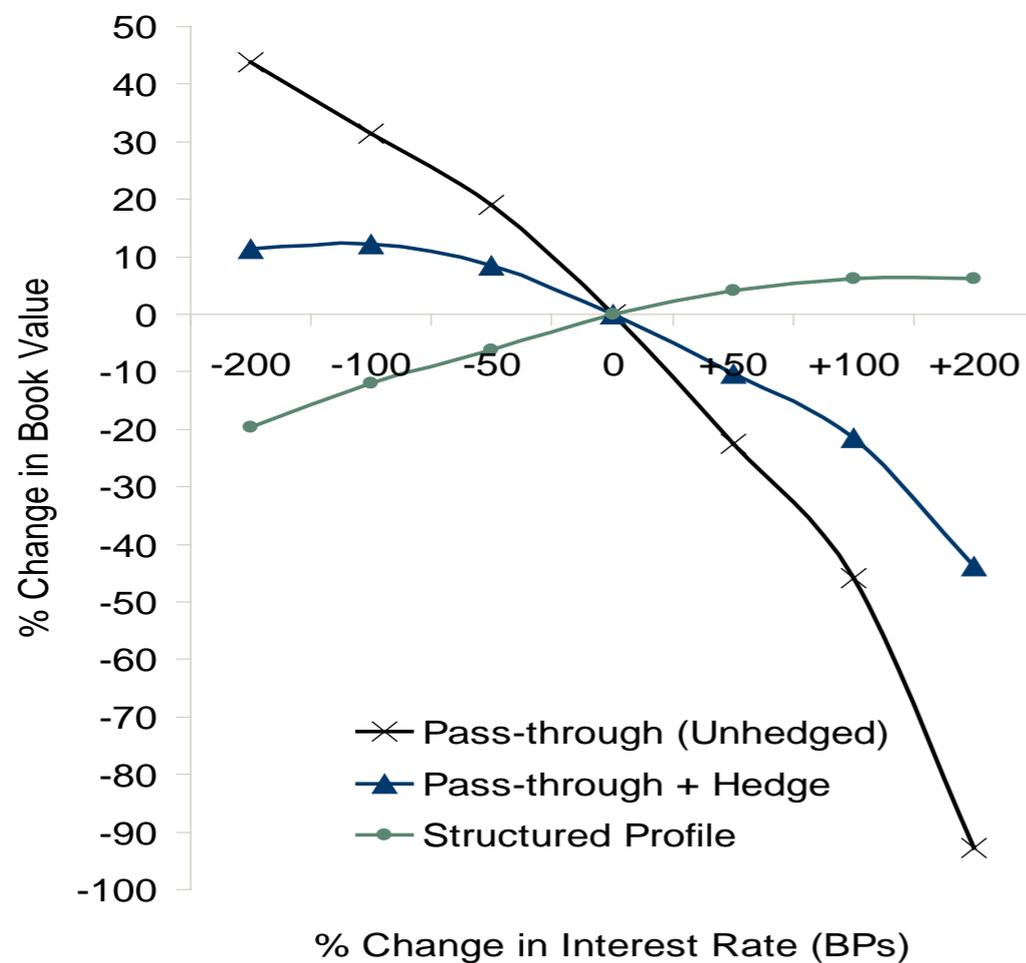
## Book Value Stability

- The combined portfolios exhibit far less interest rate sensitivity and may be constructed to reflect management bias/expectations

## Embedded Leverage

- Strategy does not require as much explicit leverage, yet has a comparable return profile to hedged Agency pass-throughs

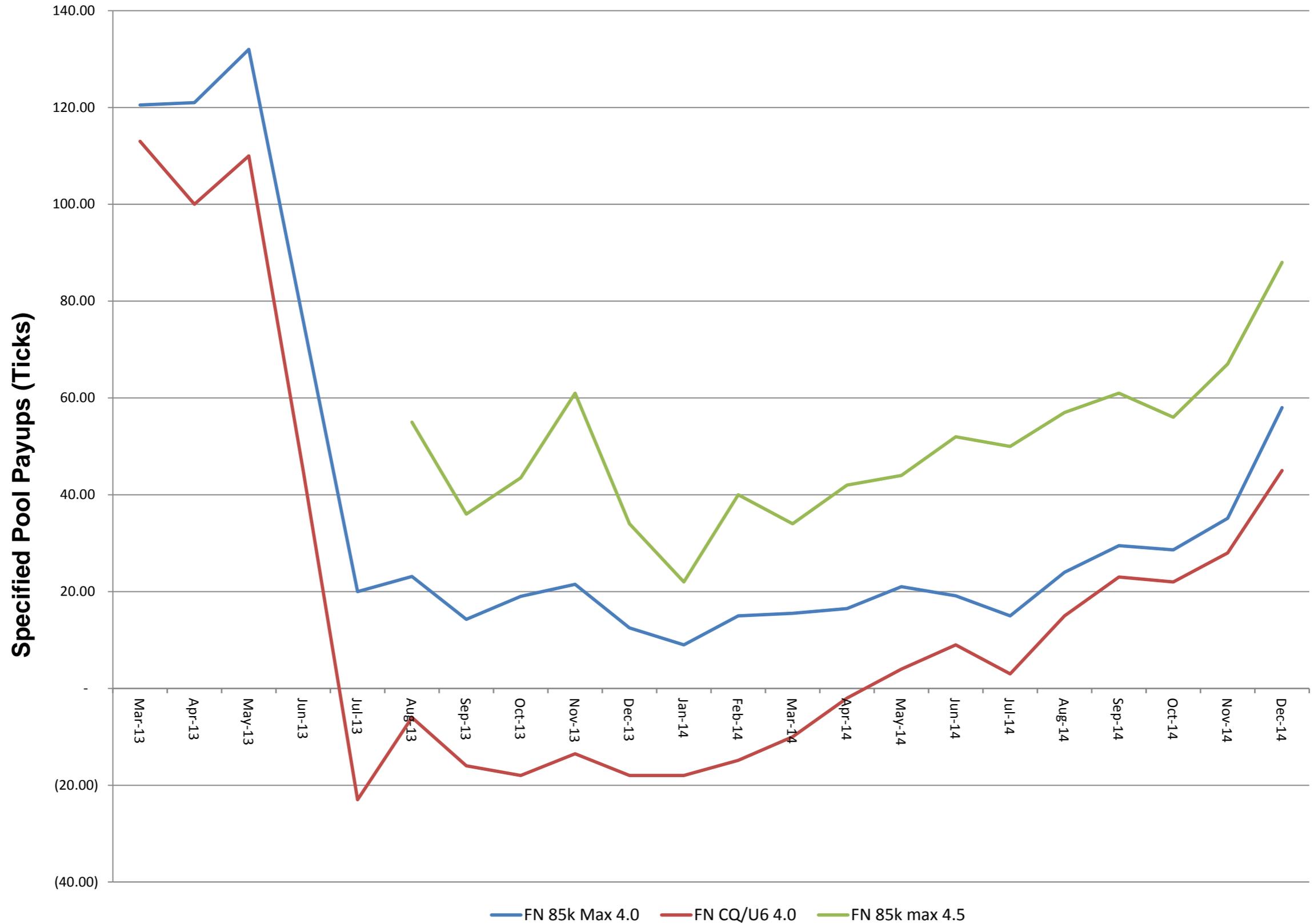
\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.



# Security Selection – Pass Through Portfolio

	1 Security Attribute	2 Examples	3 Risk Considerations
<b>Security Characteristics</b>	<ul style="list-style-type: none"> <li>Type of MBS, maturity, coupon, age</li> </ul>	<ul style="list-style-type: none"> <li>Fixed or ARM, 30 year, 15 year, premium or discount, new vs. seasoned</li> </ul>	<ul style="list-style-type: none"> <li>Duration and convexity – extension risk</li> </ul>
<b>Relative Value Considerations</b>	<ul style="list-style-type: none"> <li>Form of call protection – if any, prepayment expectations</li> <li>Rich/cheap of sector, coupon, call protection pay-ups</li> </ul>	<ul style="list-style-type: none"> <li>Low loan balance, credit impaired borrower, new, geographic concentrations</li> <li>30 year rich/cheap to 15 year or hybrids, relative demand for call protection, premiums for high quality call protection versus marginal forms</li> </ul>	<ul style="list-style-type: none"> <li>Prepayment expectations and the need for call protection, realized versus model duration and convexity</li> <li>Relative value can change or expectations prove inaccurate</li> <li>Pay back period vs. specified carry advantage</li> </ul>
<b>Risk Management Integration</b>	<ul style="list-style-type: none"> <li>Duration and convexity characteristics of security, prepayment expectations and cash management considerations</li> </ul>	<ul style="list-style-type: none"> <li>Securities are run on one of the models available to us, and we assess the model output versus our expectations</li> </ul>	<ul style="list-style-type: none"> <li>Overall performance of security versus expectations – impact on overall risk, management effectiveness</li> </ul>

# Wells Fargo Production Specified Pool Payups



# Security Selection – Structured Securities Portfolio

	1 Security Attribute	2 Examples	3 Risk Considerations
<b>Security Characteristics</b>	<ul style="list-style-type: none"> <li>Type of security and structure</li> </ul>	<ul style="list-style-type: none"> <li>IO vs IIO; PAC, XPAC, Sequential, PT, Excess Servicing</li> </ul>	<ul style="list-style-type: none"> <li>Interest rate duration, spread duration, convexity</li> </ul>
<b>Collateral Characteristics</b>	<ul style="list-style-type: none"> <li>IO's and IIO's are levered plays on prepayments – the consequences of incorrect speed expectation are magnified versus pass through securities</li> </ul>	<ul style="list-style-type: none"> <li>Term (30/20/15/10 year), loan balance, credit quality, new versus seasoned, geographic concentrations</li> </ul>	<ul style="list-style-type: none"> <li>Prepayments realized if available mortgage rates change materially; turn-over assumptions</li> </ul>
<b>Income Potential – GAAP and Tax</b>	<ul style="list-style-type: none"> <li>The interplay of price &amp; speed expectations drive income potential. For tax additional considerations apply</li> </ul>	<ul style="list-style-type: none"> <li>Securities offering significant up-rate protection may have low or negative carry and visa versa; for tax time of purchase versus security issue date</li> </ul>	<ul style="list-style-type: none"> <li>In the current interest rate environment income potential is a secondary consideration versus up rate protection</li> </ul>
<b>Risk Management Integration</b>	<ul style="list-style-type: none"> <li>Rate profile, duration and convexity characteristics, prepayment expectations</li> </ul>	<ul style="list-style-type: none"> <li>IO's – less carry/better rate protection</li> <li>IIO's better carry/less rate protection</li> </ul>	<ul style="list-style-type: none"> <li>Overall performance of security versus expectations – impact on overall risk, management effectiveness</li> </ul>

# Security Holding Period Considerations

A significant component of the security selection process is the decision of how long to own an asset

## Security Specific Factors to Consider:

- Prepayment models base prepayment projections on several variables. Prepayment behavior drives income generation and price performance of securities, so management evaluates the same variables before acquiring a security and when determining how long to hold it:
  - Securities that possess “call protection” features typically command higher prices than those that do not – the difference is referred to as the “pay-up”.
  - Pay-ups vary over time – primarily as the value of call protection varies (i.e. as rates +/-, pay-ups +/-)
  - If the call protection decreases as the loans age the pay-up will decline as well
- Generally borrowers do not refinance their loan for at least a few months after origination – therefore newer loans typically exhibit less rate sensitivity initially. The market may demand a small pay-up for new loans.
- When considering a specified/call protected pool for purchase, management evaluates the pay-up demanded versus the incremental income expected to be generated and determines how long the security will need to be held to recapture the pay-up – is this period reasonable?
- Once acquired, management evaluates all pass through assets from this perspective – what, if any, call protection does the asset have remaining and what is the market price for this protection.
- Management constantly evaluates the call protection offered by the security as market conditions and prepayment expectations change over time.
- Management evaluates the prospects for pay-ups going forward when determining how long to hold a security
  - Is it time to harvest gains/cut losses?

# Security Holding Period Considerations

Portfolio specific factors result from the risk management function and the desire to maintain stable book value

## Portfolio Specific Factors to Consider:

- The pay-ups for call protection can be very volatile and materially alter the convexity of a security. This volatility is very difficult to hedge and impacts the effectiveness of the risk management function.

-Management prefers call protected securities with lower pay-ups for this reason

- Changes in management's outlook on rates and/or the MBS market will determine what securities to hold in the portfolio – this can lead to repositioning of the portfolio from time to time and therefore impact holding periods.
- The capital allocation process, as part of the risk management function, can necessitate changes to portfolio composition.

# Risk Monitoring Process

The primary risk monitored is the expected impact on our book value of various interest rate shocks

- We use “Yield Book” to run the shocks and test the sensitivity of the portfolio to instantaneous parallel shifts of the entire term structure of rates.
  - Up and down scenarios are run – for 50, 100 and 200 basis point shocks
- The shocks are run and the results published monthly with our dividend announcement.
- Shocks are run throughout the month, at least weekly, and as market conditions warrant.

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Management views the model derived results in the context of the following:

- The realization that interest rate movements are unlikely to be instantaneous nor perfectly parallel.
- That most assets and hedge instruments may behave differently in such scenarios than as predicted by the model.
- Management focuses on scenarios that pose the greatest risk to the portfolio, the likelihood of such outcomes and management’s expectations of realized versus model predicted results.
  - Management forms revised expectations of the performance of the portfolio under scenarios deemed to represent the greatest risk based on a synthesis of model output and management judgment
  - In addition to monitoring the most likely risks, management runs portfolio scenarios to quantify the risks of outcomes outside of managements expectations - i.e., what if we are wrong?
- Cash and liquidity positions are monitored daily and projections for rolling 30 day periods are prepared.
  - Cash and liquidity needs are considered in the context of potential adverse market moves

# Tax and Income Recognition

# Overview

## Topic Point

- Income Recognition: GAAP
- Income Recognition: Tax

## Slide

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# Income Recognition: GAAP

# Sample IO – Buy Trade Ticket

BXT

1) Send (VCON)... Buy Ticket

02/01/15 12:25 Trade Date 02/01/15 9) Settings

Trade Information

Trader ROBERT E CAULEY CUSIP 3136FGJ81  
 ISIN US3136FGJ811  
 BBGID BBG000B04W10  
 TRACE Eligible

7) BUY 2,450,000,000 of FNS 404 2

Price 15-16 15.5 Prepay 18 CPR  
 Settlement 02/01/15 Yield 6.4810 To Maturity  
 WAL 4.45 Principal Window 3/15-1/40  
 Mod Duration 3.314

Notes  
 (192 chars)

Collat FNCL 4.5 CMO IO,NTL Issued 4/1/10 Maturity 5/25/40 4.96(293)58

Trade Numbers

Current Face	\$	724,019,320.50	Coupon	4.5%
Principal Value	\$	112,222,994.68	Assumed Feb'15 Factor	0.2955180900 (Jan'15)
Accrued ( 0 days )	\$	0.00	Payment Frequency	Monthly
Total	\$	112,222,994.68	Accrual Period	2/1/15-2/28/15
			Next Payment Date	3/25/15 ( 24 day delay)

Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000  
 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000  
 SN 345678 EST GMT-5:00 G687-321-0 01-Feb-2015 12:26:16  
 Copyright 2015 Bloomberg Finance L.P.

# Sample IO – Yield Assumptions

2/ 1/15 settlement is not a business day  
 {YT NEW<go>} for enhanced agency YT screen.

**Bloomberg** 66 **FNS 404 2** 4.5% 5/25/40 ADU: <PAGE>  
<GO> 3136FGJ81 CMO:IO,NTL NO Windows  
<GO> FNCL 4.5 M 4.958(293)58 MAC(WAM)AGE JAN15 87 <Go>

JAN 1mo 330P 19.80	4/30/10: 2450000000	next pay 3/25/15 (monthly)	30/360 Cashflows
'15 3mo 285 17.1	1/25/15: 724,019,321	rcd date 2/28/15 (24 Delay)	created 1/24/15
6mo 277 16.6	factor 0.295518090000	accrual 2/ 1/15- 2/28/15	1stProj 2/25/15
12mo 239 14.3			Collat: 125 Pools
Life 456 21.3			

2/ 1/15		YIELD TABLE											
		30/360 DSCNTNG											
		"Off Ramp" Implicit CPR											
		15.0			18.0			21.0					
Vary	PRICE	1	CPR	15.0	CPR	18.0	CPR	21.0	CPR		CPR		CPR
15-16				10.059			6.481						2.835
		3/15- 1/40			3/15- 1/40			3/15- 1/40					
AvgLife		5.18			4.45			3.87					
Mod Dur		3.27			3.31			3.36					
DATEWindow		3/15- 1/25/40			3/15- 1/25/40			3/15- 1/25/40					

Spread	1882	+888/AL	+544/AL	+191/AL									
NON-CALLABLE	JAN15DEC14 NOV OCT SEP AUG JUL JUN MAY APR MAR FEB14	Treasury Curve - BGN 12:32											
	330 261 262 251 231 324 237 190 243 218 128 176p	6mo -1- -2- -3- -5- -7- -10- -30-											
	19.8 15.6 15.7 15.1 13.9 19.4 14.2 11.4 14.6 13.1 7.7 10.6c	0.05 0.14 0.45 0.74 1.16 1.46 1.64 2.22											

Format# 1-YT B

Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000  
 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000  
 SN 345678 EST GMT-5:00 6687-321-0 01-Feb-2015 12:32:41  
 Copyright 2015 Bloomberg Finance L.P.

# Sample IO – Projected Cash Flows

**CFT**  
**Note: Projections start with payment on 2/25/15**

**FNS 404 2 Mtge**      **2) Export**      **Cash Flow Table**

CUSIP 3136FGJ81      4.9580(293)58      **95 Buy**      **96 Sell**

**1M**      **CPR** 19.80      **PSA** 330      **60D+** -      **WAOLS** 233M      **Geo1** NY 17.3      **Coupon** 4.500  
**Buyout** -      **LTV** 72.91      **#Pools** 125      **Geo2** CA 16.1      **1st Proj** 02/25/2015

**2) Scenarios**      **3) Bond Flows**      **3) Group Flows**      **3) Deal Flows**

1) 18 CPR  
2) 109 PSA  
3) 124 PSA  
4) 166 PSA  
5) 506 PSA  
6) 614 PSA  
7) 683 PSA

**Settle** 02/01/2015      **Table**      **Graph**

**Prepay**  
**18.00** **CPR**

**Price - Yield Calculations**

**Price** 15-16      **30/360**      **Factor** 01/2015      0.2955180900  
**Yield** 6.4810      **Call** N      **Date** mm/dd/yyyy      **Orig Bal** (USD) 2,450,000,000  
**Spread** 525.9 I      **Int Haircut** 0 %      **Your Orig Bal** 2,450,000,000  
**Idx Proj** Const.      **Prev Bal** 710,891,507

**Principal 3/25/15 - 1/25/40**  
**299 Cashflows**

Accrued 0.0000 for 0 days, Start 2/1/15, Delay 24, WAL 4.450

	Monthly	Coupon	Interest	Principal	Cashflow	Balance
1	3/25/15	4,500	2,665,843	0	2,665,843	697,994,467
2	4/25/15n	4,500	2,617,479	0	2,617,479	685,324,224
3	5/25/15n	4,500	2,569,966	0	2,569,966	672,876,870
4	6/25/15	4,500	2,523,288	0	2,523,288	660,648,564
5	7/25/15n	4,500	2,477,432	0	2,477,432	648,635,528
6	8/25/15	4,500	2,432,383	0	2,432,383	636,834,051
7	9/25/15	4,500	2,388,128	0	2,388,128	625,240,483
8	10/25/15n	4,500	2,344,652	0	2,344,652	613,851,238
9	11/25/15	4,500	2,301,942	0	2,301,942	602,662,789
10	12/25/15n	4,500	2,259,985	0	2,259,985	591,671,671
11	1/25/16	4,500	2,218,769	0	2,218,769	580,874,476

Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000  
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000  
SN 345678 EST GMT-5:00 6687-321-0 01-Feb-2015 12:31:27  
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# IO Accounting – GAAP

## Speed Assumption – Matches Realized Speeds

	Speed Assumption High	Speed Assumption Matches Realized	Speed Assumption Low
Speed Assumption	21 CPR	18 CPR	15 CPR
Yield Assumption	2.835%	6.481%	10.059%

Payment Date	Cashflow	Income Recorded	Premium Amortization	Carrying Value	Remaining Notional Balance	End of Quarter	
						Market Value	Mark to Market Gain/(Loss)
				\$ 112,222,995			
25-Feb-15	\$ 2,715,072	\$ 606,098	\$ 2,108,974	\$ 110,114,020	\$ 710,891,507		
25-Mar-15	\$ 2,665,843	\$ 594,707	\$ 2,071,136	\$ 108,042,885	\$ 697,994,467		
25-Apr-15	\$ 2,617,479	\$ 583,522	\$ 2,033,957	\$ 106,008,927	\$ 685,324,224		
25-May-15	\$ 2,569,966	\$ 572,537	\$ 1,997,429	\$ 104,011,498	\$ 672,876,870		
25-Jun-15	\$ 2,523,288	\$ 561,749	\$ 1,961,539	\$ 102,049,959	\$ 660,648,564	\$ 102,400,527	\$ 350,569
	\$ 13,091,648	\$ 2,918,612	\$ 10,173,036				
<b>Total Economic Income</b>						<b>\$ 3,269,181</b>	

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

# IO Accounting – GAAP

## Speed Assumption – Above Realized Speeds

	Speed Assumption High	Speed Assumption Matches Realized	Speed Assumption Low
Speed Assumption	21 CPR	18 CPR	15 CPR
Yield Assumption	2.835%	6.481%	10.059%

Payment Date	Cashflow	Income Recorded	Premium Amortization	Carrying Value	Remaining Notional Balance	End of Quarter	
						Market Value	Mark to Market Gain/(Loss)
				\$ 112,222,995			
25-Feb-15	\$ 2,715,072	\$ 265,127	\$ 2,449,945	\$ 109,773,050	\$ 710,891,507		
25-Mar-15	\$ 2,665,843	\$ 259,339	\$ 2,406,504	\$ 107,366,545	\$ 697,994,467		
25-Apr-15	\$ 2,617,479	\$ 253,653	\$ 2,363,826	\$ 105,002,720	\$ 685,324,224		
25-May-15	\$ 2,569,966	\$ 248,069	\$ 2,321,897	\$ 102,680,823	\$ 672,876,870		
25-Jun-15	\$ 2,523,288	\$ 242,583	\$ 2,280,705	\$ 100,400,118	\$ 660,648,564	\$ 102,400,527	\$ 2,000,409
	\$ 13,091,648	\$ 1,268,771	\$ 11,822,877				
						<b>Total Economic Income</b>	<b>\$ 3,269,181</b>

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

# IO Accounting – GAAP

## Speed Assumption – Below Realized Speeds

	Speed Assumption High	Speed Assumption Matches Realized	Speed Assumption Low
Speed Assumption	21 CPR	18 CPR	15 CPR
Yield Assumption	2.835%	6.481%	10.059%

Payment Date	Cashflow	Income Recorded	Premium Amortization	Carrying Value	Remaining Notional Balance	End of Quarter	
						Market Value	Mark to Market Gain/(Loss)
				\$ 112,222,995			
25-Feb-15	\$ 2,715,072	\$ 940,709	\$ 1,774,363	\$ 110,448,632	\$ 710,891,507		
25-Mar-15	\$ 2,665,843	\$ 925,836	\$ 1,740,007	\$ 108,708,625	\$ 697,994,467		
25-Apr-15	\$ 2,617,479	\$ 911,250	\$ 1,706,229	\$ 107,002,396	\$ 685,324,224		
25-May-15	\$ 2,569,966	\$ 896,948	\$ 1,673,018	\$ 105,329,377	\$ 672,876,870		
25-Jun-15	\$ 2,523,288	\$ 882,924	\$ 1,640,364	\$ 103,689,013	\$ 660,648,564	\$ 102,400,527	\$ (1,288,485)
	\$ 13,091,648	\$ 4,557,666	\$ 8,533,982				
<b>Total Economic Income</b>						<b>\$ 3,269,181</b>	

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

# Financial Reporting – Press Release

## Portfolio Activity for the Quarter

	Structured Security Portfolio				Total
	Pass-Through Portfolio	Interest-Only Securities	Inverse Interest Only Securities	Sub-total	
<b>Market Value - June 30, 2014</b>	<b>\$ 826,921,688</b>	<b>\$ 38,742,825</b>	<b>\$ 10,339,738</b>	<b>\$ 49,082,563</b>	<b>\$ 876,004,251</b>
Securities Purchased	611,511,944	9,470,472	9,043,948	18,514,420	630,026,364
Securities Sold	(298,635,287)	--	--	--	(298,635,287)
Losses on Sales	(1,959,822)	--	--	--	(1,959,822)
Return on Investment	n/a	(3,761,898)	(1,189,820)	(4,951,718)	(4,951,718)
Pay-downs	(23,547,236)	n/a	n/a	n/a	(23,547,236)
Premium Lost Due to Pay-downs	(1,461,801)	n/a	n/a	n/a	(1,461,801)
Mark to Market (Losses) Gains	(1,683,610)	1,495,175	246,114	1,741,289	57,679
<b>Market Value - September 30, 2014</b>	<b>\$ 1,111,145,876</b>	<b>\$ 45,946,574</b>	<b>\$ 18,439,980</b>	<b>\$ 64,386,554</b>	<b>\$ 1,175,532,430</b>

# Financial Reporting – Press Release

<b>Returns for the Quarter*</b>					
	<b>Pass-Through Portfolio</b>	<b>Structured Security Portfolio</b>			<b>Total</b>
		<b>Interest-Only Securities</b>	<b>Inverse Interest Only Securities</b>	<b>Sub-total</b>	
Income / (loss) (net of repo cost)	\$ 8,664,095	\$ (585,425)	\$ 388,676	\$ (196,749)	\$ 8,467,346
Realized and unrealized (losses) / gains	(5,105,233)	1,495,175	246,114	1,741,289	(3,363,944)
Hedge gains	3,057,651	n/a	n/a	n/a	3,057,651
<b>Total Return</b>	<b>\$ 6,616,513</b>	<b>\$ 909,750</b>	<b>\$ 634,790</b>	<b>\$ 1,544,540</b>	<b>\$ 8,161,053</b>
Beginning Capital Allocation	\$ 73,261,046	\$ 38,742,825	\$ 10,339,738	\$ 49,082,563	\$ 122,343,609
<b>Return on Invested Capital for the Quarter<sup>(1)</sup></b>	<b>9.0%</b>	<b>2.3%</b>	<b>6.1%</b>	<b>3.1%</b>	<b>6.7%</b>
Average Capital Allocation <sup>(2)</sup>	\$ 86,917,221	\$ 42,344,700	\$ 14,389,859	\$ 56,734,559	\$ 143,651,779
<b>Return on Average Invested Capital for the Quarter<sup>(3)</sup></b>	<b>7.6%</b>	<b>2.1%</b>	<b>4.4%</b>	<b>2.7%</b>	<b>5.7%</b>

\* As of September 30, 2014

(1) Calculated by dividing the Total Return by the Beginning Capital Allocation, expressed as a percentage.

(2) Calculated using two data points, the Beginning and Ending Capital Allocation balances.

(3) Calculated by dividing the Total Return by the Average Capital Allocation, expressed as a percentage.

# Financial Reporting – Form 10-Q

**ORCHID ISLAND CAPITAL, INC.**  
**STATEMENTS OF OPERATIONS**  
(Unaudited)

For the Nine and Three Months Ended September 30, 2014 and 2013

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2014	2013	2014	2013
Interest income	\$ 19,657,656	\$ 6,393,156	\$ 9,285,729	\$ 2,551,199
Interest expense	(1,904,894)	(817,219)	(818,383)	(293,913)
<b>Net interest income</b>	<b>17,752,762</b>	<b>5,575,937</b>	<b>8,467,346</b>	<b>2,257,286</b>
Realized gains (losses) on mortgage-backed securities	1,931,617	(1,490,712)	(1,959,822)	(667,182)
Unrealized gains (losses) on mortgage-backed securities	8,719,844	(9,072,712)	(1,404,122)	86,070
(Losses) gains on derivative instruments	(4,363,837)	4,095,788	3,057,651	(2,271,875)
<b>Net portfolio income (loss)</b>	<b>24,040,386</b>	<b>(891,699)</b>	<b>8,161,053</b>	<b>(595,701)</b>
<b>Expenses:</b>				
Management fees	1,275,500	489,700	543,000	179,500
Accrued incentive compensation	450,000	-	225,000	-
Directors' fees and liability insurance	404,927	207,309	164,641	82,924
Audit, legal and other professional fees	405,697	321,436	160,260	70,949
Direct REIT operating expenses	124,358	133,399	35,973	36,550
Other administrative	381,213	99,358	263,693	31,483
<b>Total expenses</b>	<b>3,041,695</b>	<b>1,251,202</b>	<b>1,392,567</b>	<b>401,406</b>
<b>Net income (loss)</b>	<b>\$ 20,998,691</b>	<b>\$ (2,142,901)</b>	<b>\$ 6,768,486</b>	<b>\$ (997,107)</b>
<b>Basic and diluted net income (loss) per share</b>	<b>\$ 2.53</b>	<b>\$ (0.74)</b>	<b>\$ 0.63</b>	<b>\$ (0.30)</b>
<b>Weighted Average Shares Outstanding</b>	<b>8,314,512</b>	<b>2,900,786</b>	<b>10,710,153</b>	<b>3,341,665</b>
<b>Dividends declared per common share</b>	<b>\$ 1.620</b>	<b>\$ 0.945</b>	<b>\$ 0.540</b>	<b>\$ 0.405</b>

*See Notes to Financial Statements*



# Income Recognition: Tax

# Sample Security – Pricing Assumptions

FNS 404 2		15-10 <sup>1</sup> / <sub>4</sub> / 15-18 <sup>1</sup> / <sub>4</sub>		CUSIP 3136FGJ81		Yield 7.638/7.150									
As of 30 Jan		Prepay 286PSA		WAL 4.61		Collateral 100.0% FNCL 4.5% BVAL									
FNS 404 2 Mtge		99 Feedback		Security Description											
CUSIP 3136FGJ81		4.958(293)58		FNCL 4.5 M		95 Buy 96 Sell									
1) Bond Summary		2) Group Summary		3) Deal Summary		4) Comments									
Issuer FANNIEMAE STRIP						5) Prospectus									
Series 404		Class 2		Maturity 05/25/2040		ISIN US3136FGJ811 6) Lead Mgr DBS									
7) Class Description IO,NTL				BBGID BBG000B04W10		8) Trustee FNM									
Current (Jan 2015)		Original Issue		Payment Details		Additional Info									
Balance	724,019,321	Bal USD	2,450,000,000	Next Pay	02/25/2015	TRACE Eligible									
Factor	0.295518090	WAL	6.4Yr @ 250PSA	Rcd Date	01/31/2015										
Coupon	4.50%	1st Coupon	4.50%	Pay Date	25th										
Beg Accrue	01/01/2015	1st Payment	05/25/2010	Frequency	Monthly										
End Accrue	01/31/2015	1st Settle	04/30/2010	Pay Delay	24 Days										
Class/Deal Pct	N/A	Dated Date	04/01/2010	Day Count	30/360										
		PX	04/07/2010	Call	Non-Callable	FFIEC	Fail								
		Class/Deal Pct	0%			Min Size	100,000								
						Incr	1								
9) Historical Paydown (CPD)												PSA	CPR		
	Jan15	Dec	Nov	Oct	Sep	Aug	Jul	Jun	May	Apr	Mar	Feb14	1m	330	19.8
PSA	330	261	262	251	231	324	237	190	243	218	128	176	3m	285	17.1
CPR	19.8	15.6	15.7	15.1	13.9	19.4	14.2	11.4	14.6	13.1	7.7	10.6	6m	277	16.6
Fct	0.30	0.30	0.31	0.31	0.32	0.32	0.33	0.33	0.34	0.34	0.35	0.35	12m	239	14.3
Cpn	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	Life	456	21.3
Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000															
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2015 Bloomberg Finance L.P.															
SN 345678 EST GMT-5:00 G627-5956-0 31-Jan-2015 10:37:00															

# Sample Security – Projected Notional Balance at Pricing Date

**CFT**  
Enter all values and hit <Go>

**FNS 404 2 Mtge**      **22) Export**      **Cash Flow Table**

CUSIP 3136FGJ81      4.9580(293)58      **95 Buy**      **96 Sell**

**1M**      **CPR** 19.80      **PSA** 330      **60D+** -      **WAOLS** 233M      **Geo1** NY 17.3      **Coupon** 4.500  
**Buyout** -      **LTV** 72.91      **#Pools** 125      **Geo2** CA 16.1      **1st Proj** 02/25/2015

**21) Scenarios**      **31) Bond Flows**      **32) Group Flows**      **33) Deal Flows**

1) 250 PSA  
2) 109 PSA  
3) 124 PSA  
4) 166 PSA  
5) 506 PSA  
6) 614 PSA  
7) 683 PSA

**31) Bond Flows**      **Settle** 04/30/2010      **ACTUAL cashflows before 2/25/15**      **Table**      **Graph**

**Prepay**  
250 PSA

**Price - Yield Calculations**

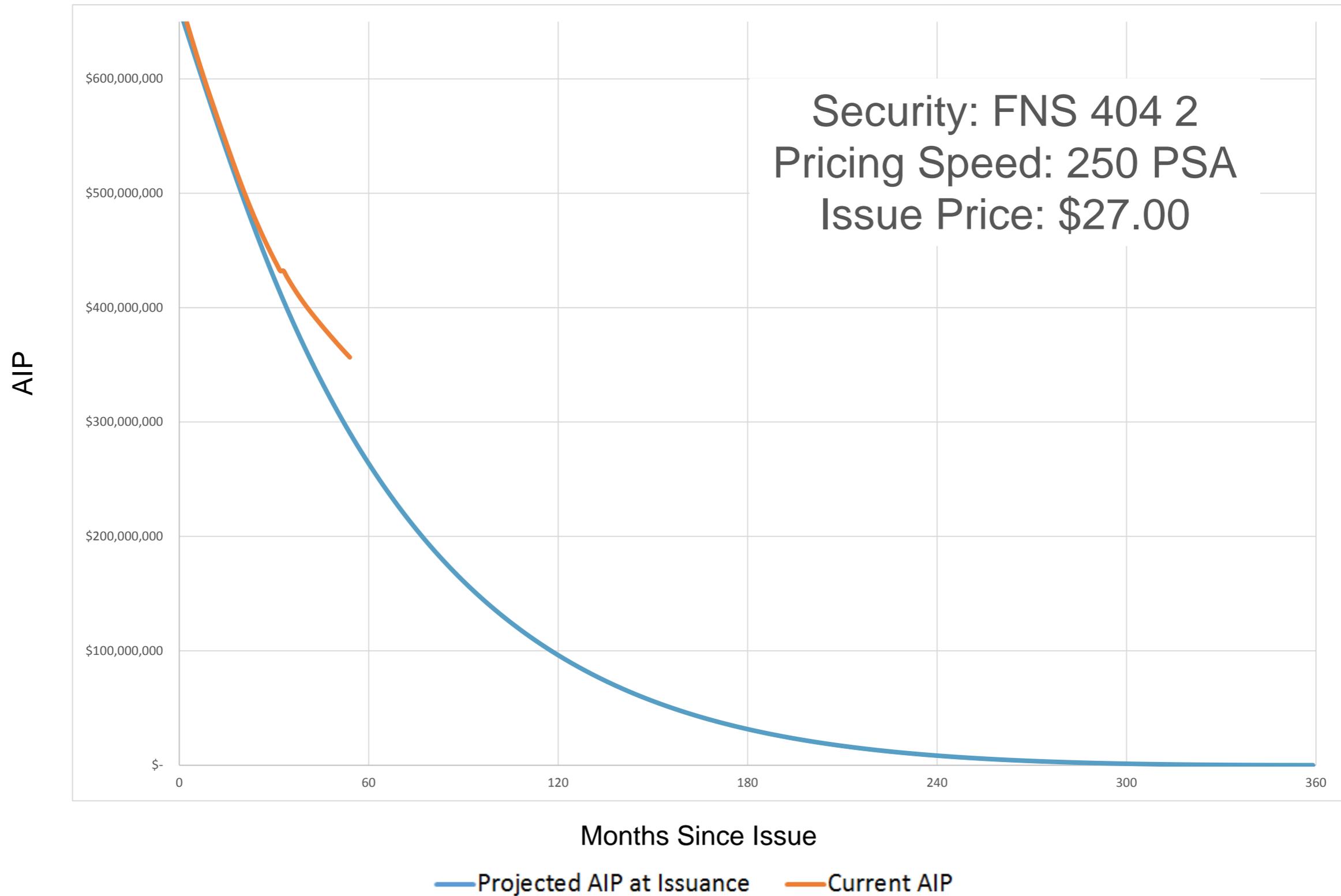
Price 15-18 1/4      30/360      **Factor** 01/2015      0.2955180900  
Yield 6.0300      Call N      **Orig Bal** (USD)      2,450,000,000  
Spread 382.3 I      **Int Haircut** 0 %      **Your Orig Bal**      2,450,000,000  
**Idx Proj** Const.      **Prev Bal**      2,450,000,000  
Principal 5/25/10 - 11/25/39

Accrued 0.3625 for 29 days, Start 4/1/10, Delay 24, WAL 4.455      355 Cashflows

	Monthly	Coupon	Interest	Principal	Cashflow	Balance
1	5/25/10	4.500	9,187,456	0	9,187,456	2,444,401,792
2	6/25/10	4.500	9,166,464	0	9,166,464	2,438,424,576
3	7/25/10n	4.500	9,144,064	0	9,144,064	2,425,698,176
4	8/25/10	4.500	9,096,320	0	9,096,320	2,407,405,056
5	9/25/10n	4.500	9,027,712	0	9,027,712	2,370,681,600
6	10/25/10	4.500	8,890,112	0	8,890,112	2,326,974,720
7	11/25/10n	4.500	8,726,144	0	8,726,144	2,275,991,424
8	12/25/10n	4.500	8,534,912	0	8,534,912	2,218,545,920
9	1/25/11	4.500	8,319,488	0	8,319,488	2,175,395,456
10	2/25/11	4.500	8,157,696	0	8,157,696	2,152,887,424
11	3/25/11	4.500	8,073,344	0	8,073,344	2,138,909,440

Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000  
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2015 Bloomberg Finance L.P.  
SN 345678 EST GMT-5:00 6627-5956-0 31-Jan-2015 10:43:32

# Adjusted Issue Price (AIP)



# IO Income Table – Tax

## Original Issue Discount (OID)

Pricing Yield Assumption

1.2%

Payment Date	Cashflow	Adjusted Issue Price	OID Income Recorded	Carrying Value	Remaining Notional Balance	End of Quarter Market Value	Mark to Market Gain/(Loss)
<i>Initial Values</i>		\$ 112,222,995		<i>Current OID and Market Value:</i> \$ 112,222,995			
25-Feb-15	\$ 2,715,072	\$ 109,620,146	\$ 112,223	\$ 109,620,146	\$ 710,891,507		
25-Mar-15	\$ 2,665,843	\$ 107,063,923	\$ 109,620	\$ 107,063,923	\$ 697,994,467		
25-Apr-15	\$ 2,617,479	\$ 104,553,508	\$ 107,064	\$ 104,553,508	\$ 685,324,224		
25-May-15	\$ 2,569,966	\$ 102,088,095	\$ 104,554	\$ 102,088,095	\$ 672,876,870		
25-Jun-15	\$ 2,523,288	\$ 99,666,895	\$ 102,088	\$ 99,666,895	\$ 660,648,564	n/a	n/a
	<b>\$ 13,091,648</b>		<b>\$ 535,549</b>				
						<b>Total Economic Income</b>	<b>\$ 535,549</b>

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

# IO Income Table – Tax

## Market Premium

Pricing Yield Assumption

1.2%

Payment Date	Cashflow	Adjusted Issue Price	OID Income Recorded	Market Premium Amortization	Taxable Income Recorded	Remaining Market Premium	Carrying Value	Remaining Notional Balance	End of Quarter Market Value	Mark to Market Gain/(Loss)
<i>Initial Values</i>		\$ 112,222,995				\$ 2,500,000	\$ 114,722,995			
25-Feb-15	\$ 2,715,072	\$ 109,620,146	\$ 112,223	\$ 46,760	\$ 65,463	\$ 2,453,240	\$ 112,120,146	\$ 710,891,507		
25-Mar-15	\$ 2,665,843	\$ 107,063,923	\$ 109,620	\$ 45,675	\$ 63,945	\$ 2,407,565	\$ 109,563,923	\$ 697,994,467		
25-Apr-15	\$ 2,617,479	\$ 104,553,508	\$ 107,064	\$ 44,610	\$ 62,454	\$ 2,362,955	\$ 107,053,508	\$ 685,324,224		
25-May-15	\$ 2,569,966	\$ 102,088,095	\$ 104,554	\$ 43,564	\$ 60,990	\$ 2,319,391	\$ 104,588,095	\$ 672,876,870		
25-Jun-15	\$ 2,523,288	\$ 99,666,895	\$ 102,088	\$ 42,537	\$ 59,551	\$ 2,276,855	\$ 102,166,895	\$ 660,648,564	n/a	n/a
	<b>\$ 13,091,648</b>		<b>\$ 535,549</b>	<b>\$ 223,145</b>	<b>\$ 312,403</b>					
									<b>Total Economic Income \$ 312,403</b>	

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

# IO Income Table – Tax

## Market Discount

Pricing Yield Assumption

1.2%

Payment Date	Cashflow	Adjusted Issue Price	OID Income Recorded	Market Discount Amortization	Taxable Income Recorded	Remaining Market Discount	Carrying Value	Remaining Notional Balance	End of Quarter Market Value	Mark to Market Gain/(Loss)
<i>Initial Values</i>		\$ 112,222,995				\$ 2,500,000	\$ 109,722,995			
25-Feb-15	\$ 2,715,072	\$ 109,900,703	\$ 112,223	\$ 280,557	\$ 392,780	\$ 2,219,443	\$ 107,400,703	\$ 710,891,507		
25-Mar-15	\$ 2,665,843	\$ 107,619,513	\$ 109,901	\$ 274,752	\$ 384,652	\$ 1,944,691	\$ 105,119,513	\$ 697,994,467		
25-Apr-15	\$ 2,617,479	\$ 105,378,702	\$ 107,620	\$ 269,049	\$ 376,668	\$ 1,675,642	\$ 102,878,702	\$ 685,324,224		
25-May-15	\$ 2,569,966	\$ 103,177,561	\$ 105,379	\$ 263,447	\$ 368,825	\$ 1,412,195	\$ 100,677,561	\$ 672,876,870		
25-Jun-15	\$ 2,523,288	\$ 101,015,395	\$ 103,178	\$ 257,944	\$ 361,121	\$ 1,154,251	\$ 98,515,395	\$ 660,648,564	n/a	n/a
	<b>\$ 13,091,648</b>		<b>\$ 538,299</b>	<b>\$ 1,345,749</b>	<b>\$ 1,884,048</b>					
									<b>Total Economic Income \$ 1,884,048</b>	

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.



# Hedging with Eurodollar Futures

# Overview

## Topic Point

## Slide

- |                          |         |
|--------------------------|---------|
| ▪ Repo Funding           | 38      |
| ▪ Hedge Options          | 39 - 40 |
| ▪ Swaps                  | 41 - 44 |
| ▪ Eurodollar Futures     | 45 - 49 |
| ▪ Total Return Scenarios | 50 - 53 |

# REITs and Repo

Orchid and many other mortgage REITs rely almost exclusively on repo funding as their primary vehicle for leveraging equity or long term debt capital

---

## Example: ORC raises \$100 million net equity capital

- Use of Proceeds: \$600 million 5 year MBS assets
  - Assume purchase price of 100-00, prepayment rate of 0% CPR, no ordinary amortization (5-year bullet), a coupon of 2.35%, repo haircut of 5% and a floating repo rate starting at 0.35% (35bps) for a 3 month repo
  - ORC buys \$100 million and borrows against 95% of the FMV of those assets, purchases more of the same, borrows against 95% of those assets....., until the target portfolio size and composition described above are achieved
- Quarter One Balance Sheet: \$600 million assets, \$570 million in 3-month repo liabilities, \$70 million in cash, leverage ratio 6x
- Quarter One Income and Cash: \$3.525 million MBS interest, no amortization (recall the oversimplified assumptions), \$498.75 thousand repo interest expense. Quarter One Net Income and Cash = \$3,026,250
- Quarter One Interest Rate Risk
  - Income DV01 \$14,250
  - MBS duration roughly 4.75 / MBS DV01 approximately \$285,000
  - If rates increase by 100 bps income immediately decreases by 47% and Book Value declines by 28.5%
  - Equity Duration approximately  $6.0 \times 4.75 = 28.5$

# Common Hedge Alternatives

Short Treasuries

Short Treasury Futures

Pay Fixed Swap

Short Eurodollar Futures

Structured MBS Products

Options

- Caps / Floors
- Swaptions
- Mid Curve Options
- Mortgage Options
- Options on Treasuries and Treasury Futures
- Options on Eurodollar Futures

The most common duration hedge for mortgage REITs is the pay fixed swap, however, shorting a series of Eurodollar futures yields virtually identical economic results with increased price transparency, liquidity and reduced margin requirements

# Orchid Island Tax Hedges

Orchid Island designates all derivative financial instruments as hedges for federal income tax reporting purposes.

- Derivative financial instruments are not good REIT assets for the purposes of the income or asset tests.
- Failure to designate derivative instruments as hedges could result in taxable income or loss of REIT status.
- Compliance with Treasury Regulations
  - Timely designation of hedge
  - Identification of Hedge Period and Matching – Our method of accounting adopted with respect to each interest rate hedging transaction will result in a reasonable matching of the timing of income deduction, gain or loss from the hedging transaction with the timing of income, deduction, gain or loss from the item or items being hedged (i.e., the repurchase agreements or other short-term financing transactions) as required by Treasury Regulations Section 1.446-4(b)
  - See table below

Common Hedge Instruments						
	Treasury Notes / Bond	Treasury Futures	Swaps	Eurodollar Futures	Structured MBS	Swaptions
<b>Trade Type</b>	Short	Short	Pay Fixed	Short	Long	Payer Swaption
<b>Tax Hedge Accounting</b>	Yes	Yes	Yes	Yes	No (Good REIT Asset)	Yes
<b>Hedge Period if Held to Maturity / Last Trade / Exercise Date</b>	Remaining Life of Note / Bond	Futures Settlement Date to Maturity of Underlying	Underlying Swap Maturity	90 Day Deposit Period Associated with Futures Contract	N/A	Exercise / Expiry Date to End of Underlying Swap
<b>Hedge Period if Hedge is Bought Back / Terminated Early</b>	Same as Above	Futures Buy Back Date Through Maturity of Underlying	Remaining Maturity of Swap	90 Day Deposit Period Associated with Futures Contract	N/A	Date Swaption is Novated / Sold Through the End of the Underlying Swap Maturity
<b>Distribution of Hedge Gains / Losses</b>	Evenly Over Hedge Period	Evenly Over Hedge Period	Evenly Over Hedge Period	Evenly Over Hedge Period	N/A	Evenly Over Hedge Period

# Hedging with Swaps

## Hypothetical Portfolio Plus \$570 million Pay Fixed Swap Funding Hedge

- IRS regulations generally prohibit REITs from hedging MBS assets
- Add \$570 million pay fixed swap with a fixed rate of 1.35% vs. receiving floating 3-Month LIBOR
- Swap DV01 for \$570 million notional balance \$276,908.75
- New Portfolio DV01 \$9,091 vs. \$285,000; new equity duration less than 1.0
- To the extent repo maintains the same spread to LIBOR over the life of the 5 year life of the asset, the income for the next five years will be \$1.46 million per quarter vs. quarter 1 income in the unhedged example of \$3.0 million

### Scenario A: Libor remains unchanged for 5 years

- If LIBOR remained at its current level of 25 basis points the foregone income associated with the portfolio hedge would be roughly \$1.6 million per quarter / \$31 million over the 5 year life of the portfolio

### Scenario B: Forwards are realized

- Using market based information forward rates can be calculated
- Forward rates have not necessarily been the best forecasting tool but they do represent the market's current expectation for future rates
- The forward curve starts at 25bps and steadily increases to 2.10% in November 2019 (the last quarter in the 5 year life of the illustrative portfolio)
- If forward 3-Month LIBOR yields are realized and the spread between repo and 3-Month LIBOR remains constant, income between the two alternatives, over the five year horizon, is identical
  - NPV of Fixed and Floating Cashflows = 0 at Inception

---

## Balance Sheet Impact

- NPV at time of trade is \$0
- Swap margin requirement of roughly 2% reduces cash by \$11.4 million
- No other changes

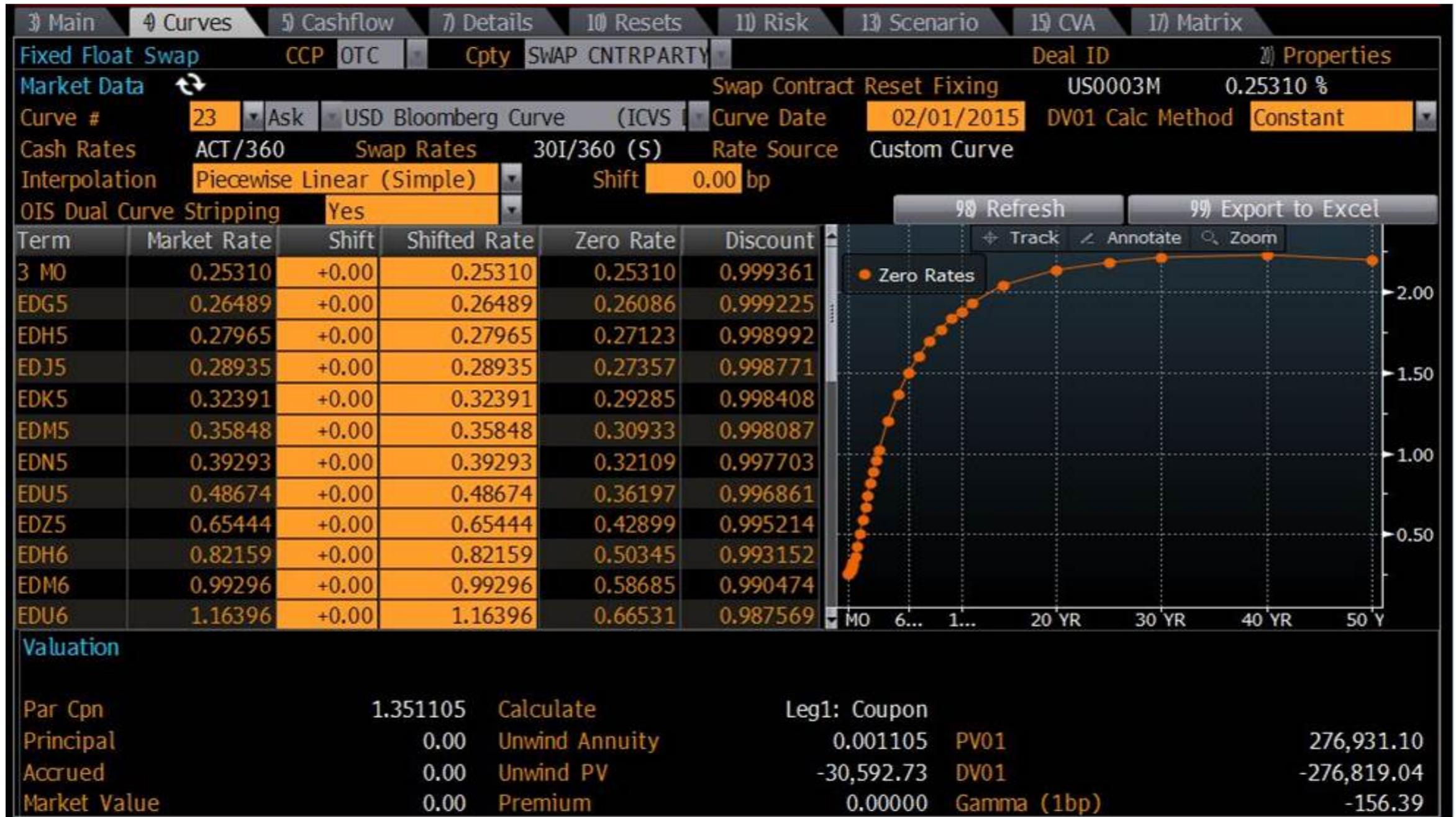
\*See Swap Exhibits

# Swap Exhibit 1

3) Main		4) Curves		5) Cashflow		7) Details		10) Resets		11) Risk		13) Scenario		15) CVA		17) Matrix							
Fixed Float Swap		CCP OTC		Cpty SWAP CNTRPARTY		Deal ID		20) Properties		31) Load		32) Save		34) Ticket		30) Trade Activity		37) CCP Margin		38) CVA		43) Send to VCON/TR	
Leg 1		Pay Fixed		Leg ID		Leg 2		Receive Float		Leg ID		Notional		570MM		Index		US0003M		Currency		USD	
Notional		570MM		Coupon		1.351105 %		Effective		02/03/2015		Latest Index		0.25310		Maturity		02/03/2020		Tenor		3 Month	
Currency		USD		Calc Basis		Money Mkt		Maturity		02/03/2020		Leverage		1.00000		Pay Freq		SemiAnnual		Unwind Cpn		1.350000 %	
Effective		02/03/2015		Day Count		30I/360		Reset Freq		Quarterly		Spread		0.00 bp		Day Count		ACT/360		MV		-570,000,000.00	
Maturity		02/03/2020		Detail				Pay Freq		Quarterly		Accrued		0.00		MV		570,000,000.00		Premium		-100.00	
Pay Freq		SemiAnnual		Detail				Day Count		ACT/360		DV01		-291,218.16		Premium		100.00		DV01		14,399.12	
Market		CSA Coll Ccy N/A		OIS DC Stripping		ON		Dscnt Curve		23 Ask		USD Bloomberg Curve		Fwd Curve		23 Ask		USD Bloomberg Curve					
Curve Date		02/01/2015		Valuation		02/03/2015																	
Valuation		Par Cpn		1.351105		Calculate		Leg1: Coupon															
Principal		0.00		Unwind Annuity		0.001105		PV01		276,931.10													
Accrued		0.00		Unwind PV		-30,592.73		DV01		-276,819.04													
Market Value		0.00		Premium		0.00000		Gamma (1bp)		-156.39													

Source: Bloomberg

# Swap Exhibit 2



Source: Bloomberg

# Swaps Table

<HELP> for explanation.  
 \*\* YOU ARE IN BLOOMBERG SEF MODE \*\*

Interest Rate Swaps | 2) Tools | 3) Settings | 4) Trading Access | IRS Multi-Dealer RFQ

14:42 \* Demo Mode \*

20) EUR				21) USD				22) USD MAC				23) USD IMM				24) GBP				25) CHF				26) AUD				27) JPY				28) SEK			
Semi 3M				S/A Crv				S/A Bfly				Annual 3M				Ann Crv				Ann Bfly				OIS				Basis							
USD Semi vs 3M Libor																USD Spreads vs Treasuries																			
30) 1 Year	0.396 / 0.399			-0.014			≡			47) 1 Year	25.241 / 26.049			-0.484			≡																		
31) 2 Year	0.689 / 0.694			-0.053			≡			48) 2 Year	23.740 / 24.448			+1.368			≡																		
32) 3 Year	0.960 / 0.965			-0.081			≡			49) 3 Year	22.322 / 23.113			+1.072			≡																		
33) 4 Year	1.168 / 1.173			-0.097			≡			50) 4 Year	22.500 / 23.250			+1.000			≡																		
34) 5 Year	1.328 / 1.332			-0.105			≡			51) 5 Year	16.938 / 17.750			+0.943			≡																		
35) 6 Year	1.459 / 1.464			-0.106			≡			52) 6 Year	14.750 / 15.750			+0.000			≡																		
36) 7 Year	1.565 / 1.569			-0.104			≡			53) 7 Year	10.188 / 10.843			-0.908			≡																		
37) 8 Year	1.651 / 1.657			-0.103			≡			54) 8 Year	12.750 / 13.750			-0.250			≡																		
38) 9 Year	1.724 / 1.729			-0.102			≡			55) 9 Year	14.000 / 14.750			+0.250			≡																		
39) 10 Year	1.784 / 1.789			-0.102			≡			56) 10 Year	14.267 / 14.734			+0.875			≡																		
40) 12 Year	1.880 / 1.885			-0.100			≡			57) 12 Year	23.500 / 24.500			+1.125			≡																		
41) 15 Year	1.979 / 1.983			-0.097			≡			58) 15 Year	18.375 / 20.375			+0.625			≡																		
42) 20 Year	2.074 / 2.079			-0.094			≡			59) 20 Year	13.875 / 14.875			+0.625			≡																		
43) 25 Year	2.119 / 2.124			-0.092			≡			60) 25 Year	3.750 / 5.625			+0.938			≡																		
44) 30 Year	2.147 / 2.151			-0.091			≡			61) 30 Year	-7.233 / -6.766			+0.626			≡																		
45) 40 Year	2.167 / 2.174			-0.090			≡																												
46) 50 Year	2.146 / 2.157			-0.091			≡																												

\*Non-benchmark spread execution coming soon

Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000  
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# Eurodollar Introduction

## Contract Description and Hedging

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- Each contract is a traded future on a 1 or 3 month LIBOR denominated deposit rate
  - For simplicity this presentation focuses on the quarterly contracts which cash settle on each March, June, September and December
- At the settlement date the final value of each contract is determined by subtracting the prevailing 3-Month LIBOR rate from a price of 100
  - As the expectation for 3-Month LIBOR increases the price of the contract declines
  - By taking a short position in one or a series of Eurodollar futures the hedger enters into a trade which increases in value as rates / expected funding costs rise

### GAAP Accounting:

- The Company designates all Eurodollar contracts as Level I assets pursuant to ASC 820
  - Level I asset values are readily observable and, in the case of Eurodollar futures, quoted trade levels published by a number of data providers
    - Note: While swaps are considered highly liquid, they are typically considered Level II assets
- Fair Value Option - The Company has elected not to treat any of its derivative financial instruments as hedges. FASB ASC Topic 815, Derivatives and Hedging, requires that all derivative instruments be carried at fair value. Changes in fair value are recorded in earnings for each period

# Eurodollar Introduction

## ...Continued

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- Eurodollar futures trade in \$1 million dollar notional values per contract
  - To replicate the \$570 million swap hedge the Company would sell-short 570 contracts for each sequential quarterly expiry over the next 20 quarters in order to achieve the desired 5 year hedge period (see Eurodollar Exhibit 1)
    - By shorting each of these contracts the Company locks-in a fixed, Eurodollar based, hedge, which is economically the same as entering into a pay fixed swap (in reality there are de-minimis differences between the forward and futures rates – this is a topic for a more technical discussion)
- Since the contracts represent highly liquid and highly visible market clearing levels for discrete 3-month LIBOR deposit rates in the future, the implied yields are frequently used in swap models to determine forward rates and thereby used to solve for the fixed swap rate
- While the economics of the Eurodollar and swap hedges are virtually identical, there are income, book value, and tax implications associated with each hedge type
  - In the illustrative example when the Company enters into the 5 year pay fixed swap it executes one trade vs. shorting several contracts throughout time
  - As discussed, the rates implied by the price of each Eurodollar future sets a forward rate. Rather than having one average fixed rate which equates to the average of the forward rates the Eurodollar futures “lock-in” several quarterly rates over the horizon of the hedging period

# Eurodollar Exhibit 1

Illustrative Eurodollar Position									Initial Margin	Initial Margin
Contract	Long / Short	Position	Notional Balance	Current Price	Implied Forward	Cumulative Forward Rate	+ 100 BP Shock Price	+ 100 BP Shock P&L	Per Contract	Requirement
EDH5 Comdty	Short	-570	(570,000,000)	99.73	0.27	0.27	98.73	1,425,000	160	(91,200)
EDM5 Comdty	Short	-570	(570,000,000)	99.64	0.36	0.31	98.64	1,425,000	350	(199,500)
EDU5 Comdty	Short	-570	(570,000,000)	99.505	0.50	0.38	98.51	1,425,000	350	(199,500)
EDZ5 Comdty	Short	-570	(570,000,000)	99.335	0.67	0.45	98.34	1,425,000	350	(199,500)
EDH6 Comdty	Short	-570	(570,000,000)	99.16	0.84	0.53	98.16	1,425,000	450	(256,500)
EDM6 Comdty	Short	-570	(570,000,000)	98.98	1.02	0.61	97.98	1,425,000	450	(256,500)
EDU6 Comdty	Short	-570	(570,000,000)	98.81	1.19	0.69	97.81	1,425,000	450	(256,500)
EDZ6 Comdty	Short	-570	(570,000,000)	98.655	1.35	0.77	97.66	1,425,000	450	(256,500)
EDH7 Comdty	Short	-570	(570,000,000)	98.53	1.47	0.85	97.53	1,425,000	575	(327,750)
EDM7 Comdty	Short	-570	(570,000,000)	98.41	1.59	0.92	97.41	1,425,000	575	(327,750)
EDU7 Comdty	Short	-570	(570,000,000)	98.315	1.69	0.99	97.31	1,425,000	700	(399,000)
EDZ7 Comdty	Short	-570	(570,000,000)	98.22	1.78	1.06	97.22	1,425,000	800	(456,000)
EDH8 Comdty	Short	-570	(570,000,000)	98.15	1.85	1.12	97.15	1,425,000	800	(456,000)
EDM8 Comdty	Short	-570	(570,000,000)	98.08	1.92	1.18	97.08	1,425,000	800	(456,000)
EDU8 Comdty	Short	-570	(570,000,000)	98.02	1.98	1.23	97.02	1,425,000	800	(456,000)
EDZ8 Comdty	Short	-570	(570,000,000)	97.955	2.05	1.28	96.95	1,425,000	800	(456,000)
EDH9 Comdty	Short	-570	(570,000,000)	97.905	2.10	1.33	96.91	1,425,000	800	(456,000)
EDU9 Comdty	Short	-570	(570,000,000)	97.805	2.19	1.38	96.81	1,425,000	800	(456,000)
EDZ9 Comdty	Short	-570	(570,000,000)	97.755	2.25	1.42	96.76	1,425,000	800	(456,000)
<b>Total / Average</b>		<b>-10,830</b>		<b>98.58</b>	<b>1.42</b>	<b>1.42</b>	<b>97.58</b>	<b>27,075,000</b>	<b>593</b>	<b>(6,418,200)</b>

Source: Bloomberg

# Eurodollar Exhibit 2: Market Depth

EDM5 COMB Comdty		95 Settings		Market Depth Monitor			
Exchanges: <input checked="" type="checkbox"/> CME							
Zoom 100%							
1) Price Book							
CC	Total	Ord	Bid Size	Price	Ask Size	Ord	Total
	0		0	Over		0	77183
				99.655	580	8	77183
				99.650	3282	17	76603
				99.645	40792	30	73321 ic
				99.640	32469	62	32529 ic
				99.635	60	3	60
ic	57619	61	57619	99.630			
ic	99182	19	41563	99.625			
	100990	16	1808	99.620			
	101695	7	705	99.615			
	102334	7	639	99.610			
90DAY EURO\$ FUTR Jun15							
				Avg Vol 30 Day	228742.17		
VWAP				99.6342	Theo Auct Price .000		
Beta				.000	Theo Auct Vol		
% Change				-.01%			
Average Buy/Sell Price							
Buy		Amount		0			
Sell		Avg Price		99.6350			
		Remaining		0			
5) Trade Recap (QR)							
	Time	Size	Price				
	13:12:31	1	99.635				
	13:12:31	1	99.635				
	13:12:02	3	99.635				
	13:12:02	2	99.635				
	13:12:02	2	99.635				
	13:12:02	7	99.635				
	13:11:21	3	99.635				
	13:11:21	5	99.640				
	13:10:29	6	99.640				
	13:10:29	2	99.640				
	13:10:29	5	99.640				
	13:10:29	6	99.640				
	13:10:27	2	99.635				
	13:10:16	2	99.635				
	13:10:16	14	99.635				
	13:10:16	17	99.635				
	13:10:16	20	99.635				
	13:10:16	82	99.635				
	13:10:12	1	99.635				

Source: Bloomberg

# Dec 17 Eurodollar Contract – Yield History



Source: Bloomberg



# Total Rate of Return Scenarios

# Taxable Income and Book Value

## Scenario A: LIBOR Remains at 25bps (Repo at 35bps) for 5 Years Beginning BV \$10 / Share

	Share Count	MBS Interest	Repo Interest	Swap Hedge					Eurodollar Hedge				
				Interest Expense Hedge Adjustment	Taxable Income	Mark to Market	Ending Book Value	Annual Tot Return	Interest Expense Hedge Adjustment	Taxable Income	Mark to Market	Ending Book Value	Annualized TROR
<b>Year 1</b>	10,000,000	\$14,100,000	\$ (1,995,000)	(\$6,270,000)	\$5,835,000	(\$3,573,221)	\$9.64	2%	(\$840,750)	\$11,264,250	\$ (9,114,158)	\$9.09	2%
<b>Year 2</b>	10,000,000	\$14,100,000	\$ (1,995,000)	(\$6,270,000)	\$5,835,000	(\$2,592,438)	\$9.38	3%	(\$4,289,250)	\$7,815,750	\$ (4,565,843)	\$8.63	4%
<b>Year 3</b>	10,000,000	\$14,100,000	\$ (1,995,000)	(\$6,270,000)	\$5,835,000	(\$1,163,407)	\$9.27	5%	(\$7,410,000)	\$4,695,000	\$ -	\$8.63	5%
<b>Year 4</b>	10,000,000	\$14,100,000	\$ (1,995,000)	(\$6,270,000)	\$5,835,000	\$1,913,866	\$9.46	8%	(\$8,855,093)	\$3,249,907	\$ 4,565,843	\$9.09	9%
<b>Year 5</b>	10,000,000	\$14,100,000	\$ (1,995,000)	(\$6,270,000)	\$5,835,000	\$5,415,200	\$10.00	12%	(\$9,954,908)	\$2,150,093	\$ 9,114,158	\$10.00	12%
<b>Total</b>	<b>10,000,000</b>	<b>\$70,500,000</b>	<b>\$ (9,975,000)</b>	<b>(\$31,350,000)</b>	<b>\$29,175,000</b>	<b>\$0</b>	<b>\$10.00</b>	<b>6%</b>	<b>(\$31,350,000)</b>	<b>\$29,175,000</b>	<b>\$ -</b>	<b>\$10.00</b>	<b>6%</b>

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

- MBS interest remains constant
- Repo interest remains constant

### Swap Hedge

- Taxable interest expense is increased in equal increments over the horizon period as the swap rolls down the curve.
- Taxable Income is constant resulting from the pay fixed swap. The lower than initially anticipated floating rate inflows are offset by lower than expected repo rates.
- The negative mark to market resulting from lower than expected rates is monetized over time which offsets the impact on book value. Total return gradually increases for the same reason.

### Eurodollar Hedge

- Taxable interest expense rises over the horizon as the largest market to market hit occurs on contracts in the 4-5 year range.
- Taxable income decreases as hedge losses are monetized over time. Alternatively the mark to market impact is higher when there are a large number of hedges outstanding.
- While taxable income is the lowest in Year 5, the MBS interest income is unchanged. The large difference between MBS interest net of repo funding expense and the taxable income distribution requirement creates an increase in book value.

# Taxable Income and Book Value

## Scenario B: Forward Curve Exactly Realized Forward Repo / LIBOR Spread 10bps - Beginning BV \$10 / Share

	Share Count	MBS Interest	Repo Interest	Swap Hedge					Eurodollar Hedge				
				Interest Expense Hedge Adjustment	Taxable Income	Mark to Market	Ending Book Value	Annual Tot Return	Interest Expense Hedge Adjustment	Taxable Income	Mark to Market	Ending Book Value	Annualized TROR
<b>Year 1</b>	10,000,000	\$14,100,000	\$ (2,835,750)	(\$5,556,607)	\$5,707,643	\$0	\$10.00	6%	\$0	\$11,264,250	\$ -	\$10.00	11%
<b>Year 2</b>	10,000,000	\$14,100,000	\$ (6,284,250)	(\$2,029,861)	\$5,785,889	\$0	\$10.00	6%	\$0	\$7,815,750	\$ -	\$10.00	8%
<b>Year 3</b>	10,000,000	\$14,100,000	\$ (9,405,000)	\$1,132,959	\$5,827,959	\$0	\$10.00	6%	\$0	\$4,695,000	\$ -	\$10.00	5%
<b>Year 4</b>	10,000,000	\$14,100,000	\$(10,850,093)	\$2,674,998	\$5,924,905	\$0	\$10.00	6%	\$0	\$3,249,907	\$ -	\$10.00	3%
<b>Year 5</b>	10,000,000	\$14,100,000	\$(11,949,908)	\$3,778,512	\$5,928,604	\$0	\$10.00	6%	\$0	\$2,150,093	\$ -	\$10.00	2%
<b>Total</b>	<b>10,000,000</b>	<b>\$70,500,000</b>	<b>\$(41,325,000)</b>	<b>\$0</b>	<b>\$29,175,000</b>	<b>\$0</b>	<b>\$10.00</b>	<b>6%</b>	<b>\$0</b>	<b>\$29,175,000</b>	<b>\$ -</b>	<b>\$10.00</b>	<b>6%</b>

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

- MBS interest remains constant
- Repo interest gradually increases over time as forwards are realized

### Swap Hedge

- Taxable interest expense is increased in years 1 and 2 resulting from swap fixed rate outflows being higher than swap floating rate inflows. Since forwards are realized there is no mark to market adjustment in any period.
- Taxable income is steady over the smoothed hedge period.

### Eurodollar Hedge

- Taxable interest expense is unchanged because the forwards are settled / covered at the same price that the shorts were initiated (forwards realized). Mark to market is \$0 for the same reason.
- Taxable income decreases as repo rates gradually rise.
- Total return, MBS Interest, Repo Interest, Taxable Income, Book Value and Mark to Market are identical for each hedge instrument.

# Taxable Income and Book Value

## Scenario C: Realized +100bps Instantaneous Parallel Curve Shift - Repo / LIBOR Spread 10bps - Beginning BV \$10 / Share

	Share Count	MBS Interest	Repo Interest	Swap Hedge					Eurodollar Hedge				
				Interest Expense Hedge Adjustment	Taxable Income	Mark to Market	Ending Book Value	Annual Tot Return	Interest Expense Hedge Adjustment	Taxable Income	Mark to Market	Ending Book Value	Annualized TROR
<b>Year 1</b>	10,000,000	\$14,100,000	\$ (8,535,750)	\$270,750	\$5,835,000	\$18,148,451	\$11.81	24%	\$5,700,000	\$11,264,250	\$22,800,000	\$12.28	34%
<b>Year 2</b>	10,000,000	\$14,100,000	\$ (11,984,250)	\$3,719,250	\$5,835,000	(\$8,967,155)	\$10.92	-3%	\$5,700,000	\$7,815,750	\$ (5,700,000)	\$11.71	2%
<b>Year 3</b>	10,000,000	\$14,100,000	\$ (15,105,000)	\$6,840,000	\$5,835,000	(\$6,578,655)	\$10.26	-1%	\$5,700,000	\$4,695,000	\$ (5,700,000)	\$11.14	-1%
<b>Year 4</b>	10,000,000	\$14,100,000	\$ (16,550,093)	\$8,285,093	\$5,835,000	(\$3,741,098)	\$9.89	2%	\$5,700,000	\$3,249,907	\$ (5,700,000)	\$10.57	-2%
<b>Year 5</b>	10,000,000	\$14,100,000	\$ (17,649,908)	\$9,384,908	\$5,835,000	\$1,138,457	\$10.00	7%	\$5,700,000	\$2,150,093	\$ (5,700,000)	\$10.00	-3%
<b>Total</b>	<b>10,000,000</b>	<b>\$70,500,000</b>	<b>\$ (69,825,000)</b>	<b>\$28,500,000</b>	<b>\$29,175,000</b>	<b>\$0</b>	<b>\$10.00</b>	<b>6%</b>	<b>\$28,500,000</b>	<b>\$29,175,000</b>	<b>\$ -</b>	<b>\$10.00</b>	<b>6%</b>

\*This example is for illustrative purposes only and does not reflect Orchid Island's projections or forecasts.

- MBS interest remains constant
- Repo interest increases sharply and continues to increase as forwards are realized

### Swap Hedge

- Taxable interest expense is decreased at an increasing rate resulting from swap fixed rate outflows being far lower than swap floating rate inflows.
- Mark to market, all else equal, is large in the rate shock year and then unwinds to \$0 over time. The same is true of book value and total rate of return.
- Taxable income is steady over the smoothed hedge period.

### Eurodollar Hedge

- Taxable interest expense is decreased evenly over time. This corresponds to the 100bps parallel shift across the curve. Mark to market is large in Year 1 and then unwinds to \$0 as the hedge gains are monetized into taxable income.
- Taxable income decreases as repo rates gradually rise.
- Horizon Total return, MBS Interest, Repo Interest, Taxable Income, Book Value and Mark to Market are identical for each hedge instrument.