TWO HARBORS Investment Corp.

A Pine River Capital Managed Company

Second Quarter 2015 Letter to Stockholders

NYSE: TWO

August 20, 2015

Dear Fellow Stockholders,

In the second quarter, we were focused on protecting book value while advancing our operational businesses. At June 30, 2015 our book value was $10.81 per share, representing a total return on book value of 2.1%[1] for the first six months of the year. During the quarter, we delivered comprehensive income of $2.7 million, or $0.01 per weighted average share. From a strategic perspective, we continue to shift capital from our legacy Agency and non-Agency residential mortgage-backed securities (RMBS) portfolios into our operational businesses, which include our mortgage loan conduit, mortgage servicing rights (MSR) and commercial real estate.

Our mortgage loan conduit continues to gain momentum. We completed two securitizations during the second quarter, totaling approximately $493 million unpaid principal balance (UPB). This brings our total securitizations through the first half of the year to four and we remain on track to complete 6-10 transactions by year-end. Our Agate Bay brand accounted for roughly 19% of the total private label RMBS issuance in the first six months of the year, according to Credit Suisse mortgage research. We are proud of this strong market share and we continue to see increased investor interest and participation. Importantly, with each securitization we are creating new subordinate and interest-only credit assets for our portfolio at attractive returns. Our prime jumbo pipeline, which includes loans and interest rate locks, was approximately $1.3 billion UPB at June 30th, providing a solid foundation to be a reliable and consistent issuer.

Subsequent to quarter-end, we launched an Expanded Credit Program that targets a broader cohort of borrowers, particularly those who are unable to get a mortgage due to the tight credit standards that exist in the market today. This program allows for borrowers with lower FICOs and higher LTVs than our standard prime jumbo program. These will be fully underwritten mortgages, meeting Ability-to-Repay requirements. We believe the expansion of credit in the market place can benefit both homeowners and the housing market generally.

We continue to focus on growing MSR as a core holding in our Rates[2] portfolio. MSR represents an excellent fit within our portfolio as it provides positive yield and negative duration, and hedges basis risk. The longer a mortgage is outstanding, which happens when interest rates increase, the more value there is to the MSR. We are focused on building MSR flow-sale relationships, especially where we can leverage relationships with existing conduit seller partners. We have made good progress and anticipate adding 5-10 of these relationships by year-end. In addition, subsequent to quarter-end, we closed a $5.0 billion bulk purchase of Fannie Mae MSR.

We believe our operational businesses will be instrumental in driving our company forward. There are many operating efficiencies and infrastructure overlap between MSR and our mortgage loan conduit. From a product development perspective, we continue to evaluate avenues that are rooted in our core competencies of prepayment and credit risk analysis and, importantly, have the potential to benefit U.S. homeowners and our stockholders alike.

We are in the early stages of deploying capital to our commercial real estate strategy. The personnel and infrastructure requirements necessary to support the program have been substantially formed. We are beginning to develop a healthy pipeline and are excited about the deal flow in the marketplace today. As we have articulated in the past, there is a large amount of refinancing that needs to be done within the next several years, and many of the traditional lenders in the commercial space are retreating. Moreover, many commercial loans are floating rate in nature, which is desirous in a rising interest rate environment.

From a macroeconomic perspective, interest rate volatility remains elevated, as the market generally expects that the Fed will raise rates later this year. Accordingly, we continue to be positioned conservatively with respect to interest rate exposure. Unemployment metrics improved year-over-year as of June 2015, falling to 5.3%. National home prices increased on a rolling 12-month basis in June to 6.5%, according to CoreLogic.

From a policy standpoint, we are in active dialogue with parties in Washington on a number of industry topics, including private label securitization, servicing standards and capital requirements, government sponsored entity risk sharing and housing finance reform. With respect to the Federal Housing Finance Agency proposed rulemaking regarding Federal Home Loan Bank membership, we have not heard anything further after submitting our response letter. It is our belief that it is still under review.

Our primary objective is to deliver total return for our stockholders over the long term. We accomplish that through dividend distributions and book value preservation and growth. We have made tremendous progress on our operational businesses and believe we are poised for growth in these segments over the next several quarters. Each of these initiatives has the potential to offer attractive expected returns, build franchise value, increase valuation and, most importantly, drive stockholder returns. Thank you for your interest in Two Harbors.

Sincerely,

Thomas Siering
President and Chief Executive Officer

(1) Total return on book value is the increase in book value, plus dividends declared, for the indicated time period as measured from June 30, 2015.
(2) Assets in “Rates” include Agency RMBS, Agency Derivatives (inverse interest-only securities), MSR and Ginne Mae buyout residential mortgage loans.