

PENNYMAC FINANCIAL SERVICES, INC.

Form 10-Q

August 09, 2016

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

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Form 10-Q

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(Mark One)

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

For the quarterly period ended June 30, 2016

Or

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: 001-35916

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PennyMac Financial Services, Inc.

(Exact name of registrant as specified in its charter)

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Delaware	80-0882793
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

3043 Townsgate Road, Westlake Village, California	91361
(Address of principal executive offices)	(Zip Code)

(818) 224-7442

(Registrant's telephone number, including area code)

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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, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting

company” in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the registrant’s classes of common stock, as of the latest practicable date.

Class	Outstanding at August 8, 2016
Class A Common Stock, \$0.0001 par value	22,193,572
Class B Common Stock, \$0.0001 par value	49

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PENNYMAC FINANCIAL SERVICES, INC.

FORM 10-Q

June 30, 2016

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SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (“Report”) contains certain forward looking statements that are subject to various risks and uncertainties. Forward looking statements are generally identifiable by use of forward looking terminology such as “may,” “will,” “should,” “potential,” “intend,” “expect,” “seek,” “anticipate,” “estimate,” “approximately,” “believe,” “predict,” “continue,” “plan” or other similar words or expressions.

Forward looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain financial and operating projections or state other forward looking information. Examples of forward looking statements include the following:

- projections of our revenues, income, earnings per share, capital structure or other financial items;
- descriptions of our plans or objectives for future operations, products or services;
- forecasts of our future economic performance, interest rates, profit margins and our share of future markets; and
- descriptions of assumptions underlying or relating to any of the foregoing expectations regarding the timing of generating any revenues.

Our ability to predict results or the actual effect of future events, actions, plans or strategies is inherently uncertain. Although we believe that the expectations reflected in such forward looking statements are based on reasonable assumptions, our actual results and performance could differ materially from those set forth in the forward looking statements. There are a number of factors, many of which are beyond our control that could cause actual results to differ significantly from management’s expectations. Some of these factors are discussed below.

You should not place undue reliance on any forward looking statement and should consider the following uncertainties and risks, as well as the risks and uncertainties discussed elsewhere in this Report and the section entitled “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the Securities and Exchange Commission (“SEC”) on March 10, 2016.

Factors that could cause actual results to differ materially from historical results or those anticipated include, but are not limited to:

- the continually changing federal, state and local laws and regulations applicable to the highly regulated industry in which we operate;
- lawsuits or governmental actions if we do not comply with the laws and regulations applicable to our businesses;
- the mortgage lending and servicing-related regulations promulgated by the Consumer Financial Protection Bureau (“CFPB”) and its enforcement of these regulations;
- our dependence on U.S. government sponsored entities and changes in their current roles or their guarantees or guidelines;

- changes to government mortgage modification programs;
- the licensing and operational requirements of states and other jurisdictions applicable to our businesses, to which our bank competitors are not subject;
- foreclosure delays and changes in foreclosure practices;
- certain banking regulations that may limit our business activities;
- our dependence on the multi-family and commercial real estate sectors for future originations and investments in commercial mortgage loans and other commercial real estate related loans;
- changes in macroeconomic and U.S. real estate market conditions;
- difficulties inherent in growing loan production volume;
- difficulties inherent in adjusting the size of our operations to reflect changes in business levels;
- purchase opportunities for mortgage servicing rights (“MSRs”) and our success in winning bids;
- changes in prevailing interest rates;

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- increases in loan delinquencies and defaults;
- our reliance on PennyMac Mortgage Investment Trust (“PMT”) as a significant source of financing for, and revenue related to, our mortgage banking business;
- any required additional capital and liquidity to support business growth that may not be available on acceptable terms, if at all;
- our obligation to indemnify third party purchasers or repurchase loans if loans that we originate, acquire, service or assist in the fulfillment of, fail to meet certain criteria or characteristics or under other circumstances;
- our obligation to indemnify PMT and certain investment funds if our services fail to meet certain criteria or characteristics or under other circumstances;
- decreases in the historical returns on the assets that we select and manage for our clients, and our resulting management and incentive fees;
- the extensive amount of regulation applicable to our investment management segment;
- conflicts of interest in allocating our services and investment opportunities among ourselves and certain advised entities;
- the effect of public opinion on our reputation;
- our recent growth;
- our ability to effectively identify, manage, monitor and mitigate financial risks;
- our initiation of new business activities or expansion of existing business activities;
  - our ability to detect misconduct and fraud; and
- our ability to mitigate cybersecurity risks and cyber incidents.

Other factors that could also cause results to differ from our expectations may not be described in this Report or any other document. Each of these factors could by itself, or together with one or more other factors, adversely affect our business, results of operations and/or financial condition.

Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update any forward-looking statement to reflect the impact of circumstances or events that arise after the date the forward-looking statement was made.



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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	June 30, 2016	December 31, 2015
	(in thousands, except share amounts)	
<b>ASSETS</b>		
Cash (includes \$124,026 and \$93,757 pledged to creditors)	\$ 143,715	\$ 105,472
Short-term investments at fair value	41,063	46,319
Mortgage loans held for sale at fair value (includes \$2,071,968 and \$1,079,489 pledged to creditors)	2,097,138	1,101,204
Derivative assets	124,542	50,280
Servicing advances, net (includes \$38,647 and \$33,458 valuation allowance)	296,581	299,354
Carried Interest due from Investment Funds pledged to creditors	70,763	69,926
Investment in PennyMac Mortgage Investment Trust at fair value	1,217	1,145
Mortgage servicing rights (includes \$526,294 and \$660,247 at fair value; \$1,285,700 and \$803,560 pledged to creditors)	1,290,928	1,411,935
Real estate acquired in settlement of loans	1,394	—
Furniture, fixtures, equipment and building improvements, net (includes \$27,240 and \$14,034 pledged to creditors)	27,851	16,311
Capitalized software, net (includes \$986 and \$783 pledged to creditors)	6,209	3,025
Note receivable from PennyMac Mortgage Investment Trust	150,000	150,000
Receivable from PennyMac Mortgage Investment Trust	22,054	18,965
Receivable from Investment Funds	1,288	1,316
Deferred tax asset	4,878	18,378
Mortgage loans eligible for repurchase	286,048	166,070
Other	50,651	45,594
Total assets	\$ 4,616,320	\$ 3,505,294
<b>LIABILITIES</b>		
Assets sold under agreements to repurchase	\$ 1,591,798	\$ 1,166,731
Mortgage loan participation and sale agreement	737,176	234,872
Notes payable	114,235	61,136
Obligations under capital lease	22,886	13,579
Excess servicing spread financing payable to PennyMac Mortgage Investment Trust at fair value	294,551	412,425
Derivative liabilities	3,734	9,083
Accounts payable and accrued expenses	102,310	89,915
Mortgage servicing liabilities at fair value	4,681	1,399

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Payable to Investment Funds	28,209	30,429
Payable to PennyMac Mortgage Investment Trust	160,712	162,379
Payable to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement	74,850	74,315
Liability for mortgage loans eligible for repurchase	286,048	166,070
Liability for losses under representations and warranties	24,277	20,611
Total liabilities	3,445,467	2,442,944

Commitments and contingencies

STOCKHOLDERS' EQUITY

Class A common stock—authorized 200,000,000 shares of \$0.0001 par value; issued and outstanding, 22,189,337 and 21,990,831 shares, respectively	2	2
Class B common stock—authorized 1,000 shares of \$0.0001 par value; issued and outstanding, 50 and 51 shares, respectively	—	—
Additional paid-in capital	176,742	172,354
Retained earnings	118,120	98,470
Total stockholders' equity attributable to PennyMac Financial Services, Inc. common stockholders	294,864	270,826
Noncontrolling interest in Private National Mortgage Acceptance Company, LLC	875,989	791,524
Total stockholders' equity	1,170,853	1,062,350
Total liabilities and stockholders' equity	\$ 4,616,320	\$ 3,505,294

The accompanying notes are an integral part of these consolidated financial statements.

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## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Quarter ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(in thousands, except earnings per share)			
Revenue				
Net gains on mortgage loans held for sale at fair value:				
From non-affiliates	\$ 132,118	\$ 85,411	\$ 225,594	\$ 162,078
Recapture payable to PennyMac Mortgage Investment Trust	(1,915)	(1,456)	(3,867)	(2,745)
Mortgage loan origination fees	130,203	83,955	221,727	159,333
Fulfillment fees from PennyMac Mortgage Investment Trust	28,907	24,421	51,341	41,103
Net mortgage loan servicing fees:				
Mortgage loan servicing fees:				
From non-affiliates	92,770	66,867	184,097	116,968
From PennyMac Mortgage Investment Trust	16,427	12,136	27,880	22,806
From Investment Funds	723	153	1,424	1,121
Ancillary and other fees	10,818	11,850	22,270	23,035
	120,738	91,006	235,671	163,930
Amortization, impairment and change in fair value of mortgage servicing rights	(111,611)	(15,324)	(228,474)	(69,008)
Change in fair value of excess servicing spread payable to PennyMac Mortgage Investment Trust	17,428	(7,133)	36,877	403
	(94,183)	(22,457)	(191,597)	(68,605)
Net mortgage loan servicing fees	26,555	68,549	44,074	95,325
Management fees:				
From PennyMac Mortgage Investment Trust	5,199	5,779	10,551	12,782
From Investment Funds	531	1,184	1,091	2,670
	5,730	6,963	11,642	15,452
Carried Interest from Investment Funds	244	182	837	1,415
Net interest expense:				
Interest income:				
From non-affiliates	18,332	12,651	30,259	21,584
From PennyMac Mortgage Investment Trust	2,222	533	3,824	533
	20,554	13,184	34,083	22,117
Interest expense:				
To non-affiliates	19,753	10,531	33,725	18,608
To PennyMac Mortgage Investment Trust	5,713	5,818	12,728	9,570
	25,466	16,349	46,453	28,178
Net interest expense	(4,912)	(3,165)	(12,370)	(6,061)

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Change in fair value of investment in and dividends received from PennyMac Mortgage Investment Trust	229	(244)	143	(137)
Result of real estate acquired in settlement of loans	393	—	(42)	—
Other	1,346	357	1,809	2,036
Total net revenue	207,806	196,351	351,207	336,665
Expenses				
Compensation	83,147	70,422	151,445	128,566
Servicing	13,430	28,603	34,317	38,338
Technology	7,733	6,490	14,580	11,428
Loan origination	4,910	4,148	9,096	8,499
Professional services	4,559	4,074	8,292	6,907
Other	9,769	7,815	19,080	14,890
Total expenses	123,548	121,552	236,810	208,628
Income before provision for income taxes	84,258	74,799	114,397	128,037
Provision for income taxes	9,963	8,619	13,559	14,733
Net income	74,295	66,180	100,838	113,304
Less: Net income attributable to noncontrolling interest	59,820	53,431	81,188	91,527
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 14,475	\$ 12,749	\$ 19,650	\$ 21,777
Earnings per share				
Basic	\$ 0.66	\$ 0.59	\$ 0.89	\$ 1.01
Diluted	\$ 0.65	\$ 0.59	\$ 0.89	\$ 1.01
Weighted average common shares outstanding				
Basic	22,078	21,700	22,042	21,647
Diluted	76,280	76,105	76,236	76,063

The accompanying notes are an integral part of these consolidated financial statements.

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## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)

	Class A Common Stock				Noncontrolling interest in Private National Mortgage Acceptance Company, LLC	
	Number of shares (in thousands)	Par value	Additional paid-in capital	Retained earnings	Private National Mortgage Acceptance Company, LLC	Total stockholders' equity
Balance at December 31, 2014	21,578	\$ 2	\$ 162,720	\$ 51,242	\$ 593,302	\$ 807,234
Income	—	—	—	21,777	91,527	113,304
Issuance of unit-based compensation	72	—	2,452	—	6,146	8,598
Contributions	—	—	—	—	(9,627)	(9,627)
Repurchase of common stock in payment of directors' fees	8	—	149	—	—	149
Exchange of Class A units of National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	133	—	2,432	—	(2,432)	—
Effect of exchange of Class A units of Private National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	—	—	(217)	—	—	(217)
Balance at June 30, 2015	21,791	\$ 2	\$ 167,536	\$ 73,019	\$ 678,916	\$ 919,491
Balance at December 31, 2015	21,991	\$ 2	\$ 172,354	\$ 98,470	\$ 791,524	\$ 1,062,348
Income	—	—	—	19,650	81,188	100,838
Issuance of unit-based compensation	93	—	2,119	—	5,917	8,036
Repurchase of common stock in payment of directors' fees	12	—	149	—	—	149
Exchange of Class A units of National Mortgage Acceptance Company, LLC to Class A common stock of PennyMac Financial Services, Inc.	93	—	2,640	—	(2,640)	—

Effect of exchange of Class  
of Private National  
ge Acceptance  
ny, LLC to  
A common stock of  
Mac Financial Services,

	—	—	(520)	—	—	(520)
at June 30, 2016	22,189	\$ 2	\$ 176,742	\$ 118,120	\$ 875,989	\$ 1,170

The accompanying notes are an integral part of these consolidated financial statements.

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## PENNYMAC FINANCIAL SERVICES, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six months ended June 30,	
	2016	2015
	(in thousands)	
Cash flow from operating activities		
Net income	\$ 100,838	\$ 113,304
Adjustments to reconcile net income to net cash used in operating activities:		
Net gains on mortgage loans held for sale at fair value	(221,727)	(159,333)
Accrual of servicing rebate payable to Investment Funds	148	1,114
Amortization, impairment and change in fair value of mortgage servicing rights and excess servicing spread	191,597	68,605
Carried Interest from Investment Funds	(837)	(1,415)
Amortization of debt issuance costs and commitment fees relating to financing facilities	5,215	3,631
Capitalization of interest on mortgage loans held for sale at fair value	(13,513)	(4,745)
Accrual of interest on excess servicing spread financing	12,728	9,570
Change in fair value of investment in common shares of PennyMac Mortgage Investment Trust	(72)	275
Results of real estate acquired in settlement in loans	42	—
Stock and unit-based compensation expense	8,036	8,598
Provision for servicing advance losses	12,519	16,013
Depreciation and amortization	2,274	911
Purchase of mortgage loans held for sale from PennyMac Mortgage Investment Trust	(16,783,840)	(13,514,568)
Originations of mortgage loans held for sale	(2,730,709)	(2,052,648)
Purchase of mortgage loans from Ginnie Mae securities and early buyout investors for modification and subsequent sale	(703,464)	(531,842)
Purchase of commercial real estate loans from non-affiliates	(5,912)	—
Sale and principal payments of mortgage loans held for sale	19,176,697	15,619,191
Sale of loans held for sale to PennyMac Mortgage Investment Trust	8,139	10,828
Repurchase of mortgage loans and real estate acquired in settlement of loans subject to representations and warranties	(11,399)	(11,567)
Increase in servicing advances	(11,182)	(32,189)
Increase in receivable from Investment Funds	(120)	(971)
(Increase) decrease in receivable from PennyMac Mortgage Investment Trust	(2,056)	9,175
Decrease in deferred tax asset	13,515	12,826
Payments to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement	—	(4,299)

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Increase in other assets	(10,941)	(14,282)
Increase in accounts payable and accrued expenses	9,781	20,941
Decrease in payable to Investment Funds	(2,220)	(4,653)
(Decrease) increase in payable to PennyMac Mortgage Investment Trust	(2,332)	16,120
Net cash used in operating activities	(958,795)	(421,410)
Cash flow from investing activities		
Decrease (increase) in short-term investments	5,256	(1,890)
Advance on note receivable from PennyMac Mortgage Investment Trust	—	(71,072)
Repayment of note receivable from PennyMac Mortgage Investment Trust	—	18,546
Purchase of mortgage servicing rights	(11)	(270,133)
Net settlement of derivative financial instruments used for hedging	138,801	(8,293)
Purchase of furniture, fixtures, equipment and building improvements	(14,459)	(2,277)
Acquisition of capitalized software	(3,342)	(860)
(Increase) decrease in margin deposits and restricted cash	(16,443)	19,932
Net cash provided by (used in) investing activities	109,802	(316,047)
Cash flow from financing activities		
Sale of assets under agreements to repurchase	18,461,897	14,379,136
Repurchase of assets sold under agreements to repurchase	(18,037,356)	(13,937,711)
Issuance of mortgage loan participation certificates	10,843,858	7,937,026
Repayment of mortgage loan participation certificates	(10,341,436)	(7,884,705)
Advances on notes payable	68,000	129,012
Repayment of notes payable	(15,671)	(29,411)
Issuance of excess servicing spread financing	—	187,287
Repayment of excess servicing spread financing	(38,281)	(31,083)
Repurchase of excess servicing spread financing	(59,045)	—
Advances of obligations under capital lease	12,652	—
Repayment of obligation under capital lease	(3,345)	(5)
Payment of debt issuance costs	(4,037)	(3,990)
Distribution to Private National Mortgage Acceptance Company, LLC members	—	(9,627)
Net cash provided by financing activities	887,236	735,929
Net increase (decrease) in cash	38,243	(1,528)
Cash at beginning of period	105,472	76,256
Cash at end of period	\$ 143,715	\$ 74,728

The accompanying notes are an integral part of these consolidated financial statements.



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PENNYMAC FINANCIAL SERVICES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1—Organization and Basis of Presentation

PennyMac Financial Services, Inc. (“PFSI” or the “Company”) was formed as a Delaware corporation on December 31, 2012. Pursuant to a reorganization, the Company became a holding corporation and its primary asset is an equity interest in Private National Mortgage Acceptance Company, LLC (“PennyMac”). The Company is the managing member of PennyMac and operates and controls all of the businesses and affairs of PennyMac subject to the consent rights of other members under certain circumstances, and consolidates the financial results of PennyMac and its subsidiaries.

PennyMac is a Delaware limited liability company which, through its subsidiaries, engages in mortgage banking and investment management activities. PennyMac’s mortgage banking activities consist of residential mortgage loan production (including correspondent production and consumer direct lending) and mortgage loan servicing. PennyMac’s investment management activities and a portion of its mortgage loan servicing activities are conducted on behalf of investment vehicles that invest in residential mortgage loans and related assets. PennyMac’s primary wholly owned subsidiaries are:

- PNMAC Capital Management, LLC (“PCM”)—a Delaware limited liability company registered with the Securities and Exchange Commission (“SEC”) as an investment adviser under the Investment Advisers Act of 1940, as amended. PCM enters into investment management agreements with entities that invest in residential mortgage loans and related assets.

Presently, PCM has management agreements with PennyMac Mortgage Investment Trust (“PMT”), a publicly held real estate investment trust (“REIT”), PNMAC Mortgage Opportunity Fund, LLC and PNMAC Mortgage Opportunity Fund, L.P., (the “Master Fund”), both registered under the Investment Company Act of 1940, as amended, an affiliate of these registered funds and PNMAC Mortgage Opportunity Fund Investors, LLC (collectively, the “Investment Funds”). Together, the Investment Funds and PMT are referred to as the “Advised Entities.”

- PennyMac Loan Services, LLC (“PLS”)—a Delaware limited liability company that services residential mortgage loans on behalf of non-affiliates and the Advised Entities, purchases and originates new prime credit quality residential mortgage loans, and engages in other mortgage banking activities for its own account and the account of PMT.

PLS is approved as a seller/servicer of mortgage loans by the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Corporation (“Freddie Mac”) and as an issuer of securities guaranteed by the

Government National Mortgage Association (“Ginnie Mae”). PLS is a licensed Federal Housing Administration Nonsupervised Title II Lender with the U.S. Department of Housing and Urban Development (“HUD”) and a lender/servicer with the Veterans Administration (“VA”) and U.S. Department of Agriculture (“USDA”) (each an “Agency” and collectively the “Agencies”).

- PNMAC Opportunity Fund Associates, LLC (“PMOFA”)—a Delaware limited liability company and the general partner of the Master Fund. PMOFA is entitled to incentive fees representing allocations of profits (“Carried Interest”) from the Master Fund.

The accompanying consolidated financial statements have been prepared in compliance with accounting principles generally accepted in the United States (“GAAP”) as codified in the Financial Accounting Standards Board’s (“FASB”) Accounting Standards Codification (“ASC”) for interim financial information and with the SEC’s instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these financial statements and notes do not include all of the information required by GAAP for complete financial statements. The interim consolidated information should be read together with the Company’s Annual Report on Form 10-K for the year ended December 31, 2015.

The accompanying unaudited consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, income, and cash flows for the interim periods, but are not necessarily

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indicative of the results of operations to be anticipated for the full year ending December 31, 2016. Intercompany accounts and transactions have been eliminated.

Preparation of financial statements in compliance with GAAP requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the reporting period. Actual results will likely differ from those estimates.

Note 2—Concentration of Risk

A substantial portion of the Company's activities relate to the Advised Entities. Fees (generally comprised of fulfillment fees, mortgage loan servicing fees, management fees and Carried Interest) and interest charged to these entities totaled 26% and 10% of total net revenue for the quarters ended June 30, 2016 and 2015, respectively, and 28% and 17% for the six months ended June 30, 2016 and 2015, respectively.

Note 3—Transactions with Affiliates

Transactions with PMT

Operating Activities

Mortgage Loan Production Activities

Following is a summary of mortgage lending and sourcing activity between the Company and PMT:

	Quarter ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			
Fulfillment fee revenue	\$ 19,111	\$ 15,333	\$ 32,046	\$ 28,199

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Unpaid principal balance of mortgage loans fulfilled for PMT	\$ 5,174,020	\$ 3,579,078	\$ 8,433,383	\$ 6,469,210
Sourcing fees paid to PMT	\$ 2,824	\$ 2,427	\$ 4,773	\$ 3,848
Unpaid principal balance of mortgage loans purchased from PMT	\$ 9,409,399	\$ 8,082,764	\$ 15,905,121	\$ 12,818,138
Proceeds from sale of mortgage loans held for sale to PMT	\$ 3,424	\$ 2,423	\$ 8,139	\$ 10,828
Tax service fee from PMT	\$ 1,464	\$ 1,113	\$ 2,471	\$ 2,002
Mortgage servicing rights and excess servicing spread recapture incurred	\$ 1,915	\$ 1,456	\$ 3,867	\$ 2,745
Mortgage banking and warehouse service fees paid by PMT	\$ 1	\$ —	\$ 2	\$ —

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## Mortgage Loan Servicing Activities

Following is a summary of mortgage loan servicing fees earned from PMT:

	Quarter ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			
Mortgage loans acquired for sale at fair value:				
Base and supplemental	\$ 79	\$ 42	\$ 135	\$ 68
Activity-based	172	59	287	90
	251	101	422	158
Mortgage loans at fair value:				
Base and supplemental	2,959	4,210	6,359	8,272
Activity-based	8,518	3,093	11,967	5,987
	11,477	7,303	18,326	14,259
Mortgage servicing rights:				
Base and supplemental	4,583	4,627	8,927	8,253
Activity-based	116	105	205	136
	4,699	4,732	9,132	8,389
	\$ 16,427	\$ 12,136	\$ 27,880	\$ 22,806

## Investment Management Activities

The base management fee and the performance incentive fee are both receivable quarterly in arrears. The performance incentive fee may be paid in cash or a combination of cash and PMT's common shares (subject to a limit of no more than 50% paid in common shares), at PMT's option.

Following is a summary of the base management and performance incentive fees earned from PMT:

	Quarter ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			

Base management	\$ 5,199	\$ 5,709	\$ 10,551	\$ 11,439
Performance incentive	—	70	—	1,343
	\$ 5,199	\$ 5,779	\$ 10,551	\$ 12,782

The term of the management agreement, as amended, expires on February 1, 2017, subject to automatic renewal for additional 18 month periods, unless terminated earlier in accordance with the terms of the management agreement.

In the event of termination of the management agreement between PMT and the Company, the Company may be entitled to a termination fee in certain circumstances. The termination fee is equal to three times the sum of (a) the average annual base management fee, and (b) the average annual performance incentive fee earned by the Company, in each case during the 24-month period before termination.

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## Expense Reimbursement

PMT reimburses the Company for other expenses, including common overhead expenses incurred on its behalf by the Company, in accordance with the terms of its management agreement. Such amounts are summarized below:

	Quarter ended June 30,		Six months ended	
	2016	2015	June 30,	2015
	(in thousands)			
Reimbursement of:				
Common overhead incurred by the Company (1)	\$ 2,435	\$ 2,702	\$ 4,996	\$ 5,431
Expenses incurred on (the Company's) PMT's behalf	(169)	83	(114)	462
	\$ 2,266	\$ 2,785	\$ 4,882	\$ 5,893
Payments and settlements during the period (2)	\$ 28,952	\$ 24,114	\$ 56,613	\$ 46,866

- (1) For the quarter ended June 30, 2015, reimbursement of common overhead incurred by the Company included a discretionary waiver, in accordance with the terms of the management agreement, of \$700,000 of overhead expenses otherwise allocable to PMT. On December 15, 2015, the Company and PMT amended their management agreement to provide that the total overhead costs and expenses incurred by the Company in any quarter and reimbursable by PMT is capped at an amount equal to the product of (A) 70 basis points (0.0070), multiplied by (B) PMT's shareholders' equity (as defined in the management agreement) as of the last day of such quarter, divided by four (4).
- (2) Payments and settlements include payments for operating, investment and financing activities itemized in this Note and netting settlements made pursuant to master netting agreements between the Company and PMT.

Amounts due from and payable to PMT are summarized below:

	June 30,	December 31,
	2016	2015
	(in thousands)	
Receivable from PMT:		
Management fees	\$ 5,200	\$ 5,670
Servicing fees	9,154	3,682
Correspondent production fees	2,567	2,729
Fulfillment fees	1,890	1,082
Interest on note receivable	1,042	412
Conditional reimbursement	900	900
Allocated expenses	847	1,043

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Expenses incurred on PMT's behalf	454	3,447
	\$ 22,054	\$ 18,965
Payable to PMT:		
Deposits made by PMT to fund servicing advances	\$ 148,337	\$ 153,573
Mortgage servicing rights ("MSR") recapture payable	605	781
Other	11,770	8,025
	\$ 160,712	\$ 162,379

Conditional Reimbursement of Underwriting Fees

In connection with its initial public offering of common shares on August 4, 2009 ("IPO"), PMT conditionally agreed to reimburse the Company up to \$2.9 million for underwriting fees paid to the IPO underwriters by the Company on PMT's behalf. The Company received reimbursement payments from PMT totaling \$73,000 and \$230,000 for the quarter and six months ended June 30, 2015, respectively, and received no reimbursement from PMT during the six months ended June 30, 2016.



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In the event a termination fee is payable to the Company under the management agreement, and the Company has not received the full amount of the reimbursements and payments under the reimbursement agreement, such amount will be paid in full. The term of the reimbursement agreement expires on February 1, 2019.

## Investing Activities

Following is a summary of investing activities between the Company and PMT:

	Quarter ended June 30, 2016		Six months ended June 30, 2016	
	2015	2015	2015	2015
	(in thousands)			
Note receivable from PennyMac Mortgage Investment Trust:				
Interest income	\$ 2,222	\$ 533	\$ 3,824	\$ 533
Common shares of beneficial interest of PennyMac Mortgage Investment Trust:				
Dividends received from PennyMac Mortgage Investment Trust	\$ 36	\$ 46	\$ 71	\$ 138
Change in fair value of investment in PennyMac Mortgage Investment Trust	193	(290)	72	(275)
	\$ 229	\$ (244)	\$ 143	\$ (137)

	June 30, 2016	December 31, 2015
	(in thousands)	
Note receivable from PennyMac Mortgage Investment Trust:	\$ 150,000	\$ 150,000
Common shares of beneficial interest of PennyMac Mortgage Investment Trust:		
Fair value	\$ 1,217	\$ 1,145
Number of shares	75	75

## Financing Activities

Following is a summary of financing activities between the Company and PMT:

	Quarter ended June 30,		Six months ended	
	2016	2015	June 30,	2015
	(in thousands)			
Excess servicing spread financing:				
Issuance:				
Cash	\$ —	\$ 140,875	\$ —	\$ 187,287
Pursuant to recapture agreement	\$ 1,690	\$ 1,319	\$ 3,601	\$ 2,565
Repayment	\$ (17,400)	\$ (18,352)	\$ (38,281)	\$ (31,083)
Repurchase	\$ —	\$ —	\$ (59,045)	\$ —
Change in fair value	\$ (17,428)	\$ (7,133)	\$ (36,877)	\$ 403
Interest expense	\$ 5,713	\$ 5,818	\$ 12,728	\$ 9,570
Excess servicing spread recapture incurred pursuant to refinancings by the Company of mortgage loans subject to excess servicing spread	\$ 1,604	\$ 1,456	\$ 3,426	\$ 2,745

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## Investment Funds

Amounts due from and payable to the Investment Funds are summarized below:

	June 30, 2016	December 31, 2015
	(in thousands)	
Carried Interest due from Investment Funds:		
PNMAC Mortgage Opportunity Fund, LLC	\$ 42,430	\$ 41,893
PNMAC Mortgage Opportunity Fund Investors, LLC	28,333	28,033
	\$ 70,763	\$ 69,926
Receivable from Investment Funds:		
Management fees	\$ 455	\$ 655
Expense reimbursements	359	45
Mortgage loan servicing fees	247	392
Mortgage loan servicing rebate	227	224
	\$ 1,288	\$ 1,316
Payable to Investment Funds—Servicing advances	\$ 28,209	\$ 30,429

## Exchanged Private National Mortgage Acceptance Company, LLC Unitholders

The Company entered into a tax receivable agreement with PennyMac's existing unitholders on the date of the IPO that will provide for the payment by the Company to PennyMac's exchanged unitholders an amount equal to 85% of the amount of the benefits, if any, that the Company is deemed to realize as a result of (i) increases in tax basis of PennyMac's assets resulting from such unitholders' exchanges and (ii) certain other tax benefits related to entering into the tax receivable agreement, including tax benefits attributable to payments under the tax receivable agreement. Based on the PennyMac unitholder exchanges to date, the Company has recorded a \$74.9 million and \$74.3 million Payable to exchanged Private National Mortgage Acceptance Company, LLC unitholders under tax receivable agreement as of June 30, 2016 and December 31, 2015, respectively. The Company made payments under the tax receivable agreement totaling \$0 and \$4.3 million during the quarter and six months ended June 30, 2015, respectively. There were no payments made during the six months ended June 30, 2016.

## Note 4—Earnings Per Share of Common Stock

Basic earnings per share of common stock is determined using net income attributable to the Company's common stockholders divided by the weighted average number of shares of common stock outstanding during the period.

Diluted earnings per share of common stock is determined by dividing diluted net income attributable to the Company's common stockholders by the weighted average number of shares of common stock outstanding, assuming all potentially dilutive shares of common stock were issued.

Potentially dilutive shares of common stock include non-vested unit and stock-based compensation awards and PennyMac Class A units. The Company applies the treasury stock method to determine the diluted weighted average shares of common stock outstanding represented by the non-vested unit and stock-based compensation awards. The diluted earnings per share calculation assumes the exchange of PennyMac Class A units for shares of common stock. Accordingly, earnings attributable to the Company's common stockholders is also adjusted to include the earnings allocated to the PennyMac Class A units after taking into account the income taxes that would be applicable to the shares of common stock assumed to be exchanged.

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The following table summarizes the basic and diluted earnings per share calculations:

	Quarter ended		Six months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
	(in thousands, except per share amounts)			
Basic earnings per share of common stock:				
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 14,475	\$ 12,749	\$ 19,650	\$ 21,777
Weighted average shares of common stock outstanding	22,078	21,700	22,042	21,647
Basic earnings per share of common stock	\$ 0.66	\$ 0.59	\$ 0.89	\$ 1.01
Diluted earnings per share of common stock:				
Net income attributable to PennyMac Financial Services, Inc. common stockholders	\$ 14,475	\$ 12,749	\$ 19,650	\$ 21,777
Effect of net income attributable to PennyMac Class A units exchangeable to common stock, net of income taxes	35,433	31,925	48,040	54,688
Diluted net income attributable to common stockholders	\$ 49,908	\$ 44,674	\$ 67,690	\$ 76,465
Weighted average shares of common stock outstanding	22,078	21,700	22,042	21,647
Dilutive shares:				
PennyMac Class A units exchangeable to common stock	54,021	53,620	54,032	53,592
Non-vested PennyMac Class A units issuable under unit-based stock compensation plan and exchangeable to common stock	—	650	—	714
Common shares issuable under stock-based compensation plan	181	135	162	110
Diluted weighted average shares of common stock outstanding	76,280	76,105	76,236	76,063
Diluted earnings per share of common stock	\$ 0.65	\$ 0.59	\$ 0.89	\$ 1.01

Potentially dilutive securities are excluded from the calculation of diluted earnings per share when their inclusion would be anti-dilutive. The following table summarizes the anti-dilutive weighted-average number of outstanding stock options and performance-based restricted stock units (“RSUs”) excluded from the calculation of diluted earnings per share:

	Quarter ended		Six months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
	(in thousands except for weighted-average exercise price)			
Stock options (1)	2,795	1,875	2,450	1,635

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Performance-based RSUs (2)	2,684	2,389	2,512	2,126
Total anti-dilutive stock-based compensation units	5,479	4,264	4,962	3,761
Weighted-average exercise price of anti-dilutive stock options (1)	\$ 15.81	\$ 18.17	\$ 15.81	\$ 18.17

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- (1) Certain stock options were outstanding but not included in the computation of diluted earnings per share because the weighted-average exercise prices were anti-dilutive.
- (2) Certain performance-based RSUs were outstanding but not included in the computation of diluted earnings per share due to performance thresholds not being achieved.

Note 5—Loan Sales and Servicing Activities

The Company originates or purchases and sells mortgage loans in the secondary mortgage market without recourse for credit losses. However, the Company maintains continuing involvement with the mortgage loans sold in the form of servicing arrangements and the liability under representations and warranties it makes to purchasers and insurers of the mortgage loans sold.

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The following table summarizes cash flows between the Company and transferees as a result of the sale of mortgage loans in transactions where the Company maintains continuing involvement with the mortgage loans:

	Quarter ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			
Cash flows:				
Sales proceeds	\$ 11,234,497	\$ 9,853,346	\$ 19,176,697	\$ 15,619,191
Servicing fees received (1)	\$ 60,623	\$ 35,317	\$ 119,103	\$ 69,312
Net servicing advances	\$ (1,264)	\$ (5,248)	\$ (9,545)	\$ (8,955)

(1) Net of guarantee fees paid to the Agencies.

	June 30, 2016 (in thousands)	December 31, 2015
Unpaid principal balance of mortgage loans outstanding at end of period	\$ 71,436,178	\$ 60,687,246
Delinquencies:		
30-89 days	\$ 1,796,640	\$ 1,539,568
90 days or more:		
Not in foreclosure	\$ 434,899	\$ 340,313
In foreclosure or bankruptcy	\$ 347,221	\$ 227,025
Foreclosed	\$ 2,630	\$ 755

The unpaid principal balance (“UPB”) of the Company’s mortgage loan servicing portfolio is summarized as follows:

	June 30, 2016		
	Servicing rights owned (in thousands)	Contract servicing and subservicing	Total mortgage loans serviced
Investor:			
Non-affiliated entities	\$ 117,787,996	\$ —	\$ 117,787,996
Affiliated entities	—	51,958,636	51,958,636
Mortgage loans held for sale	1,971,903	—	1,971,903

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	\$ 119,759,899	\$ 51,958,636	\$ 171,718,535
Amount subserviced for the Company (1)	\$ 12,375	\$ —	\$ 12,375
Delinquent mortgage loans:			
30 days	\$ 2,621,050	\$ 324,346	\$ 2,945,396
60 days	788,609	117,638	906,247
90 days or more:			
Not in foreclosure	1,340,898	640,677	1,981,575
In foreclosure or bankruptcy	638,916	910,346	1,549,262
Foreclosed	24,855	493,441	518,296
	\$ 5,414,328	\$ 2,486,448	\$ 7,900,776
Custodial funds managed by the Company (2)	\$ 3,163,812	\$ 804,003	\$ 3,967,815

- 
- (1) Certain of the mortgage loans serviced by the Company are subserviced on the Company's behalf by other mortgage loan servicers. Mortgage loans are subserviced for the Company on a transitional basis when the Company has obtained the rights to service the mortgage loans but servicing of the loans has not yet transferred to the Company's servicing system.
- (2) Borrower and investor custodial cash accounts relate to mortgage loans serviced under the servicing agreements and are not recorded on the Company's consolidated balance sheets. The Company earns placement fees on certain of



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the custodial funds it manages on behalf of the mortgage loans' investors, which is included in Interest income in the Company's consolidated statements of income.

	December 31, 2015		
	Servicing rights owned (in thousands)	Contract servicing and subservicing	Total mortgage loans serviced
Investor:			
Non-affiliated entities	\$ 111,409,601	\$ —	\$ 111,409,601
Affiliated entities	—	47,810,632	47,810,632
Mortgage loans held for sale	1,052,485	—	1,052,485
	\$ 112,462,086	\$ 47,810,632	\$ 160,272,718
Amount subserviced for the Company (1)	\$ 14,454	\$ —	\$ 14,454
Delinquent mortgage loans:			
30 days	\$ 2,666,435	\$ 349,859	\$ 3,016,294
60 days	834,617	136,924	971,541
90 days or more:			
Not in foreclosure	1,270,236	788,410	2,058,646
In foreclosure or bankruptcy	656,617	1,180,014	1,836,631
Foreclosed	23,372	542,031	565,403
	\$ 5,451,277	\$ 2,997,238	\$ 8,448,515
Custodial funds managed by the Company (2)	\$ 2,242,146	\$ 502,751	\$ 2,744,897

- (1) Certain of the mortgage loans serviced by the Company are subserviced on the Company's behalf by other mortgage loan servicers. Mortgage loans are subserviced for the Company on a transitional basis when the Company has obtained the rights to service the loans but servicing of the loans has not yet been transferred to the Company's servicing system.
- (2) Borrower and investor custodial cash accounts relate to mortgage loans serviced under the servicing agreements and are not recorded on the Company's consolidated balance sheets. The Company earns placement fees on custodial funds it manages on behalf of the mortgage loans' investors, which is included in Interest income in the Company's consolidated statements of income.

Following is a summary of the geographical distribution of mortgage loans included in the Company's servicing portfolio for the top five and all other states as measured by UPB:

State	June 30, 2016 (in thousands)	December 31, 2015
-------	------------------------------------	----------------------

California	\$ 40,010,729	\$ 39,007,363
Texas	13,679,577	12,191,722
Virginia	11,194,022	9,816,114
Florida	10,897,536	9,709,940
Maryland	7,090,073	6,151,945
All other states	88,846,598	83,395,634
	\$ 171,718,535	\$ 160,272,718

#### Note 6—Netting of Financial Instruments

The Company uses derivative financial instruments to manage exposure to interest rate risk for the interest rate lock commitments (“IRLCs”) it makes to purchase or originate mortgage loans at specified interest rates, its inventory of mortgage loans held for sale and MSRs. The Company has elected to present net derivative asset and liability positions, and cash collateral obtained from (or posted to) its counterparties when subject to a master netting arrangement that is legally enforceable on all counterparties in the event of default. The derivatives that are not subject to a master netting arrangement are IRLCs.

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## Offsetting of Derivative Assets

Following are summaries of derivative assets and related netting amounts.

	June 30, 2016			December 31, 2015		
	Gross amount of recognized assets (in thousands)	Gross amount offset in the consolidated balance sheet	Net amount of assets in the consolidated balance sheet	Gross amount of recognized assets	Gross amount offset in the consolidated balance sheet	Net amount of assets in the consolidated balance sheet
Derivatives not subject to a master netting arrangement - IRLCs	\$ 91,607	\$ —	\$ 91,607	\$ 45,885	\$ —	\$ 45,885
Derivatives subject to a master netting arrangement:						
Forward purchase contracts	125,358	—	125,358	4,181	—	4,181
Forward sale contracts	664	—	664	4,965	—	4,965
Mortgage-backed security ("MBS") put options	1,777	—	1,777	404	—	404
Put options on interest rate futures purchase contracts	1,618	—	1,618	1,832	—	1,832
Call options on interest rate futures purchase contracts	8,279	—	8,279	1,555	—	1,555
Netting	—	(104,761)	(104,761)	—	(8,542)	(8,542)
	137,696	(104,761)	32,935	12,937	(8,542)	4,395
	\$ 229,303	\$ (104,761)	\$ 124,542	\$ 58,822	\$ (8,542)	\$ 50,280

Derivative Assets, Financial Assets, and Collateral Held by Counterparty

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The following table summarizes by significant counterparty the amount of derivative asset positions after considering master netting arrangements and financial instruments or cash pledged that do not qualify for set off accounting.

	June 30, 2016				December 31, 2015			
	Gross amount not offset in the consolidated balance sheet			Net amount of assets in the consolidated balance sheet (in thousands)	Gross amount not offset in the consolidated balance sheet			Net amount of assets in the consolidated balance sheet (in thousands)
	Net amount of assets in the consolidated balance sheet (in thousands)	Cash collateral instruments	Cash received		Net amount of assets in the consolidated balance sheet (in thousands)	Cash collateral instruments	Cash received	
Interest rate lock commitments	\$ 91,607	\$ —	\$ —	\$ 91,607	\$ 45,885	\$ —	\$ —	\$ 45,885
Fannie Mae	10,279	—	—	10,279	453	—	—	453
Barclays Capital	7,483	—	—	7,483	72	—	—	72
RJ O'Brien	7,341	—	—	7,341	2,246	—	—	2,246
Bank of America, N.A.	4,141	—	—	4,141	—	—	—	—
JP Morgan	2,661	—	—	2,661	—	—	—	—
Morgan Stanley Bank, N.A.	383	—	—	383	—	—	—	—
Wells Fargo Bank, N.A.	370	—	—	370	53	—	—	53
Goldman Sachs	125	—	—	125	471	—	—	471
Jefferies & Co.	—	—	—	—	888	—	—	888
Others	152	—	—	152	212	—	—	212
	\$ 124,542	\$ —	\$ —	\$ 124,542	\$ 50,280	\$ —	\$ —	\$ 50,280

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## Offsetting of Derivative Liabilities and Financial Liabilities

Following is a summary of net derivative liabilities and assets sold under agreements to repurchase and related netting amounts. As discussed above, all derivatives with the exception of IRLCs are subject to master netting arrangements. The mortgage loans sold under agreements to repurchase do not qualify for set off accounting.

	June 30, 2016		Net amount of liabilities in the consolidated balance sheet	December 31, 2015		Net amount of liabilities in the consolidated balance sheet
	Gross amount of recognized liabilities (in thousands)	Gross amount offset in the consolidated balance sheet		Gross amount of recognized liabilities	Gross amount offset in the consolidated balance sheet	
Derivatives not subject to a master netting arrangement - IRLCs	\$ 1,345	\$ —	\$ 1,345	\$ 2,112	\$ —	\$ 2,112
Derivatives subject to a master netting arrangement:						
Forward purchase contracts	119	—	119	9,004	—	9,004
Forward sale contracts	101,772	—	101,772	7,497	—	7,497
Put options on interest rate futures purchase contracts	2,070	—	2,070	203	—	203
Call options on interest rate futures purchase contracts	234	—	234	47	—	47
Netting	—	(101,806)	(101,806)	—	(9,780)	(9,780)
	104,195	(101,806)	2,389	16,751	(9,780)	6,971
	105,540	(101,806)	3,734	18,863	(9,780)	9,083

Total derivatives						
Mortgage loans sold under agreements to repurchase:						
Amount outstanding	1,591,947	—	1,591,947	1,167,405	—	1,167,405
Unamortized debt issuance costs	(149)	—	(149)	(674)	—	(674)
	1,591,798	—	1,591,798	1,166,731	—	1,166,731
	\$ 1,697,338	\$ (101,806)	\$ 1,595,532	\$ 1,185,594	\$ (9,780)	\$ 1,175,814

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## Derivative Liabilities, Financial Liabilities, and Collateral Held by Counterparty

The following table summarizes by significant counterparty the amount of derivative liabilities and assets sold under agreements to repurchase after considering master netting arrangements and financial instruments or cash pledged that do not qualify under the accounting guidance for netting. All assets sold under agreements to repurchase are secured by sufficient collateral or have fair value that exceeds the liability amount recorded on the consolidated balance sheets.

	June 30, 2016			December 31, 2015				
	Net amount of liabilities in the consolidated balance sheet (in thousands)	Gross amounts not offset in the consolidated balance sheet Financial instruments	Cash collateral pledged	Net amount of liabilities in the consolidated balance sheet	Net amount of liabilities in the consolidated balance sheet	Gross amounts not offset in the consolidated balance sheet Financial instruments	Cash collateral pledged	Net amount of liabilities in the consolidated balance sheet
Interest rate lock commitments	\$ 1,345	\$ —	\$ —	\$ 1,345	\$ 2,112	\$ —	\$ —	\$ 2,112
Bank of America, N.A.	372,742	(372,742)	—	—	271,130	(269,510)	—	1,620
Credit Suisse	856,725	(855,962)	—	763	795,179	(794,470)	—	709
First Boston Mortgage Capital LLC	168,200	(168,200)	—	—	49,763	(49,521)	—	242
Morgan Stanley Bank, N.A.	157,201	(157,201)	—	—	55,948	(53,904)	—	2,044
Citibank, N.A.	37,842	(37,842)	—	—	—	—	—	—
Barclays	330	—	—	330	—	—	—	—
Capital Nomura	271	—	—	271	—	—	—	—
Raymond James & Associates	195	—	—	195	—	—	—	—
Cantor Fitzgerald LP	497	—	—	497	135	—	—	135
Bank of Oklahoma	—	—	—	—	154	—	—	154

Bank of New York Mellon								
JP Morgan	—	—	—	—	672	—	—	672
BNP Paribas	—	—	—	—	738	—	—	738
Others	333	—	—	333	657	—	—	657
Unamortized debt issuance costs	(149)	149	—	—	(674)	674	—	—
	\$ 1,595,532	\$ (1,591,798)	\$ —	\$ 3,734	\$ 1,175,814	\$ (1,166,731)	\$ —	\$ 9,083

#### Note 7—Fair Value

The Company's consolidated financial statements include assets and liabilities that are measured based on their fair values. The application of fair value may be on a recurring or nonrecurring basis depending on the accounting principles applicable to the specific asset or liability and whether management has elected to carry the item at its fair value as discussed in the following paragraphs.

The Company groups its assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the observability of the inputs used to determine fair value. These levels are:

- Level 1—Quoted prices in active markets for identical assets or liabilities.
- Level 2—Prices determined or determinable using other significant observable inputs. Observable inputs are inputs that other market participants would use in pricing an asset or liability and are developed based on market data obtained from sources independent of the Company. These may include quoted prices for similar assets and liabilities, interest rates, prepayment speeds, credit risk and other inputs.
- Level 3—Prices determined using significant unobservable inputs. In situations where observable inputs are unavailable (for example, when there is little or no market activity for an asset or liability at the end of the period), unobservable inputs may be used. Unobservable inputs reflect the Company's own judgments about the factors that market participants use in pricing an asset or liability, and are based on the best information available in the circumstances.



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As a result of the difficulty in observing certain significant valuation inputs affecting “Level 3” fair value assets and liabilities, the Company is required to make judgments regarding these items’ fair values. Different persons in possession of the same facts may reasonably arrive at different conclusions as to the inputs to be applied in valuing these assets and liabilities and their fair values. Likewise, due to the general illiquidity of some of these assets and liabilities, subsequent transactions may be at values significantly different from those reported.

## Fair Value Accounting Elections

Management identified all of its non-cash financial assets, its originated MSR’s relating to loans with initial interest rates of more than 4.5%, purchased MSR’s subject to excess servicing spread financing (“ESS”) and mortgage servicing liabilities (“MSLs”) to be accounted for at fair value so changes in fair value will be reflected in income as they occur and more timely reflect the results of the Company’s performance. Management has also elected to account for its ESS at fair value as a means of hedging the related MSR’s fair value risk.

## Financial Statement Items Measured at Fair Value on a Recurring Basis

Following is a summary of financial statement items that are measured at fair value on a recurring basis:

	June 30, 2016			Total
	Level 1 (in thousands)	Level 2	Level 3	
Assets:				
Short-term investments	\$ 41,063	\$ —	\$ —	\$ 41,063
Mortgage loans held for sale at fair value	—	2,059,059	38,079	2,097,138
Derivative assets:				
Interest rate lock commitments	—	—	91,607	91,607
Forward purchase contracts	—	125,358	—	125,358
Forward sales contracts	—	664	—	664
MBS put options	—	1,777	—	1,777
Put options on interest rate futures purchase contracts	1,618	—	—	1,618
Call options on interest rate futures purchase contracts	8,279	—	—	8,279
Total derivative assets before netting	9,897	127,799	91,607	229,303
Netting	—	—	—	(104,761)
Total derivative assets	9,897	127,799	91,607	124,542
Investment in PennyMac Mortgage Investment Trust	1,217	—	—	1,217
Mortgage servicing rights at fair value	—	—	526,294	526,294
	\$ 52,177	\$ 2,186,858	\$ 655,980	\$ 2,790,254

Liabilities:

Excess servicing spread financing at fair value payable to PennyMac Mortgage Investment Trust	\$ —	\$ —	\$ 294,551	\$ 294,551
Derivative liabilities:				
Interest rate lock commitments	—	—	1,345	1,345
Forward purchase contracts	—	119	—	119
Forward sales contracts	—	101,772	—	101,772
Put options on interest rate futures purchase contracts	2,070	—	—	2,070
Call options on interest rate futures purchase contracts	234	—	—	234
Total derivative liabilities before netting	2,304	101,891	1,345	105,540
Netting	—	—	—	(101,806)
Total derivative liabilities	2,304	101,891	1,345	3,734
Mortgage servicing liabilities	—	—	4,681	4,681
	\$ 2,304	\$ 101,891	\$ 300,577	\$ 302,966

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	December 31, 2015			Total
	Level 1 (in thousands)	Level 2	Level 3	
Assets:				
Short-term investments	\$ 46,319	\$ —	\$ —	\$ 46,319
Mortgage loans held for sale at fair value	—	1,052,673	48,531	1,101,204
Derivative assets:				