TWO Fourth Quarter 2024 Financial Results Call

Thursday, January 30, 2025

9:00am ET

Operator

Good morning. My name is Maddie and I will be your conference facilitator. At this time, I would like to welcome everyone to the TWO Fourth Quarter 2024 Earnings Call. All participants will be in a listen-only mode. After the speakers' remarks, there will be a question-and-answer period. I would now like to turn the call over to Maggie Karr.

Maggie Karr

Good morning, everyone, and welcome to our call to discuss TWO's fourth quarter 2024 financial results. With me on the call this morning are Bill Greenberg, our President and Chief Executive Officer, Nick Letica, our Chief Investment Officer, and William Dellal, our Interim Chief Financial Officer.

The earnings press release and presentation associated with today's call have been filed with the SEC and are available on the SEC's website, as well as the Investor Relations page of our website at twoinv.com. In our earnings release and presentation, we have provided reconciliations of GAAP to non-GAAP financial measures, and we urge you to review this information in conjunction with today's call.

As a reminder, our comments today will include forward-looking statements, which are subject to risks and uncertainties that may cause our results to differ materially from expectations. These are described on page 2 of the presentation and in our Form 10-K and subsequent reports filed with the SEC. Except as may be required by law, TWO does not update forward-looking statements and disclaims any obligation to do so. I will now turn the call over to Bill.

Bill Greenberg

Thank you, Maggie. Good morning, everyone, and welcome to our fourth quarter earnings call. Before turning to our results, I'd like to take a moment to remember our board member, Reid Sanders, who passed away this month. Reid served as a member of our Board of Directors since our company's inception in October of 2009. He was a trusted advisor and partner to TWO and our management team, and to me personally, and we will miss him greatly.

Please turn to slide 3. Our book value at December 31st was $14.47 per common share, and which, including the fourth quarter common stock dividend of $0.45 per share, represented a 0.0% quarterly economic return on book value. For the full year of 2024, we generated a 7.0% total economic return on book value.

Please turn to slide 4. Figure 1 shows the evolution of the market's expectations for the Fed's interest rate policy over the past year. While the Fed delivered two 25 basis point cuts over the quarter, robust jobs and inflation data, along with hawkish comments from Chairman Powell at the Fed's December meeting, tempered rate expectations for 2025. Indeed, at the beginning of the fourth quarter, the market was pricing in more than 100 basis points worth of additional Fed cuts, shown by the blue line, but by the end of the quarter, the market had reconsidered, only pricing in roughly 35 basis points, as seen by the purple line. Over the quarter, the 10-year Treasury yield went up by 79 basis points to finish at 4.57%, while the 2-year increased by 60 basis points to 4.24%, steepening the yield curve by 19 basis points, as seen in figure 2.

While short-term rates may yet decline in 2025, the Fed remains very data dependent. Further, a decline in short-term rates does not necessarily correlate to a decline in longer-term Treasury rates or mortgage rates. Rather, it's our expectation that mortgage rates are likely to remain above 6% in the intermediate-term. At that level, the so-called "lock-in effect" should keep housing activity muted and, incidentally, will also help prepayments slow which is a benefit to the value of MSR portfolios like ours. Interest rate volatility is likely to remain high for the foreseeable future, with the biggest risk being that inflation re-emerges, and the Fed pauses, or reverses, the rate cutting cycle. We continue to keep our interest rate exposures low and believe that our MSR-centric strategy will generate favorable returns independent of any short-term fluctuations in Fed-driven funding rates.

Please turn to slide 5. At year-end, we serviced $212 billion UPB of MSR across 861,000 loans, 58,000 – or $11.2 billion UPB – of which are serviced for third-party clients.

Looking back, 2024 concludes our first full year owning an operating mortgage company, and I'm pleased to say that the integration of RoundPoint into TWO has largely gone according to the plan that we laid out in August of 2022. In particular, we are already reaping the improved economics that we estimated due to lower costs and increased revenue streams from servicing the loans from our own MSR portfolio. Specifically, we have benefited from increased economies of scale and additional cash flows from the servicing asset, which had previously benefited our subservicers and not us.

In 2024, we also launched a direct-to-consumer originations platform, with the intent of maintaining our current servicing portfolio through recapture of the underlying mortgage loans when the borrower refinances or moves into a new loan product. We think of this effort primarily as being a hedge to our MSR portfolio that serves to protect our asset from faster than expected prepayment speeds, should interest rates drop precipitously. Taken altogether, the value of TWO's MSR portfolio benefits from the success of servicing, which directly affects the success of originations, which circles back to a positive value contribution to the MSR portfolio.

With a weighted average note rate of 3.46% in our MSR portfolio, and mortgage rates currently around 7%, roughly only 0.2% of our customers would benefit from a rate and term refinance. With that as background, we funded $42 million UPB of first mortgages in the quarter, and there is approximately another $21 million UPB currently in the pipeline. We recognize that these are small numbers, but we are very pleased with the proof-of-concept and progress thus far. In less than one year, we stood up a brand-new platform entirely from scratch, with no legacy risks and for a de minimis cost. The challenge, and opportunity, in 2025 is to bring this platform fully to scale.

Despite the small number of refinanceable loans in our servicing portfolio, we are utilizing the platform to bring incremental revenue and returns to our shareholders. With mortgage rates north of 7%, many of our customers are looking for ways to extract equity while not giving up their ultra-low mortgage rates and so, in the latter half of the year, we began to offer second lien loans to our borrowers. In the quarter, we acted as a broker on $33 million UPB in a combination of both open ended and closed end loans. We intend to expand this effort, which will likely include originating the loans in our own name.

With mortgage rates expected to remain above 6% in 2025, our focus at RoundPoint is on generating additional cost efficiencies in servicing – especially through the use of technology and AI applications. From a customer experience perspective, we are dedicated to creating a strong platform and brand for our customers to turn to for all their mortgage and home equity needs.

Our results in 2024 demonstrated the benefits of our portfolio with its core focus on hedged MSR. With roughly two-thirds of our capital allocated to MSR that is almost 400 basis points out of the money, that asset should generate relatively stable cashflows going forward, regardless of the path of short-term interest rates. RMBS spreads remain wide on a nominal basis, reflective of continued elevated levels of implied interest rate volatility. While 2024 saw RMBS spreads meaningfully tighten, the outlook for RMBS in 2025 is still attractive, but the risks are more balanced. The efforts we have made, and continue to make, regarding process improvements and product offerings at RoundPoint allow us to shape our return profile in a way that owning only a portfolio of securities cannot. I'm very proud of what we have accomplished in the past year and I'm tremendously excited about where we are going. With that, I'd like to hand the call over to William to discuss our financial results.

William Dellal

Thank you, Bill.

Please turn to slide 6. Our book value was $14.47 per share at December 31st, compared to $14.93 on September 30th. Including the $0.45 common stock dividend, this resulted in a flat quarterly economic return, as Bill has already mentioned. For the year, we generated an economic return of 7.0%.

Please turn to slide 7. The company incurred a Comprehensive Loss of $1.6 million, or $0.03 per weighted average common share in the fourth quarter.

Net interest expense of $35 million was lower in the fourth quarter by $7.4 million due to lower RMBS borrowing balances as a result of sales of RMBS. Additionally, we shifted a portion of our MSR financing from credit facilities to VFN repurchase agreements, which on average carry lower floating rate spreads. This was slightly offset by higher overall average MSR borrowing balances.

Net servicing income was $168 million, minus $5 million of nonoperating MSR related servicing costs. This is down slightly from the third quarter due to lower float income resulting from lower average outstanding balances, and lower rates earned on the balances given the decline in short-term rates. The lower float was offset partially by higher servicing fee collections and higher subservicing related income earned.

As expected, due to higher yields, investment securities gain and change in OCI swung from a gain of $270 million in the third quarter to a loss of $267 million in the fourth quarter.

Additionally, net swap and other derivative gains in our RMBS hedge portfolio were $145 million in the fourth quarter compared to losses of $205 million in the third quarter, resulting from market movements on swaps and futures, offset by market movement on TBAs and slightly lower swap interest spread income.

The servicing assets showed a gain of $82.5 million in the fourth quarter after a loss of $133.4 million in the third quarter. Higher rates and lower projected prepayments resulted in a positive $139.4 million change in the valuation of MSR, as opposed to a negative $93.8 million change in the third quarter. Runoff declined in the fourth quarter to $57 million from $62 million in the third quarter. The decline in runoff was a result of lower UPB, due to the sale of MSR in the third quarter, as well as the decline in realized prepayment rates.

It is important to look at changes in values for the assets and the hedges together, rather than in isolation. The net change in the sum of investment securities gain and changes in OCI, net swap and other derivative gains, and the servicing asset gains shows a loss of $47.5 million in the fourth quarter, compared to a loss of $67.3 million in the third quarter.

Please turn to slide 8. RMBS funding markets remain stable and available throughout the quarter, with spreads for repurchase agreements at SOFR plus 35 basis points. Concerns about anticipated year-end funding pressures and uncertainty around Fed actions have dissipated, and rates have reverted back to more normal ranges around SOFR plus 15-20 basis points. In retrospect, year-end was uneventful in the funding markets and early indications in 2025 are that spreads are normalizing into a tighter historical context. At quarter end, our weighted average days to maturity for our Agency RMBS repo was 49 days, compared to 78 days at the end of Q3. Our days to maturity are typically lower at December 31st, as we intentionally roll repos in the third quarter past year-end to avoid any disruption in funding that can sometimes occur.

We finance our MSR activities across five lenders with $1.8 billion of outstanding borrowings under bilateral facilities. We ended the quarter with a total of $865 million in unused MSR asset financing capacity and $60 million in unused capacity for servicing assets. I will now turn the call over to Nick.

Nick Letica

Thank you, William. Before I launch into the slides and provide more detail, let's talk a little bit about the fourth quarter performance at a high level. This was an “interesting” quarter, particularly for mortgage performance, as mortgage spreads didn't exactly follow the usual playbook.

In total, we started the quarter with less mortgage spread risk than any recent quarter, with most of our exposure in 5.5s and up. As rates rose and spreads widened, we let our spread exposure increase, which contributed positively to our performance.

Our MSR was aided by slower than expected prepayment speeds, though the quick rise in rates in October, which triggered a fair amount of rehedging, impacted our MSR performance. As we discussed in last quarter's earnings call, the risk of our MSR varies as rates move, both in terms of duration and coupon exposure. As rates increase, the duration of exposure declines and shifts into higher coupons. In practice, that means having to sell some of our RMBS at lower prices, both due to higher rates, and, in a month like October, at wider spreads.

Higher rates have typically spelled trouble for mortgage performance, and it did again in October as interest rates increased and volatility spiked ahead of the Presidential election, which negatively affected many mortgage REIT book values.

However, in November, following the decisive election results, investors aggressively returned to the market, leading to a recovery in spreads that would not have been predicted based on the move in rates. Over that two-month time period the 10-year Treasury yield increased by 39 basis points, and the slope of the 2-year/10-year Treasury curve flattened by 12 basis points, yet the index turned in a net positive excess return of +5 basis points.

Though hawkish comments from the Fed in December drove rates higher yet again and pushed the quarterly index excess returns to -11 basis points, the muted reaction of mortgage spreads compared to prior periods was notable. Of course, the index is heavily weighted to lower coupons, and performance across the stack varied widely. Higher coupons, especially in pool form, outperformed, turning in a positive hedged return performance.

Jumping into the deck, please turn to slide 9. Our portfolio at December 31st was $14.8 billion, including $10.4 billion in settled positions and $4.4 billion in TBAs. Our economic debt-to-equity decreased slightly to 6.5x, though as you can see in figure 3, our mortgage spread exposure increased into a more normal range as spreads became more attractive in the quarter. As we have said in the past, the leverage exposure is but one of many risk metrics we manage, and it can't be taken by itself to assess our overall risk. We continue to manage our exposure to rates across the curve closely. You can see more detail on our risk exposures on Appendix slide 17.

Please turn to slide 10. As you can see in figure 1, our preferred implied volatility gauge, 2-year options on 10-year rates, increased from 94 to 101 basis points on an annualized basis, right in the middle of its range for 2024. Implied volatility and nominal spreads remained higher than longer-term averages, while option-adjusted spreads are close to longer-term averages. The level of mortgage spread volatility has materially declined from earlier parts of this interest rate cycle, improving the risk adjusted return profile. The nominal spread on TBA current coupon MBS finished 11 basis points wider at 117 basis points of the Treasury curve, while the option-adjusted spread finished 6 basis points wider at +23. Note that some of the spread widening reflects the shift from about a 5% current coupon at the start of the quarter to something in between 5.5 and 6.0 by quarter-end. As you can see in figure 2, the nominal spread curve steepened, with peak spreads around the 6% coupon at quarter-end. The OAS curve flattened, with higher coupons picking up spread as prepayment risk diminished.

Please turn to slide 11 to review our Agency RMBS portfolio. Figure 1 shows the performance of TBAs compared to the specified pools we owned throughout this quarter. As I mentioned earlier, given that the interest rate curve bear steepened and implied volatility ticked up, lower coupons underperformed higher coupons. Higher coupons specified pools were the best performer, as you can see in figure 1, outperforming TBAs by at least a quarter point and rate hedges by about a half point.

In terms of activity, we shifted TBA exposure up in coupon and replaced some specified pools with TBAs. We also bought some higher coupon pools to improve carry as dollar rolls weakened. Incorporating the effect that our MSR has on our net notional mortgage exposure, our position increased by about $1.5 billion over the quarter.

Though primary mortgage rates increased by about 75 basis points in the quarter, overall prepayment rates for 30-year Agency RMBS rose by 0.4 percentage points over the quarter to 6.9% CPR, as higher coupon speeds reflected the lagged effect of the mini refi wave triggered by the fall in rates in Q3. Borrowers with a refinance incentive responded to the lower rates in September with a propensity similar to borrower behavior in 2019. Figure 2 on the bottom right shows our specified pool prepayment speeds by coupon. On aggregate, speeds increased to 8.1% from 7.6% in the third quarter, led by an increase in speeds from 5.5s, 6.0s, and 6.5s.

Please turn to slide 12 as we discuss the market for investing in MSR. The MSR market remained stable and well supported, with bulk deals consistently receiving double digit competitive bids. Some large-scale bids and acquisitions in Q4 lifted 2024 transfers to $662 billion UPB, approximately the same amount in 2023, though the number of bulk bid opportunities dropped by about 25% year-over-year, as you can see in figure 1. While demand for MSR continues to be strong from both bank and non-bank portfolios, we expect there to be ample opportunities in 2025 to add MSR at attractive spreads.

Please turn to slide 13, where we will discuss our MSR portfolio. Figure 1 is an overview of our portfolio at quarter-end, the details of which can be found on Appendix slide 23. The portfolio was $202 billion UPB at December 31st, reflecting the settlement of $2.5 billion UPB through bulk and flow channels, and portfolio recapture. With mortgage rates increasing in the quarter, the price multiple of our MSR increased slightly to 5.9x from 5.6x, and 60+ day delinquencies remained low at under 1%. Our MSR portfolio, with a low gross mortgage rate of 3.46%, experienced a 4.9% CPR in Q4, down 0.4 percentage points compared to Q3, as slower seasonal factors kicked in. In order to facilitate comparison of our MSR prepayment rates with the larger universe, we map our portfolio into cohorts by mortgage rate so that they resemble RMBS. Figure 2 compares CPRs across those implied security coupons in our portfolio of MSR versus TBAs. You can see that prepays remain low and steady for the majority of our portfolio, with 5.5s and above slightly increasing.

Finally, please turn to slide 14. Our Return Potential and Outlook slide. The top half of this table is meant to show what returns we believe are available on the assets in our portfolio. We estimate that about 61% of our capital is allocated to Servicing with a static return projection of 11% to 14%. The remaining capital is allocated to Securities with a static return estimate of 14% to 15%.

With our portfolio allocations shown in the top half of the table, and after expenses, the static return estimate for our portfolio is between 9.8% to 12.1% before applying any capital structure leverage to the portfolio. After giving effect to our outstanding convertible notes and preferred stock, we believe that the potential static return on common equity falls in the range of 10.8% to 14.4%, or a prospective quarterly static return per share of $0.39 to $0.52.

We like that our current capital allocation is focused on MSR, and believe it will result in strong returns for our stockholders. Slow prepayments are a positive tailwind for our servicing portfolio, but even if prepayments picked up, we believe that the significant progress we have made at RoundPoint on our direct-to-consumer originations platform will serve as a hedge to our MSR portfolio. Additionally, our focus on generating additional cost efficiencies in servicing – especially through technology and process improvements at RoundPoint – will contribute positively to the value of MSR. We continue to actively manage our RMBS positioning to complement our MSR portfolio, and aim to extract additional returns from historically wide nominal current coupon spreads. We believe that our unique, hedged MSR-centric strategy will continue to generate attractive levered returns in 2025 and beyond.

Thank you very much for joining us today, and now, we will be happy to take any questions you might have.

Operator

If you would like to ask a question, please signal by pressing star 1 on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, that is star 1 to ask a question. We will pause for just a moment to allow everyone an opportunity to signal for questions.

We will take our first question from Doug Harter with UBS.

Marissa Lobo, UBS

Thanks, and good morning. It's Marissa Lobo on for Doug. I was hoping you could give us an update on how book has performed so far in the quarter?

Bill Greenberg

Yeah. Good morning, Marissa. Thanks for the question. It's been a reasonably quiet quarter, although I'll stress that it's early in the quarter. It's only been one month, of course, but our total return is estimated to be up between about 1.5% and 2% as of last night.

Marissa Lobo, UBS

Got it. Thank you. Second, how does the lower leverage level impact your view on earnings power? What would the normalized range for earnings be?

Nick Letica

Thank you for the question. This is Nick. As I mentioned in my prepared remarks, our overall debt-to-economic ratio is really but one measure that we look at in terms of our return potential and our earnings power. You can see from our return potential slide that overall, the central tendency of our returns and the range of our returns is still supportive of our dividend and very much in the range of what it was in prior quarters. The leverage itself determines some of the components of the debt-to-equity. If you look at other components of our risk, such as the amount of mortgage spread risk we have, again, as I said in my prepared remarks, quarter-over-quarter that increased into a more normal range. That's really reflective of how we feel about spreads and how they look right now. Beyond that, the overall mix of our assets of having over 60% of our capital in MSR is very supportive of stable, and in our opinion, predictable returns for future periods.

Bill Greenberg

One thing I might add, Marissa, also, is that the way that we hedge our MSR and we're hedging the current coupon risk that as rates rise, we need less MBS to hedge the current coupon risk of the portfolio. As rates go down we need more. That has a direct impact in when we're keeping everything unchanged, our risk unchanged, as rates move. That has an impact on the overall leverage, which is why Nick stressed that the leverage is just one component of the risk that we manage and measure.

Marissa Lobo, UBS

Thanks for that. Finally, your earnings power outlook, does that reflect the cost of volatility?

Bill Greenberg

No. As it says, those are static spreads.

Marissa Lobo, UBS

Static. Okay. Thank you. That's it for me.

Bill Greenberg

Thank you.

Operator

We will take our next question from Mikhail Goberman with Citizens JMP.

Mikhail Goberman, JMP Securities

Hey, good morning, guys. Could you maybe expand a bit on your outlook for Agency MBS spreads for this year? Also, how do you guys see the allocation to MSRs versus MBS evolving throughout the year? Thank you.

Nick Letica

Hey, Mikhail, thank you for the question. What I would say is, we have seen and we've made note of it, is that there has been a much more controlled response of mortgage spreads. I would say really notably since November when we got through the Presidential election and slightly before that when the Fed first cut. I think that's really a reflection of the fact that there is a more predictable Fed path than there was in earlier parts of the cycle. I still think this is a very data-dependent set. It's still quarter-to-quarter. There's a lot of other things that are being factored into the risk equation out there in the world. The overall amount of spread risk has declined. There are reasons to be positive about mortgage spreads this year. Net supply and supply, demand seems to be pretty much in balance. We have something like a net amount of supply in the low $200 billion, which has been reasonably absorbed by the market. There has been better uptake by banks. I think the general consensus is the uptake by banks has been more than what the market was generally assuming, kind of a consistent amount of demand from money managers and flows into funds that buy mortgages. The RV of mortgages looks quite good relative to other spread assets in the world. Funding rates, they spiked a little bit towards the end of last year, but now they've come right back into the zone they've been in, which is good. Of course, if the Fed does cut more this year, the steeper yield curve is usually constructive for mortgage spreads because it encourages institutions, mostly banks, to go further out on the curve and buy mortgages.

All of those things are good points. Our overall feeling, and we're kind of keeping it down the fairway here, is that mortgages should continue to be constructive for us from a return perspective. Where spreads are right now, we don't really need spreads. We say this every quarter, but it's true. We really do not need spreads to tighten to get performance. I think the part of it that is difficult is when you have a tremendous amount of volatility and that really has come down. Overall, I'd say we're positive on mortgage spreads. And we know from the volatility that this market has given us that there's always something that can change that. However, one of the key parts of our strategy, which we can't really overemphasize, is the core of our MSR. That really does provide a lot of stability to our return profile. If you look at our returns over the last many quarters, you can see we've had a lot of stability in book value and good economic returns. We think that will bode us well for the foreseeable future.

Mikhail Goberman, JMP Securities

Great. Given that, I'm guessing that the MSR allocation versus MBS is going to be steady as she goes, similar to what it's been in the recent quarter for TWO?

Nick Letica

Correct. Sorry, I didn't mean to not answer that question. Yes, we don't expect to see a material change in our MSR allocation. We're always looking at the asset allocation to move asset allocation as we get cashflows to invest in new capital. We don't see a material change in the allocation to our MSR.

Mikhail Goberman, JMP Securities

Great. Thank you. If I can squeeze in one more, any thoughts on potential GSE reform and the nomination of this new FHFA person to lead it? Thanks.

William Dellal

Hi, this is William. I don't think we have more information than what the market has regarding GSE reform, but I think we can break the GSE reform question into two questions, actually. What is the status of privatization, and what is the status of the guarantee? The guarantee itself breaks into two sub questions. What is going to happen to existing securities that have the guarantee, and what is going to happen to prospective securities whether they will carry the guarantee or not? Once we have more detail about potential plans, we can look at the implications through the lens of those two questions. We really don't have any more information currently and we don't want to speculate about what's going on.

Mikhail Goberman, JMP Securities

Gotcha. Well, thank you very much and best of luck going forward.

Bill Greenberg

Thanks very much, Mikhail.

William Dellal

Thank you.

Operator

We will take our next question from Bose George with KBW.

Frank Labetti, Keefe, Bruyette & Woods

Hi. Good morning. This is actually Frank Labetti on for Bose. Just to start, can you discuss the main differences between the EAD and the static return range you provide on slide 14?

Nick Letica

Sure. Thank you, Frank, for the question. I'll get started. Yeah. The return potential that we show on slide 14 is our actual portfolio quarter-end. It is projected out. It's a mark-to-market basis where everything in the portfolio is marked contemporaneously at that date and valued at that date. In our opinion, it's a good assessment of where the return potential of the static yields are to the forward curve when you take our entire portfolio marked on the same day, and generate a yield or a return potential. EAD, the word that we use about it is that it's asynchronous so that the EAD is something where if you have assets that are like many of our mortgage pools we bought long ago. The EAD reflects the purchase price of the return at that time. Whereas other components of our overall business structure, such as our funding, our repo, are more contemporaneous. So that you can have a real difference in timing between those things and it can create distortions to how we see the portfolio on a day-to-day basis and manage it on a day-to-day basis, if that makes sense to you.

Bill Greenberg

The way I like to think about it is that if you were to buy and sell the portfolio every day, the EAD would look something more like what we have on slide 14.

Frank Labetti, Keefe, Bruyette & Woods

Great. That's very helpful. Thank you. Just to stay on that slide, the return of your MSR fell to like 11% to 14% from 12% to 16% last quarter. Given the higher rate environment, is the driver of the lower returns the increase in the mark-to-market on the MSR this quarter?

Nick Letica

It's a very good question. It's a combination of things. The biggest thing that it is, again, this is a slice in time. It is one day. We manage our portfolio through time. A component of the return of our MSR portfolio is its hedge. That hedge is our RMBS securities or current coupon securities typically, which also add to the return of the strategy. It's a paired strategy of MSR plus MBS and the MBS add return. When rates go up, as I mentioned in my comments, the amount of MBS that we need to hedge that MSR declines. Overall, if you think about it that way, the leverage of that part of the portfolio goes down. There are less securities that are attached to the MSR. Consequently, the return potential, all else being equal, will tend to go down as that hedge becomes a smaller part of the overall pair.

Frank Labetti, Keefe, Bruyette & Woods

Great. Thank you very much. Appreciate it.

Bill Greenberg

Thank you.

Operator

We will take our next question from Eric Hagen with BTIG.

Jake Katsikas, BTIG, LLC

Good morning. This is Jake Katsikas on for Eric. Thanks for taking my questions. Are you guys seeing any new financing counterparties or sources of leverage to support the MSR portfolio?

Bill Greenberg

Go ahead, William.

William Dellal

We've been working with traditional lenders. There are some new entrants that are trying to gain traction in the market. We've seen a few requests, inbound calls, from people who want to expand into MSR financing.

Bill Greenberg

Yeah. In general – I would just add to what William just said there – I think that the depth of the market for MSR financing continues to grow and expand. As William said, there's more counterparties entering the market all the time. It's a very healthy market for that product right now.

Jake Katsikas, BTIG, LLC

Great. Thank you. Can you also just share how much the costs have changed in response to the first 100 bips of rate cuts that we've seen?

Bill Greenberg

Which costs are you thinking of specifically?

Jake Katsikas, BTIG, LLC

In the MSR portfolio.

Bill Greenberg

I'm not sure I understand your question.

William Dellal

Are you talking about our financing costs?

Jake Katsikas, BTIG, LLC

Yeah, I can just back it up to maybe just kind of cost in general, how they've shaped in response to the 100 bips of cuts that we saw, things like that.

Bill Greenberg

Our financing costs on the MSR asset are floating rates and are indexed to short-term funding rates so far, right? As the Fed has cut rates, our funding costs have gone down, just like they have on the RMBS side of the portfolio. Lower SOFR rates also impact the float income that we have generated by the MSR asset as well, which offsets some of that. In general, I would say that we hedge the entire yield curve, right? Changes in rates in one part of the curve or another generally have a very small effect on our portfolio. I'm not fully understanding what you're getting at, so maybe we can follow up more fully later. I hope that answers some of your question.

Jake Katsikas, BTIG, LLC

Yeah, it does definitely. Thank you, guys very much.

Bill Greenberg

Okay. Yeah.

Operator

We do not have any further questions. I would like to turn the call back to Bill Greenberg for closing remarks.

Bill Greenberg

I'd just like to thank everyone for joining us today. Thank you all for your interest in Two Harbors.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.