

STARWOOD PROPERTY TRUST, INC.  
Form 10-Q  
August 09, 2010

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended June 30, 2010

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

Commission file number 001-34436

**Starwood Property Trust, Inc.**

(Exact name of registrant as specified in its charter)

**Maryland**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**27-0247747**  
(I.R.S. Employer  
Identification No.)

**591 West Putnam Avenue**  
**Greenwich, Connecticut**  
(Address of principal executive offices)

**06830**  
(Zip Code)

Registrant's telephone number, including area code:

**(203) 422-8100**

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) 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 definition of "accelerated filer, large accelerated filer, and smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company   
(Do not check if  
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

The number of shares of the issuer's common stock, \$0.01 par value, outstanding as of August 5, 2010, was 47,583,800.

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**Special Note Regarding Forward Looking Statements**

This Quarterly Report on Form 10-Q contains certain forward-looking statements, including without limitation, statements concerning our operations, economic performance and financial condition. These forward-looking statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are developed by combining currently available information with our beliefs and assumptions and are generally identified by the words "believe," "expect," "anticipate" and other similar expressions. Forward-looking statements do not guarantee future performance, which may be materially different from that expressed in, or implied by, any such statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their dates.

These forward-looking statements are based largely on our current 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 within our control, and which could materially affect actual results, performance or achievements. Factors that may cause actual results to vary from our forward-looking statements include, but are not limited to:

factors described in our Annual Report on Form 10-K for the year ended December 31, 2009, including those set forth under the caption "Risk Factors";

defaults by borrowers in paying debt service on outstanding items;

impairment in the value of real estate property securing our loans;

availability of mortgage origination opportunities acceptable to us;

national and local economic and business conditions;

general and local commercial real estate property conditions;

changes in federal government policies;

changes in federal, state and local governmental laws and regulations;

increased competition from entities engaged in mortgage lending;

changes in interest rates; and

the availability of and costs associated with sources of liquidity and financing.

In light of these risks and uncertainties, there can be no assurances that the results referred to in the forward-looking statements contained in this Quarterly Report on Form 10-Q will in fact occur. Except to the extent required by applicable law or regulation, we undertake no obligation to, and expressly disclaim any such obligation to, update or revise any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, changes to future results over time or otherwise.

## PART I FINANCIAL INFORMATION

## Item 1. Condensed Consolidated Financial Statements.

## Starwood Property Trust, Inc. and Subsidiaries

## Condensed Consolidated Balance Sheets

(Unaudited, amounts in thousands, except share and per share data)

	June 30, 2010	December 31, 2009
<b>Assets:</b>		
Cash and cash equivalents	\$ 210,469	\$ 645,129
Loans held for investment, net	865,373	214,521
Mortgage backed securities, held-to-maturity	247,962	245,896
Mortgage backed securities, available-for-sale	69,538	
Other investments	8,480	
Accrued interest receivable	7,181	2,180
Other assets	1,722	1,060
<b>Total Assets</b>	<b>\$ 1,410,725</b>	<b>\$ 1,108,786</b>
<b>Liabilities and Stockholders' Equity</b>		
<b>Liabilities:</b>		
Payable for unsettled securities purchased	\$ 11,685	\$
Accounts payable and accrued expenses	2,005	1,034
Related-party payable	3,941	3,546
Dividends payable	12,157	5,349
Derivative liabilities	5,016	
Secured financing agreements	449,548	171,394
Deferred offering costs	27,195	27,195
Other liabilities	5,383	4,233
<b>Total Liabilities</b>	<b>516,930</b>	<b>212,751</b>
<b>Commitments and contingencies (Note 12)</b>		
<b>Equity:</b>		
<b>Starwood Property Trust, Inc. Stockholders' Equity:</b>		
Preferred stock, \$0.01 par value per share 100,000,000 shares authorized, no shares issued and outstanding		
Common stock, \$0.01 par value per share, 500,000,000 shares authorized, 47,583,800 shares issued and outstanding	476	476
Additional paid-in capital	898,763	895,857
Accumulated other comprehensive loss	(1,943)	
Accumulated deficit	(14,430)	(8,366)
<b>Total Starwood Property Trust, Inc. Stockholders' Equity</b>	<b>882,866</b>	<b>887,967</b>
Non-controlling interests in consolidated subsidiaries	10,929	8,068
<b>Total Equity</b>	<b>893,795</b>	<b>896,035</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 1,410,725</b>	<b>\$ 1,108,786</b>

See notes to condensed consolidated financial statements

## Starwood Property Trust, Inc. and Subsidiaries

## Condensed Consolidated Statement of Operations

(Unaudited, amounts in thousands, except share and per share data)

	For the Three-Month Period Ended June 30, 2010	For the Six-Month Period Ended June 30, 2010
<b>Net interest margin:</b>		
Interest income from mortgage-backed securities	\$ 4,703	\$ 9,034
Interest income from loans	16,627	26,326
Interest expense	(3,352)	(4,984)
<b>Net interest margin</b>	<b>17,978</b>	<b>30,376</b>
<b>Expenses:</b>		
Management fees (including \$1,327 and \$2,869 of non-cash stock-based compensation)	4,792	9,762
General and administrative (including \$19 and \$37 of non-cash stock based compensation)	1,665	3,444
<b>Total expenses</b>	<b>6,457</b>	<b>13,206</b>
<b>Income before other income (expense) and taxes</b>	<b>11,521</b>	<b>17,170</b>
Interest income from cash balances	229	840
Loss on sale of available-for-sale securities	(2)	(2)
Unrealized loss on currency hedges	(3,694)	(3,694)
Unrealized foreign currency remeasurement gain	3,396	3,396
<b>Income before taxes</b>	<b>11,450</b>	<b>17,710</b>
Income tax provision	40	40
<b>Net income</b>	<b>11,410</b>	<b>17,670</b>
Net income attributable to non-controlling interests	561	880
<b>Net income attributable to Starwood Property Trust, Inc.</b>	<b>\$ 10,849</b>	<b>\$ 16,790</b>

**Net income per share of common stock:**

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Basic	\$	0.23	\$	0.35
Diluted	\$	0.22	\$	0.35
<b>Weighted average number of shares of common stock outstanding:</b>				
Basic		47,749,705		47,706,032
Diluted		48,626,300		48,626,300

See notes to condensed consolidated financial statements

**Starwood Property Trust, Inc. and Subsidiaries**  
**Consolidated Statement of Equity**  
(Unaudited, amounts in thousands, except share and per share data)

	Common Stock		Additional	Accumulated	Accumulated	Total	Non-controlling	Total
	Shares	Par Value	Paid-In Capital	Deficit	Other Comprehensive Income(Loss)	Starwood Property Trust, Inc. Stockholders' Equity	interests	Equity
<b>Balance at August 17, 2009</b> <b>(Commencement of Operations)</b>	100	\$	\$ 1	\$	\$	\$ 1	\$	\$ 1
Proceeds from public offering of common stock	46,575,000	466	931,034			931,500		931,500
Underwriting and offering costs			(57,588)			(57,588)		(57,588)
Proceeds from private placement	1,000,000	10	19,990			20,000		20,000
Cancellation of shares	(100)		(1)			(1)		(1)
Stock-based compensation	8,800		2,421			2,421		2,421
Net loss				(3,017)		(3,017)	437	(2,580)
Dividends declared, \$0.11 per share				(5,349)		(5,349)		(5,349)
Contribution from non-controlling interests							50,855	50,855
Distribution to non-controlling interests							(43,224)	(43,224)
<b>Balance at December 31, 2009</b>	<b>47,583,800</b>	<b>\$ 476</b>	<b>\$ 895,857</b>	<b>\$ (8,366)</b>	<b>\$</b>	<b>\$ 887,967</b>	<b>\$ 8,068</b>	<b>\$ 896,035</b>
Stock-based compensation			2,906			2,906		2,906
Net income				16,790		16,790	880	17,670
Dividends declared, \$0.47 per share				(22,854)		(22,854)		(22,854)
Other comprehensive loss, net					(1,943)	(1,943)		(1,943)
Contribution from non-controlling interests							2,579	2,579
Distribution to non-controlling interests							(598)	(598)
<b>Balance at June 30, 2010</b>	<b>47,583,800</b>	<b>\$ 476</b>	<b>\$ 898,763</b>	<b>\$ (14,430)</b>	<b>\$ (1,943)</b>	<b>\$ 882,866</b>	<b>\$ 10,929</b>	<b>\$ 893,795</b>

See notes to condensed consolidated financial statements

## Starwood Property Trust, Inc. and Subsidiaries

## Condensed Consolidated Statements of Comprehensive Income (Loss)

(Unaudited, amounts in thousands)

	For the Three-Month Period Ended June 30, 2010	For the Six-Month Period Ended June 30, 2010
<b>Net income</b>	\$ 11,410	\$ 17,670
Other comprehensive loss		
Change in fair value of interest rate hedge	(1,202)	(1,322)
Change in fair value of available-for-sale securities	(294)	(621)
<b>Total other comprehensive loss</b>	<b>(1,496)</b>	<b>(1,943)</b>
<b>Comprehensive income</b>	<b>\$ 9,914</b>	<b>\$ 15,727</b>

See notes to condensed consolidated financial statements



**Starwood Property Trust, Inc. and Subsidiaries**  
**Condensed Consolidated Statement of Cash Flows**  
(Unaudited, amounts in thousands)

	<b>Six Months Ended June 30, 2010</b>
<b>Cash Flows from Operating Activities:</b>	
Net Income	\$ 17,670
Adjustments to reconcile net income to net cash provided by operating activities:	
Amortization of deferred financing costs	120
Amortization of net discount on mortgage backed securities (MBS)	(1,792)
Amortization of net deferred loan fees and discounts	(883)
Stock-based compensation	2,906
Loss on sale of available-for-sale securities	(2)
Unrealized losses on currency hedges	3,694
Unrealized remeasurement gain	(3,396)
Changes in operating assets and liabilities:	
Related-party payable	395
Accrued interest receivable, less purchased interest	(2,352)
Other assets	559
Accounts payable and accrued expenses	971
Other liabilities	1,150
<b>Net cash provided by operating activities</b>	<b>19,040</b>
<b>Cash Flows from Investing Activities:</b>	
Investment in mortgage-backed securities	(77,402)
Proceeds from sales of mortgage-backed securities	7,357
Mortgage-backed securities investment repayments	11,842
Investment in loans	(652,871)
Loan investment repayments	6,289
Purchased interest on investments, net	(2,640)
Investments in other investments	(9,023)
<b>Net cash used in investing activities</b>	<b>(716,448)</b>
<b>Cash Flows from Financing Activities:</b>	
Borrowings of secured financing arrangements	278,960
Principal repayments on borrowings	(806)
Payment of deferred financing costs	(1,341)
Payment of dividends	(16,046)
Contribution from non-controlling interests	2,579
Distribution to non-controlling interests	(598)
<b>Net cash provided by financing activities</b>	<b>262,748</b>
Net decrease in cash and cash equivalents	(434,660)
Cash and cash equivalents, beginning of period	645,129
<b>Cash and cash equivalents, end of period</b>	<b>\$ 210,469</b>
Supplemental disclosure of cash flow information:	
Cash paid for interest	\$ 4,207
Supplemental disclosure of non-cash investing and financing activities:	
Dividends declared, not yet paid	\$ 12,157
Unsettled securities purchased	\$ 11,685

See notes to condensed consolidated financial statements



**Starwood Property Trust, Inc. and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements**

**June 30, 2010 (unaudited)**

**1. Business and Organization**

Starwood Property Trust, Inc. (together with its subsidiaries, the "Company") is a Maryland corporation that commenced operations on August 17, 2009 upon the completion of its initial public offering. The Company is focused primarily on originating, investing in, financing and managing commercial mortgage loans and other commercial real estate debt investments. The Company also invests in residential mortgage-backed securities and residential mortgage loans. The Company is externally managed and advised by SPT Management, LLC (the "Manager").

The Company is organized and conducts its operations to qualify as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code"). As such, the Company will generally not be subject to U.S. federal corporate income tax on that portion of its net income that is distributed to stockholders if it distributes at least 90% of its taxable income to its stockholders by prescribed dates and complies with various other requirements.

The Company is organized as a holding company that conducts its business primarily through three wholly-owned subsidiaries, SPT Real Estate Sub I, LLC, SPT TALF Sub I, LLC, and SPT Operations, LLC. The Company has formed joint ventures (the "Joint Ventures") with Starwood Hospitality Fund II ("Hotel II") and Starwood Opportunity Fund VIII ("SOF VIII") in accordance with the co-investment and allocation agreement with the Manager. These Joint Ventures are owned 75% (and controlled) by the Company and are therefore consolidated into the Company's consolidated financial statements.

**2. Summary of Significant Accounting Policies**

***Basis of Accounting and Principles of Consolidation***

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") and include our accounts and those of our consolidated subsidiaries. All significant intercompany amounts have been eliminated. Certain information and footnote disclosures normally included in financial statements prepared under GAAP have been condensed or omitted pursuant to the instructions for Form 10-Q and Rule 10-01 of Regulation S-X. In the opinion of the Company's management, all adjustments (consisting of normal recurring adjustments) considered necessary for fair presentation of the Company's financial position, results of operations, comprehensive income, and cash flows have been made. The preparation of financial statements in conformity with GAAP requires the Company's management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2009, as filed with the Securities and Exchange Commission ("SEC"). The results of operations for the three and six months ended June 30, 2010 are not necessarily indicative of the operating results for the full year.

A non-controlling interest in a consolidated subsidiary is defined as "the portion of the equity (net assets) in a subsidiary not attributable, directly or indirectly, to a parent". Non-controlling interests are required to be presented as a separate component of equity in the consolidated balance sheet. In

**Starwood Property Trust, Inc. and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**June 30, 2010 (unaudited)**

**2. Summary of Significant Accounting Policies (Continued)**

addition, the presentation of net income must attribute earnings to controlling and non-controlling interests.

The Company uses plain English when describing or referencing accounting standards in the notes to the financial statements. As a result, there may be no reference to particular accounting standards by name, standard number, or ASC reference number.

***Recent Accounting Pronouncements***

*Amendments to Variable Interest Entity Accounting:* In June 2009, the FASB issued a statement which amends the consolidation guidance applicable to variable interest entities ("VIEs"). The amendments change the way a VIE's primary beneficiary is determined and how entities account for securitizations and special purpose entities as a result of the elimination of the qualified special purpose entity concept. The adoption of this statement on January 1, 2010 did not have a material effect on the Company's consolidated financial statements.

***Segment Reporting***

The Company is a REIT focused on originating and acquiring real estate related debt investments and currently operates in one reportable segment.

***Debt Securities***

GAAP requires that at the time of purchase, the Company designate debt securities as held-to-maturity, available-for-sale, or trading depending on its intent and ability to hold such securities to maturity. Held-to-maturity investments are stated at cost plus any premiums or discounts, which are amortized through the consolidated statements of income using the effective interest method. Securities that the Company does not hold for the purpose of selling in the near-term, but may dispose of prior to maturity, are designated as available-for-sale and are carried at estimated fair value with the net unrealized gains or losses recorded as a component of accumulated other comprehensive loss in stockholders' equity. As of June 30, 2010, \$248.0 million of the Company's commercial mortgage backed securities ("CMBS") were designated as held-to-maturity, and \$11.4 million, along with all the Company's residential mortgage backed securities ("RMBS"), were designated as available for sale.

The Company evaluates securities for other-than-temporary impairment ("OTTI") at least quarterly. Securities are considered to be other-than-temporarily impaired when the estimated fair value of a security is less than amortized cost and (i) we intend to sell the security, (ii) it is more likely than not that we will be required to sell the security before recovery, or (iii) we do not expect to recover the entire amortized cost basis of the security. The evaluation of a security's estimated cash flows includes the following, as applicable: (1) review of the credit of the issuer or the borrower, (2) review of the credit rating of the security, (3) review of the key terms of the security, (4) review of the performance of the loan or underlying loans, including debt service coverage and loan-to-value ratios, (5) analysis of the value of the collateral for the loan or underlying loans, (6) analysis of the effect of local, industry, and broader economic factors, and (7) analysis of historical and anticipated trends in defaults and loss severities for similar securities. If an OTTI has occurred, the carrying value of the security will be reduced to fair value, with the unrealized losses being charged against earnings

**Starwood Property Trust, Inc. and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**June 30, 2010 (unaudited)**

**2. Summary of Significant Accounting Policies (Continued)**

as a loss on the consolidated statements of operations. For securities held to maturity, only the credit component of the unrealized loss will be charged against earnings and the component of the loss related to factors other than credit will be recognized in other comprehensive income ("OCI").

***Loans Held for Investment***

The Company purchases and originates commercial real estate debt and related instruments (collectively, "Loans") generally to be held to maturity. Loans that are held for investment are carried at cost, net of unamortized loan fees, acquisition premiums or discounts, and other related costs, unless the loans are deemed impaired. Interest income is recognized using the effective interest method. Net deferred loan fees and origination and acquisition costs are recognized in interest income over the loan term as a yield adjustment. Loans that the Company plans to sell or liquidate in the near term will be held at the lower of cost or fair value. As of June 30, 2010, all of the Company's Loans were designated as held for investment.

The Company must periodically evaluate each of its Loans for possible impairment. Impairment is indicated when it is deemed probable that we will not be able to collect all amounts due according to the contractual terms of the Loan. If a Loan were determined to be impaired, we would record an allowance to reduce the carrying amount of the Loan to its estimated fair value through a charge to the provision for loan losses. Impairment on these Loans is measured by comparing a valuation based on discounted cash flows to the carrying value of the respective Loan. These valuations require significant judgments, which include assumptions regarding capitalization rates, leasing, creditworthiness of major tenants, occupancy rates, availability of financing, exit plans, loan sponsorship, actions of other lenders and other factors deemed necessary by management. Actual losses, if any, could ultimately differ from these estimates.

***Revenue Recognition***

Interest income is accrued based on the outstanding principal amount of the investment security or loan and the contractual terms. Discounts or premiums associated with the purchase of an investment security are amortized into interest income on an effective yield or "interest" method, based on expected cash flows through the expected maturity date of the security. Depending on the nature of the investment, changes to expected cash flows may result in a prospective change to yield or a retrospective change, which would include a catch up adjustment. Upon settlement of securities, the excess (or deficiency) of net proceeds over the net carrying value of such security or loan is recognized as a gain (or loss) in the period of settlement. Investment security transactions are recorded on the trade date.

***Foreign Currency Transactions***

The Company's assets and liabilities denominated in foreign currencies are translated into U.S. dollars using foreign currency exchange rates at the end of the reporting period. Income and expenses are translated at the approximate weighted average exchange rates for each reporting period. At June 30, 2010, the functional currency of all investments denominated in foreign currencies was the U.S. Dollar. Accordingly, effects of translating the assets, liabilities and income of our foreign

**Starwood Property Trust, Inc. and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**June 30, 2010 (unaudited)**

**2. Summary of Significant Accounting Policies (Continued)**

investments is included in unrealized foreign currency remeasurement gain in the statements of operations.

***Concentration of Credit Risk***

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash investments, single asset CMBS, loan investments and interest receivable. The Company may place cash investments in excess of insured amounts with high quality financial institutions. The Company performs an ongoing analysis of credit risk concentrations in its investment portfolio by evaluating exposure to various markets, underlying property types, contract terms, tenant mix and other credit metrics.

***Derivative Instruments and Hedging Activities***

GAAP provides the disclosure requirements for derivatives and hedging activities with the intent to provide users of financial statements with an enhanced understanding of: (a) how and why an entity uses derivative instruments, (b) how the entity accounts for derivative instruments and related hedged items, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. Further, the Company must provide qualitative disclosures that explain its objectives and strategies for using derivatives, as well as quantitative disclosures about the fair value of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments.

As required by GAAP, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Derivatives may also be designated as hedges of the foreign currency exposure of a net investment in a foreign operation. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts that are intended to economically hedge certain of its risk, even though hedge accounting does not apply or the Company elects not to apply hedge accounting. In such cases, changes in the fair value of the derivatives are recorded in earnings.

***Deferred Financing Costs***

Costs incurred in connection with secured financing are capitalized and amortized over the respective loan terms as a component of interest expense. As of June 30, 2010, the Company had approximately \$1.5 million of capitalized financing costs, net of amortization. For the three and six

## Starwood Property Trust, Inc. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Continued)

June 30, 2010 (unaudited)

## 2. Summary of Significant Accounting Policies (Continued)

months ended June 30, 2010, approximately \$90,000 and \$120,000, respectively, of amortization was included in interest expense on the statement of operations.

*Income Taxes*

The Company will elect to be taxed as a REIT and intends to comply with the Code with respect thereto. Accordingly, the Company will not be subject to federal income tax to the extent of its dividends to stockholders as long as certain asset, income and stock ownership tests are met. Many of these requirements are technical and complex and if we fail to meet these requirements we may be subject to federal, state, and local income tax and penalties.

The Company formed a taxable REIT subsidiary ("TRS") in 2010 that will be subject to federal and state income taxes as a domestic C corporation based upon its income. For the three and six month periods ended June 30, 2010, the Company's taxable REIT subsidiary recorded \$40,000 of income tax expense.

## 3. Debt Securities

*Mortgage-Backed Securities Held to Maturity*

The following table summarizes the weighted average coupon, rating and life of the Company's investments in CMBS accounted for at amortized cost based on the book values as of June 30, 2010 and December 31, 2009:

June 30, 2010	Carry Value	Par Value	Coupon(1)	Rating	Life (years)
Multi-Asset CMBS	\$ 202,692	\$ 202,699	5.64%	AAA	1.6
Single Borrower CMBS	45,270	54,873	5.27%	B-	4.6
	\$ 247,962	\$ 257,572			

December 31, 2009	Carry Value	Par Value	Coupon(1)	Rating	Life (years)
Multi-Asset CMBS	\$ 202,646	\$ 202,699	5.70%	AAA	2.1
Single Borrower CMBS	43,250	53,712	5.40%	BB+	6.3
	\$ 245,896	\$ 256,411			

(1) Calculated using the June 30, 2010 and December 31, 2009 one month LIBOR rates of 0.3484% and 0.2309%, respectively, as applicable.

The Company's investments in multi-asset CMBS were acquired through a joint venture in which the Company owns a 75% controlling interest and which the Company is required to consolidate under GAAP. The majority of loans backing the CMBS investments are fixed rate instruments. Approximately \$12.6 million, or 5%, of the CMBS are variable rate and pay interest at LIBOR plus a weighted average spread of 1.30%.





## Starwood Property Trust, Inc. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Continued)

June 30, 2010 (unaudited)

## 3. Debt Securities (Continued)

*Mortgage-Backed Securities Available-for-Sale*

The Company classified some CMBS and all RMBS investments as available for sale to allow it the flexibility of selling these securities before maturity. The RMBS and CMBS classified as available for sale are accounted for at fair value and are utilized by the Company as an alternative to its available cash that has not been deployed while the Company identifies appropriate investments. The table below summarizes the weighted average coupon, rating and life of the Company's investments in mortgage back securities available for sale as of June 30, 2010:

June 30, 2010	Cost	Fair Value		Fair Value	Coupon	Rating	Life (Years)
		Adj					
RMBS	\$ 58,146	\$ (52)	\$ 58,094	0.44%	BB	0.88	
CMBS	11,470	(26)	11,444	7.03%	BB+	0.94	
	\$ 69,616	\$ (78)	\$ 69,538				

The fair value of all of the securities listed in the table above has been below their respective carrying amounts for less than 12 months.

The Company has allocated \$70 million to be invested in RMBS with expected durations on each of the individual securities of 15 months or less and less than 12 months in the aggregate. The Company has engaged a third party manager who specializes in RMBS to execute the purchase of RMBS. As of June 30, 2010, approximately \$57.8 million, or 99.5%, of the RMBS are variable rate and pay interest at LIBOR plus a weighted average spread of 0.09%. The Company purchased all of the RMBS at a discount which will be accreted into income over the expected remaining life of the security, which in all cases is less than 15 months. The majority of the income from this strategy is earned from the amortization of these discounts.

## Starwood Property Trust, Inc. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Continued)

June 30, 2010 (unaudited)

## 4. Loans Held for Investment

The Company's investments in mortgages and loans are accounted for at amortized cost. The following table summarizes the Company's investments in mortgages and loans as of June 30, 2010 and December 31, 2009.

June 30, 2010	Carry Value	Face Amount	Weighted Average Coupon	Weighted Average Life (years)
First Mortgages	\$ 674,951	\$ 710,476	8.0%	3.0
Subordinated Debt(1)	190,422	208,279	5.6%	2.8
<b>Total Loans</b>	<b>\$ 865,373</b>	<b>\$ 918,755</b>		

(1) Includes one GBP denominated loan with a face value of £62.9 million at the June 30, 2010 spot rate of \$1.507

December 31, 2009	Carry Value	Face Amount	Weighted Average Coupon	Weighted Average Life (years)
First Mortgages	\$ 182,829	\$ 212,424	8.7%	7.2
Subordinated Debt	31,692	42,560	8.1%	12.6
<b>Total Loans</b>	<b>\$ 214,521</b>	<b>\$ 254,984</b>		

For the six months ended June 30, 2010, the Company originated and acquired loans held for investment as follows:

Beginning Balance	\$ 214,521
Acquisitions/Origination	651,934
Additional fundings(1)	939
Principal repayments	(6,289)
Discount/premium amortization	883
Unrealized foreign currency remeasurement gain	3,385
<b>Balance June 30, 2010</b>	<b>\$ 865,373</b>

(1) Represents accrued interest income on loans whose terms do not require current payment of interest.

All loans were paying in accordance with their terms as of June 30, 2010 and the asset management review process did not note any issues indicating impairment or requiring further evaluation. Therefore, no allowance for loan losses was deemed necessary as of June 30, 2010.



## Starwood Property Trust, Inc. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Continued)

June 30, 2010 (unaudited)

**5. Other Investments**

In January 2010, the Company committed \$6.3 million to acquire a 5.6% interest in a venture formed to acquire assets of a commercial real estate debt management and servicing business primarily for an opportunity to participate in debt opportunities arising from the venture's special servicing business (the "Participation Right"). In May 2010, the Company made an additional \$3.4 million commitment to the venture to maintain at least a 5% ownership and its corresponding Participation Right. Because the Company does not have control or significant influence over the venture, the investment is accounted for under the cost method. As of June 30, 2010, the Company had funded \$6.0 million of its commitment. A member of the Company's board of directors has a \$50,000 investment in the same venture.

In March and April of 2010, the Company purchased a total of \$3.0 million of publicly traded equity securities that are classified as available for sale and carried at fair value with changes in fair value recorded to other comprehensive loss. As of June 30, 2010, these marketable securities have an unrealized loss of \$0.5 million.

**6. Secured Financing Agreements**

On August 28, 2009 and September 25, 2009, the Company entered into multiple Federal Reserve Bank of New York Term Asset-backed securities Loan Facilities ("TALF") through a joint venture with SOF VIII. The TALF loans are non-recourse, bear a fixed interest rate and mature five years from the loan closing dates. The loans are collateralized by the Company's Multi-Asset CMBS investments, which are held in a Master TALF Collateral Account and are under the control of the lender until the loan is satisfied.

<b>June 30, 2010</b>	<b>Debt Carry Value</b>	<b>Collateral Carry Value</b>
August 28, 2009, TALF loans, fixed rate 3.872%, mature August 2014	\$ 54,942	\$ 64,884
September 25, 2009, TALF loans, fixed rate 3.796%, mature September 2014	116,364	137,808
<b>Total</b>	<b>\$ 171,306</b>	<b>\$ 202,692</b>

<b>December 31, 2009</b>	<b>Debt Carry Value</b>	<b>Collateral Carry Value</b>
August 28, 2009, TALF loans, fixed rate 3.872%, mature August 2014	\$ 55,030	\$ 64,898
September 25, 2009, TALF loans, fixed rate 3.796%, mature September 2014	116,364	137,748
<b>Total</b>	<b>\$ 171,394</b>	<b>\$ 202,646</b>

Principal repayments are due on the TALF financing when principal is collected on the underlying CMBS securities, which principal can be paid off earlier or later than expected based on certain market factors including asset sales or loan defaults. As of June 30, 2010, the Company had no anticipation of early principal repayments or loan defaults of the underlying CMBS.

**Starwood Property Trust, Inc. and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**June 30, 2010 (unaudited)**

**6. Secured Financing Agreements (Continued)**

On March 31, 2010, the Company entered into a Master Repurchase and Securities Contract (the "Repurchase Agreement") with Wells Fargo Bank, National Association ("Wells Fargo"). The Repurchase Agreement is secured by approximately \$400 million of the diversified loan portfolio (the "TIAA Assets") purchased from Teachers Insurance and Annuity Association of America on February 26, 2010. The Repurchase Agreement provides for asset purchases of up to \$280 million (the "Facility").

Advances under the Repurchase Agreement accrue interest at a per annum pricing rate equal to the sum of (i) 30 day LIBOR plus (ii) the pricing margin of 3.0%. During the existence of an event of default (as defined in the Repurchase Agreement), interest accrues at the default rate, which is equal to the pricing rate plus 4.0%. The maturity date of the Repurchase Agreement is May 31, 2013. The Facility allowed for advances through May 31, 2010 and was fully drawn. As of June 30, 2010, \$278.2 million was outstanding under the Facility.

The following table represents our five-year principal repayments schedule for the secured financings assuming no early prepayments or defaults and including expected extensions of the underlying CMBS assets and the Facility.