

PennyMac Mortgage Investment Trust
Form 10-Q
May 07, 2010

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2010

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: 001-34416**

PennyMac Mortgage Investment Trust

(Exact name of registrant as specified in its charter)

Maryland

(State or other jurisdiction of
incorporation or organization)

27-0186273

(IRS Employer Identification No.)

27001 Agoura Road, Calabasas, California

(Address of principal executive offices)

91301

(Zip Code)

(818) 224-7442

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

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

Edgar Filing: PennyMac Mortgage Investment Trust - Form 10-Q

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

(Do not check if a
smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes ☐ No ☒

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

Class	Outstanding at May 5, 2010
Common Shares of Beneficial Interest, \$.01 par value	16,735,317

Table of Contents

PENNYMAC MORTGAGE INVESTMENT TRUST
FORM 10-Q
March 31, 2010
TABLE OF CONTENTS

	Page
<u>PART I. FINANCIAL INFORMATION</u>	<u>1</u>
<u>Item 1.</u> Financial Statements (Unaudited):	<u>1</u>
Consolidated Balance Sheets March 31, 2010 and December 31, 2009	<u>1</u>
Consolidated Statement of Income Quarter Ended March 31, 2010	<u>2</u>
Consolidated Statement of Changes in Shareholders' Equity Quarter Ended March 31, 2010	<u>3</u>
Consolidated Statement of Cash Flows Quarter Ended March 31, 2010	<u>4</u>
Notes to Consolidated Financial Statements	<u>5</u>
<u>Item 2.</u> Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>17</u>
Overview	<u>17</u>
Observations on Current Market Opportunities	<u>18</u>
Results of Operations for the Quarter Ended March 31, 2010	<u>19</u>
Asset Acquisitions	<u>19</u>
Net Investment Income	<u>20</u>
Investment Portfolio Composition	<u>21</u>
Cash Flows	<u>24</u>
Liquidity and Capital Resources	<u>25</u>
Off-Balance Sheet Arrangements and Aggregate Contractual Obligations	<u>25</u>
Quantitative and Qualitative Disclosures About Market Risk	<u>26</u>
Accounting Developments	<u>27</u>
Factors That May Affect Our Future Results	<u>27</u>
<u>Item 3.</u> Quantitative and Qualitative Disclosures About Market Risk	<u>30</u>
<u>Item 4T.</u> Controls and Procedures	<u>30</u>
<u>PART II. OTHER INFORMATION</u>	<u>30</u>
<u>Item 1.</u> Legal Proceedings	<u>30</u>
<u>Item 1A.</u> Risk Factors	<u>30</u>
<u>Item 2.</u> Unregistered Sales of Equity Securities and Use of Proceeds	<u>30</u>
<u>Item 3.</u> Defaults Upon Senior Securities	<u>31</u>
<u>Item 4.</u> Other Information	<u>31</u>
<u>Item 5.</u> Exhibits	<u>32</u>

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(In thousands, except share data)****(Unaudited)**

	March 31, 2010	December 31, 2009
ASSETS		
Cash	\$ 2,125	\$ 54
Short-term investment	115,485	213,628
Mortgage-backed securities at fair value	76,389	83,771
Mortgage loans at fair value	123,464	26,046
Real estate acquired in settlement of loans	1,511	
Principal and interest collections receivable	6,131	
Interest receivable	602	492
Due from affiliates	51	
Other assets	930	455
Total assets	\$ 326,688	\$ 324,446
LIABILITIES		
Accounts payable and accrued liabilities	\$ 563	\$ 527
Contingent underwriting fees payable	5,883	5,883
Income taxes payable	127	
Payable to affiliates	4,635	4,238
Total liabilities	11,208	10,648
Commitments and contingencies		
SHAREHOLDERS' EQUITY		
Common shares of beneficial interest authorized, 500,000,000 shares of \$0.01 par value; issued and outstanding, 16,735,317 shares	167	167
Additional paid-in capital	315,942	315,514
Accumulated deficit	(629)	(1,883)
Total shareholders' equity	315,480	313,798
Total liabilities and shareholders' equity	\$ 326,688	\$ 324,446

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF INCOME**

(In thousands, except per share data)

(Unaudited)

	Quarter ended March 31, 2010
Investment Income	
Interest income:	
Mortgage-backed securities	\$ 1,284
Mortgage loans	1,335
Other	45
	2,664
Change in fair value of investments:	
Mortgage-backed securities	57
Mortgage loans	1,133
	1,190
 Net investment income	 3,854
 Expenses	
Management fees	1,211
Compensation	803
Insurance	197
Professional services	94
Other	168
 Total expenses	 2,473
 Income before provision for income taxes	 1,381
 Provision for income taxes	 127
 Net income	 \$ 1,254
 Earnings per share, basic and diluted	 \$ 0.07
Weighted average shares outstanding:	
Basic	16,735
Diluted	17,110

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(In thousands, except share data)

(Unaudited)

	Number of shares	Par value	Additional paid-in capital	Accumulated deficit	Total
Balance at December 31, 2009	16,735,317	\$ 167	\$ 315,514	\$ (1,883)	\$ 313,798
Share-based compensation			578		578
Stock issuance costs			(150)		(150)
Net income				1,254	1,254
Balance at March 31, 2010	16,735,317	\$ 167	\$ 315,942	\$ (629)	\$ 315,480

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF CASH FLOWS****(In thousands)****(Unaudited)**

	Quarter ended March 31, 2010
Cash flows from operating activities:	
Net income	\$ 1,254
Adjustments to reconcile net income to net cash used by operating activities:	
Accrual of unearned discounts on mortgage-backed securities	(765)
Appreciation in fair value of mortgage loans and mortgage-backed securities	(1,190)
Share-based compensation expense	578
Purchase of mortgage loans for sale	(13,782)
Proceeds from sale of mortgage loans	13,782
Increase in principal and interest collections receivable	(1,264)
Increase in interest receivable	(110)
Increase in due from affiliates	(51)
Increase in other assets	(475)
Increase in accounts payable and accrued liabilities	36
Increase in income taxes payable	127
Increase in payable to affiliates	397
Net cash used by operating activities	(1,463)
Cash flows from investing activities:	
Net decrease in short-term investment	98,143
Purchase of mortgage-backed security	(414)
Proceeds from repayments of mortgage-backed securities	8,618
Purchases of mortgage loans	(101,425)
Purchases of real estate acquired in settlement of loans	(1,238)
Net cash provided by investing activities	3,684
Cash flows from financing activities:	
Payment of stock issuance costs initial exchange listing fees	(150)
Net cash used by financing activities	(150)
Net increase in cash	2,071
Cash at beginning of period	54
Cash at end of period	\$ 2,125
Supplemental Cash Flow Information:	
Non cash investing activity transfer of mortgage loans to real estate acquired in settlement of loans	\$ 273

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 Organization and Basis of Presentation

PennyMac Mortgage Investment Trust ("PMT" or the "Company") was organized in Maryland on May 18, 2009, and began operations on August 4, 2009, when it completed its initial offerings of common shares of beneficial interest ("shares"). The Company is a specialty finance company, which, through its subsidiaries (all of which are wholly-owned), invests primarily in residential mortgage loans and mortgage-related assets. The Company's investment objective is to maximize the value of the mortgage loans that it acquires, a substantial portion of which may be distressed and acquired at discounts to their unpaid principal balances, through proprietary loan modification programs, special servicing and other initiatives focused on keeping borrowers in their homes, or, when necessary, through timely acquisition and liquidation of the property securing the loan.

The Company intends to qualify as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Internal Revenue Code"), beginning with its taxable period ended on December 31, 2009. To maintain its tax status as a REIT, the Company plans to distribute at least 90% of its taxable income in the form of qualifying distributions to holders of shares.

The Company is externally managed by an affiliate, PNMAC Capital Management, LLC ("PCM" or the "Manager"), an investment adviser registered with the Securities and Exchange Commission (the "SEC") that specializes in and focuses on residential mortgage loans. Under the terms of a management agreement, PCM is paid a management fee with a base component and a performance incentive component. Determination of the amount of management fees is discussed in Note 3 *Transactions with Related Parties*.

The accompanying consolidated financial statements have been prepared in compliance with accounting principles generally accepted in the U.S. ("U.S. GAAP") for interim financial information and with the SEC's instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these financial statements and notes do not include all of the information required by U.S. GAAP for complete financial statements.

Preparation of financial statements in compliance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the reporting period. Actual results will likely differ from those estimates.

In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the quarter ended March 31, 2010 are not necessarily indicative of the results for the year ending December 31, 2010. Comparable year information related to the Consolidated Statement of Income and Consolidated Statement of Cash Flows are omitted as the Company began operations on August 4, 2009.

Note 2 Concentration of Risks

PMT's operations and investing activities are centered in real estate-related assets, a substantial portion of which are distressed at acquisition. Because of the Company's investment strategy, many of the mortgage loans in its targeted asset class are purchased at discounts reflecting their distressed state or perceived higher risk of default. PCM performs diligence on the portfolios of mortgage loans and mortgage-related assets it targets for acquisition to evaluate the prospective acquisition's credit risk and establish a purchase bid that reflects PCM's assessment of that risk.

Table of Contents

PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Note 2 Concentration of Risks (Continued)

Through its management agreement with PCM and, where applicable, the loan servicing agreement between its operating partnership and an affiliated company, PennyMac Loan Services, LLC ("PLS"), PMT will work with borrowers to perform loss mitigation activities. Such activities include the use of proprietary and federally sponsored loan modification programs (such as the U.S. Department of Housing and Urban Development's Home Affordable Modification Program, or HAMP) and workout options that PCM believes have the highest probability of successful resolution for both borrowers and PMT. Loan modifications may include PMT accepting a write down of the principal balances of certain mortgage loans in its investment portfolio.

Because of the Company's investment focus, PMT is exposed, to a greater extent than traditional mortgage investors, to the risks that more borrowers than anticipated default on their mortgage loans and to the effects of fluctuations in the residential real estate market on the performance of its investments. Factors influencing these risks include, but are not limited to, changes in the overall economy, unemployment, residential real estate values in the markets where the Company's mortgage loans are secured, PCM's ability to identify and PLS's ability to execute optimal resolutions of problem mortgage loans, the accuracy of borrower representations and PMT's ability to validate borrower capacity to meet the terms of workout agreements, PCM's ability to effectively model and develop appropriate model assumptions that properly anticipate future outcomes, the level of government support for problem loan resolution and the effect of current and future proposed and enacted legislative and regulatory changes on the Company's ability to effect cures to distressed loans or foreclose on and liquidate the real estate securing its portfolio of distressed mortgage loans. Due to these uncertainties, there can be no assurance that risk management activities identified and executed on PMT's behalf will prevent significant losses arising from the Company's investments in real estate-related assets.

As discussed in Note 3 *Transactions with Related Parties*, the Company's short-term money market investment is made in an uninsured institutional money market fund that is managed by a strategic investor of the parent company of the Company's Manager and PLS.

Note 3 Transactions with Related Parties

The Company is managed externally by PCM under the terms of a management agreement that expires on August 4, 2012 and will be automatically renewed for a one-year term each anniversary date thereafter unless previously terminated. The management agreement provides for an annual review of PCM's performance under the management agreement by the Company's independent trustees. PMT's Board of Trustees reviews the Company's financial results, policy compliance and strategic direction.

PMT pays PCM a base management fee and a performance incentive fee, both payable quarterly and in arrears. The base management fee is calculated at the annual rate of 1.5% of shareholders' equity (as defined in the management agreement). The performance incentive fee is calculated at 20% per annum of the amount by which "core earnings," on a rolling four-quarter basis and before the incentive fee, exceeds an 8% "hurdle rate."

"Core earnings," for purposes of determining the amount of the performance incentive fee, is defined as U.S. GAAP net income adjusted to exclude non-cash equity compensation expense, unrealized gains and losses or other non-cash items recognized during the period, any conditional payment amounts relating to PMT's initial public offering ("IPO") paid to PCM and

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Note 3 Transactions with Related Parties (Continued)**

the underwriters of PMT's share offering, and any "one-time events" pursuant to changes in U.S. GAAP and certain other non-cash charges after discussions as agreed between PCM and PMT's independent trustees and approval by a majority of PMT's independent trustees.

The "hurdle rate" is calculated as the product of (1) the weighted average of the issue price per share of all of the Company's public offerings multiplied by the weighted average number of shares outstanding (including, for the avoidance of doubt, restricted share units) in the four-quarter period and (2) 8%. During PMT's first four quarters, core earnings will be calculated based on the annualized results of the preceding quarters.

For purposes of calculating the incentive fee, to the extent PMT has a net loss in core earnings from a period prior to the rolling four-quarter period that has not been offset by core earnings in a subsequent period, such loss will continue to be included in the rolling four-quarter calculation until it has been fully offset. This term is not applicable for purposes of determining whether the conditional payment of the underwriting discount is payable.

For the quarter ended March 31, 2010, the Company recorded management fee expense and its related liability as summarized below:

	Quarter ended March 31, 2010 (in thousands)
Base fee	\$ 1,211
Performance incentive fee	
Total incurred during the period	\$ 1,211
Fee paid during the period	(1,169)
Fee outstanding at December 31, 2009	1,169
 Fee due to Manager at March 31, 2010	 \$ 1,211

If the Company terminates the management agreement without cause, or PCM terminates the management agreement upon a default in the Company's performance of any material term in the management agreement, PMT will pay a termination fee to PCM. The termination fee will be equal to three times (a) the average annual base management fee and (b) the average annual (or, if the period is less than 24 months, annualized) incentive fee earned by PCM during the prior 24-month period before termination. Under circumstances where the termination fee is payable, PMT will pay to PCM its portion of the conditional payment of the underwriting discount discussed in Note 9 *Shareholders' Equity*.

The Company, through its operating partnership, also has a loan servicing agreement with PLS that provides for servicing fees at rates that are expected to range between 30 and 100 basis points per annum on the unpaid principal balance of the mortgage loans serviced on the Company's behalf.

Under the loan servicing agreement, PLS is also entitled to certain customary market-based fees and charges, including boarding and de-boarding fees, disposition fees, assumption, modification and origination fees and late charges, as well as interest on funds on deposit in custodial or escrow accounts. In the event PLS effects a refinancing of a loan on the Company's behalf and not through a third party lender and the resulting loan is readily saleable, PLS is entitled to receive from the

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Note 3 Transactions with Related Parties (Continued)**

Company an origination fee of 1.0% of the unpaid principal balance of the loan plus \$750. Similarly, when PLS originates a loan to facilitate the disposition of real estate that the Company has acquired in settlement of a loan, PLS is entitled to a fee in the same amount. In addition, the Company currently participates in HAMP (or other similar mortgage loan modification programs), which establishes standard loan modification guidelines for "at risk" homeowners and provides incentive payments to certain participants, including loan servicers, for achieving modifications and successfully remaining in the program. The loan servicing agreement entitles PLS to retain any incentive payments made to it and to which it is entitled under HAMP; provided, however, that with respect to any such incentive payments paid to PLS in connection with a mortgage loan modification for which the Company previously paid PLS a modification fee, PLS shall reimburse the Company an amount equal to the lesser of such modification fee and such incentive payments.

Servicing fee rates are based on the risk characteristics of the mortgage loans serviced and total servicing compensation is established at levels that management believes are competitive with those charged by other specialty servicers.

During the quarter ended March 31, 2010, the Company recorded \$233,000 in expenses incurred and \$250,000 of purchase deposits acquired on its behalf by PCM and its affiliates in accordance with the terms of the management agreement. Amounts due to affiliates are summarized below as of the dates presented:

	March 31, 2010	December 31, 2009
	(in thousands)	
Contingent offering costs	\$ 2,941	\$ 2,941
Management fee	1,211	1,169
Expense and purchase deposit reimbursements	483	128
	\$ 4,635	\$ 4,238

During the quarter ended March 31, 2010, the Company made payments to PCM relating to management fees and reimbursed expenses totaling \$1,294,000.

Due from affiliates at March 31, 2010 represents expenses paid on behalf of affiliated companies during the quarter ended March 31, 2010. No such amounts were outstanding at December 31, 2009.

The Company's short-term money market investment represents an investment in a liquidity management fund that is managed by BlackRock, Inc., which is a strategic investor of the parent company of the Company's Manager and PLS. Investments in the fund are not insured. The fund invests exclusively in first-tier securities as rated by a nationally recognized rating organization. The fund's investments are comprised primarily of domestic commercial paper, securities issued or guaranteed by the U.S. Government or its agencies, U.S. and Yankee bank obligations, fully collateralized repurchase agreements and variable and floating rate demand notes.

Note 4 Earnings Per Share

Basic earnings per share is determined using net earnings divided by the weighted-average shares outstanding during the period. Diluted earnings per share is computed by dividing net earnings available to common shareholders by the weighted-average shares outstanding, assuming all potentially

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Note 4 Earnings Per Share (Continued)**

dilutive common shares were issued. In periods in which the Company records a loss, potentially dilutive shares are excluded from the diluted loss per share calculation as their effect on loss per share is anti-dilutive.

The following table summarizes the basic and diluted earnings per share calculations for the period indicated:

	Quarter ended March 31, 2010		
	Net income	Shares	Per-share amount
	(in thousands, except per share data)		
Basic net income per share	\$ 1,254	16,735	\$ 0.07
Effect of dilutive securities share-based compensation instruments		375	
Diluted net income per share	\$ 1,254	17,110	\$ 0.07

Note 5 Fair Value

The Company's financial statements include assets and liabilities that are measured based on their estimated fair values. The application of fair value estimates may be on a recurring or nonrecurring basis depending on the accounting principles applicable to the specific asset or liability and whether management has elected to carry the item at its estimated fair value as discussed in the following paragraphs.

Fair Value Accounting Elections

Management identified its short-term investment, mortgage loans and mortgage-backed securities ("MBS") to be accounted for at estimated fair value so such changes in fair value will be reflected in earnings as they occur. Fair value accounting more timely reflects the results of the Company's investment performance.

Fair Value Measurements

For the period ended March 31, 2010, the Company recorded in its income \$1,133,000 and \$57,000 of appreciation in estimated fair values of its mortgage loans and MBS, respectively, under the fair value option. Gains and losses from changes in the estimated fair value of mortgage loans and MBS are included in change in fair value of investments.

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Note 5 Fair Value (Continued)**

The following financial statement items are measured at estimated fair value on a recurring basis as of the dates presented:

March 31, 2010			
	Level 1	Level 2	Level 3
	(in thousands)		
			Total
Short-term investment	\$ 115,485	\$	\$ 115,485
Mortgage loans			123,464
Mortgage-backed securities			76,389
	\$ 115,485	\$	\$ 199,853
			\$ 315,338

December 31, 2009			
	Level 1	Level 2	Level 3
	(in thousands)		
			Total
Short-term investment	\$ 213,628	\$	\$ 213,628
Mortgage-backed securities			83,771
Mortgage loans			26,046
	\$ 213,628	\$	\$ 109,817
			\$ 323,445

The Company measures its investment in real estate acquired in settlement of loans at estimated fair value on a nonrecurring basis. The Company has classified real estate acquired in settlement of loans as a Level 3 asset. At March 31, 2010, the Company carried approximately \$1,511,000 of real estate acquired in settlement of loans on its Consolidated Balance Sheet. There was no real estate acquired in settlement of loans at December 31, 2009.

All of the mortgage loans and mortgage-backed securities were measured using Level 3 inputs. The following is a summary of changes in items measured using Level 3 inputs on a recurring basis for the period:

Quarter ended March 31, 2010			
	Mortgage loans	Mortgage-backed securities	Total
	(in thousands)		
Balance, December 31, 2009	\$ 26,046	\$ 83,771	\$ 109,817
Total changes in fair value included in results of operations	1,133	57	1,190
Purchases	115,207	414	115,621
Accrual of unearned discounts		765	765
Repayments	(4,867)	(8,618)	(13,485)
Transfers of mortgage loans to real estate acquired in settlement of loans	(273)		(273)
Sale	(13,782)		(13,782)
Balance, March 31, 2010	\$ 123,464	\$ 76,389	\$ 199,853
Changes in gains relating to assets still held at March 31, 2010	\$ (790)	\$ 57	\$ (733)

[Table of Contents](#)**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Note 5 Fair Value (Continued)**

Following are the fair values and related principal amounts due upon maturity of mortgage loans accounted for under the fair value option as of the dates presented:

	Fair value	March 31, 2010 Unpaid principal balance (in thousands)	Fair value over (under) unpaid principal balance
Current through 89 days delinquent	\$ 38,156	\$ 59,488	\$ (21,332)
90 or more days delinquent	85,308	153,360	(68,052)
	\$ 123,464	\$ 212,848	\$ (89,384)

	Fair Value	December 31, 2009 Unpaid principal balance (in thousands)	Fair value over (under) unpaid principal balance
Current through 89 days delinquent	\$ 26,046	\$ 40,071	\$ (14,025)
90 or more days delinquent			
	\$ 26,046	\$ 40,071	\$ (14,025)

Valuation Techniques

The following describes the methods used in estimating the fair values of Level 3 financial statement items:

Mortgage-Backed Securities

Fair value of non-Agency MBS is estimated using broker indications of value. For indications of value received as of March 31, 2010, PCM's Capital Markets staff reviewed, and its senior management Valuation Committee reviewed and approved, the securities' values. PCM's review is for the purpose of evaluating the reasonableness of the broker's indication of value and may result in the broker modifying its indications of value. PCM does not intend to adjust its fair value estimates to amounts different from the broker's indications of value.

Mortgage Loans

Fair value of mortgage loans is estimated based on whether the mortgage loans are salable into liquid markets with established counterparties and transparent pricing. Fair value is estimated for mortgage loans that are not salable into liquid markets using a discounted cash flow valuation model. Inputs to the model include current interest rates, loan amount, payment status and property type; forecasts of future interest rates, home prices, prepayment speeds, defaults and loss severities. Mortgage loans which are salable into liquid markets are valued at their quoted market price or market price equivalent.

Table of Contents**PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Note 5 Fair Value (Continued)**

Management incorporates lack of liquidity into its fair value estimates based on the type of asset or liability measured and the valuation method used. For example, for mortgage loans where the significant inputs have become unobservable due to illiquidity in the markets for distressed mortgage loans or non-Agency, non-conforming mortgage loans, PMT uses a discounted cash flow technique to estimate fair value. This technique incorporates forecasting of expected cash flows discounted at an appropriate market discount rate to reflect the lack of liquidity in the market.

Real Estate Acquired in Settlement of Loans

Fair value of real estate acquired in settlement of loans is based on a current estimate of value as determined by a broker's price opinion or a full appraisal.

Note 6 Mortgage-Backed Securities at Fair Value

Investments in MBS were as follows for the dates presented:

March 31, 2010							
Credit rating							
	Total	AAA	AA	A	BBB	Non investment grade	Not rated
	(in thousands)						
Security collateral type:							
Non-Agency subprime	\$ 35,817	\$ 1,323	\$ 7,542	\$ 7,484	\$ 2,605	\$ 11,718	\$ 5,145
Non-Agency Alt-A	24,582	827	7,804		856	15,095	
Non-Agency prime jumbo	15,990		14,010			1,980	
	\$ 76,389	\$ 2,150	\$ 29,356	\$ 7,484	\$ 3,461	\$ 28,793	\$ 5,145

December 31, 2009							
Credit rating							
	Total	AAA	AA	A	BBB	Non investment grade	Not rated
	(in thousands)						
Security collateral type:							
Non-Agency subprime	\$ 39,522	\$ 1,910	\$ 8,085	\$ 8,704	\$ 3,151	\$ 12,620	\$ 5,052
Non-Agency Alt-A	27,060	9,022			1,071	16,967	
Non-Agency prime jumbo	17,189		14,737			2,452	
	\$ 83,771	\$ 10,932	\$ 22,822	\$ 8,704	\$ 4,222	\$ 32,039	\$ 5,052

Table of Contents

PENNYMAC MORTGAGE INVESTMENT TRUST AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Note 7 Mortgage Loans

Following is a summary of the distribution of the Company's mortgage loans as of the dates presented:

Loan Type	March 31, 2010			December 31, 2009		
	Fair value	% total	Average note rate	Fair value	% total	Average note rate
(dollars in thousands)						
Nonperforming loans	\$ 85,308	69%	6.48%	\$	0%	
Performing loans:						
Fixed	31,130	25%	7.78%	24,533	94%	8.15