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Sound Strategy. Unique Advantages.

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## First Quarter Earnings Presentation

*May 7, 2014*

# Safe Harbor Statement

## NOTE:

This presentation contains certain statements that are not historical facts and that constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Statements in this presentation addressing expectations, assumptions, beliefs, projections, future plans, strategies, and events, developments that we expect or anticipate will occur in the future, and future operating results or financial condition are forward-looking statements. Forward-looking statements in this presentation may include, but are not limited to statements about projected future investment strategies, investment opportunities, financial performance, dividends, leverage ratios, capital raising activities, share issuances and repurchases, the use or impact of NOL carryforwards, and interest rates. The words “will,” “believe,” “expect,” “forecast,” “anticipate,” “intend,” “estimate,” “assume,” “project,” “plan,” “continue,” and similar expressions also identify forward-looking statements. These forward-looking statements reflect our current beliefs, assumptions and expectations based on information currently available to us, and are applicable only as of the date of this presentation. Forward-looking statements are inherently subject to risks, uncertainties, and other factors, some of which cannot be predicted or quantified and any of which could cause the Company’s actual results and timing of certain events to differ materially from those projected in or contemplated by these forward-looking statements. Not all of these risks, uncertainties and other factors are known to us. New risks and uncertainties arise over time, and it is not possible to predict those risks or uncertainties or how they may affect us. The projections, assumptions, expectations or beliefs upon which the forward-looking statements are based can also change as a result of these risks and uncertainties or other factors. If such a risk, uncertainty, or other factor materializes in future periods, our business, financial condition, liquidity and results of operations may differ materially from those expressed or implied in our forward-looking statements.

While it is not possible to identify all factors, some of the factors that may cause actual results to differ from historical results or from any results expressed or implied by our forward-looking statements, or that may cause our projections, assumptions, expectations or beliefs to change, include the risks and uncertainties referenced in our Annual Report on Form 10-K for the year ended December 31, 2013 and subsequent filings with the Securities and Exchange Commission, particularly those set forth under the caption “Risk Factors”.



## 1Q 2014 PERFORMANCE



# First Quarter 2014 Highlights

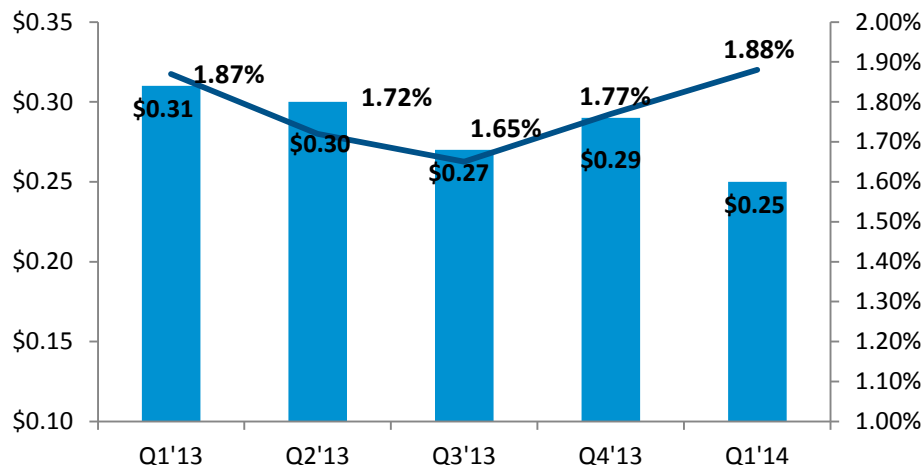
- GAAP net loss of \$0.06 per common share and a return on common equity of (2.5)%, reflecting change in fair value of derivatives over the quarter
- Core net operating income<sup>(1)</sup> of \$0.25 and an adjusted return on common equity<sup>(1)</sup> of 11.3%
- Common dividend declared of \$0.25 per share, for an annualized 11.7% yield based on \$8.54 closing stock price on May 6, 2014
- GAAP net interest spread of 1.87% and adjusted net interest spread<sup>(1)</sup> of 1.88%
- Increase in book value per common share of 2.1% to \$8.87 from \$8.69 at December 31, 2013
- Decline during the quarter in overall leverage to 5.9x from 6.2x
- Continued decline in portfolio CPR to 10.3% from 11.7% in the fourth quarter of 2013

*(1) Non-GAAP measures. See reconciliations on slides 33 and 34.*



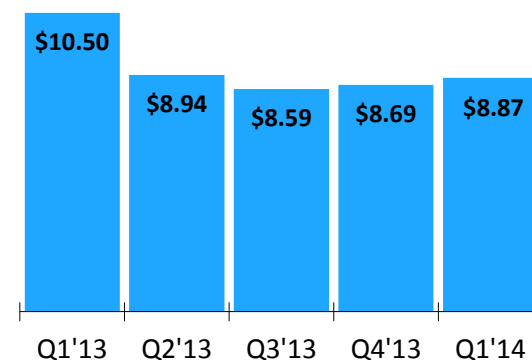
# Key Financial Metrics

Core Net Operating Income per Common Share and Adjusted Net Interest Spread <sup>(1)</sup>



- Core net operating income per share for the first quarter was \$0.25 equal to the dividend of \$0.25 per share
- Investment portfolio purchases and repositioning on both investments and funding/hedging contributed to wider net interest spread in the quarter

Book Value per Common Share



- Book value per common share increased \$0.18 in the first quarter as spreads tightened on investments and interest rates declined.

(1) Non-GAAP measures. See reconciliation on slides 33 and 34.

## OUTLOOK AND STRATEGY





# Macroeconomic and Policy factors

- Macroeconomic environment remains complex
- The US economic growth trajectory is still uncertain and forecasting economic performance is difficult given structural and demographic shifts
  - Weather impact in 1Q14 highlights vulnerability of economy to exogenous shocks
- Global geopolitical situations exacerbate risk environment
- Global inflation levels could become a surprise factor
- Excess liquidity from global monetary policy is unprecedented and has led to asset value distortions. Foreign central bank action plans remain uncertain and could cause unexpected results
- Regulatory policy: housing finance and banking sector reform
  - Uncertain, restrictive and changing rapidly
  - Application of supplemental leverage ratio may impact repo markets in 2014
- Fiscal Policy
  - Fall elections could lead to a surprise
- Bond market psychology is extremely bearish
  - Technical indicators show investors most short since 2010
- Interest rates have been range bound, but we are still vulnerable to exogenous shocks that could increase volatility



# Investment Environment

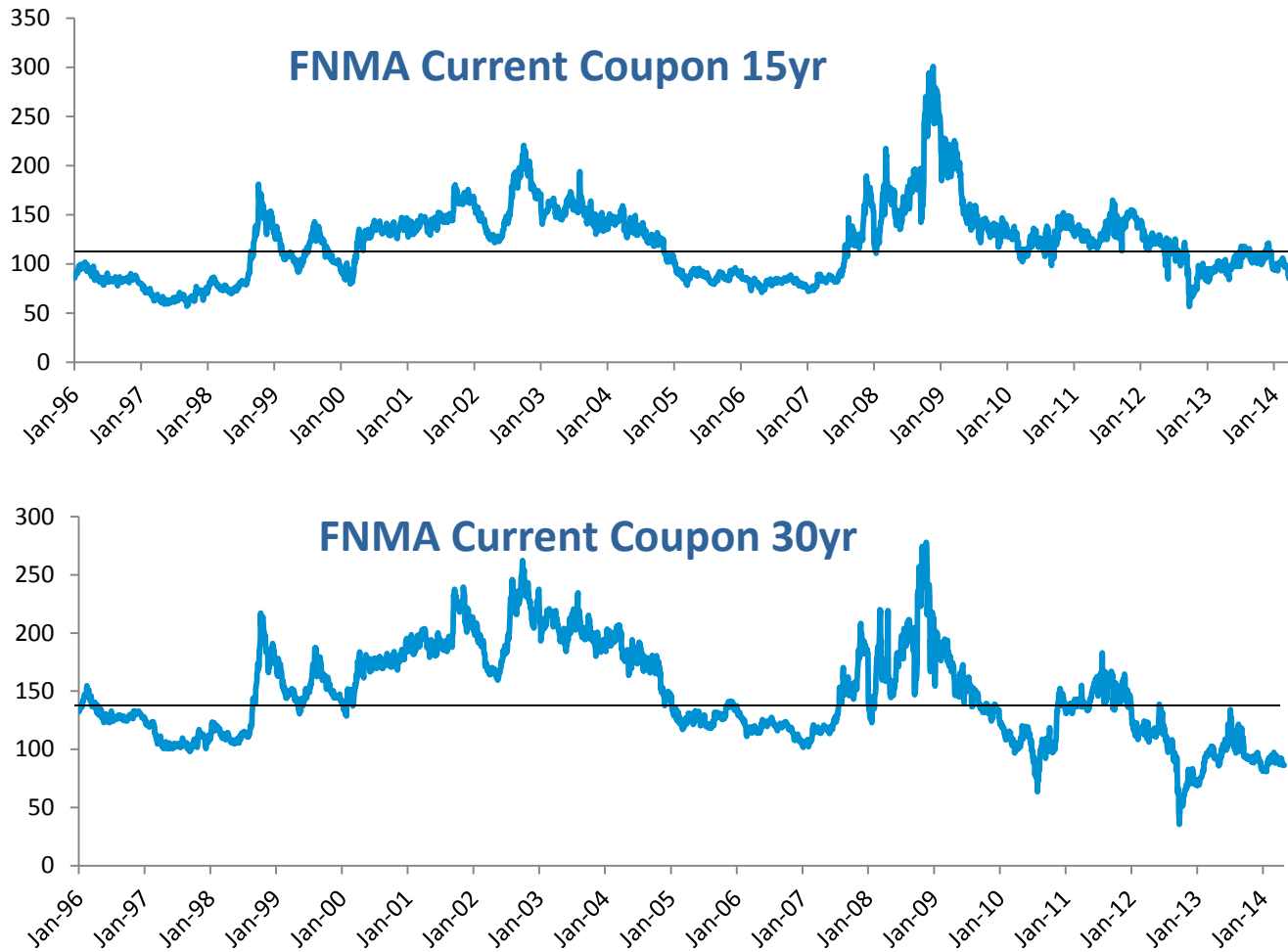
- Market Fundamentals:
  - Risk premiums have declined as cash seeks to find higher returns – spreads significantly tighter across many risk assets
    - Higher degree of vigilance and discipline required in this environment
    - Vulnerability to exogenous shocks
  - Commercial real estate fundamentals are solid, especially in the multifamily sector
    - Rents, vacancies and property price appreciation remain on a positive trajectory
  - Homeownership rates continue to decline, higher mortgage rates are impacting refinancing and purchase activity, resulting in slower prepayment speeds
  - Funding costs have declined, reflecting balance sheet capacity and scarcity of high quality collateral
  - GSE reform remains uncertain and no stand alone credit markets exist to replace GSEs
- Market Technicals: Prices have been distorted by global central bank participation in the capital markets and the Fed's exit is a key factor
  - Global reach for yield has substantially reduced risk adjusted returns across major asset classes
  - Residential mortgage production is dramatically lower than the market anticipated; net supply likely to be lower longer than expected, which reinforces tighter spread environment
  - Competition in commercial real estate originations is strong – underwriting standards loosening, conduit CMBS and agency multifamily supply lower than expected, spreads tighter
- Market Psychology
  - Data driven Fed means psychology will move with data, resulting in unexpected spikes in volatility
  - Bond market participants have been extremely bearish in 2014 and the market is net short





# Investment Environment

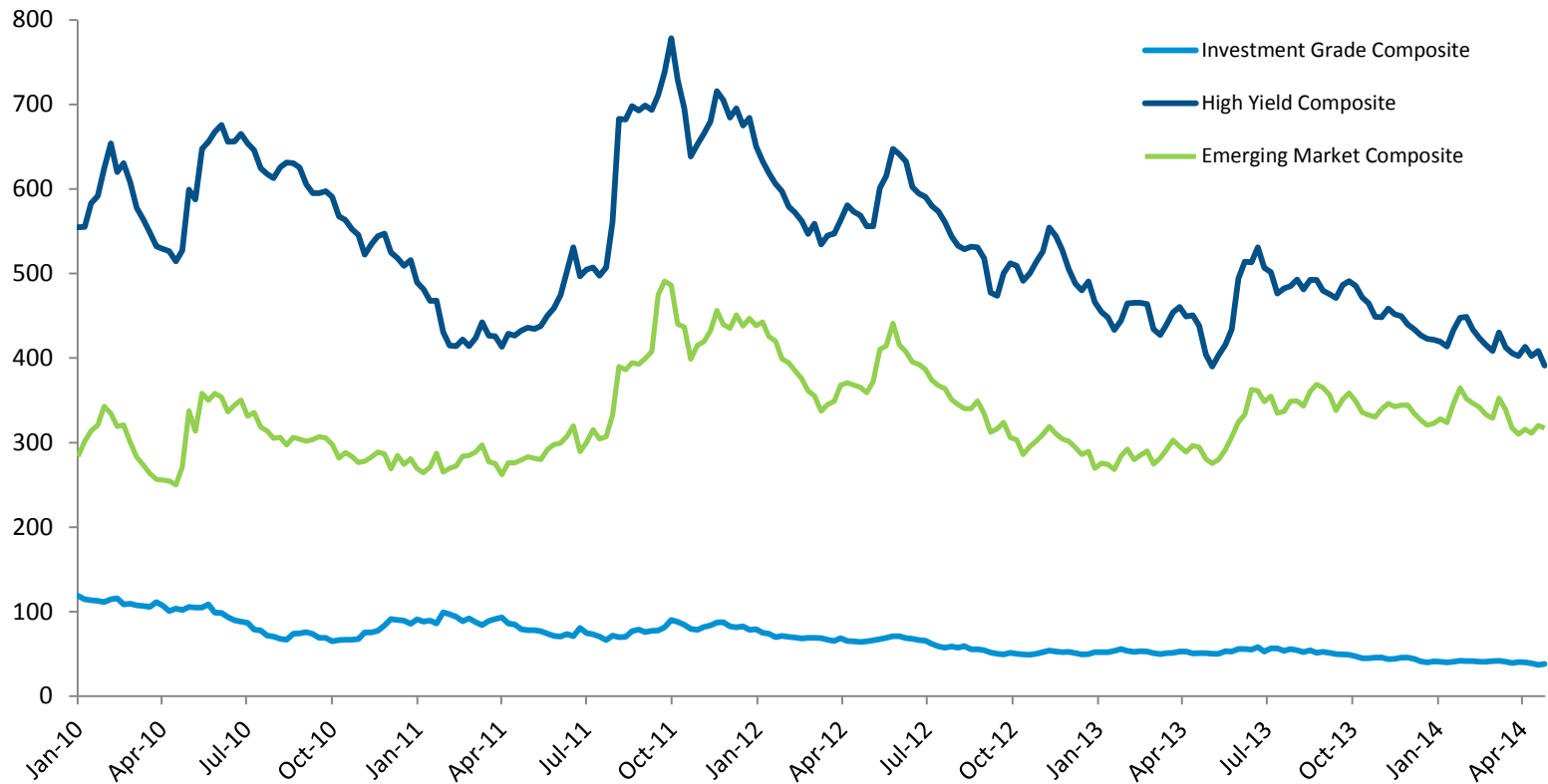
Mortgage Nominal Spreads to Treasuries (*in basis points*)



Source: JP Morgan and Company data

# Investment Environment

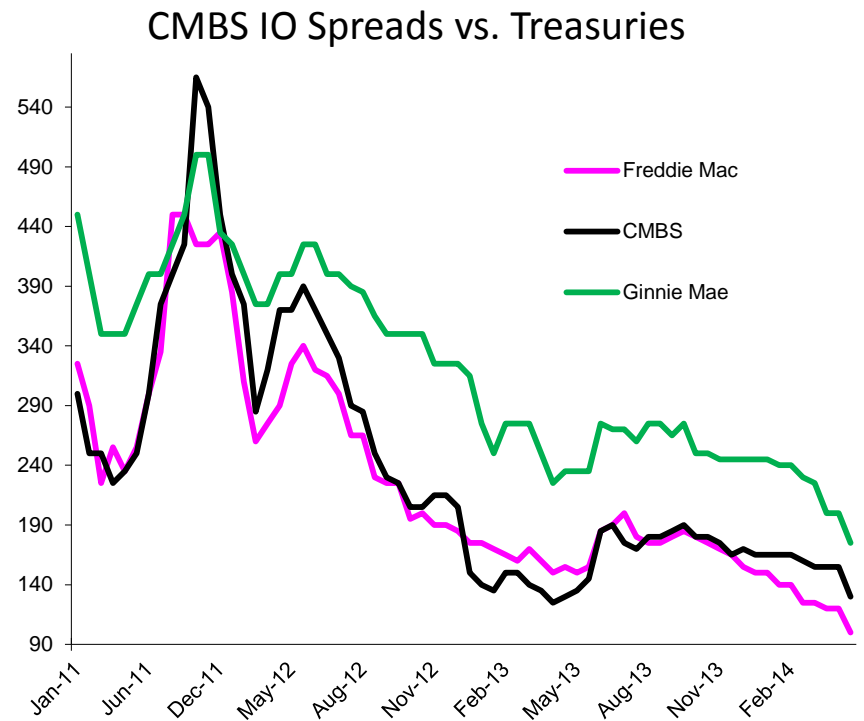
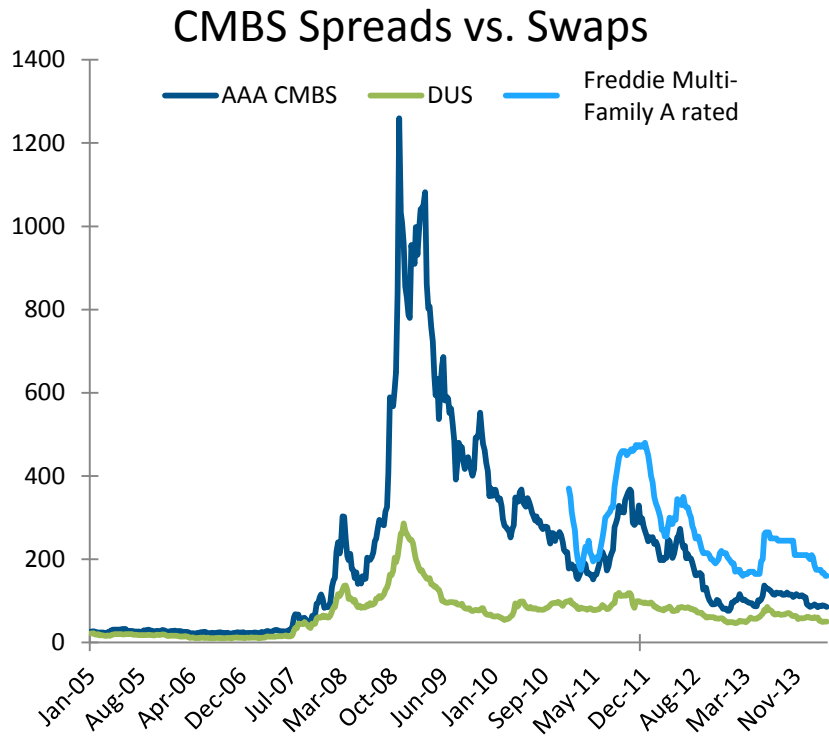
Non-Mortgage Spreads to Treasuries (*in basis points*)



Source: Bloomberg Composite Indexes

# Investment Environment

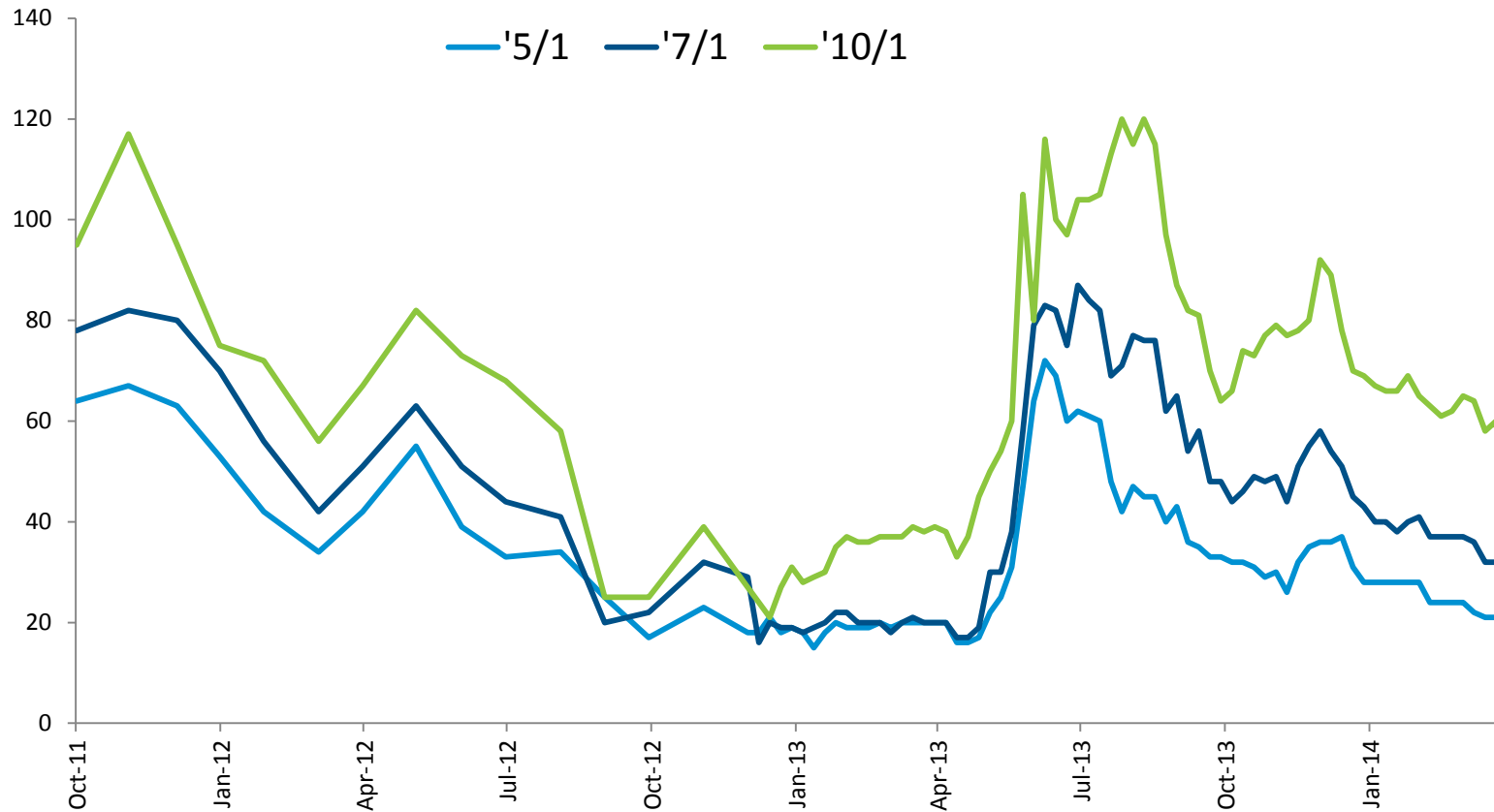
## CMBS Spreads (in basis points)



Source: Company Data

# Investment Environment

Generic Discount Hybrid ARM Zero-Volatility Spreads *(in basis points)*



Source: Company Data



# Implications for Dynex Strategy

- The decline in risk premiums across asset classes, when viewed against the backdrop of macro and market factors, requires a higher level of discipline and caution. Our leverage as of 12/31/2013 of 6.2x and the subsequent decline to 5.9x at 3/31/2014 reflects this view.
- Going forward, we expect to:
  - Maintain investments in current portfolio and continue to earn cash flow with the opportunity to roll down the curve
  - Maintain positive duration on the front end of the yield curve
  - Exercise more diligence when making investments because returns are lower. We continue our disciplined approach to capital deployment – assessing risk adjusted returns in the context of net interest income and book value volatility
  - Maintain leverage levels respecting the current environment and opportunistically reposition asset portfolio and hedges
  - Actively manage repo counterparty relationships and funding portfolio



# Interest Rate Sensitivity *(as of March 31, 2014)*

Treasury Yields	
2Y	0.42%
5Y	1.72%
10Y	2.72%
30Y	3.56%

Parallel Change in Treasury Yields (in basis points)	Percentage Change in Projected Market Value of Assets Net of Hedges
+100	(1.46)%
+50	(0.69)%
+25	(0.33)%

Curve Shift 2 year Treasury (in basis points)	Curve Shift 10 year Treasury (in basis points)	Percentage Change in Projected Market Value of Assets Net of Hedges
0	+25	(0.11)%
+10	+50	(0.32)%
+10	+75	(0.49)%
+25	+75	(0.59)%
+25	0	(0.20)%
+50	0	(0.41)%
-10	-50	0.19%

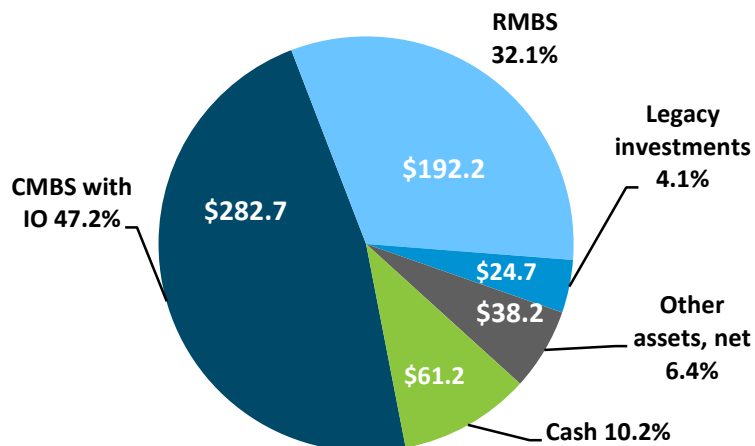
*Intermediate curve point shifts are interpolated for non-parallel scenarios*



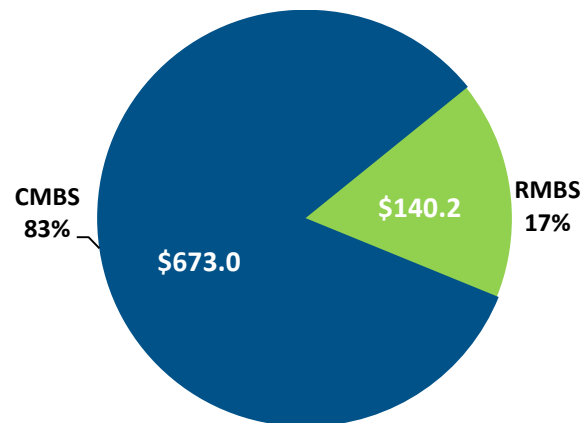
# Portfolio Update *(as of March 31, 2014)*

(\$ in millions)

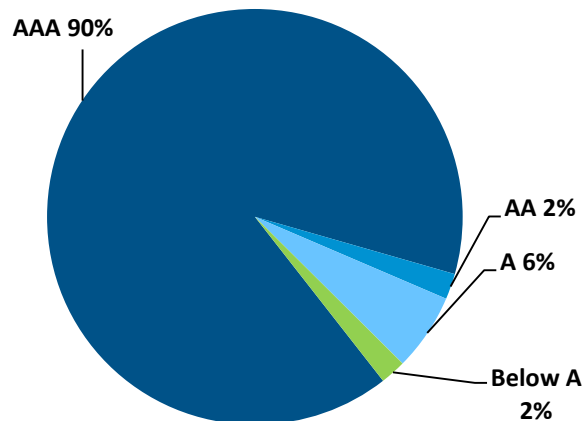
## Equity Capital Allocation



## Net Premium by Asset Type

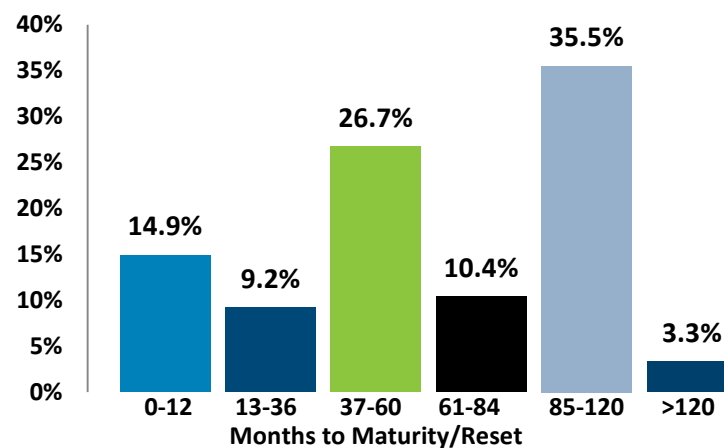


## MBS Credit Quality



Agency MBS are considered AAA-rated for purposes of this chart.

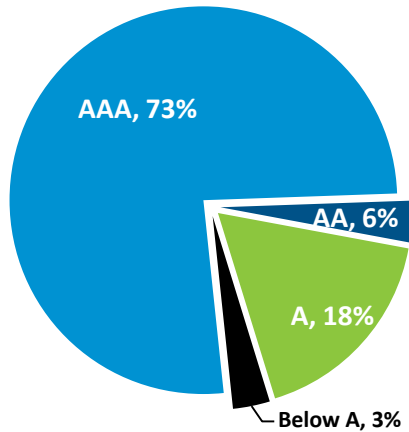
## MBS Expected Maturity/Reset Distribution



# CMBS Portfolio *(as of March 31, 2014)*

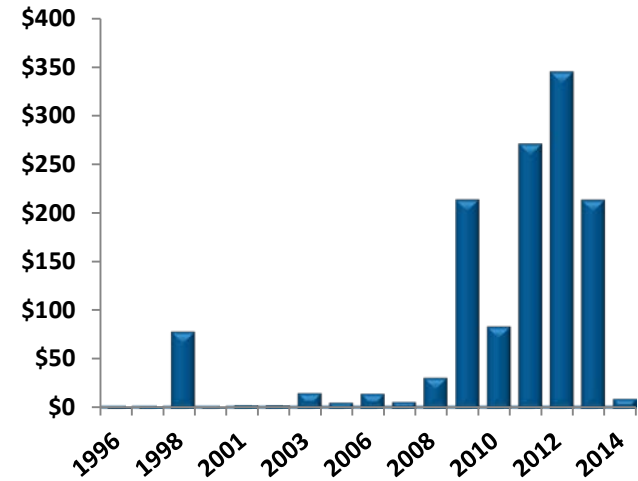
\$ in millions

## Credit Quality

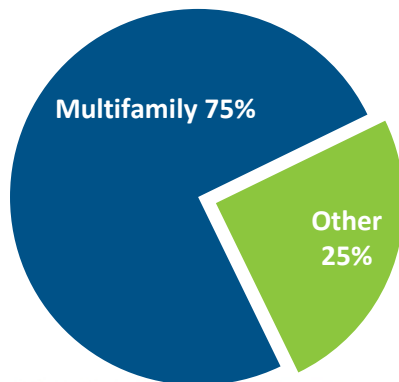


Agency MBS are considered AAA-rated for purposes of this chart.

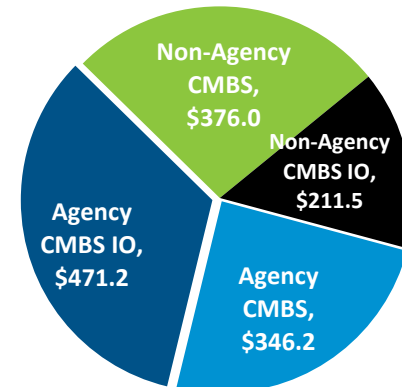
## Vintage (by year of origination)



## Collateral



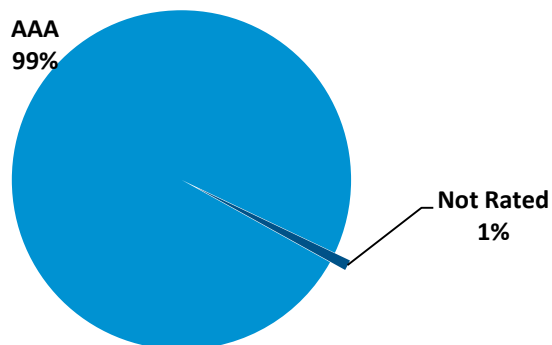
## Asset Type



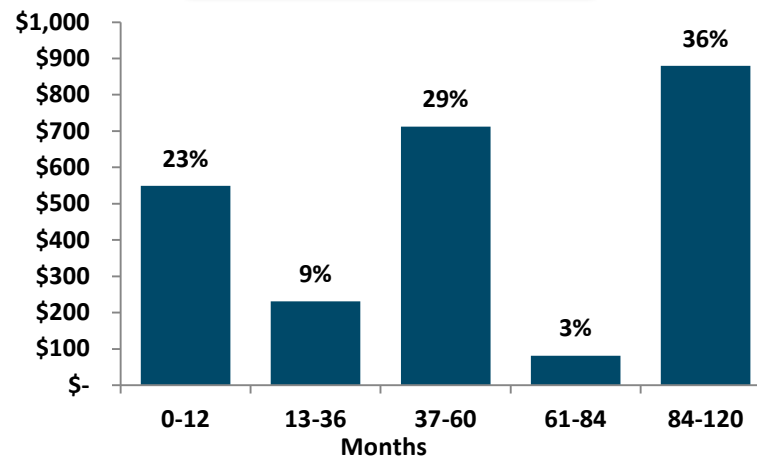
# RMBS Portfolio *(as of March 31, 2014)*

\$ in millions

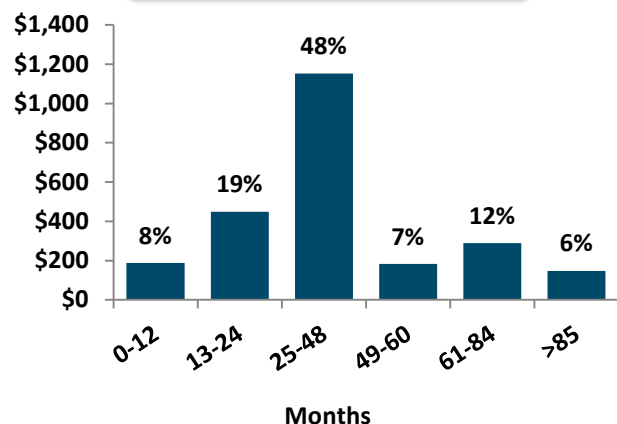
Credit Quality



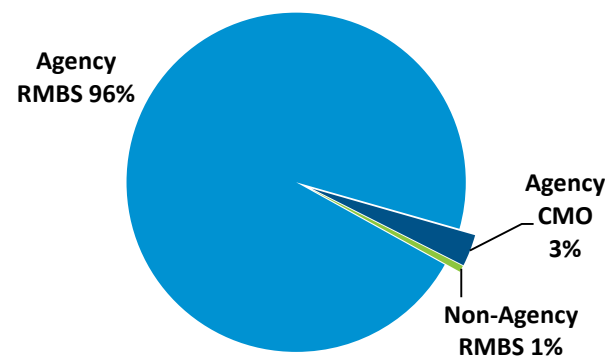
Months to Maturity/Reset



Weighted Average Loan Age



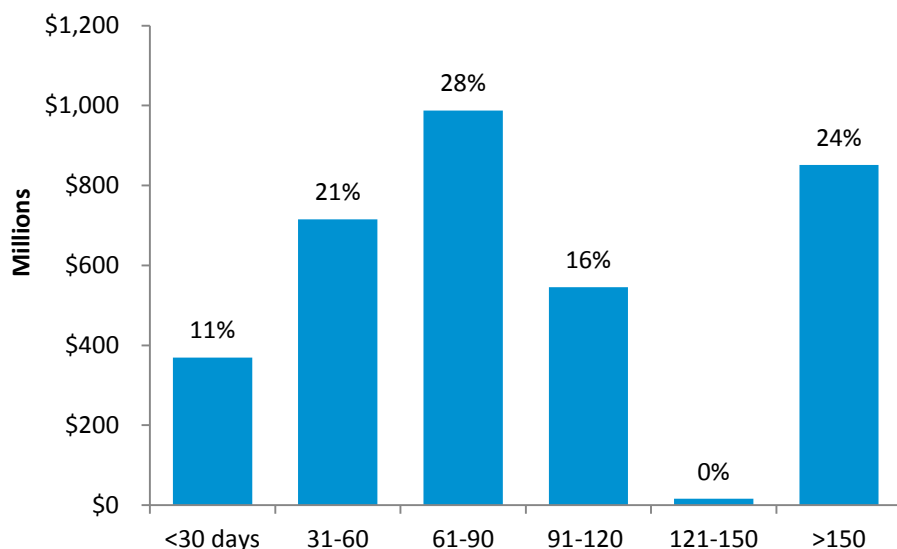
Asset Type



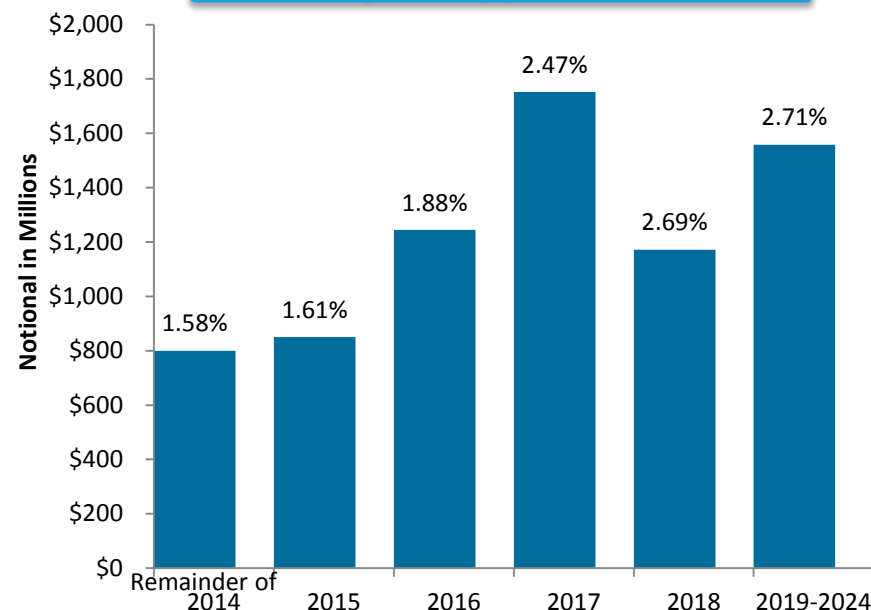
# Financing Details

(as of March 31, 2014)

Repurchase Agreements by Original Maturity



Hedges Detail (by Effective Date)



- Our weighted average contractual maturities were 93 days compared to 114 days at December 31, 2013.
- Our repurchase agreement balance was \$3,485,544 at March 31, 2014 with 21 counterparties compared to \$3,580,754 with 22 counterparties at December 31, 2013. We have repurchase agreements available to us with 31 counterparties.

# Conclusion

- The current market environment is complex. Uncertainty around economic growth, regulatory changes, market reaction and global market imbalances require discipline and vigilance
- Our investment strategy and thesis has not changed – our portfolio continues to generate an above average dividend yield with a conservative profile
- Funding costs have recently declined and there is excess capacity in the system
- Longer term, we see opportunities for investments in both residential and commercial assets and in markets currently dominated by the Fed/GSEs
  - At the conclusion of QE3, private capital for the first time will need to replace the government as the dominant purchaser of MBS
  - As the US housing system is reformed, there should be more opportunity to invest in residential credit



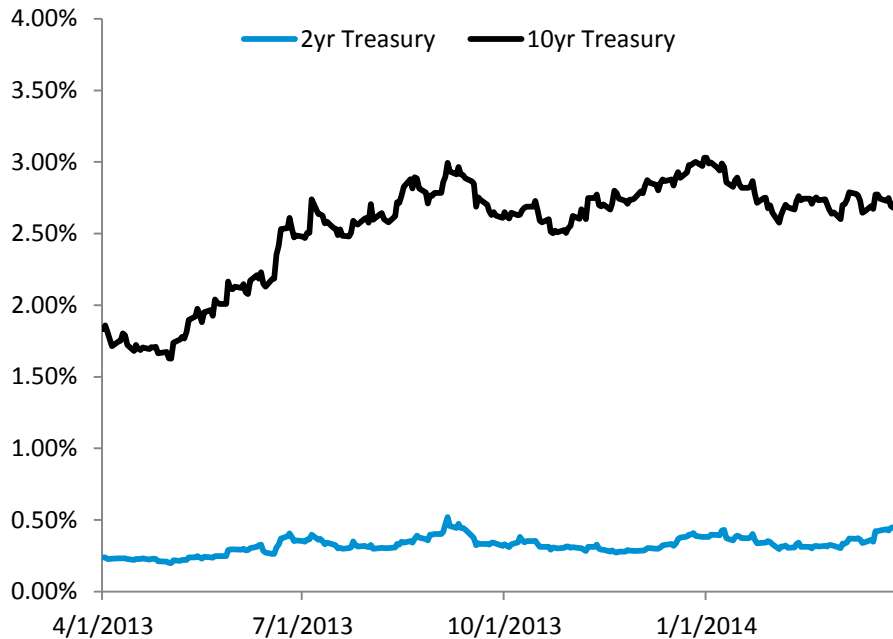
# APPENDIX





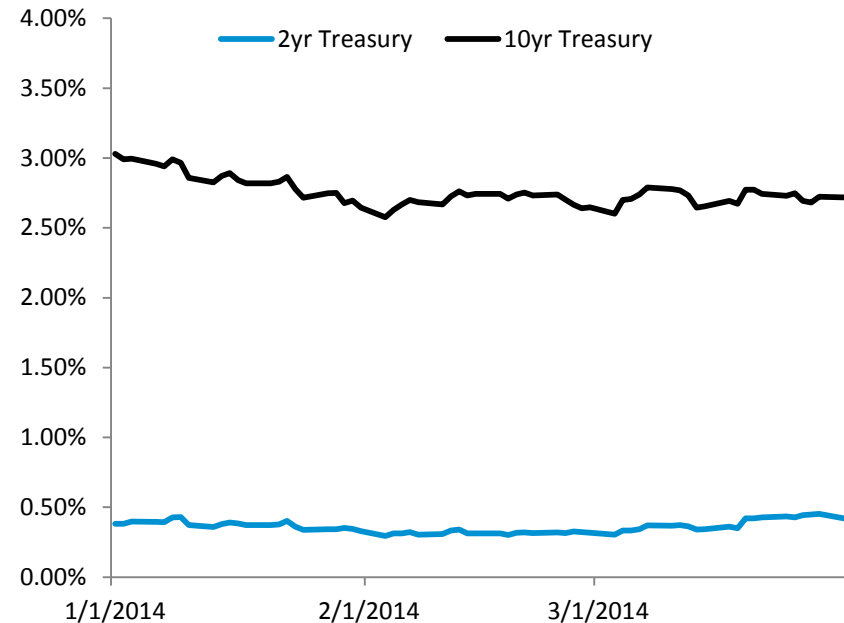
# Market Environment

Annual Comparison



- Treasury yield curve has steepened dramatically over the last twelve months
- 2 year rate remains anchored, reflecting Fed's intention to keep short rates low

Quarterly Comparison



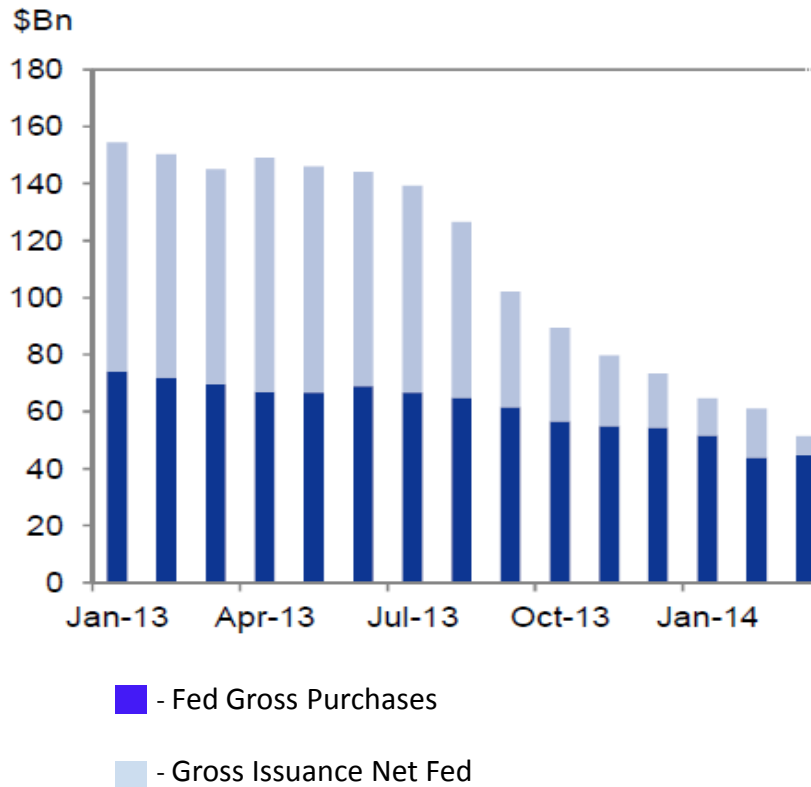
- 10 year treasury yields were under pressure at year end but have since rallied
- 2 year remains relatively stable in comparison

Source: Bloomberg

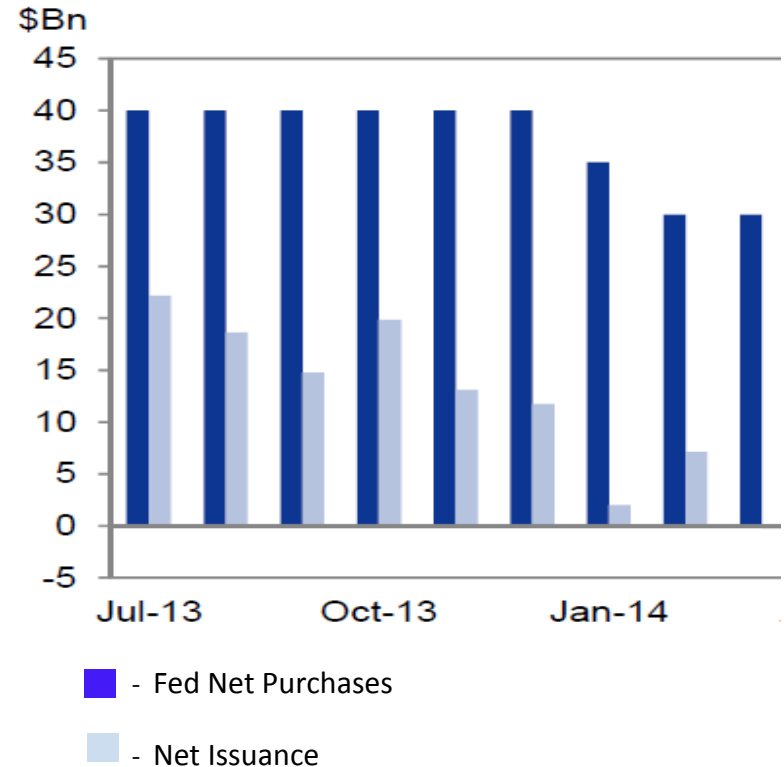
# Market Environment

## Net RMBS Supply

Gross issuances



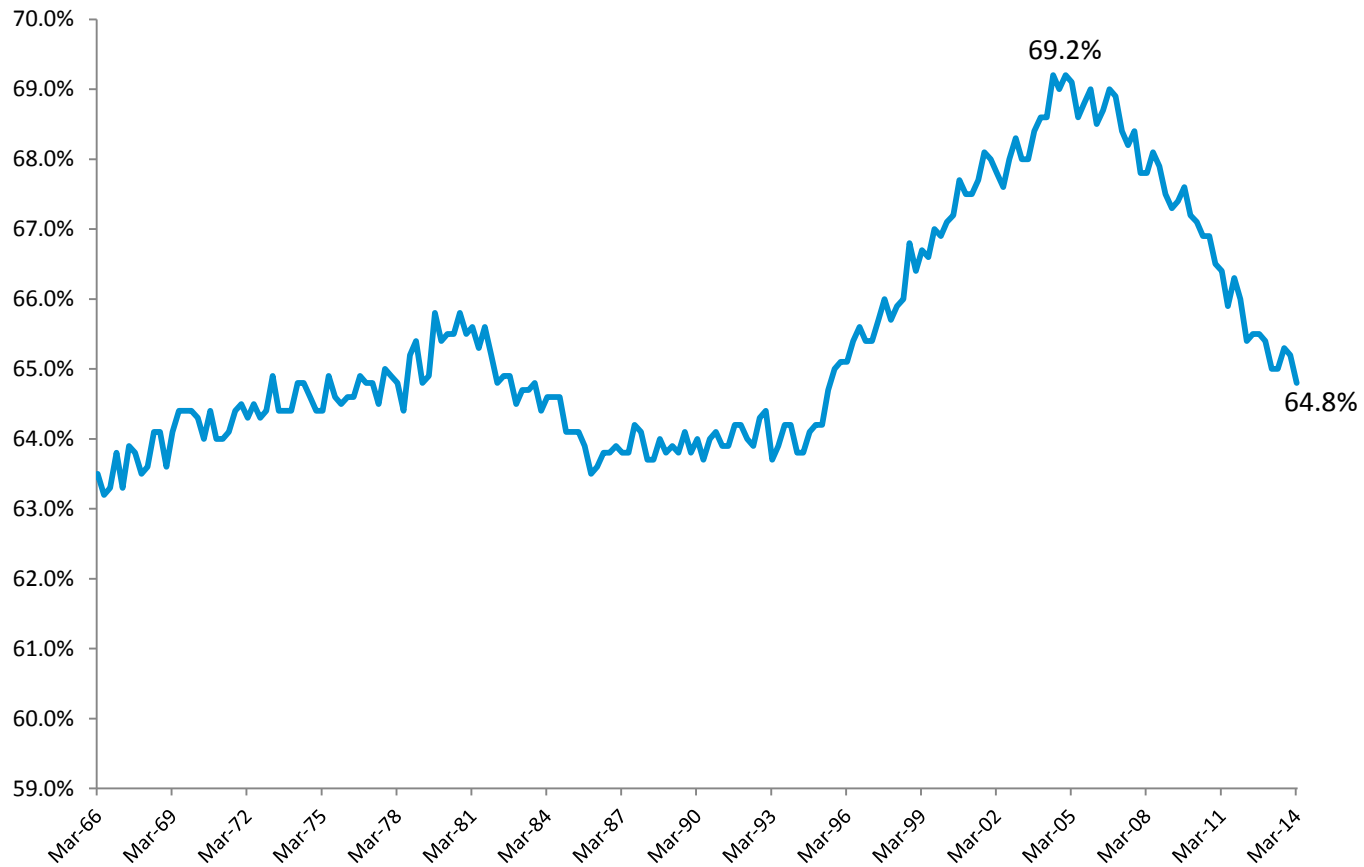
FOMC net purchases versus net issuances



Source: eMBS, Federal Reserve and Goldman Sachs

# Market Environment

## Homeownership Rates



Source: U.S. Census Bureau



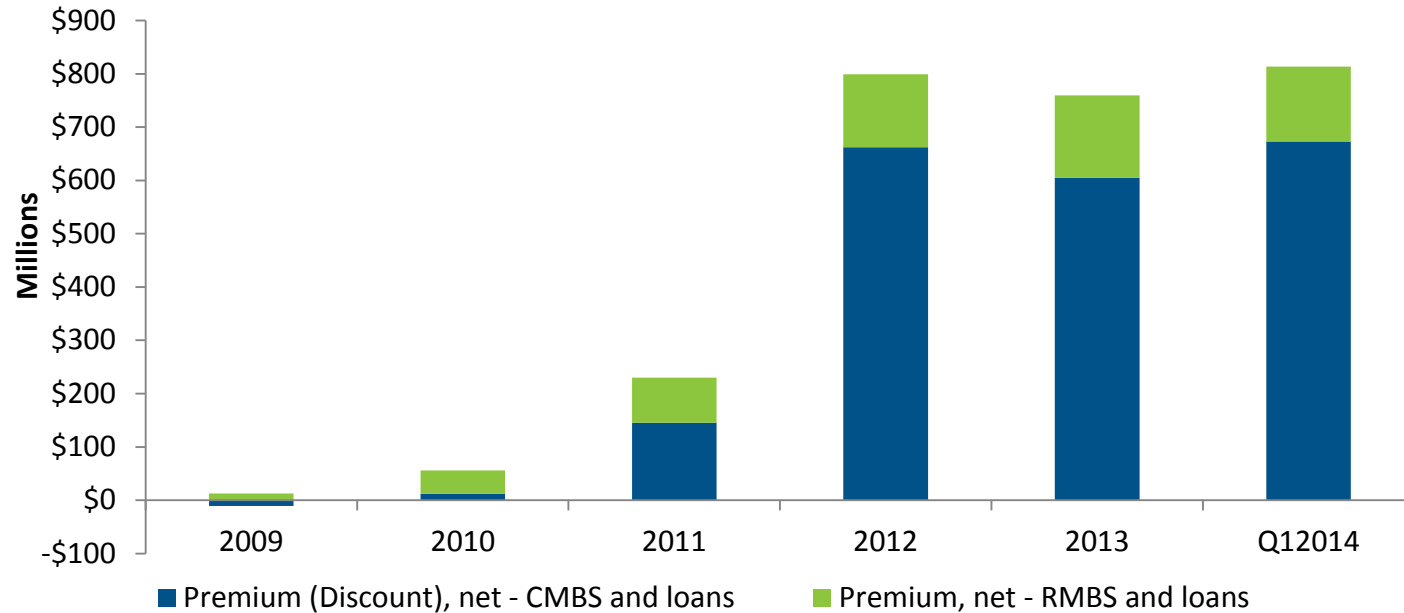
# Capital Allocation *(as of March 31, 2014)*

(\$ in thousands)	Asset Carrying Basis	Associated Financing <sup>(1)</sup> / Liability Carrying Basis	Allocated Shareholders' Equity	% of Shareholders' Equity
<b>Agency MBS</b>	\$ 3,356,759	\$ 2,998,479	\$ 358,280	59.8 %
<b>Non-Agency MBS</b>	603,093	486,459	116,634	19.5 %
<b>Mortgage loans held for investment, net</b>	53,804	29,086	24,718	4.1 %
<b>Derivative assets (liabilities)</b>	12,064	11,137	927	0.2 %
<b>Cash and cash equivalents</b>	61,168	—	61,168	10.2 %
<b>Restricted cash</b>	18,242	—	18,242	3.0 %
<b>Other assets/other liabilities</b>	39,152	20,106	19,046	3.2 %
	\$ 4,144,282	\$ 3,545,267	\$ 599,015	100.0 %

*<sup>(1)</sup>Associated financing for investments includes repurchase agreements and securitization financing issued to third parties (which is presented on the Company's balance sheet as "non-recourse collateralized financing"). Associated financing for derivative instruments represents the fair value of the derivative instruments in a liability position.*

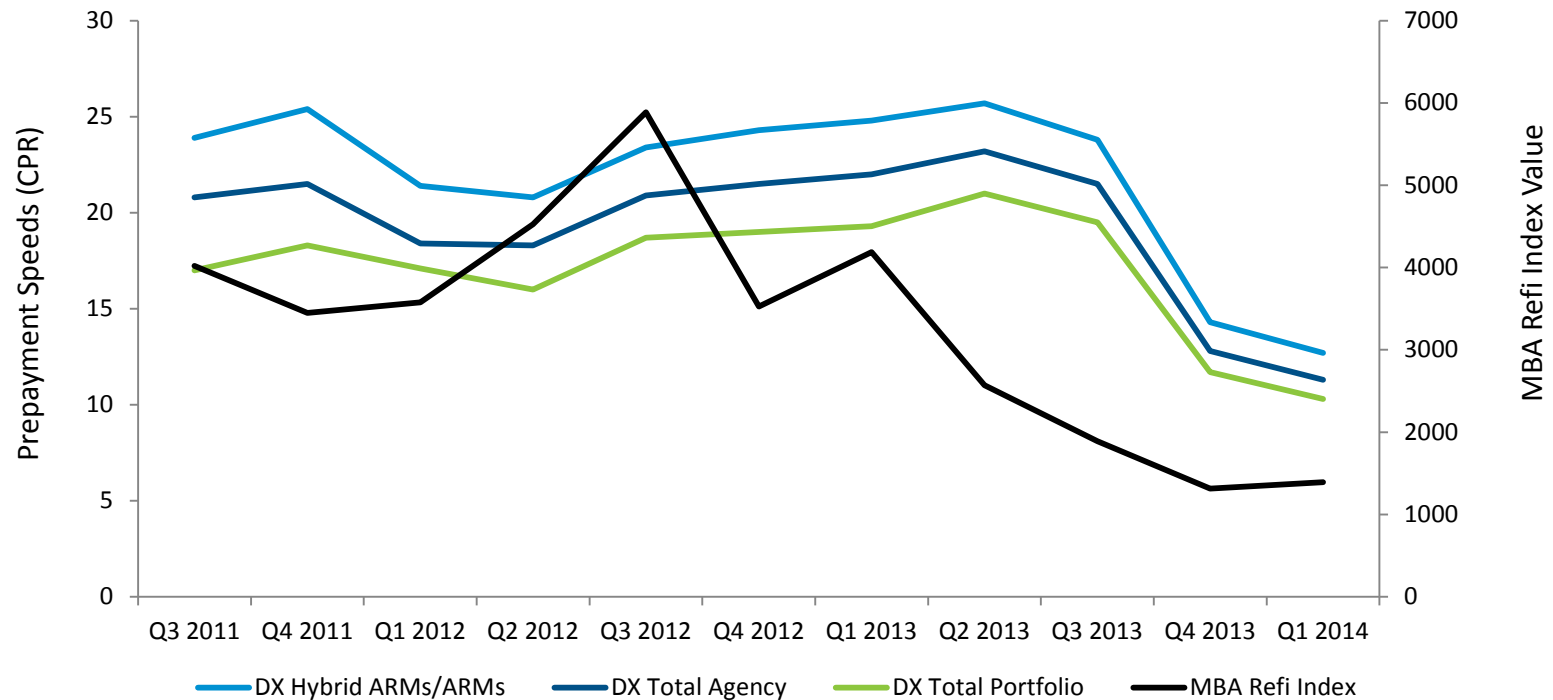
# Investment Premium Allocation

(as of end of period)



## Drivers of EPS

# ARM Prepayment Speeds vs MBA Refinancing Index



Source : MBA REFI Index (Bloomberg)



## Spread Risk

- An asset's "spread" is the market premium above a benchmark rate that reflects the relative riskiness of the asset versus the benchmark.
- Spread risk is the uncertainty in pricing resulting from the expansion and contraction of the risk premium over the benchmark.
- Spreads (and therefore prices) are impacted by the following factors:
  - **Fundamentals:** Probability of default, cash flow uncertainty
  - **Technicals:** Supply and demand for various assets
  - **Psychology:** Reflects the risk appetite of the market and the perceived riskiness of specific assets
- Most mortgage REIT business models are inherently exposed to spread risk. At Dynex, we focus on all three aspects of spread risk. However, changes in pricing due to technicals and psychology are very difficult to predict. We manage spread risk over the long-term through portfolio construction.



## Drivers of Book Value

# Spread Changes

Assets	March 31, 2014	December 31, 2013	Change
2 year vs. 10 year UST spread	230	265	-35
Hybrid ARM 5/1 spread to UST	21	30	-9
Hybrid ARM 10/1 spread to UST	57	76	-19
Agency CMBS spread to interest rate swaps	50	58	-8
'A'-rated CMBS spread to interest rate swaps	190	220	-30
Agency CMBS IO spread to UST	155	165	-10
IG Index spread to UST	131	135	-4
HY Index spread to UST	435	460	-25
CMBX.NA.A.6 (2012 'A'-rated)	195	205	-10

*Note: Amounts represent basis point spread to benchmark as noted.*

*Source: JP Morgan*

## Drivers of Book Value and EPS

# Risk Management

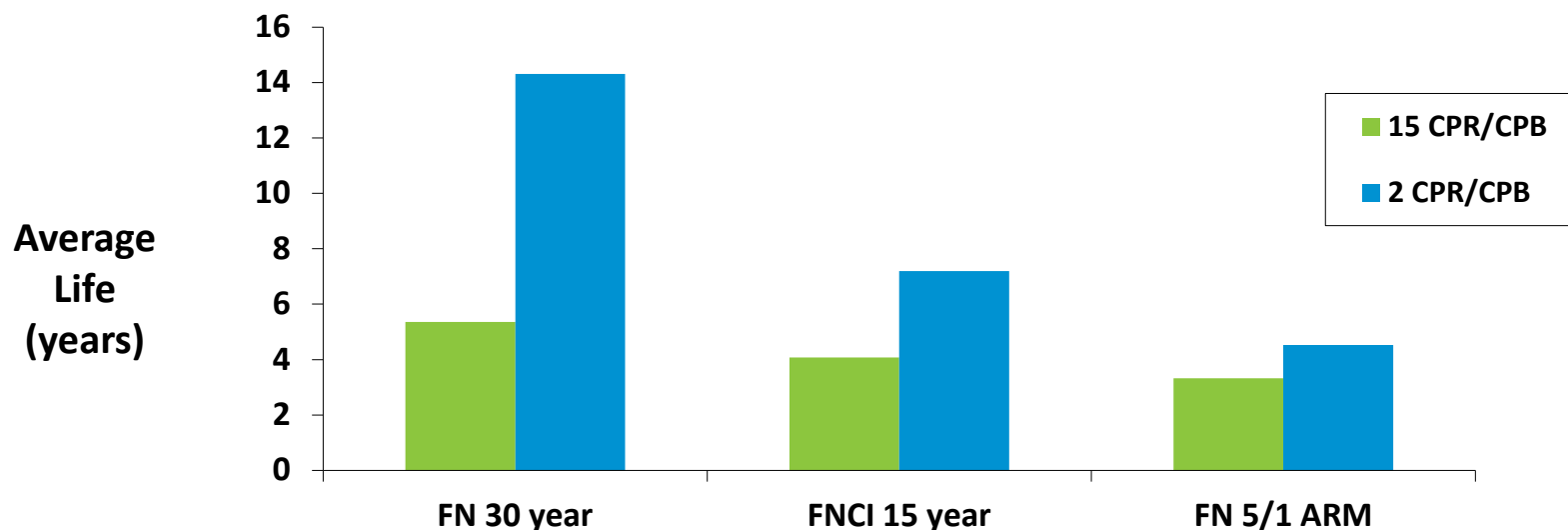
Key Risk	Mitigating Strategy
Interest Rate/Extension Risk	Duration target of <u>0.5 to 1.5 years</u> Derivatives to economically hedge interest rate risk Invest in credit assets that should increase in value as rates rise Short duration assets and more predictable cash flows
Prepayment Risk	CMBS investments with call protection RMBS specified pools with diversity of prepayment risk
Credit Risk	90% of MBS are AAA-rated*at March 31, 2014 Current credit risk is multifamily focused
Spread Risk	Portfolio construction and long-term portfolio strategy
Liquidity Risk	Diversified repurchase agreement counterparties and low leverage Unencumbered liquidity to meet expected risk events

*\*Agency MBS are considered AAA-rated as of the date presented.*



## Drivers of Book Value

# Extension Risk *(as of April 30, 2014)*



	Price	Coupon	WAC	Speed	Average Life	Average Life Extension
FN 30yr	\$101-13	3.50%	4.01%	15 CPR 2 CPR	5.36 years 14.31 years	~9 years
FNCI 15yr	\$103-5	3.0%	3.48%	15 CPR 2 CPR	4.07 years 7.19 years	~3 years
FN 5/1 ARM	\$103-10	2.78%	3.42%	15 CPB 2 CPB	3.33 years 4.53 years	~1 year

## Selected Financial Highlights *(as of and for the quarter ended)*

(\$ in thousands, except per share amounts)	1Q2014	4Q2013	1Q2013
Net interest income	\$ 20,007	\$ 20,186	\$ 22,526
(Loss) gain on derivative instruments, net	(13,422)	2,607	(17)
Net (loss) income to common shareholders	(3,028)	19,266	18,381
Net (loss) income per common share	(0.06)	0.35	0.34
Comprehensive income to common shareholders	26,532	19,813	27,427
Comprehensive income per common share	\$ 0.49	\$ 0.36	\$ 0.51
Core net operating income to common shareholders <sup>(1)</sup>	13,746	15,544	16,973
Core net operating income per common share <sup>(1)</sup>	\$ 0.25	\$ 0.29	\$ 0.31
Return on average common equity (annualized)	(2.5)%	16.1%	13.0%
Adjusted return on average common equity (annualized) <sup>(1)</sup>	11.3%	13.0%	12.0%
Dividends per common share	\$ 0.25	\$ 0.27	\$ 0.29
Book value per common share, end of period	\$ 8.87	\$ 8.69	\$ 10.50
Interest earning assets, end of period	\$ 4,013,656	\$ 4,073,584	\$ 4,531,342
Average interest earning assets	\$ 4,002,555	\$ 4,123,224	\$ 4,098,681
Average interest bearing liabilities	\$ 3,509,889	\$ 3,620,795	\$ 3,641,654
Weighted average effective yield	2.74%	2.72%	3.04%
Annualized cost of funds	0.87%	0.90%	1.15%
Net interest spread	1.87%	1.82%	1.89%
Adjusted net interest spread <sup>(1)</sup>	1.88%	1.77%	1.87%
Portfolio CPR	10.3%	11.7%	19.3%
Debt to shareholders' equity ratio, end of period	5.9x	6.2x	6.3x

<sup>(1)</sup> Core net operating income to common shareholders (including on a per share basis), adjusted return on average common equity and adjusted net interest spread are non-GAAP financial measures. Reconciliations of these non-GAAP financial measures are provided on slides 33 and 34.

# Book Value Reconciliation

	Book Value (\$ in thousands)	Book Value Per Common Share
<b>Shareholders' equity, December 31, 2013</b>	<b>\$ 585,876</b>	<b>\$ 8.69</b>
GAAP net loss to common shareholders:		
Core net operating income	13,746	0.25
Amortization of de-designated cash flow hedges	(2,288)	(0.04)
Change in fair value of derivative instruments, net	(11,211)	(0.21)
Loss on sale of investments, net	(3,307)	(0.06)
Fair value adjustments, net	32	—
Other comprehensive income	29,560	0.54
Common dividends declared	(13,674)	(0.25)
<b>Balance before capital transactions</b>	<b>598,734</b>	<b>8.92</b>
Restricted stock amortization	672	0.01
Stock issued, including incentive stock issued to employees, net of forfeitures and issuance costs	(391)	(0.06)
<b>Shareholders' equity, March 31, 2014</b>	<b>\$ 599,015</b>	<b>\$ 8.87</b>
Common Shares outstanding March 31, 2014		54,697,307



# Reconciliation of GAAP Measures to Non-GAAP Measures

(\$ in thousands except per share data)

	Quarter Ended				
	3/31/2014	12/31/2013	9/30/2013	6/30/2013	3/31/2013
<b>Net (loss) income to common shareholders</b>	<b>\$ (3,028)</b>	<b>\$ 19,266</b>	<b>\$ (6,921)</b>	<b>\$ 29,442</b>	<b>\$ 18,381</b>
Adjustments:					
Amortization of de-designated cash flow hedges <sup>(1)</sup>	2,288	2,609	2,583	—	—
Change in fair value on derivatives instruments, net	11,211	(5,636)	18,548	(11,626)	(157)
Loss (gain) on sale of investments, net	3,307	(757)	825	(2,031)	(1,391)
Fair value adjustments, net	(32)	62	(150)	600	140
<b>Core net operating income to common shareholders</b>	<b>\$ 13,746</b>	<b>\$ 15,544</b>	<b>\$ 14,885</b>	<b>\$ 16,385</b>	<b>\$ 16,973</b>
<b>Core net operating income per share</b>	<b>\$ 0.25</b>	<b>\$ 0.29</b>	<b>\$ 0.27</b>	<b>\$ 0.30</b>	<b>\$ 0.31</b>
ROAE based on annualized net (loss) income to common shareholders	(2.5)%	16.1 %	(5.7)%	21.0 %	13.0 %
Amortization of de-designated cash flow hedges	1.9%	2.2 %	2.1 %	—%	—%
Change in fair value on derivatives instruments, net	9.2%	(4.7)%	15.3 %	(8.3)%	(0.1)%
Loss (gain) on sale of investments	2.7%	(0.6)%	0.7 %	(1.4)%	(1.0)%
Fair value adjustments, net	—%	0.1 %	(0.1)%	0.4 %	0.1 %
<b>Adjusted ROAE, based on annualized core net operating income</b>	<b>11.3%</b>	<b>13.0 %</b>	<b>12.3 %</b>	<b>11.7 %</b>	<b>12.0 %</b>
Average common equity during the period	\$ 485,044	\$ 477,432	\$ 484,356	\$ 560,449	\$ 567,489

<sup>(1)</sup> Amount recorded as a portion of "interest expense" in accordance with GAAP related to the amortization of the balance remaining in accumulated other comprehensive loss as of June 30, 2013 as a result of the Company's discontinuation of hedge accounting.

## Accounting Disclosure

# Reconciliation of GAAP Measures to Non-GAAP Measures

(\$ in thousands)

	Quarter Ended									
	3/31/2014		12/31/2013		9/30/2013		6/30/2013		3/31/2013	
GAAP Interest income/annualized yield	\$27,640	2.74%	\$28,594	2.72%	\$31,666	2.82%	\$33,890	2.86%	\$32,982	3.04%
GAAP Interest expense/annualized cost of funds <sup>(1)</sup>	7,633	0.87%	8,408	0.90%	8,718	0.88%	11,446	1.11%	10,456	1.15%
<b>GAAP net interest income/spread</b>	<b>20,007</b>	<b>1.87%</b>	<b>20,186</b>	<b>1.82%</b>	<b>22,948</b>	<b>1.94%</b>	<b>22,444</b>	<b>1.75%</b>	<b>22,526</b>	<b>1.89%</b>
GAAP interest expense/annualized cost of funds (from above)	7,633	0.87%	8,408	0.90%	8,718	0.88%	11,446	1.11%	10,456	1.15%
Amortization of de-designated cash flow hedges <sup>(2)</sup>	(2,288)	(0.26)%	(2,609)	(0.28)%	(2,583)	(0.26)%	—	—%	—	—%
Net periodic interest costs <sup>(3)</sup>	2,211	0.25%	3,029	0.33%	5,471	0.55%	274	0.03%	174	0.02%
Effective borrowing costs	7,556	0.86%	8,828	0.95%	11,606	1.17%	11,720	1.14%	10,630	1.17%
<b>Adjusted net interest income/spread</b>	<b>\$20,084</b>	<b>1.88%</b>	<b>\$19,766</b>	<b>1.77%</b>	<b>\$20,060</b>	<b>1.65%</b>	<b>\$22,170</b>	<b>1.72%</b>	<b>\$22,352</b>	<b>1.87%</b>

(1) Rates shown are based on annualized interest expense amounts divided by average interest bearing liabilities. Recalculation of annualized cost of funds using total interest expense shown in the table may not be possible because certain expense items use a 360-day year for the calculation while others use actual number of days in the year.

(2) Amount recorded as a portion of "interest expense" in accordance with GAAP related to the amortization of the balance remaining in accumulated other comprehensive loss as of June 30, 2013 as a result of the Company's discontinuation of hedge accounting.

(3) Amount equals the net interest payments (including accrued amounts) related to interest rate derivatives during the period which are not already included in "interest expense" in accordance with GAAP.