

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

Apollo Commercial Real Estate Finance, Inc.
Form 10-Q
May 02, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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, 2018

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: 001-34452

Apollo Commercial Real Estate Finance, Inc.
(Exact name of registrant as specified in its charter)

Maryland 27-0467113
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification Number)

Apollo Commercial Real Estate Finance, Inc.
c/o Apollo Global Management, LLC
9 West 57th Street, 43rd Floor,
New York, New York 10019
(Address of registrant's principal executive offices)
(212) 515-3200
(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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. "

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

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

As of May 1, 2018, there were 123,020,301 shares, par value \$0.01, of the registrant's common stock issued and outstanding.

Table of Contents

	Page
<u>Part I — Financial Information</u>	
<u>Item 1. Financial Statements</u>	<u>4</u>
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>23</u>
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	<u>32</u>
<u>Item 4. Controls and Procedures</u>	<u>34</u>
<u>Part II — Other Information</u>	
<u>Item 1. Legal Proceedings</u>	<u>34</u>
<u>Item 1A. Risk Factors</u>	<u>34</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>34</u>
<u>Item 3. Defaults Upon Senior Securities</u>	<u>34</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>34</u>
<u>Item 5. Other Information</u>	<u>34</u>
<u>Item 6. Exhibits</u>	<u>34</u>

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Apollo Commercial Real Estate Finance, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)
(in thousands—except share data)

	March 31, 2018	December 31, 2017
Assets:		
Cash	\$98,310	\$ 77,671
Commercial mortgage loans, net (includes \$2,176,126 and \$2,148,368 pledged as collateral under secured debt arrangements in 2018 and 2017, respectively)	3,029,240	2,653,826
Subordinate loans, net	1,038,254	1,025,932
Loan proceeds held by servicer	30,281	302,756
Other assets	46,087	28,420
Total Assets	\$4,242,172	\$ 4,088,605
Liabilities and Stockholders' Equity		
Liabilities:		
Secured debt arrangements, net (net of deferred financing costs of \$14,037 and \$14,348 in 2018 and 2017, respectively)	\$ 1,212,749	\$ 1,330,847
Convertible senior notes, net	585,972	584,897
Derivative liabilities, net	14,499	5,644
Accounts payable, accrued expenses and other liabilities	73,330	70,906
Payable to related party	8,092	8,168
Total Liabilities	1,894,642	2,000,462
Commitments and Contingencies (see Note 15)		
Stockholders' Equity:		
Preferred stock, \$0.01 par value, 50,000,000 shares authorized:		
Series B preferred stock, 6,770,393 shares issued and outstanding (\$169,260 aggregate liquidation preference) in 2018 and 2017	68	68
Series C preferred stock, 6,900,000 shares issued and outstanding (\$172,500 aggregate liquidation preference) in 2018 and 2017	69	69
Common stock, \$0.01 par value, 450,000,000 shares authorized, 122,992,231 and 107,121,235 shares issued and outstanding in 2018 and 2017, respectively	1,230	1,071
Additional paid-in-capital	2,444,036	2,170,078
Accumulated deficit	(97,873)	(83,143)
Total Stockholders' Equity	2,347,530	2,088,143
Total Liabilities and Stockholders' Equity	\$4,242,172	\$ 4,088,605

See notes to unaudited condensed consolidated financial statements.

4

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

Apollo Commercial Real Estate Finance, Inc. and Subsidiaries
 Condensed Consolidated Statement of Operations (Unaudited)
 (in thousands—except share and per share data)

	Three months ended March 31,	
	2018	2017
Net interest income:		
Interest income from commercial mortgage loans	\$52,114	\$ 34,398
Interest income from subordinate loans	33,853	34,390
Interest income from securities	—	6,054
Interest expense	(22,740)	(17,030)
Net interest income	63,227	57,812
Operating expenses:		
General and administrative expenses (includes equity-based compensation of \$3,342 and \$3,791 in 2018 and 2017, respectively)	(4,998)	(5,758)
Management fees to related party	(8,092)	(7,432)
Total operating expenses	(13,090)	(13,190)
Income from unconsolidated joint venture	—	458
Other income	203	108
Realized loss on sale of assets	—	(1,042)
Unrealized gain on securities	—	2,852
Foreign currency gain	10,125	3,172
Loss on derivative instruments (includes unrealized losses of \$(8,855) and \$(2,889) in 2018 and 2017, respectively)	(11,032)	(3,045)
Net income	49,433	47,125
Preferred dividends	\$(6,835)	\$(9,310)
Net income available to common stockholders	42,598	37,815
Net income per share of common stock	\$0.38	\$ 0.41
Basic weighted average shares of common stock outstanding	110,211,858	111,612,447
Diluted weighted average shares of common stock outstanding	111,871,492	112,998,250
Dividend declared per share of common stock	\$0.46	\$ 0.46

See notes to unaudited condensed consolidated financial statements.

5

Apollo Commercial Real Estate Finance, Inc. and Subsidiaries
Condensed Consolidated Statement of Comprehensive Income (Unaudited)
(in thousands)

	Three months ended March 31,	
	2018	2017
Net income available to common stockholders	\$42,598	\$37,815
Foreign currency translation adjustment	—	251
Comprehensive income	\$42,598	\$38,066

See notes to unaudited condensed consolidated financial statements.

6

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

Apollo Commercial Real Estate Finance, Inc. and Subsidiaries
 Condensed Consolidated Statement of Changes in Stockholders' Equity (Unaudited)

(in thousands—except share and per share data)

	Preferred Stock		Common Stock		Additional	Accumulated	Total
	Shares	Par	Shares	Par	Paid-In-Capital	Deficit	
Balance at January 1, 2018	13,670,393	\$ 137	107,121,235	\$ 1,071	\$ 2,170,078	\$ (83,143)) \$2,088,143
Capital increase (decrease) related to Equity Incentive Plan	—	—	345,996	4	(1,389)) —	(1,385)
Issuance of common stock	—	—	15,525,000	155	275,724	—	275,879
Offering costs	—	—	—	—	(377)) —	(377)
Net income	—	—	—	—	—	49,433	49,433
Dividends declared on preferred stock	—	—	—	—	—	(6,835)) (6,835)
Dividends declared on common stock - \$0.46 per share	—	—	—	—	—	(57,328)) (57,328)
Balance at March 31, 2018	13,670,393	\$ 137	122,992,231	\$ 1,230	\$ 2,444,036	\$ (97,873)) \$2,347,530

See notes to unaudited condensed consolidated financial statements.

7

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

Apollo Commercial Real Estate Finance, Inc. and Subsidiaries
Condensed Consolidated Statement of Cash Flows (Unaudited)
(in thousands)

	For the three months ended March 31,	
	2018	2017
Cash flows (used in) provided by operating activities:		
Net income	\$49,433	\$47,125
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of discount/premium and PIK	(15,695)	(3,517)
Amortization of deferred financing costs	2,545	1,203
Equity-based compensation	(1,385)	1,461
Unrealized gain on securities	—	(2,852)
Income from unconsolidated joint venture	—	(458)
Foreign currency gain	(9,853)	(2,808)
Unrealized loss on derivative instruments	8,855	2,897
Realized loss on sale of assets	—	1,042
Changes in operating assets and liabilities:		
Proceeds received from PIK	55,000	—
Other assets	(2,620)	(10,926)
Accounts payable, accrued expenses and other liabilities	2,075	(8,011)
Payable to related party	(76)	418
Net cash (used in) provided by operating activities	88,279	25,574
Cash flows used in investing activities:		
New funding of commercial mortgage loans	(476,951)	(258,950)
Add-on funding of commercial mortgage loans	(13,185)	(60,649)
New funding of subordinate loans	(11,687)	(117,500)
Add-on funding of subordinate loans	(5,208)	(55,182)
Payments received on commercial mortgage loans	90,547	6,336
Payments received on subordinate loans	257,548	37,738
Origination and exit fees received on commercial mortgage and subordinate loans	19,085	6,294
Funding of unconsolidated joint venture	—	(726)
Funding of other assets	—	(1,379)
Increase in collateral held related to derivative contracts	(15,220)	(960)
Payments and proceeds received on securities	—	70,033
Net cash (used in) provided by investing activities	(155,071)	(374,945)
Cash flows from financing activities:		
Proceeds from issuance of common stock	275,879	—
Payment of offering costs	(38)	(58)
Proceeds from secured debt arrangements	416,549	407,955
Repayments of secured debt arrangements	(538,562)	(67,286)
Repayments of participations sold	—	(434)
Payment of deferred financing costs	(2,234)	(4,394)
Dividends on common stock	(57,328)	(42,947)
Dividends on preferred stock	(6,835)	(9,310)
Net cash (used in) provided by financing activities	87,431	283,526
Net increase (decrease) in cash and cash equivalents	20,639	(65,845)
Cash and restricted cash, beginning of period	77,671	263,452
Cash and restricted cash, end of period	\$98,310	\$197,607
Supplemental disclosure of cash flow information:		

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

Interest paid	\$26,517	\$18,965
Supplemental disclosure of non-cash financing activities:		
Dividend declared, not yet paid	\$63,598	\$51,109
Offering costs payable	\$339	\$222
Loan proceeds held by servicer	\$30,281	\$—

See notes to unaudited condensed consolidated financial statements.

8

Apollo Commercial Real Estate Finance Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 – Organization

Apollo Commercial Real Estate Finance, Inc. (together with its consolidated subsidiaries, is referred to throughout this report as the “Company,” “ARI,” “we,” “us” and “our”) is a corporation that has elected to be taxed as a real estate investment trust (“REIT”) for U.S. federal income tax purposes and primarily originates, acquires, invests in and manages performing commercial first mortgage loans, subordinate financings, and other commercial real estate-related debt investments in the United States. These asset classes are referred to as the Company’s target assets.

The Company, organized in Maryland on June 29, 2009, commenced operations on September 29, 2009 and is externally managed and advised by ACREFI Management, LLC (the “Manager”), an indirect subsidiary of Apollo Global Management, LLC (together with its subsidiaries, “Apollo”).

The Company elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended, commencing with the taxable year ended December 31, 2009. To maintain its tax qualification as a REIT, the Company is required to distribute at least 90% of its taxable income, excluding net capital gains, to stockholders and meet certain other asset, income, and ownership tests.

Note 2 – Summary of Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements include the Company’s accounts and those of its consolidated subsidiaries. All intercompany amounts have been eliminated. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires us 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. The Company’s most significant estimates include loan loss reserves and impairment. Actual results could differ from those estimates.

These unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017, as filed with the Securities and Exchange Commission (the “SEC”). In the opinion of management, all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the Company’s financial position, results of operations and cash flows have been included. The Company’s results of operations for the three months ended March 31, 2018 are not necessarily indicative of the results to be expected for the full year or any other future period.

The Company currently operates in one reporting segment.

Recent Accounting Pronouncements

In August 2017, the FASB issued ASU 2017-12 “Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities” (“ASU 2017-12”). The intention of ASU 2017-12 is to align an entity’s financial reporting for hedging activities with the economic objectives of those activities. Upon adoption of ASU 2017-12, the cumulative ineffectiveness previously recognized on existing cash flow and net investment hedges will be adjusted and removed from beginning retained earnings and placed in accumulated other comprehensive income (loss). The Company notes that this guidance will not have a material impact on the Company’s condensed consolidated financial statements. ASU 2017-12 is effective for fiscal years beginning after December 15, 2018 and is applied retrospectively.

In November 2016, the FASB issued ASU 2016-18 “Statement of Cash Flows (Topic 230): Restricted Cash” (“ASU 2016-18”). ASU 2016-18 is intended to clarify how entities present restricted cash in the statement of cash flows. The guidance requires entities to show the changes in the total of cash and cash equivalents and restricted cash in the statement of cash flows. As a result, entities will no longer present transfers between cash and cash equivalents and restricted cash in the statement of cash flows. When cash and cash equivalents and restricted cash are presented in more than one line item on the balance sheet, the new guidance requires a reconciliation of the totals in the statement of cash flows to the related captions in the balance sheet. This reconciliation can be presented either on the face of the statement of cash flows or in the notes to the financial statements. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017 and is to be applied retrospectively. The Company early adopted ASU 2016-18 on June 30,

2017, which changed the Company's condensed consolidated statement of cash flows and related disclosures for all periods presented. The following is a reconciliation of the Company's cash, cash equivalents, and restricted cash to the total presented in the Company's condensed consolidated statement of cash flows for the

9

three months ended March 31, 2018 and March 31, 2017, respectively (\$ in thousands):

	Balance at March 31, 2018	Balance at March 31, 2017
Cash	\$98,310	\$142,905
Restricted cash	\$—	\$54,702
Total cash and restricted cash shown in the condensed consolidated statement of cash flows	\$98,310	\$197,607

In June 2016, the FASB issued ASU 2016-13 “Financial Instruments - Credit Losses - Measurement of Credit Losses on Financial Instruments (Topic 326)” (“ASU 2016-13”). ASU 2016-13 significantly changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. The guidance will replace the “incurred loss” approach under existing guidance with an “expected loss” model for instruments measured at amortized cost, and require entities to record allowances for available-for-sale debt securities rather than reduce the carrying amount, as they do today under the other-than-temporary impairment model. It also simplifies the accounting model for purchased credit-impaired debt securities and loans. The guidance is effective for fiscal years beginning after December 15, 2019 and is to be adopted through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. While the Company is currently evaluating the impact ASU 2016-13 will have on its condensed consolidated financial statements, we expect that the adoption will result in higher provisions for potential loan losses.

Note 3 – Fair Value Disclosure

GAAP establishes a hierarchy of valuation techniques based on the observability of the inputs utilized in measuring financial instruments at fair values. Market based or observable inputs are the preferred source of values, followed by valuation models using management assumptions in the absence of market inputs. The three levels of the hierarchy as noted in ASC 820, Fair Value Measurements and Disclosures, are described below:

Level I — Quoted prices in active markets for identical assets or liabilities.

Level II — Prices are determined using other significant observable inputs. Observable inputs are inputs that other market participants would use in pricing a security. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.

Level III — Prices are determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used.

While the Company anticipates that its valuation methods will be appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. The Company will use inputs that are current as of the measurement date, which may include periods of market dislocation, during which price transparency may be reduced.

The estimated fair values of the Company’s derivative instruments are determined using a discounted cash flow analysis on the expected cash flows of each derivative. The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash receipts (or payments) and the discounted expected variable cash payments (or receipts). The fair values of interest rate caps are determined using the market standard methodology of discounting the future expected cash receipts (or payments) that would occur if variable interest rates rise above the strike rate of the caps. The variable interest rates used in the calculation of projected cash flows are based on an expectation of future interest rates derived from observable market interest rate curves and volatilities. The fair values of foreign exchange forwards are determined by comparing the contracted forward exchange rate to the current market exchange rate. The current market exchange rates are determined by using market spot rates, forward rates and interest rate curves for the underlying countries. The Company’s derivative instruments are classified as Level II in the fair value hierarchy.

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

The following table summarizes the levels in the fair value hierarchy into which the Company's financial instruments were categorized as of March 31, 2018 and December 31, 2017 (\$ in thousands):

	Fair Value as of March 31, 2018			Fair Value as of December 31, 2017		
	Level II	Level III	Total	Level II	Level III	Total
Derivative instruments, net	\$ (14,499)	\$	—\$(14,499)	\$ (5,644)	\$	—\$(5,644)

10

Note 4 – Securities

The Company previously held CMBS, all of which were sold in 2017. During the three months ended March 31, 2017, the Company sold CMBS resulting in a net realized loss of \$1.0 million.

During the three months ended March 31, 2017, the Company recorded interest income from securities of \$6.1 million, of which \$2.8 million was interest income from CMBS (Held-to-Maturity) and \$3.3 million of CMBS (Fair Value Option).

To conform to the 2018 presentation of the condensed consolidated statement of cash flows, the Company reclassified \$69.2 million of proceeds from sale of securities, \$0.8 million of principal payments received on securities, CMBS (Held-to-Maturity) and \$0.03 million of principal payments received on CMBS (Fair Value Option) and combined into payments and proceeds received on securities.

Note 5 – Commercial Mortgage and Subordinate Loans, Net

The Company's loan portfolio was comprised of the following at March 31, 2018 and December 31, 2017 (\$ in thousands):

Loan Type	March 31, 2018	December 31, 2017
Commercial mortgage loans, net	\$3,029,240	\$ 2,653,826
Subordinate loans, net	1,038,254	1,025,932
Total loans, net	\$4,067,494	\$ 3,679,758

The Company's loan portfolio consisted of 89% and 88% floating rate loans, based on amortized cost, as of March 31, 2018 and December 31, 2017, respectively.

Activity relating to our loan investment portfolio was as follows (\$ in thousands):

	Principal Balance	Deferred Fees/Other Items ⁽¹⁾	Provision for Loan Loss ⁽²⁾	Carrying Value
December 31, 2017	\$3,706,169	\$ (9,430)	\$ (16,981)	\$3,679,758
New loan fundings	488,638	—	—	488,638
Add-on loan fundings	18,393	—	—	18,393
Loan repayments	(137,947)	—	—	(137,947)
Unrealized gain (loss) on foreign currency translation	13,555	(113)	—	13,442
Deferred fees and other items ⁽¹⁾	—	(11,561)	—	(11,561)
PIK interest, amortization of fees and other items ⁽¹⁾	10,564	6,207	—	16,771
March 31, 2018	\$4,099,372	\$ (14,897)	\$ (16,981)	\$4,067,494

(1) Other items primarily consist of purchase discounts or premiums, exit fees and deferred origination expenses.

(2) In addition to the \$17.0 million provision for loan loss, the Company recorded an impairment of \$3.0 million against an investment previously recorded under other assets on the Company's consolidated balance sheet.

The following table details overall statistics for our loan portfolio (\$ in thousands):

	March 31, 2018	December 31, 2017
Number of loans	63	59
Principal balance	\$4,099,372	\$3,706,169
Carrying value	\$4,067,494	\$3,679,758

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

Unfunded loan commitments ⁽¹⁾	\$852,508	\$435,627	
Weighted-average cash coupon ⁽²⁾	8.6	% 8.4	%

Unfunded loan commitments are primarily funded to finance property improvements or lease-related expenditures (1) by the borrowers. These future commitments are funded over the term of each loan, subject in certain cases to an expiration date.

(2) For floating rate loans, based on applicable benchmark rates as of the specified dates.

The table below details the property type of the properties securing the loans in our portfolio (\$ in thousands):

Property Type	March 31, 2018		December 31, 2017	
	Carrying Value	% of Portfolio	Carrying Value	% of Portfolio
Predevelopment	\$710,992	17.5%	\$654,736	17.8%
Residential - for sale	704,020	17.3%	442,177	12.0%
Hotel	654,631	16.1%	645,056	17.6%
Office	584,990	14.4%	513,830	14.0%
Residential Rental	467,605	11.5%	465,057	12.6%
Mixed Use	356,079	8.7%	354,640	9.6%
Retail Center	199,463	4.9%	198,913	5.4%
Healthcare	158,292	3.9%	173,870	4.7%
Other	154,084	3.8%	154,141	4.2%
Industrial	77,338	1.9%	77,338	2.1%
	\$4,067,494	100.0%	\$3,679,758	100.0%

The table below details the geographic distribution of the properties securing the loans in our portfolio (\$ in thousands):

Geographic Location	March 31, 2018		December 31, 2017	
	Carrying Value	% of Portfolio	Carrying Value	% of Portfolio
Manhattan, NY	\$1,209,678	29.7%	\$1,173,833	31.9%
Brooklyn, NY	358,425	8.8%	357,611	9.7%
Northeast	107,671	2.7%	100,536	2.7%
Midwest	737,780	18.1%	683,380	18.6%
Southeast	447,450	11.0%	531,582	14.4%
West	270,170	6.6%	227,024	6.2%
Mid Atlantic	182,320	4.5%	191,976	5.2%
Southwest	33,384	0.8%	33,615	0.9%
United Kingdom	645,338	15.9%	303,488	8.3%
Other International	75,278	1.9%	76,713	2.1%
Total	\$4,067,494	100.0%	\$3,679,758	100.0%

The Company assesses the risk factors of each loan, and assigns a risk rating based on a variety of factors, including, without limitation, loan-to-value ratio ("LTV"), debt yield, property type, geographic and local market dynamics, physical condition, cash flow volatility, leasing and tenant profile, loan structure and exit plan, and project sponsorship. This review is performed quarterly. Based on a 5-point scale, our loans are rated "1" through "5," from less risk to greater risk, which ratings are defined as follows:

1. Very low risk
2. Low risk
3. Moderate/average risk
4. High risk/potential for loss: a loan that has a risk of realizing a principal loss
5. Impaired/loss likely: a loan that has a high risk of realizing principal loss, has incurred principal loss or has been impaired

The following table allocates the carrying value of our loan portfolio based on the Company's internal risk ratings (\$ in thousands):

Risk Rating	March 31, 2018			December 31, 2017		
	Number of Loans	Carrying Value	% of Loan Portfolio	Number of Loans	Carrying Value	% of Loan Portfolio
1	—	\$—	— %	—	\$—	— %
2	6	395,212	10 %	5	399,326	10 %
3	54	3,431,086	84 %	51	3,034,358	83 %
4	1	168,677	4 %	1	168,208	5 %
5	2	72,519	2 %	2	77,866	2 %
	63	\$4,067,494	100 %	59	\$3,679,758	100 %

The Company evaluates its loans for possible impairment on a quarterly basis. The Company regularly evaluates the extent and impact of any credit deterioration associated with the performance and/or value of the underlying collateral property as well as the financial and operating capability of the borrower/sponsor on a loan by loan basis. Specifically, a property's operating results and any cash reserves are analyzed and used to assess (i) whether cash from operations is sufficient to cover the debt service requirements currently and into the future, (ii) the ability of the borrower to refinance the loan and/or (iii) the property's liquidation value. The Company also evaluates the financial wherewithal of any loan guarantors as well as the borrower's competency in managing and operating the properties. In addition, the Company considers the overall economic environment, real estate sector and geographic sub-market in which the borrower operates. Such loan loss analysis is completed and reviewed by asset management and finance personnel who utilize various data sources, including (i) periodic financial data such as debt service coverage ratio, property occupancy, tenant profile, rental rates, operating expenses, the borrower's exit plan, and capitalization and discount rates, (ii) site inspections and (iii) current credit spreads and discussions with market participants. An allowance for loan loss is established when it is deemed probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan.

During 2017, the Company recorded a loan loss provision of \$2.0 million on a commercial mortgage loan secured by fully-built, for-sale residential condominium units located in Bethesda, MD. In addition to the \$2.0 million provision for loan loss, the Company recorded an impairment of \$3.0 million on a related investment previously recorded under other assets on the Company's condensed consolidated balance sheet. The loan loss provision and impairment were based on the difference between fair value of the underlying collateral, and the carrying value of the loan (prior to the loan loss provision and related impairment). Fair value of the collateral was determined using a discounted cash flow analysis. The significant unobservable inputs used in determining the collateral value were sales price per square foot and discount rate which were an average of \$678 dollars per square foot across properties and 15%, respectively. Effective April 1, 2017, the Company ceased accruing all interest associated with the loan and accounts for the loan on a cost-recovery basis (all proceeds are applied towards the loan balance). As of March 31, 2018 and December 31, 2017, this was assigned a risk rating of 5.

During 2016, the Company recorded a loan loss provision of \$10.0 million on a commercial mortgage loan and \$5.0 million on a contiguous subordinate loan secured by a multifamily property located in Williston, ND. The loan loss provision was based on the difference between fair value of the underlying collateral, and the carrying value of the loan (prior to the loan loss provision). Fair value of the collateral was determined using a discounted cash flow analysis. The significant unobservable inputs used in determining the collateral value were terminal capitalization rate and discount rate which were 11% and 10%, respectively. The Company ceased accruing payment in kind ("PIK") interest associated with the loan and recognizing interest income upon receipt of cash. As of March 31, 2018 and December 31, 2017, this was assigned a risk rating of 5.

As of March 31, 2018 and December 31, 2017, the aggregate loan loss provision was \$12.0 million and \$5.0 million for commercial mortgage loans and subordinate loans, respectively.

For the three months ended March 31, 2018 and March 31, 2017, the Company recognized PIK interest of \$10.6 million and \$7.9 million, respectively.

For the three months ended March 31, 2018 and March 31, 2017, the Company did not receive any pre-payment penalties or accelerated fees.

13

Note 6 – Loan Proceeds Held by Servicer

Loan proceeds held by servicer represents principal payments held by the Company's third-party loan servicer as of the balance sheet date which were remitted to us subsequent to the balance sheet date. Loan proceeds held by servicer was \$30.3 million and \$302.8 million as of March 31, 2018 and December 31, 2017, respectively.

Note 7 – Other Assets

The following table details the components of the Company's other assets (\$ in thousands):

	March 31, December 31,	
	2018	2017
Interest receivable	\$ 25,548	\$ 23,101
Collateral deposited under derivative agreements	20,150	4,930
Other	389	389
Total	\$ 46,087	\$ 28,420

Note 8 – Secured Debt Arrangements, Net

At March 31, 2018 and December 31, 2017, the Company's borrowings had the following secured debt arrangements, maturities and weighted average interest rates (\$ in thousands):

	March 31, 2018				December 31, 2017			
	Maximum Amount of Borrowings	Borrowings Outstanding	Maturity ⁽¹⁾	Weighted Average Rate ⁽²⁾	Maximum Amount of Borrowings	Borrowings Outstanding	Maturity ⁽¹⁾	Weighted Average Rate ⁽²⁾
JPMorgan Facility ⁽³⁾	\$ 1,382,000	\$ 800,535	March 2020	USD L + 2.30%	\$ 1,393,000	\$ 944,529	March 2020	USD L + 2.30%
DB Repurchase Facility (USD) ⁽⁴⁾	402,390	157,460	March 2020	USD L + 2.48%	472,090	225,367	March 2020	USD L + 2.56%
DB Repurchase Facility (GBP) ⁽⁴⁾	165,766	165,766	March 2020	GBP L + 2.60%	93,919	93,919	March 2020	GBP L + 2.60%
Goldman Facility ⁽⁵⁾	327,750	103,025	November 2020	USD L + 2.57%	331,130	81,380	November 2020	USD L + 2.73%
Sub-total	2,277,906	1,226,786			2,290,139	1,345,195		
less: deferred financing costs	N/A	(14,037)		N/A	N/A	(14,348)		N/A
Total / Weighted Average	\$ 2,277,906	\$ 1,212,749		USD L + 2.35% / GBP L + 2.60%	\$ 2,290,139	\$ 1,330,847		USD L + 2.37% / GBP L + 2.60%

(1) Maturity date assumes extensions at the Company's option are exercised.

(2) Based on applicable benchmark rates as of the specified dates on floating rate debt.

(3) As of March 31, 2018, the Company's secured debt arrangement with JPMorgan Chase Bank, National Association (the "JPMorgan Facility") provided

for maximum total borrowings comprised of a \$1.3 billion repurchase facility and \$132.0 million of an asset specific financing.

(4) As of March 31, 2018, the Company's secured debt arrangement with Deutsche Bank AG, Cayman Islands Branch and Deutsche Bank AG, London Branch (the "DB Repurchase Facility") provided for maximum total borrowings comprised of a \$450.0 million repurchase facility and \$55.1 million and £45.0 million of asset specific financings.

(5) As of March 31, 2018, the Company's secured debt arrangement with Goldman Sachs Bank USA (the "Goldman Facility") provided for maximum total borrowings comprised of a \$300.0 million repurchase facility and \$27.8 million

of an asset specific financing.

At March 31, 2018, the Company's borrowings had the following remaining maturities (\$ in thousands):

14

Edgar Filing: Apollo Commercial Real Estate Finance, Inc. - Form 10-Q

	Less than 1 year ⁽¹⁾	1 to 3 years ⁽¹⁾	3 to 5 years	More than 5 years	Total
JPMorgan Facility	\$132,715	\$667,820	\$ —	—	—\$800,535
DB Repurchase Facility	131,419	191,807	—	—	323,226
Goldman Facility	—	103,025	—	—	103,025
Total	\$264,134	\$962,652			