

ANNALY CAPITAL MANAGEMENT INC  
Form 10-K  
February 28, 2012

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C.20549

FORM 10-K

(MARK ONE)

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

FOR THE FISCAL YEAR ENDED: DECEMBER 31, 2011

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: 1-13447

ANNALY CAPITAL MANAGEMENT, INC.  
(Exact Name of Registrant as Specified in its Charter)

MARYLAND 22-3479661  
(State or other jurisdiction of incorporation of organization) (I.R.S. Employer Identification Number)

1211 Avenue of the Americas, Suite 2902  
New York, New York 10036  
(Address of Principal Executive Offices) (Zip Code)

(212) 696-0100  
(Registrant's telephone number, including area code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value \$.01 per share	New York Stock Exchange
7.875% Series A Cumulative Redeemable Preferred Stock	New York Stock Exchange

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

None.

Edgar Filing: ANNALY CAPITAL MANAGEMENT INC - Form 10-K

Indicate by check mark whether the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  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 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 (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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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, or a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  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  No .

At June 30, 2011, the aggregate market value of the voting stock held by non-affiliates of the Registrant was \$14,913,563,080.

The number of shares of the Registrant's Common Stock outstanding on February 24, 2012 was 970,269,506.

#### Documents Incorporated by Reference

The registrant intends to file a definitive proxy statement pursuant to Regulation 14A within 120 days of the end of the fiscal year ended December 31, 2011. Portions of such proxy statement are incorporated by reference into Part III of this Form 10-K.

---

ANNALY CAPITAL MANAGEMENT, INC.  
2011 FORM 10-K ANNUAL REPORT  
TABLE OF CONTENTS

PART I

		PAGE
<u>ITEM 1.</u>	<u>BUSINESS</u>	1
<u>ITEM 1A.</u>	<u>RISK FACTORS</u>	17
<u>ITEM 1B.</u>	<u>UNRESOLVED STAFF COMMENTS</u>	34
<u>ITEM 2.</u>	<u>PROPERTIES</u>	34
<u>ITEM 3.</u>	<u>LEGAL PROCEEDINGS</u>	35
<u>ITEM 4.</u>	<u>MINE SAFETY DISCLOSURE</u>	35

PART II

<u>ITEM 5.</u>	<u>MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	36
<u>ITEM 6.</u>	<u>SELECTED FINANCIAL DATA</u>	39
<u>ITEM 7.</u>	<u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	40
<u>ITEM 7A.</u>	<u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	56
<u>ITEM 8.</u>	<u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	57
<u>ITEM 9.</u>	<u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	57
<u>ITEM 9A.</u>	<u>CONTROLS AND PROCEDURES</u>	57
<u>ITEM 9B.</u>	<u>OTHER INFORMATION</u>	58

PART III

<u>ITEM 10.</u>	<u>DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u>	59
-----------------	-------------------------------------------------------------------	----

<u>ITEM 11.</u>	<u>EXECUTIVE COMPENSATION</u>	59
<u>ITEM 12.</u>	<u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	59
<u>ITEM 13.</u>	<u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE</u>	59
<u>ITEM 14.</u>	<u>PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	59
PART IV		
<u>ITEM 15.</u>	<u>EXHIBITS AND FINANCIAL STATEMENT SCHEDULES</u>	60
<u>EXHIBIT INDEX</u>		60
<u>FINANCIAL STATEMENTS</u>		63
<u>SIGNATURES</u>		II-1

---

### SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements contained in this annual report may not be based on historical facts and are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements, which are based on various assumptions (some of which are beyond our control), may be identified by reference to a future period or periods or by the use of forward-looking terminology, such as “may,” “will,” “believe,” “expect,” “anticipate,” “continue,” or similar terms or variations on those terms or the negative of those terms. Actual results could differ materially from those set forth in forward-looking statements due to a variety of factors, including, but not limited to:

changes in interest rates,

changes in the yield curve,

changes in prepayment rates,

the availability of mortgage-backed securities and other securities for purchase,

the availability of financing and, if available, the terms of any financing,

changes in the market value of our assets,

changes in business conditions and the general economy,

our ability to consummate any contemplated investment opportunities,

risks associated with the investment advisory business of our wholly owned subsidiaries, including:

- o the removal by clients of assets managed,
- o their regulatory requirements, and
- o competition in the investment advisory business,

risks associated with the broker-dealer business of our subsidiary,

changes in government regulations affecting our business,

our ability to maintain our exemption from registration under the Investment Company Act of 1940, and

our ability to maintain our qualification as a REIT for federal income tax purposes.

No forward-looking statements can be guaranteed and actual future results may vary materially and we caution you not to place undue reliance on these forward-looking statements. For a discussion of the risks and uncertainties which could cause actual results to differ from those contained in the forward-looking statements, please see the information under the caption “Risk Factors” described in this Form 10-K. We do not undertake, and specifically disclaim any obligation, to publicly release the result of any revisions which may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements except as required by law.



## PART I

### ITEM 1. BUSINESS

All references to “we,” “us,” or “our” mean Annaly Capital Management, Inc. and all entities owned by us, except where it is made clear that the term means only the parent company. The following defines certain of the commonly used terms in this annual report on Form 10-K: Agency refers to a federally chartered corporation, such as Fannie Mae or Freddie Mac, or an agency of the U.S. Government, such as Ginnie Mae; Agency mortgage-backed securities refers to residential mortgage-backed securities that are issued or guaranteed by an Agency; Investment Securities refers to Agency mortgage-backed securities, Agency debentures, corporate debt securities and reverse repurchase agreement loans; and Interest Earning Assets refers to Investment Securities, securities borrowed and U.S. Treasury Securities.

### THE COMPANY

#### Background

We own, manage, and finance a portfolio of real estate related investments, including mortgage pass-through certificates, collateralized mortgage obligations (or CMOs), Agency callable debentures, and other securities representing interests in or obligations backed by pools of mortgage loans. Our principal business objective is to generate net income for distribution to our stockholders from the spread between the interest income on our Interest Earning Assets and the cost of borrowings to finance our acquisition of Interest Earning Assets and from dividends we receive from our subsidiaries. Our wholly-owned subsidiaries offer diversified real estate, asset management and other financial services.

We are a Maryland corporation that commenced operations on February 18, 1997. We are self-advised and self-managed. We acquired Fixed Income Discount Advisory Company (or FIDAC) on June 4, 2004 and Merganser Capital Management, Inc. (or Merganser) on October 31, 2008. FIDAC and Merganser manage a number of investment vehicles and separate accounts for which they earn fee income. Our subsidiary, RCap Securities, Inc. (or RCap), operates as a broker-dealer, and was granted membership in the Financial Industry Regulatory Authority (or FINRA) in January 2009. In 2010, we established Shannon Funding LLC (or Shannon), which provides warehouse financing to residential mortgage originators in the United States. In 2010, we also established Charlesfort Capital Management LLC (or Charlesfort), which engages in corporate middle market lending transactions. In 2011, FIDAC established FIDAC Europe Limited (or FIDAC Europe), which provides advice on commercial real estate transactions, including sale-leaseback and single tenant net leased properties across Europe. In 2011, we established FIDAC FSI LLC (or FIDAC FSI), which invests in trading securities. We also own an additional subsidiary which owns trading securities.

We have elected and believe that we are organized and have operated in a manner that qualifies us to be taxed as a real estate investment trust (or REIT) under the Internal Revenue Code of 1986, as amended (or the Code). If we qualify for taxation as a REIT, we generally will not be subject to federal income tax on our taxable income that is distributed to our stockholders. Therefore, substantially all of our assets, other than FIDAC, Merganser and RCap, which are our taxable REIT subsidiaries, consist of qualified REIT real estate assets (of the type described in Section 856(c)(5)(B) of the Code). We have financed our purchases of Agency mortgage-backed securities and Agency debentures with the net proceeds of equity offerings and borrowings under repurchase agreements whose interest rates adjust based on changes in short-term market interest rates.

#### Capital Investment Policy



Under our capital investment policy, at least 75% of our total assets must be comprised of high-quality mortgage-backed securities and short-term investments. High quality securities means securities that (1) are rated within one of the two highest rating categories by at least one of the nationally recognized rating agencies, (2) are unrated but are guaranteed by the United States government or an agency of the United States government, or (3) are unrated but we determine them to be of comparable quality to rated high-quality mortgage-backed securities.

1

---

The remainder of our assets, comprising not more than 25% of our total assets, may consist of other qualified REIT real estate assets which are unrated or rated less than high quality, but which are at least “investment grade” (rated “BBB” or better by Standard & Poor’s Corporation (or S&P) or the equivalent by another nationally recognized rating agency) or, if not rated, we determine them to be of comparable credit quality to an investment which is rated “BBB” or better. In addition, we may directly or indirectly invest part of this remaining 25% of our assets in other types of securities, including but without limitation, unrated debt, equity or derivative securities, to the extent consistent with our REIT qualification requirements. The derivative securities in which we invest may include securities representing the right to receive interest only or a disproportionately large amount of interest, as well as inverse floaters, which may have imbedded leverage as part of their structural characteristics. We intend to structure our portfolio to maintain a minimum weighted average rating (including our deemed comparable ratings for unrated mortgage-backed securities) of our mortgage-backed securities of at least single “A” under the S&P rating system and at the comparable level under the other rating systems.

We may acquire mortgage-backed securities backed by single-family residential mortgage loans as well as securities backed by loans on multi-family, commercial or other real estate related properties. To date, substantially all of the mortgage-backed securities that we have acquired have been backed by single-family residential mortgage loans.

To date, substantially all of the mortgage-backed securities that we have acquired have been Agency mortgage-backed securities which, although not rated, carry an implied “AAA” rating. Agency mortgage-backed securities consist of agency pass-through certificates and CMOs issued or guaranteed by an Agency. Pass-through certificates provide for a pass-through of the monthly interest and principal payments made by the borrowers on the underlying mortgage loans. CMOs divide a pool of mortgage loans into multiple tranches with different principal and interest payment characteristics.

Our adjustable-rate pass-through certificates are backed by adjustable-rate mortgage loans and have coupon rates which adjust over time, subject to interest rate caps and lag periods, in conjunction with changes in short-term interest rates. Our fixed-rate pass-through certificates are backed by fixed-rate mortgage loans and have coupon rates which do not adjust over time. CMO floaters are tranches of mortgage-backed securities where the interest rate adjusts in conjunction with changes in short-term interest rates. CMO floaters may be backed by fixed-rate mortgage loans or, less often, by adjustable-rate mortgage loans. In this Form 10-K, except where the context indicates otherwise, we use the term “adjustable-rate interest-earning assets” to refer to adjustable-rate pass-through certificates, CMO floaters, Agency debentures and corporate debt.

We may also invest in Agency debentures, which consist of debentures issued by the Federal Home Loan Bank (FHLB), Freddie Mac and Fannie Mae. We intend to continue to invest in adjustable-rate pass-through certificates, fixed-rate mortgage-backed securities, CMO floaters, and Agency debentures. We may also invest on a limited basis in derivative securities which include securities representing the right to receive interest only or a disproportionately large amount of interest as well as inverse floaters, which may have imbedded leverage as part of their structural characteristics. We have not and will not invest in real estate mortgage investment conduit (REMIC) residuals and other CMO residuals.

## Borrowings

We attempt to structure our collateralized borrowings to have interest rate adjustment indices and interest rate adjustment periods that, on an aggregate basis, correspond generally to the interest rate adjustment indices and periods of our adjustable-rate interest-earning assets. However, periodic rate adjustments on our collateralized borrowings are generally more frequent than rate adjustments on our Investment Securities.

We generally expect to maintain a ratio of debt-to-equity of between 8:1 and 12:1, although the ratio may vary, as it currently does because of market conditions, from this range from time to time based upon various factors, including our management's opinion of the level of risk of our assets and liabilities, our liquidity position, our level of unused borrowing capacity and over-collateralization levels required by lenders when we pledge assets to secure borrowings. For purposes of calculating this ratio, our equity is equal to the value of our investment portfolio on a mark-to-market basis, less the book value of our obligations under repurchase agreements and other collateralized borrowings and convertible senior notes. At December 31, 2011, our ratio of debt-to-equity was 5.4:1.

During 2010, we issued \$600.0 million in aggregate principal amount of our 4% convertible senior notes due 2015 (Convertible Senior Notes) for net proceeds following underwriting expenses of approximately \$582.0 million. Interest on the notes is paid semi-annually at a rate of 4% per year and the notes will mature on February 15, 2015 unless earlier repurchased or converted. As of December 31, 2011 the notes were convertible into shares of common stock at a conversion rate of 62.2331 shares of common stock per \$1,000 principal amount of notes, which is equivalent to a conversion price of approximately \$16.0686 per share of common stock, subject to adjustment in certain circumstances.

### Hedging

To the extent consistent with our election to qualify as a REIT, we enter into hedging transactions to attempt to protect our Agency mortgage-backed securities and Agency debentures and related borrowings against the effects of major interest rate changes. This hedging is used to mitigate declines in the market value of our Agency mortgage-backed securities and Agency debentures during periods of increasing interest rates and to limit or cap the interest rates on our borrowings. These transactions are entered into solely for the purpose of hedging interest rate or prepayment risk and not for speculative purposes. In connection with our interest rate risk management strategy, we hedge a portion of our interest rate risk by entering into derivative financial instrument contracts.

### Our Subsidiaries

FIDAC, an investment advisor registered with the SEC, is a fixed-income investment management company specializing in managing fixed income investments in residential mortgage-backed securities, commercial mortgage-backed securities and collateralized debt obligations for various investment vehicles and separate accounts. FIDAC also has experience in managing and structuring debt financing associated with various asset classes and as a liquidation agent of collateralized debt obligations. FIDAC commenced active investment management operations in 1994. At December 31, 2011, FIDAC was the adviser or sub-adviser for REITs and other investment vehicles. The team managing Annaly perform the same roles at FIDAC.

Merganser, an investment advisor registered with the SEC, has expertise in a variety of fixed income strategies and focuses on managing each portfolio based on each client's specific investment principles. Merganser serves a diverse group of clients in a variety of disciplines nationwide including pension, public, operating, Taft-Hartley and endowment funds as well as defined contribution plans. Merganser's investment team maintains a careful balance of risk management and performance by employing fundamental security analysis and by trading in an environment supported by state-of-the-art technology, infrastructure and operations.

RCap operates as a broker-dealer and has been a member in the Financial Industry Regulatory Authority (or FINRA) since January 2009.

In 2010, we established Shannon, which provides warehouse financing to residential mortgage originators in the United States. In 2010, we also established Charlesfort, which engages in corporate middle market lending transactions. In 2011, FIDAC established FIDAC Europe Limited, which provides advice on commercial real estate transactions, including sale-leaseback and single tenant net leased properties across Europe. In 2011, we established FIDAC FSI LLC, which invests in trading securities. We also own an additional subsidiary which owns trading securities.

### Compliance with REIT and Investment Company Requirements

We constantly monitor our investments and the income from these investments and, to the extent we enter into hedging transactions, we monitor income from our hedging transactions as well, so as to ensure at all times that we

maintain our qualification as a REIT and our exemption from registration under the Investment Company Act of 1940, as amended.

3

---

## Executive Officers of the Company

The following table sets forth certain information as of February 25, 2012 concerning our executive officers:

Name	Age	Position held with the Company
Michael A.J. Farrell	60	Chairman of the Board, Chief Executive Officer and President
Wellington J. Denahan-Norris	48	Vice Chairman of the Board, Chief Investment Officer and Chief Operating Officer
Kathryn F. Fagan	45	Chief Financial Officer and Treasurer
R. Nicholas Singh	52	Chief Legal Officer, Secretary and Chief Compliance Officer
James P. Fortescue	38	Managing Director, Head of Liabilities and Chief of Staff
Kristopher Konrad	37	Managing Director and Head Portfolio Manager
Rose-Marie Lyght	38	Managing Director and Chief Investment Officer of FIDAC
Jeremy Diamond	48	Managing Director and Head of Research and Corporate Communications
Ronald Kazel	44	Managing Director and Head of Asset Management Group
Matthew Lambiase	45	Managing Director and Head of Business Development
Kevin Keyes	44	Managing Director and Chief Strategy Officer

Mr. Farrell and Ms. Denahan-Norris have had years of experience in the investment banking and investment management industries where, in various capacities, they have each managed portfolios of mortgage-backed securities, arranged collateralized borrowings and utilized hedging techniques to mitigate interest rate and other risk within fixed-income portfolios. Ms. Fagan is a certified public accountant and, prior to becoming our Chief Financial Officer and Treasurer, served as Chief Financial Officer and Controller of a publicly owned savings and loan association. Mr. Singh joined Annaly in 2005. Mr. Fortescue joined Annaly in 1997. Mr. Konrad joined Annaly in 1997. Ms. Lyght joined Annaly in 1999. Mr. Diamond joined Annaly in 2002. Mr. Kazel joined Annaly in 2001. Mr. Lambiase joined Annaly in 2004. Mr. Keyes joined Annaly in September 2009.

## Distributions

To maintain our qualification as a REIT, we must distribute substantially all of our