



November 29, 2016

Dear Fellow Stockholders,

At Two Harbors, we are focused on employing a flexible model that allows us to allocate capital in a manner to generate attractive returns, leading to strong dividends, while keeping a conservative risk profile and protecting investors' capital. In fact, this approach is the primary reason why we have outperformed our peer group by over 40%<sup>(1)</sup> in total stockholder return over the past seven years since we became a public company, and have done so with less book value volatility.

We delivered strong results in the third quarter, driving solid increases in book value, Comprehensive Income and Core Earnings. Our Rates<sup>(2)</sup>, Credit<sup>(3)</sup> and Commercial<sup>(4)</sup> strategies all contributed to this performance. Our return on book value for the quarter was 4.2%<sup>(5)</sup> and Comprehensive Income was \$136.5 million, or \$0.39 per share. This success is reflective of our team's disciplined approach to risk management and smart portfolio choices.

In our Rates strategy, we maintained low interest rate and prepayment exposure. In fact, we believe that as a result of our conservative risk profile, we are largely insulated to changes in interest rates, not only in terms of book value but also in terms of income and earnings. Additionally, approximately 65% of our Agency holdings had some form of prepayment protection as of September 30. Strategically, we are focused on thoughtfully managing our Agency portfolio and, particularly, on building our mortgage servicing rights (MSR) position by adding high-quality, new issue, conventional MSR at low coupon rates. In the quarter, we added approximately \$10.6 billion in unpaid principal balance (UPB) of MSR, largely from flow sale arrangements. In the near-term, we anticipate flow sale MSR volumes of about \$3.0 billion per month. We also sold substantially all of our Ginnie Mae MSR position in the quarter, improving operational efficiencies. As a reminder, we are investing in high-quality, new issue, conventional MSR as we believe that it pairs best with our Agency holdings.

In our Credit strategy, we will continue to capitalize on the fundamental and economic factors that support our non-Agency position. We've seen an uplift in recovery expectations and believe that this is sustainable for the foreseeable future with potential upside. Housing price appreciation and the age of our portfolio in respect to principal payments gives upside to prepayment speeds. We believe that our portfolio is positioned to benefit from these tailwinds. In the quarter, our legacy non-Agency holdings delivered an attractive yield of 9.1%. Given that performance continues to be better than our initial expectations, we again released credit reserves against this portfolio and, as a result, anticipate maintaining strong yields for our legacy non-Agency portfolio. Combined with a weighted average market price of about \$75, we believe that there continues to be further upside. With respect to the discontinuation of the mortgage loan conduit, we remain on track to wind down that business by the end of the year. As we outlined last quarter, this reduces our operating complexity and costs and positions us to redeploy capital to areas of the business that we believe will generate stronger returns for our shareholders, particularly MSR and commercial real estate assets.

With respect to commercial real estate, we expect to continue to increase capital allocated to this strategy and grow our portfolio of high-quality loans with attractive rates and structures. The fundamentals underlying the commercial real estate market remain positive, providing attractive return opportunities given refinancing and transactional needs. This is particularly true for non-traditional lenders, like Two Harbors, as they can provide capital that is harder for bank and CMBS lenders to provide, given changes in the regulatory environment for them. We grew our portfolio in the quarter to \$1.1 billion as we added four senior loans.

We continue to maintain flexibility across our financing profile with a diversified counterparty mix and lengthy maturity profile. A highlight of the third quarter was the addition of financing for mortgage servicing rights. This \$30 million facility represents our initial step forward on obtaining financing on our MSR portfolio. We anticipate expanding upon this source of financing in the future as we work with other counterparties and the GSEs. In addition, we have two facilities in place for financing commercial real estate assets and continued to expand usage of these in the third quarter.

Overall, we delivered another quarter of strong results and we are focused on streamlining the business model, deploying capital to maximize returns, and improving efficiencies. As we head toward the end of the year and into 2017, we are not only excited about the results we delivered in the third quarter, but we are even more encouraged about the momentum we are building for 2017. Thank you for your interest in Two Harbors.

Sincerely,



Thomas Siering  
President and Chief Executive Officer

- (1) Two Harbors' total stockholder return is calculated for the period October 29, 2009 through September 30, 2016. Total stockholder return is defined as stock price appreciation including dividends. Source: Bloomberg
- (2) Assets in "Rates" include Agency RMBS, Agency Derivatives, MSR and Ginnie Mae buyout residential mortgage loans.
- (3) Assets in "Credit" include non-Agency RMBS, prime jumbo residential mortgage loans, net economic interest in securitization trusts and credit sensitive residential mortgage loans.
- (4) Commercial consists of senior and mezzanine commercial real estate debt and related instruments.
- (5) Return on book value for the quarter ended September 30, 2016 is defined as the increase in book value from June 30, 2016 to September 30, 2016 of \$0.18, plus the dividend declared of \$0.23 per share, divided by June 30, 2016 book value of \$9.83 per share.

#### Forward-Looking Statements

This presentation includes "forward-looking statements" within the meaning of the safe harbor provisions of the United States Private Securities Litigation Reform Act of 1995. Actual results may differ from expectations, estimates and projections and, consequently, readers should not rely on these forward-looking statements as predictions of future events. Words such as "expect," "target," "assume," "estimate," "project," "budget," "forecast," "anticipate," "intend," "plan," "may," "will," "could," "should," "believe," "predicts," "potential," "continue," and similar expressions are intended to identify such forward-looking statements. These forward-looking statements involve significant risks and uncertainties that could cause actual results to differ materially from expected results, including, among other things, those described in our Annual Report on Form 10-K for the year ended December 31, 2015, and any subsequent Quarterly Reports on form 10-Q, under the caption "Risk Factors." Factors that could cause actual results to differ include, but are not limited to: the state of credit markets and general economic conditions; changes in interest rates and the market value of our assets; changes in prepayment rates of mortgages underlying our target assets; the rates of default or decreased recovery on the mortgages underlying our target assets; the occurrence, extent and timing of credit losses within our portfolio; the concentration of credit risks we are exposed to; declines in home prices; our ability to establish, adjust and maintain appropriate hedges for the risks in our portfolio; the availability and cost of our target assets; the availability and cost of financing; changes in the competitive landscape within our industry; our ability to successfully implement new strategies and to diversify our business into new asset classes; our ability to manage various operational risks and costs associated with our business; interruptions in or impairments to our communications and information technology systems; our ability to successfully securitize or sell mortgage loans; our ability to acquire mortgage servicing rights (MSR) and successfully operate our seller-servicer subsidiary and oversee our subservicers; the impact of any deficiencies in the servicing or foreclosure practices of third parties and related delays in the foreclosure process; the state of commercial real estate markets and our ability to acquire or originate commercial real estate loans or related assets; our exposure to legal and regulatory claims; legislative and regulatory actions affecting our business; the impact of new or modified government mortgage refinance or principal reduction programs; our ability to maintain our REIT qualification; and limitations imposed on our business due to our REIT status and our exempt status under the Investment Company Act of 1940.

Readers are cautioned not to place undue reliance upon any forward-looking statements, which speak only as of the date made. Two Harbors does not undertake or accept any obligation to release publicly any updates or revisions to any forward-looking statement to reflect any change in its expectations or any change in events, conditions or circumstances on which any such statement is based. Additional information concerning these and other risk factors is contained in Two Harbors' most recent filings with the Securities and Exchange Commission (SEC). All subsequent written and oral forward-looking statements concerning Two Harbors or matters attributable to Two Harbors or any person acting on its behalf are expressly qualified in their entirety by the cautionary statements above.