Resource Capital Corp.
Form 10-K
March 17, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2007

OR

o 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: 1-32733

RESOURCE CAPITAL CORP.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Maryland | 20-2287134 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 712 5th Avenue, 10th Floor New York, NY | 10019 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: 212-506-3870

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, $.001 par value | New York Stock Exchange (NYSE) |

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ¨ Yes x No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the

Act. ¨ Yes x No

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. x Yes ¨ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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).

| | | | |
|---|---|---|---|
| Large accelerated filer | ¨ | Accelerated filer | x |
| Non-accelerated filer | ¨ | Smaller reporting company | ¨ |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). ¨ Yes x No

The aggregate market value of the voting common equity held by non-affiliates of the registrant, based on the closing price of such stock on the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2007) was approximately $258,130,718.

The number of outstanding shares of the registrant's common stock on March 10, 2008 was 25,264,793 shares.

DOCUMENTS INCORPORATED BY REFERENCE

[None]

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## FORWARD-LOOKING STATEMENTS

This report contains certain forward-looking statements. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. In some cases, you can identify forward-looking statements by terms such as "anticipate," "believe," "could," "estimate," "expects," "intend," "may," "plan," "potential," "project," "should," "will" and "would" or the terms or other comparable terminology.

Forward-looking statements contained in this report are based on our beliefs, assumptions and expectations of our future performance, taking into account all information currently available to us. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to us or are within our control. If a change occurs, our business, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. Forward-looking statements we make in this report are subject to various risks and uncertainties that could cause actual results to vary from our forward-looking statements, including:

- the factors described in this report, including those set forth under the sections captioned "Risk Factors" and "Business;"
- changes in our industry, interest rates, the debt securities markets, real estate markets or the general economy;
- increased rates of default and/or decreased recovery rates on our investments;
- availability, terms and deployment of capital;
- availability of qualified personnel;
- changes in governmental regulations, tax rates and similar matters;
- changes in our business strategy;
- availability of investment opportunities in commercial real estate-related and commercial finance assets;
- the degree and nature of our competition;
- the adequacy of our cash reserves and working capital; and
- the timing of cash flows, if any, from our investments.

We caution you not to place undue reliance on these forward-looking statements which speak only as of the date of this report. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Except to the extent required by applicable law or regulation, we undertake no obligation to update these forward-looking statements to reflect events or circumstances after the date of this filing or to reflect the occurrence of unanticipated events.

# PART I

## ITEM 1. BUSINESS

General

We are a specialty finance company that focuses primarily on commercial real estate and commercial finance. We are organized and conduct our operations to qualify as a real estate investment trust, or REIT, for federal income tax purposes. Our objective is to provide our stockholders with total returns over time, including quarterly distributions and capital appreciation, while seeking to manage the risks associated with our investment strategy. We invest in a combination of commercial real estate debt and other real estate-related assets and, to a lesser extent, higher-yielding commercial finance assets. We finance a substantial portion of our portfolio investments through borrowing strategies seeking to match the maturities and repricing dates of our financings with the maturities and repricing dates of those investments, and to mitigate interest rate risk through derivative instruments.

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We are externally managed by Resource Capital Manager, Inc., which we refer to as the Manager, a wholly-owned indirect subsidiary of Resource America, Inc. (Nasdaq: REXI), a specialized asset management company that uses industry specific expertise to generate and administer investment opportunities for its own account and for outside investors in the commercial finance, real estate, and financial fund management sectors. As of December 31, 2007, Resource America managed approximately $17.9 billion of assets in these sectors. To provide its services, the Manager draws upon Resource America, its management team and their collective investment experience.

Our investments target the following asset classes:

| Asset Class | Principal Investments |
|---|---|
| Commercial real estate-related assets | · First mortgage loans, which we refer to as whole loans<br>· First priority interests in first mortgage real estate loans, which we refer to as A notes<br>· Subordinated interests in first mortgage real estate loans, which we refer to as B notes<br>· Mezzanine debt related to commercial real estate that is senior to the borrower's equity position but subordinated to other third-party financing<br>· Commercial mortgage-backed securities, which we refer to as CMBS |
| Commercial finance assets | · Senior secured corporate loans, which we refer to as bank loans<br>· Other asset-backed securities, which we refer to as other ABS, backed principally by small business and bank loans and, to a lesser extent, by consumer receivables<br>· Equipment leases and notes, principally small- and middle-ticket commercial direct financing leases and notes<br>· Trust preferred securities of financial institutions<br>· Debt tranches of collateralized debt obligations, which we refer to as CDOs<br>· Private equity investments, principally issued by financial institutions |
| Residential real estate-related assets | · Residential mortgage-backed securities, which we refer to as ABS-RMBS |

Beginning in the second half of 2007, there have been unprecedented disruptions in the credit markets, abrupt and significant devaluations of assets directly or indirectly linked to the U.S. real estate finance markets, and the attendant removal of liquidity, both long and short term, from the capital markets. These conditions have had, and we expect will continue to have, an adverse effect on us and companies we finance. During the second half of 2007, we recorded material asset impairments of $26.3 million on our ABS-RMBS portfolio due primarily to credit defaults.

The events occurring in the credit markets have impacted our financing strategies. The market for securities issued by securitizations collateralized by assets similar to those in our investment portfolio has contracted severely. While we were able to sponsor two new securitizations in 2007, we expect our ability to sponsor new securitizations will be limited for the foreseeable future. Short-term financing through warehouse lines of credit and repurchase agreements has become less available and reliable as increasing volatility in the valuation of assets similar to those we originate has increased the risk of margin calls. These events have impacted (and we expect will continue to impact) our ability to finance our business on a long-term, match-funded basis and may impede our ability to originate loans and securities.

Beginning in the second half of 2007, we have focused on managing our exposure to liquidity risks primarily by reducing our exposure to possible margin calls under repurchase agreements and seeking to conserve our liquidity. We have continued to manage our liquidity and originate new assets primarily through capital recycling as payoffs occur and through existing capacities within our completed securitizations. While we recorded asset impairments as a result of the developments in the capital markets resulting in our reduced GAAP net income during 2007, we declared common dividends of $1.62 per share on estimated REIT taxable income of $1.70 per share.

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We calculate our distributions to our shareholders based on our estimate of our REIT taxable income, which may vary from our net income calculated in accordance with U.S. generally accepted accounting principles, or GAAP. We expect that our REIT taxable income will be comprised primarily of our net investment income and our fee income. We expect that our REIT taxable income will be greater than our GAAP net income primarily because of asset impairments, provisions for loan and lease losses until realized for tax purposes, net book to tax adjustments for our taxable foreign REIT subsidiaries and fee income received by our taxable REIT subsidiaries, or TRSs, that is dividended to us is included in our REIT taxable income but deferred or eliminated for GAAP. For further discussion, see "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Our Business Strategy

The core components and values of our business strategy are described below.

Disciplined credit underwriting and active risk management. The core of our investment process is credit analysis and active risk management. Senior management of our Manager and Resource America has extensive experience in underwriting the credit risk associated with our targeted asset classes, and conducts detailed due diligence on all credit-sensitive investments, including the use of proprietary credit stratifications and collateral stresses. After making an investment, the Manager and Resource America engage in active monitoring of our investments for early detection of troubled and deteriorating securities. If a default occurs, we will use our senior management team's asset management skills to mitigate the severity of any losses, and we will seek to optimize the recovery from assets if we foreclose upon them.

Investment in higher-yielding assets. Our portfolio is, and we expect will continue to be substantially comprised of assets such as commercial real estate whole loans, B notes, mezzanine debt, CMBS rated below AAA by Standard & Poors, or S&P, commercial finance assets, including bank loans that generally have higher-yields than more senior or more highly-rated obligations and to a lesser extent, direct financing leases and notes and when appropriate, ABS-RMBS. In line with this strategy, our equity at December 31, 2007 was invested 74.9% in commercial real estate loans, 24.1% in commercial bank loans and 1% in direct financing lease and notes.

Diversification of investments. We invest in a diversified portfolio of real estate debt and other real estate-related assets, and commercial finance assets and seek to continually allocate our capital to the most attractive sectors. Our objective is to enhance the returns we will be able to achieve, while reducing the overall risk of our portfolio through the autonomous nature of these various asset classes. The percentage of assets that we may invest in certain of our targeted asset classes is subject to the federal income tax requirements for REIT qualification and the requirements for exclusion from Investment Company Act regulation.

Use of leverage. Subject to market conditions and credit availability, we seek to use leverage to increase the potential returns to our stockholders and to achieve leverage consistent with our analysis of the risk profile of the investments we finance and the borrowing sources available to us. We generate our income primarily from the net spread between the interest income we earn on our investment portfolio and the cost of our borrowings and hedging activities. Leverage can enhance returns but also magnifies losses.

Active management of interest rate risk and liquidity risk. Historically, we have sought to finance a substantial portion of our portfolio investments on a long-term basis through borrowing strategies that seek to match the maturity and repricing dates of our investments with the maturities and repricing dates of our financing. We believe that these strategies have allowed us to mitigate our interest rate risk and liquidity risk, resulting in more stable and predictable cash flows. Depending upon market conditions and credit availability, we will seek to continue these strategies. Historically, we have used CDOs structured for us by the Manager to provide long-term match funding for our investments, and will seek to continue to do so if market conditions permit. We typically retain the equity portion of the CDO and may retain one or more series of the subordinated obligations issued by the CDO. We also use derivative instruments such as interest rate swaps and interest rate caps to hedge the borrowings we use to finance our assets on a short-term basis.

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Our Operating Policies and Strategies

Investment guidelines. We have established investment policies, procedures and guidelines that are reviewed and approved by our investment committee and board of directors. The investment committee meets regularly to monitor the execution of our investment strategies and our progress in achieving our investment objectives. As a result of our investment strategies and targeted asset classes, we acquire our investments primarily for income. We do not have a policy that requires us to focus our investments in one or more particular geographic areas.

Financing policies. We use leverage in order to increase potential returns to our stockholders and for financing our portfolio. We do not speculate on changes in interest rates. While we have identified our leverage targets for each of our targeted asset classes, our investment policies require no minimum or maximum leverage and our investment committee will have the discretion, without the need for further approval by our board of directors, to increase the amount of leverage we incur above our targeted range for individual asset classes.

We have historically used borrowing and securitization strategies, substantially through CDOs, to accomplish our long-term match funding, financing strategy and, depending upon market conditions, expect to seek to do so in the future. However, the developments in the credit markets, particularly during the second half of 2007, have significantly limited our ability to execute our long term financing strategy. In the foreseeable future, we will seek to finance our investments through investing restricted cash and reinvesting loan repayments received under our current securitized financings, joint venture opportunities and to a lesser extent, bank lines of credit and other methods that preserve our capital.

Hedging and interest rate management strategy. We use derivative financial instruments to hedge all or a portion of the interest rate risk associated with our borrowings. Under the federal income tax laws applicable to REITs, we generally will be able to enter into certain transactions to hedge indebtedness that we may incur, or plan to incur, to acquire or carry real estate assets, provided that our total gross income from such hedges and other non-qualifying sources must not exceed 25% of our total gross income. These hedging transactions may include interest rate swaps, collars, caps or floors, puts and calls and options.

Credit and risk management policies. Our Manager focuses its attention on credit and risk assessment from the earliest stage of the investment selection process. In addition, the Manager screens and monitors all potential investments to determine their impact on maintaining our REIT qualification under federal income tax laws and our exclusion from investment company status under the Investment Company Act of 1940. Risks related to portfolio management, including the management of risks related to credit losses, interest rate volatility, liquidity and counterparty credit are generally managed on a portfolio-by-portfolio basis by each of Resource America’s asset management divisions, although there is often interaction and cooperation between divisions in this process.

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Our Investment Strategy

The following table describes certain characteristics of our commercial real estate loans, bank loans, CMBS, other ABS and equipment leases and notes as of December 31, 2007 (dollars in thousands):

| | Amortized cost | Estimated fair value (1) | Percent of portfolio | Weighted average coupon |
|---|---|---|---|---|
| Loans Held for Investment | | | | |
| Commercial real estate loans | | | | |
| Mezzanine loans | $ 223,162 | $ 221,555 | 11.8% | 7.80% |
| B notes | 89,577 | 89,353 | 4.8% | 7.67% |
| Whole loans | 528,718 | 527,396 | 28.1% | 7.99% |
| Bank loans | 931,101 | 874,736 | 46.7% | 7.24% |
| | 1,772,558 | 1,713,040 | 91.4% | |
| Investments in Available-for-Sale Securities | | | | |
| CMBS | 82,373 | 64,564 | 3.4% | 6.03% |
| Other ABS | | | | |