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EDITED TRANSCRIPT

RWT - Redwood Trust Inc Investor Day

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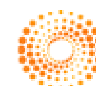

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PRESENTATION

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

Good morning, everybody. Welcome to Redwood Trust's 2019 Investor Day. I'm so happy to see a full house here. My name's Lisa Hartman, I'm the Senior Vice President, Head of Investor Relations, and I'm going to take you guys through our agenda, some safe harbor information and some housekeeping. So for those in the room, the restrooms are through these doors that you came in. If you make a left, go down the stairs, those are the closest facilities.

So we have a really great day planned for you. I'll run through the agenda. We have today broken out into 3 sessions, closing each session with an opportunity for Q&A and a short break. So we'll start off today with a welcome from our Chairman, Rick; and then Chris and Dash will walk through our company vision and our forward progress and strategic path, and then we'll close the session with a founders fireside chat hosted by Gar. We'll go for break and when we come back, we'll have Bo Stern come up and walk through the evolution of the investment portfolio, followed by Collin, he'll go through how we're delivering shareholder value. And then we have a really great Q&A with one of our -- our COO of Wintrust, one of our top sellers who we work with here at Redwood. And then another opportunity for Q&A and then going into break. And then when we come back, we'll have our third session and here, Sasha will walk through how we're building our organization's capability through human capital, and we'll also have a very interesting housing finance reform panel discussion hosted by Blake Eger, and then we'll close with Matt Tomiak walking through

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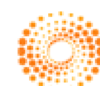

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our mortgage banking. And Chris will give us some final remarks before we open again for a general Q&A. And then it will be followed by a lunch reception that'll be back here in the bar area and we hope you can say for that and attend.

I want to remind everybody that this meeting is being webcast and webcast live. During the Q&A session, we ask that you wait for the microphone so that your questions and then also the responses are picked up on the webcast. That being said, I want to read through some safe harbor language and remind everybody that statements made during today's presentations with respect to future financial or business performance may constitute forward-looking statements. Forward-looking statements are based on current expectations, forecasts and assumptions that involve risks and uncertainties that could cause actual results to differ materially. We encourage you to read the company's annual report on Form 10-K, which provides a description of some of the factors that could cause actual results to differ from those that may be expressed in forward-looking statements. During today's presentations, we will also refer to both GAAP and non-GAAP financial measures. A reconciliation between GAAP and non-GAAP financial measures is provided on the company's website. Also note that the content of today's presentations contain time-sensitive information that is accurate only as of today. The company does not intend and undertakes no obligation to update this information to reflect subsequent changes, events or circumstances. Finally, today's meeting is being webcast live and a replay will be available on the company's website later today. And with that, I'm going to turn it over for welcoming remarks from Rick Baum.

Richard D. Baum - *Redwood Trust, Inc. - Chairman of the Board*

Good morning. I'm Rick Baum, Chairman of the Redwood board and I welcome you all to our second annual Investor Day, which also marks our 25th year of our founding. It's been a time of great transition for Redwood, as we completed a successful move to new -- a new leadership team of Chris and Dash. And the succession was a product of deliberate and decisive action on the part of both the board and management. Additionally, the team has just completed the -- its 5 Arches acquisition. What they told the employees of 5 Arches gives, I think, great insight into Redwood and its leadership. They assured our partners at 5 Arches that the foundation of our success will be the key values that we share: Honesty, humility, partnership and a commitment to transparent and fair dealing. It's this same assurance of our commitment to transparency and fair dealing that I want to extend to you, our investors and analysts, on behalf of Redwood's board and management. As you go forward through the day, I think you're going to experience that. And with that, I'd like to introduce our CEO, Chris Abate, who will led us through the rest of the day.

Christopher J. Abate - *Redwood Trust, Inc. - CEO & Director*

Good morning, everyone. We finally have our captive audience, all here to think about Redwood, which is pretty cool. So certainly appreciate our long-term shareholders that are in attendance, some prospective investors. I think all of our equity analysts are here. So I very much appreciate you guys coming. We have the management team, obviously, and then as Lisa mentioned, we have some esteemed panelists who will help us think about housing finance reform and also give you some perspectives from the other side of the table, from the CEO of Wintrust.

So I'm going to start by acknowledging the obvious. This week, we ran the opening bell at the New York Stock Exchange and we're celebrating 25 years. So 25 years is a long time and as I was saying to one of you earlier, if anybody owns a REIT that's older than 25 years in their portfolio, you get 2 sandwiches at lunch, because that's actually pretty rare. But you know to sustain us this long, and you'll hear from Doug, it really does come down to people. I wouldn't be a good CEO if I didn't brag for a few minutes about our people. You know, just a quick story, when I joined the company, I was at Freddie Mac doing consulting work, and we were looking at pipeline hedging. And really, what was going on was we came in because their interpretation of the accounting guidance was very simple and they ended up with a very complicated result and so earnings were like this and then there was adjustments and then there were bad things happened. But a year or so later, after that experience, I came to Redwood, similar engagement, we were looking at income recognition on loans and securities, and I couldn't believe, I was blown away by the complexity of these models. And these guys, I met Bo and a few other people, and you name it, they had a model for it, caps, corridors, picking, subordination, prospective, retrospective adjustments. There was all this complexity and I realized what they were trying to do was they were trying to internalize it all to result in something simple for outside investors and stakeholders. And it was a complete contrast from the other side of the country with the GSEs at the time. And I realized a few things, 2 things actually: Number one, they were right, the models were right and the concept was right, is doing the hard stuff to make things simple; and number two, I realized that that's the type of place that I wanted to go to work. And I joined the company a few years later, and I can honestly say that since our founding, the emphasis on top-tier people has never been greater. I'll give you one more quick analogy that's more recent, a person I love to brag about the most, Dash here. Dash has been with us for about 1.5 years, but only

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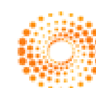

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recently, it was actually this past December, thanks to our friends actually at JPMorgan, I was -- I ended up having a one-on-one meeting with Tim Sloan, the CEO of Wells Fargo. And outside of exchanging pleasantries with Tim, he was so intrigued and was so interested in learning about Redwood, because he just couldn't fathom losing a star like Dash to a much smaller company. And we talked about just his track at the bank and Tim relaying to me that it was one of his biggest losses over the past few years. And the point of this is, whether you're an investor or you're a mortgage company, or you're a servicer or you're the CEO of a $2 trillion bank, I think everybody acknowledges that the talent of this company is top-notch and very, very relevant. And we're going to need to be top-notch, because I want to walk you guys through our vision and then our investment philosophy before we get into some of the, the -- more numeric concepts and some of the strategic initiatives.

You know from a vision perspective, we get this question a lot, and it's hard to answer sometimes because so much is changing in our industry. Basically, since the crisis, we've been in a state of change. And so you're trying to guide the ship, you're trying to -- somebody says what's the end of the movie? Where does Redwood fit in? Where do you want to be? What do you define as success? And there's a lot of ways to answer that. We could say we want to be this big or we want to have this growth rate. But to me, there's a simpler way and this is it: Whenever a loan changes hands in this country, we want to participate on the private capital side. And just to make this a little clearer for the captive audience, whenever a non-agency loan changes hands, we want to get paid. And that's a big initiative. We're not the largest company in the markets. That's something that, I think, very few people would aspire to do. But there's some really interesting things that we have that others don't and frankly, money can't buy. And I'll cite a few examples. I think the easiest one to understand, because it's the most public, is our Sequoia program. And we have the leaders of the program here today. We've done over 50 post-crisis transactions. Our bonds are actually the closest thing to a benchmark to Fannie and Freddie guaranteed pass-throughs. So when you're in the markets and some of you on your fixed income sides of the house have investors in our Sequoia issuances, they will tell you that the way this market trades is back of Sequoia. So you hear about where TBA is priced, I don't care if you are a money center bank, or you're another REIT, whoever the issuer is, you talk about it in terms of where Sequoia trades. And there's a few reasons for that, which I want to get into. But first of all, we've strived to build a brand and not best axe each deal. What we're not trying to do is arbitrage the rating agencies, we're not trying to throw in some loans that we couldn't sell into a transaction. We're not trying to water down the investor protections. Since the crisis, the one word that defines the brand is consistency, but also trust. Redwood is all about trust and what our investors have learned is that through a consistent track record, the first thing when we issue a deal and many of the participants look at -- they get the issuance and they get the tape, the first thing they say is not, "What are the strats, what's the yield profile, how diverse is this deal?" The first thing they say is, "It's a Redwood deal, I got it." And when you think about the power of that and how we could monetize that in the coming years, I think it's a huge, huge opportunity. And we layer in, and we're going to have a conversation later today about some concepts around GSE reform. And without giving away what you're going to hear, one of the hallmark aspects of the Crapo outline, which I believe is shared by the administration, is this concept of private guarantors. So when you think about who's better positioned to do that, I don't think there's anybody in the industry that's better positioned than Redwood. So we're very, very excited about that. Our real business is acting as that intermediary in the markets. We are a buyer, we are a seller, we are a securitizer. Many people don't know this, because it's not as public, but we sell tons of whole loan pools, that don't make it into the press as securitizations. So we've got a prolific whole loan description network, insurance companies, pension funds, banks, you name it. So it's really -- our business is as an intermediary and to us, we're going to talk about some innovative things that we're working on that we've got going on in the lab that I think you'll find really, really interesting and as things evolve here with housing reform, our goal is to be positioned and to be ready.

Next I want to get into our investment philosophy. Most of the day, we're going to be talking about portfolio-related initiatives because most of your capital is invested there. I think of our portfolio as the byproduct of what we do every day. So by acting as a market maker, we are in the markets and we have access to cash flows that just can't be replicated. We've got -- we've layered in a bunch of bespoke transactions over the past year. We've been able to turbocharge our investing activity, and we're very, very mindful of capital allocation and where we're focused. But I think sometimes repetition is important, and I probably talked about this last year, but understanding how we approach investing, I think, is paramount, because we have -- we've seated a new management team, and some things, however, never change. Some things of the company that have sustained us, never change. And when we think about investing, the first thing that we always think about is preservation of capital. Next, profitability. And then, superior returns. And this is important because this isn't always the way that it's done in our world, as you guys know. We saw that through the crisis. The first thing we want to do is not lose money. And that guides where we take risk, how we take risk. We are investing when the odds are with us. We're not gambling when the odds are against us. And that to me is job one as CEO, and how we've approached our investing over the past year. We are also a public company. We want to be able to generate consistent dividends and cash flows for shareholders and returns. To do that, we need to focus on long, durable streams of cash flows. So when you look at our recent activity, which Bo will walk through, we're focused on the long term. We're focused on years and years of cash flows. We're not a trading organization. So that's another thing that I think

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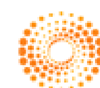

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makes us unique. And then tying it together with the vision is scaling this platform. It's putting ourselves in a position to be that intermediary, to really scale and really turbocharge the unleashing of leverage that's really embedded today and trapped that needs to be realized.

I've included a launch slide. I know there's a lot of finance geeks here like me. But I think this slide, if you can hang with it, really illustrates how we engineer returns. So we're focused on ROE. There's different ways to get there, as you guys know. And I think the way we get there is a little unique. We're very focused on margin, and right now, we're extremely focused on efficiency. Leverage is really what differentiates us. So the durability of our returns, where we're involved in the markets, if the magnifier is generating ROE, that can be very good and it can be very bad and it's just generally not the way that we do business. And so what I think is the most exciting is the efficiency column, which, that can be efficiency with assets. So we're trying to improve our loan sale margins. We're trying to get our cost of funds down. That can be capital efficiency. I think we announced in our fourth quarter results that we're going to lower the capital base in our mortgage banking business. That's because we're more efficient. We're buying loans faster, we're selling loans faster, we're holding less loans in inventory that are sucking up capital. There's a lot of just leverage that we're pulling within the organization to get much more efficient. And then, of course, is the big one, which is operating scale, which Collin is going to talk about. And as we grow our asset base, not our capital base but our asset base, we really start to realize some of the sort of untapped earnings potential of the company.

To sum up, I have about 2.5 minutes left, people also ask, what are you guys rooting for, how do I know what scenario is good for Redwood? And we wanted to update this for you. And the first one, which has changed, is we are really no longer tethered to the homeownership rate in the sense that we're no longer just focused on consumer lending. So we acquired 5 Arches very recently. Shawn Miller is in the crowd somewhere, the CEO. And that business, which is a tremendous business, puts us in a position where we can be relatively indifferent on the direction of homeownership. So what we really care about, however, is why homeownership is moving in any particular direction. If the homeownership rate is going up for the wrong reasons due to affordability products, you're starting to see more subprime loans being made, from our perspective, we'd rather be lending to the professional investors and writing some of those folks. We like the cash flow profile better. Doesn't make that a bad opportunity, but the market is just a lot bigger, as you've seen through some of our disclosures. And overall, the underwriting and the risk profile, we think, is advantageous.

Continuing to involve the role of passive investors. We are trying to continually push our bonds into commodity status. We want to increase the value of loans. We feel like if we can continue to keep our cost of funds as the lowest in the industry, from a securitization perspective, more and more competitors will start to think, I could spend all the money, set up a platform, obtain a 10-year track record and equalize these guys, but why don't I just sell them the loans? Just like you sell the loans to Fannie or you sell the loans to Freddie. That's really what we're trying to do when I say act as a market maker in the securitization space. We're trying to do the same thing in the whole loan space and we have some innovations there that we'll be talking about in the coming months.

Credit tiering. I think this one, everyone in this room would agree, it's been hard to differentiate yourself over the past 7 to 8 years, but you have seen -- you started to see a turn in housing. And I do think you will know where that extra money has been spent. We've never sacrificed on our credit disciplines, something that we never have and we never will. We don't always tag the markets in that sense because we spend a little bit more to get it right, but I do think in the long run, this will pay off.

Balance in the bank's business model, we've talked about that for a long time. Banks are in a position where they can do uneconomic things. We have to abide by the rules of capitalism. So that's something that is always apparent. That said, there's a lot of talk about risk transfer opportunities with banks, there's talk about the QM patch and how that might apply to some banks. So there is some interesting discussions going on in Washington that could enable us to effect some risk transfers from a third-party independent perspective.

And then, as I mentioned, to close, housing reform. The Crapo outline to me is pretty exciting because it's the first really formal call for private guarantors and this idea of putting Fannie and Freddie on a level playing field. I always like to tell people, we're not building a business model around these ideas. They're not probable, they're not estimable, but they're there. And when we think about the option value within firm, there's different ways to unlock that and that certainly would be one in the coming years. So those are my prepared remarks. I think we're going to do Q&A a little bit later, so I'll hand it over now to Dash Robinson.

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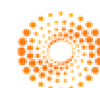

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Dashiell I. Robinson - *Redwood Trust, Inc. - President*

Thank you, Chris. I appreciate it. I haven't talked to Tim in a while, but I'm fairly certain he would have rather been here today than what he's been dealing with earlier this week. I appreciate everyone coming. Dash Robinson, Redwood's President. I'm going to spend my time today trying to draw a link between Chris's remarks and some of the more detailed content from Bo Stern, our CIO, and Collin Cochrane, our CFO. And really trying to dig a bit deeper into some of the strategic progress we've made over the past year or so, and a little bit more of what's to come.

So firstly, a little bit of a summary of executing on our strategic initiatives. As you all are aware, for the better part of 18 months now, we have been very public and very detailed in how we think about evolving the platform and leveraging our core competencies to be continuously more meaningful to the market. We like to think about it, and this is a common term, as sort of expanding and enhancing our strategic moat. As Rick alluded to, the 25 year history of the firm is extremely meaningful. As Chris mentioned, the 10-year head start that we have in terms of having built the mortgage banking business into what it is today, have given us an extremely valuable strategic moat. And the task in front of us has been and will continue to be how do we expand that within the boundaries of our core competencies, which from our perspective, is housing credit, structuring, the ability to understand and analyze counterparties, and again, just being very, very strong on credit and sticking to our knitting in that regard. And so that's -- when you think about the rest of the morning, think about that string throughout what we're saying, because it really is about expanding that moat and ultimately from that expansion, driving more durable cash flows and being in markets and in areas that we can put our capital to work most accretively.

So that meant a few things, and we've begun executing on this in earnest, really, over the past year or so. The first thing is deepening our partnerships. So obviously, for years, the mortgage banking business has been an incredible strategic advantage for us because of its ability to source assets and the ability it creates for us to customize investments, sell cash flows that others are better holders of and keep the cash flows that we are better holders of. If you expand that thinking a bit, what we have been working on in earnest is really expanding other partnerships within the market and there's a couple of examples here. What Bo will go through in more detail is what the power of those partnerships represents. It allows us access to investments that our peers simply can't source by looking at screens, which we feel adds significant alpha to the book and allow us to continue to invest within our risk tolerances in an accretive way. Two good examples of that are the Freddie Mac program, where we've been very active investors across single and multifamily, as well as investments that we have made with some of our partners in the origination and servicing space, where we have provided more rifle shot targeted capital to them, which in and of themselves have been great investments that have also allowed us to deepen those partnerships and source other investments along the way.

Chris touched on mortgage banking, and obviously, the continued innovation there and we'll hear more from Matt Tomiak to close out the morning on that. Redwood Choice, which is a product that we have been developing now for 3 years, continues to be a great story and really is a good microcosm of where we feel the business can continue to go. Choice was born out of observing great borrowers that were just not being efficiently financed. And now that's -- that was a $2 billion overall production product for us last year, which was up significantly over the prior year. Some more growth, notwithstanding some of the headwinds in overall mortgage production, Choice has been a great story and like I said, from our perspective, a real microcosm of what the firm can really continue to do well. And of course, the secular shifts in housing that Chris alluded to and how we've expressed that view through the partnership and the acquisition of 5 Arches as well as some other adjacent activities, which we feel will continue to bear good fruit for us in the coming years.

I'll spend a minute on the portfolio. I won't steal Bo's thunder, but a couple of key points to make here, these are charts we've shared before, but one of them shows the annual capital deployment and then breaks down the nature of that capital deployment. And these are my favorite charts because they say a couple of things. First of all, the quantum of deployment in the portfolio has gone up significantly. We close to doubled our capital deployment in 2018 versus the prior year. But the big takeaway is the amount of green in those bar charts. So over half of the $810 million of capital that we deployed last year was into what we call proprietary investments. Those are Sequoia securities, investments created by partnerships that we have, just cash flows and opportunities that our competitors can't source. And there's a significant amount of shoe leather that has gone into sourcing those things and we're thrilled with where they are. And on the capital deployment side, to the right, this is the mix of where Bo and the team deployed the capital last year and you can see the mix. Sequoia was 12%. So that was a lot of deployment. We did 12 Sequoia transactions last year. We deployed over $100 million into that program, but it was 12% of the overall deployment. And what that represents is a continued commitment to Sequoia complemented by continuing to try and diversify the investment opportunities that we see.

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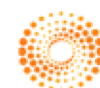

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Quickly on mortgage banking, I think there is -- there are a few key points to make here and I'll borrow from Chris's remarks for a moment. One really important thing to take away from the mortgage banking business is when the conduit, as it is currently formed, was really sort of rebuilt coming out of the crisis. The rules in private label securitization were completely unwritten. Obviously, a lot has been -- has come into play since then around ability to repay and TRID and things of that nature, which have impacted the markets in a very meaningful way, but the foundation of the business 10 years ago was really trying to create a commitment to quality control, product development and really engaging with our sellers to make sure they understood what it meant to make a loan the right way and what it meant to sell a loan to Redwood. And obviously, in the intervening years, other competitors have come, many have gone, frankly. But the bedrock of the business is the commitment to quality and the commitment to transparency, to Rick's point. And a commitment to basically teaching our partners and helping them learn what it means at Redwood to buy loans well. And that's the sort of commitment and partnership that is going to ultimately survive the cycles, wherever production volume goes, whatever the purchase and refinance mix ultimately does with interest rates. That's the sort of commitment to quality that's going to be very durable through those sorts of cycles, and so that's extremely important to us.

One other theme that I would mention is just the amount of private capital that, frankly, continues to be more and more interested in what we do well in mortgage banking. There continues to be a significant amount of private equity broadly raised in the market, I think everyone knows that. A significant amount of that, close to $0.5 trillion, is actually focused on private debt. Some of it is corporate, some of it's structured. And from our perspective, that's a market that's really coming our way. If you think about where a lot of that capital has been invested since the crisis, if people wanted to access U.S. mortgage credit, they did so through nonperforming loans, legacy servicing rights, things of that nature. Lo and behold, 10 years out of the crisis, those opportunities have started to taper off as the markets recover. And all of a sudden, what we've been doing well for 10 years is now very much in vogue. And so we are exploring actively opportunities in addition to distributing through the whole loan market like Chris touched on and of course, through Sequoia, trying to cultivate other opportunities, other pools of capital that can't do what we do, but have a very robust demand for the risk that we can source. And so from our perspective, that's an incredible opportunity, from a profitability perspective, as well as from a capital efficiency perspective, how quickly we can sell loans, and ultimately, the cost to produce those loans, we think there's significant tailwind at our back from that perspective.

One other remark on mortgage banking, which picks up on something that Chris said as well, that from a securitization perspective, our foothold is extremely strong. Chris talked through some of the qualitative reasons for that. Most specifically, the focus that we have on making sure that we have a durable program, not always trying to get the last tick out of every transaction and this chart really represents the outcome of that. So this chart represents the cumulative prime and expanded prime securitization since the crisis. So we're at the top. The depositories, there's about 4 banks that have securitized jumbo loans since the crisis, and then the slew of other non-depositories that have securitized across the private label spectrum. And what you see here is that there's a very long tail in the market away from Redwood. There have been 28 issuers in the non-depository space that have done 90 deals, so call it an average of 3 to 4 per shelf. We've done 53. And actually, just passed 100, I think, since the firm was founded in '94 going past -- pre-crisis. These numbers really matter. And we're excited to share them and so because I think you -- what they really sum up is just the power of our staying power in the market, what it means to the liquidity of the bonds and the durability of the platform overall.

Now as Chris touched on, in addition to Sequoia and the jumbo business, we have spent a lot of time thinking about where is liquidity in housing moving, who are the new entrants? And as you're all aware, the housing investor has become a very important part of things, particularly over the past 5 to 7 years, and so what these charts represent is a little bit of that. Firstly, it's housing stock, as we know, is continuing to age. There's a significant delta in household formation versus housing supply. People are not moving out of their homes, rates are higher. So they're less interested in moving out of their starter home even if they need more space. So this a very important piece of things. And then secondly, with single-family rental, this continues to be, from our perspective, a very important opportunity. And on the chart to the right, you can see the yellow line. Obviously, it has gone up significantly and starting to -- started to taper off a little bit, and one comment I would make there is a lot of -- there has been a lot of ink recently about the homeownership rate all of a sudden turning around and no one is renting anymore. And from our perspective, to piggyback Chris's comment, if homeownership goes up a bit, that's fine, but rental demand and homeownership rate are not mutually exclusive, particularly when you think about, again, the pace of household formation versus the actual amount of housing supply. There is a need for housing in this market, particularly starter homes. Bo will go through that in a little bit more detail. And so the big point here is notwithstanding where homeownership goes, the rental market and single-family, we believe, is here to stay. And we believe there's a significantly underserved cohort of borrowers that we're continuing to try and penetrate.

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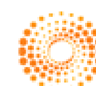

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And so of course, how are we going about doing that? As you guys are all aware, we announced 2 weeks ago that we had closed the formal acquisition of 5 Arches. We announced in January that we were intending to do so. Well, that was a big moment for Redwood and 5 Arches. Frankly, it was the culmination of over a year of working together and making sure that the 2 platforms were compatible. As you all know, being right on a housing thesis doesn't mean you're going to be right on how you approach the investment. And so we were very, very careful to make sure that we gave ourselves and frankly, the 5 Arches folks, the time to make sure that this was going to work; to Rick's point, that there was cultural alignment. Those are the sorts of things that even if you get the strategy right, it could ultimately derail the actual execution. And so we took a 20% stake in the business, as most of you know, in May and gave ourselves a year, and frankly, took the better part of that year, to make sure that this was the right move for us. And we obviously feel it was, and we're thrilled that we've completed the transaction and are excited to move forward. What this chart really represents is a few different things. First of all, the overlap between the businesses, the strength of the credit culture, the maturity of both of our operating platforms and the market footprint that we feel complement each other very, very well. But there were also -- this is -- we consider this a highly strategic transaction. There were things that we brought to the table, obviously, the Sequoia brand, Redwood's brand in the market broadly as a securitizer and an issuer was very important. That's not something that 5 Arches currently has. Our correspondent platform, we buy jumbo loans from over 180 different sellers across the country. That's a skill set that we feel can be overlaid on top of some of the products that 5 Arches brings to the table. Then of course, what are we getting? We're getting a significant footprint, an established footprint, in an area that we were not in before. The ability to generate product and generate fees and business purpose lending is something that, that platform has been doing for about 6 years, as well as direct loan administration. These loans are a little bit different than consumer loans. They require a little bit more ongoing work in terms of draws and handling borrower needs and that is also a competency that we're getting as part of the platform. So we're very excited about it. Again, as Rick alluded to, there's overlap where it's important to have overlap and there's strategy and synergy as well. So we're very -- we're very, very thrilled that this transaction is closed and excited to move forward.

From a future state perspective, I think there is a lot to potentially do here. From a volume perspective, we've said this -- we put out a deck when we announced the acquisition. 5 Arches produced about $850 million of loans in 2018, we expect that to be between $900 million and $1 billion in 2019. A mix of the shorter-term bridge products as well as single-family rental. That in and of itself is a great business, but where we ultimately see the potential real future of this is frankly, analogous to how we run the current jumbo business today. So if this chart looks similar to the way the mortgage banking business works and fits into Redwood broadly, it should, because this is a very similar road map to what we are hoping to achieve here. We have the direct origination, we're exploring opportunities to source these sorts of loans from third parties, overlay all of the existing core competencies and again, maintain the distribution flexibility that we have in mortgage banking, either by producing investments for the portfolio or being able to continue to generate fee-based activities through asset management, whole loan sales, et cetera.

I'll close with a couple of slides. Underpinning all of this, as Chris said, is the continued culture of risk management. From our perspective, the bedrock hasn't changed, as Chris alluded to. The things that have kept the company successful and going for 25 years are not going to change. But that said, whenever you're do -- doing as much new and different initiatives as we are, risk management is something that you're supposed to constantly probe and should evolve, in terms of how you think about it and the efficacy of your risk management framework and how effective it is to the current business model. And so here there's a few things, controlling production quality, from our perspective at this point in the market, is critically important. We talked a year ago about our access to investments when investing is constrained as being very valuable. Think about where the markets are today, the ability to directly control production quality, we think, is at a premium and we're thrilled to have 5 Arches on board complementing our conduit to continue to be able to do that. Centralized decision-making, to the extent we're in more businesses to make sure we are completely in sync and decisions made in one part of the firm are consistent, either qualitatively or quantitatively, with other parts of the firm. The next few, financially, obviously, rigorous liquidity management has been the hallmark of the firm for 25 years. It's a large part of what got the firm through the tough times in '08 and '09. Of course, modest financial leverage, Collin will get into that more in a moment. And again, to piggyback Rick's comment, a continued commitment to being transparent and continue to maintain the culture of integrity and openness and honesty that has been a hallmark of the firm for 25 years.

And I'll close with this slide. This is, we were having dinner with one of our investors last night, or a couple of them, and the term that we talked about was virtuous cycle. How do we ultimately continue this momentum and really build on what we've been doing? And so from our perspective, the left-hand column are things that are already well underway and continuing to evolve. It's the diversification of the portfolios, as Bo will allude to. The expansion of some of the capital-light and fee-based opportunities that we've begun to do more of in earnest, and of course, beginning to scale the platform. Obviously, we've raised capital over the past 6 months or so. We feel like we've done so effectively and we continue -- we feel like we continue to do so accretively with the opportunities in front of us. And ultimately, what that, we hope that leads to over time is continued

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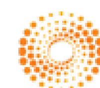

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growth of earnings and book value, as we continue to invest accretively, grow the platform, and realize a lot of the operating leverage that we feel is still embedded in the business. So that concludes my remarks. I appreciate, again, everyone coming and spending their morning with us. I'm going to turn it over to Gar Kanouse, who runs our residential banking platform and he's going to spend some time with one of our co-founders, Doug Hansen.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

Thank you, Dash. Good morning, everyone. As Dash said, I'm Gar Kanouse, I do manage our mortgage banking business at Redwood. I have the distinct honor of sitting here with one of our co-founders, Doug Hansen, today. Doug Hansen, back in 1994, founded Redwood Trust, along with George Bull. Today, Doug is still involved as a member of our Board of Directors. So when he has time to focus, when he's not on the beach in Southern California or skiing out in Austria, if that's right, next week, good. So we thought we'd have an opportunity just to kind of pick Doug's brain today and give you some insight into where his head was when they founded the company. So let's start there, Doug. What was the business opportunity or the void in the market, that you guys saw that convinced you that Redwood Trust was a good idea?

Douglas B. Hansen

Well, first of all, Gar, thank you for inviting me. This is fun for me. I've been involved with Redwood since the beginning, but at a much lesser level, so it's kind of fun to be a little bit more official at this point. So the void in the market that we saw. So in 1989, '90, '91, that era, George Bull and I had a consulting firm where we worked on turning around failed insurance companies and also advised banks on their asset liability management and on management of their mortgage portfolios. And in 1988, was the first -- when securitization first came into the market and the idea of what securitization was and knowledge of what it was spread very slowly. But we were near at the beginning of it, because we were helping our banks decide how to manage their mortgage portfolios and one topic du jour was, well, should we -- what is securitization and can we -- should we securitize our loans and what would that look like from an economic perspective and accounting perspective and asset liability perspective and then how would we actually do that? So George and I became fairly versed in this new growing thing. And some of our clients, it looked like they probably should securitize their loans. So we helped them get ready for that and we went to Wall Street and said, "Hey, we would like to do a securitization." And the response we got from everybody was the same. It was, "We would love to do securitization, and we can definitely place the investment-grade bonds, but for the B-Pieces, the credit enhancement pieces, we don't have any buyers for that. Nobody knows what it is. So if you guys can place the B-Pieces, we'll be happy to do the securitization for you." We're like, "Well, come on, isn't that your job?" But anyway, that was the reality. And so we were stymied and when we were running our models, we kept looking at the B-Pieces, which were much bigger in those days than they are now, because the rating agencies were just getting used to this idea. We kept saying, "Well, we would like to buy these for our own account." Because these looked like great investments, we can't figure why nobody wants them. But we didn't have $2 million or $5 million, whatever, to invest in securitization. So we decided that this was going to be a wave of the future. And that we would start a hedge fund to buy these B-Pieces, because they were going to kick off good returns. And hedge funds were, back then, like they are today, it wasn't a new concept, but it was -- not everybody knew what hedge funds were. So we started -- we drew up all the hedge funds documents and we were sitting late one night with our lawyer, and he looked up and he said, "You know, look, why don't you guys be a REIT instead of a hedge fund?" We were like, "A REIT, are you kidding me? We don't even know what that is." Or we thought REITs invested in buildings. These aren't buildings. He said, "No, no, I was involved in the original REIT legislation, blah blah blah, and REITs can own mortgages and mortgage securities." And so we quickly figured out that, that was actually a better structure for investing in these B-Pieces because the B-Pieces are completely illiquid and it's best to have permanent capital that you would have in a REIT. So we re-did all our documents, our business plan, we figured out that we needed $25 million to start the company, and we went on the road and we tried to explain to everybody that we were going to be kind of like a savings and loan, or kind of like a Fannie Mae or Freddie Mac and kind of like a bank, doing this new thing, securitization, owning these things that nobody wants. And the people who understood it were public market investors in savings and loan stocks, bank stocks, they got it. But they didn't have any money to invest in a private placement. And then the private placement people had never seen anything like this and didn't want to touch it with a 10-foot pole. So we didn't know quite what to do, and we talked to Joe Jolson at Montgomery Partners, who was a savings and loan analyst at the time. He said, "I totally get this, I'm going to help you make this work." So he was really instrumental in introducing us to people and helping us push the idea. Then after 2 years of trying, we finally got $25 million together and we closed. And then from there, it worked great. We were buying B-Pieces and making money and it was all -- worked out as forecast, so we were lucky enough to be able to go public a year later in 1995 and raise enough money to really get the company going.

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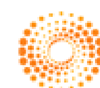

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Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

We did a lot of different things between kind of going public and obviously the financial crisis, but the majority of it was really based around that strategy of investing in B-Pieces, right, really investing in what we create.

Douglas B. Hansen

Right. We did have a -- I don't think many people know this, we did have a portfolio of Fannie Mae and Freddie Mac securities on repo, similar to what other mortgage REITs have done at the beginning to help employ our capital and that worked out well, but as we got more and more into credit in different ways, we decided that it was incompatible to have the large leverage of a sort of a standard mortgage REIT, if you like, combined with concentrated credit risk. So even though it was prime credit risk and the chances of it blowing up were not as big as say, a lot of other credit investments, we didn't want to combine leverage with credit risk. So we abandoned that business and we've done a number of things over the years, but the idea of investing in prime residential credit, and also the idea of acting like Fannie Mae and Freddie Mac, where we'll help mortgage originators with their business by giving them quotes on a loan-by-loan basis, to take in loans using software, so that they can manage their business and we can bring in loans as a wholesaler and securitize them or sell them as whole loans, that's always been there.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

Yes. And still here, today, obviously. And you know the investments in the prime subordinates are still a kind of a foundation of the portfolio, but the portfolio composition has changed quite a bit, as you saw from Dash's presentation earlier, and Bo will speak to a little bit more later. But looking back, what was your vision for what Redwood would look like in the long term? When you started the company, I know you saw the opportunity out there, you knew where you could put capital to work accretively and fast, but long term, what did you think Redwood would be back then?

Douglas B. Hansen

Well, first of all, we didn't have any idea it would become a big -- well, not a large public company, but a company that would -- reasonable size with so many employees and so many assets and capital. We didn't -- that wasn't our vision. We -- I like to say that we were lifestyle entrepreneurs. So our goal was to start a company so we could have a great life, live in Mill Valley, raise our kids, have fun, work with people that we wanted to work with, and in an organization that we were proud of. So the fact that it became -- lasted 25 years and got to billions of dollars of assets, that wasn't necessarily in our vision, it wasn't contrary to it, but that wasn't what we were looking for. I think that we've always felt, at the core, that we're essentially a private market, Fannie Mae or Freddie Mac and that over time, we would hope to dominate the portion of the market that they didn't control and hopefully, that, that portion of the market would get bigger. Obviously, with the crisis, it got smaller, but in the future, that gives us a big opportunity to grow, if that changes back.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

Definitely. You guys -- I know talking with both you and George, obviously, a big part of what you envisioned was creating a great culture, a culture where people wanted to come to work. We added value for our shareholders, and ultimately, it just felt a little bit more like -- than just a job. But what is it when you guys sat down, how would you describe the culture that you wanted to create within Redwood Trust?

Douglas B. Hansen

Well, I have to give huge credit to George for this. He was really the one who articulated the idea of culture, tried to define it and embedded it in the organization, which he has done a fantastic job. I would say it really didn't come from a vision at the beginning. We didn't sit down and say, "This is how we want our culture to be." We just ran it the way we were. And we wanted to work for an organization that we wanted to work for. And we want everybody to feel that we treated them as we would wanted to have been treated ourselves. We wanted to have fun. We wanted to

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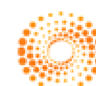

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work hard and be successful but not play games with people. We weren't trying to maximize every dollar or anything like that. We didn't want to have -- we didn't really suffer people who didn't perform very well. And I think it's one thing we did, is we weeded people out fairly quickly. We gave them a chance or two, helped them, coached them. If that didn't work, they had to go and that was very helpful for keeping the people who were good at their jobs happy, because everybody knew that all the other team members were pulling on their oars and able to do so. And it was just fun to be around a bunch of people who were highly motivated and had good values. And it's really about values and I think that's one of the things I'm proud of, to see that we're still, obviously, every day, dealing with the strong values, and that's what we started off with.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

Yes. And a lot of those thoughts that you just articulated are the basis of how we're thinking about culture today and we'll hear from Sasha a little bit later on regarding her efforts on kind of furthering that cultural development at Redwood. But I can tell you, it does feel quite a bit today like it did back then that everybody has just bought in, right? And when I joined in '05, that was one of the first things that I noticed, is that it felt like everyone that was there, or most of the people that were there, had bought into this idea of creating a really good culture. So it was a fun place to work, that's for sure. So just -- we've got a couple of minutes left, but I think, you know, it would be interesting to hear, and we talked a little bit about this earlier, other than hiring me, what is the thing, the one thing at Redwood Trust that you can point to that you're the most proud of?

Douglas B. Hansen

Let's see, that certainly was the thing that would come first to my mind.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

I just wanted to take it off the table.

Douglas B. Hansen

The thing that I'm most proud of, that was the question. Well, first of all, that we're here for 25 years and still kicking, that's really good. And I think that the culture is still here. I mentioned that. That's pretty gratifying. I think what we -- one of the hardest things for any organization to do is to outlive its founders, and so I feel very, very proud that we have an organization that not only has had 1 management transition, but 2 successful management transitions. And I couldn't be more happy with the current administration and where they're headed, and it's a big part of my net worth, and so I'm very happy to be involved in that. And I think that there's a lot of people can -- not everybody can start a company, but even fewer companies can move beyond their founders and still be successful.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

And we obviously survived a fairly turbulent time through the financial crisis. Just to close, what do you think, what was it? How were we able to get through and so many of our competitors and peers went away?

Douglas B. Hansen

Well, I think it's in part because we invest in high-quality assets. But at the time, we did have lower-quality assets. We had Alt-A assets, we had neg am ARMs, we had some subprime securities. And so what really differentiated us, I think, was the structure of our balance sheet. So most of our obligations were securitized. So that meant that it was off -- it wasn't direct liability to Redwood Trust if there was a problem. And then with respect to the actual real leverage we had on our balance sheet as opposed to sort of the fake leverage that looks like on GAAP, we were very low leverage. And we also, and I have to give most of the credit to Marty Hughes for this, we anticipated that there was going to be a big problem and we cut back and sold a lot of assets, which tanked our stock at the time and people said, "Why are you cutting back, why are you paying off your debt?"

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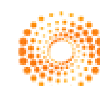

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And we said, "Well, we don't think -- we think that things are not going to be that good going forward." And they were, "Well, what do you mean, what's going to happen?" And we were like, "We don't know, but we don't think it's going to be good." So when it hit, we suffered a lot of credit losses, but we never had any liquidity problems and we were able to grow out of that.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

But not as many credit losses as we would have had, had we not sold that portfolio?

Douglas B. Hansen

True.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

Well, good. Well, thank you very much for your time, Doug. It's been a pleasure speaking with you up here. Hopefully, you enjoyed it.

Douglas B. Hansen

I did.

Garnet W. Kanouse - *Redwood Trust, Inc. - MD & Head of Residential*

And I will turn it over to Lisa, who I believe is going to take it from here.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

I invite Chris and Dash to come up and (inaudible) has got a handheld mic, the mic around to...

(technical difficulty)

QUESTIONS AND ANSWERS

Unidentified Analyst

Yes. How would you describe the credit quality of the 5 Arches loan product?

Dashiell I. Robinson - *Redwood Trust, Inc. - President*

Well, we think it's very strong. The underwriting approach in what we call the business purpose lending space is fairly different than with -- on the consumer side with jumbo. You're underwriting more of a business plan than an actual consumer, per se. And so you're looking at different things, you're looking at track record, overall liquidity, the ability to continue executing, particularly on the shorter-term bridge, where you're underwriting a business plan, the ability for that particular investor or developer to get out of the project in a timely period of time and with profitability. So it's important to look at those things upfront, which is very, very different than on the consumer side. On the single-family rental, we have spent a lot of time developing our underwriting guidelines there over the past year. And again, it's partly track record. We're careful on both asset types not to lend to investors who have just started 6 or 12 months ago. So there's a certain track record and a certain portfolio size that are important to us.

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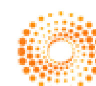

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But also, particularly on the single-family rental side, it's cash flow coverage. It's really understanding what the market rents look like, understanding the relationship between in-place rents and market rents, being rigorous in terms of underwriting costs and things of that nature and making sure that the loan carries well with the net cash flow of the investment. So it's a different underwrite. At the end of the day, the quality of the borrower needs to be high, but it's a different approach than what we have done historically, and they have, from our perspective, done a very nice job building that out over the past 6 years.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Bose George from KBW. Can you just talk about the competitive landscape for the non-QM product? Seems like there's already a lot of lenders are getting active in that market. How is it impacting profitability? Anything you're seeing on the credit side there?

Dashiell I. Robinson - *Redwood Trust, Inc. - President*

Sure. So as I alluded to on one of the slides, there's clearly an increasing number of entrants into that space. I think one of the things that we try and do is really differentiate what non-QM means at Redwood. As you well know, and others, a few years ago, non-QM became a defined term with the ability to repay rules, but there's many ways to have a non-QM investing strategy. Our non-QM products are about 1/3 of our choice production, they're largely higher debt-to-income loans, things of that nature, which are very, very different from alt doc loans, which a lot of other folks are buying, bank statement type lending, things of that nature. So the first thing, Bose, to sort of emphasize is non-QM means a lot of different things, and the team here has been extremely diligent about differentiating what non-QM means at Redwood from an underwriting rigor perspective and trying to differentiate the fact that all non-QMs are certainly not created equal. That said, there are more issuers in the space, but we think the Choice product sort of fits a niche that's still very much valued in the market. Our margins there continue to be strong. So we see good momentum there. The Choice loans are about 75 or so basis points in coupon above Select, and we see some competition there, but frankly, most of the completion in non-QM comes from platforms that are more PE sponsored and have needed coupons in the 6% or 7% range to make their returns work. And so while we see sort of the upper crust of their production start to compete a little bit with Choice, it's less than you otherwise might think because they still think we're operating in an area that has less competition. And you think that coupon in the mid-5%, what borrower that's serving, there's still an underserved borrower there, versus where a lot of the capital has migrated to, which is up in coupon and just a fundamental different underwriting quality from our perspective than where we focus.

Christopher J. Abate - *Redwood Trust, Inc. - CEO & Director*

Yes, I would just like to remark again on the -- what I like to refer to as the marginal buyer in housing. And sometimes we'll use an analogy, take Yankees tickets or any sports tickets, and you look at what's happened with the price of going to a baseball game over the past few years, and it's basically skyrocketed. And the reason is not because more fans are attending, it's because corporations are buying the tickets, they're the marginal buyer. And what you're starting to see in housing is just more and more investors competing for homes. So when you think about if you're in an area where there's a lot of investors, if you're really reaching for an affordability product, it's tough competition, and in many cases, as I said earlier, we'd rather be financing the investor with a much stronger credit profile than looking to make loans more affordable, high coupon loans that, in my opinion, would be substantially riskier. So again, it's not to say that either one is good or bad, but I think we're really happy with the risk profile of what we're seeing in the single-family rental space.

Unidentified Analyst

Can you talk about how you're thinking about managing capital? And how much the need for additional capital kind of given the goal of kind of continuing to build and enhance scale?

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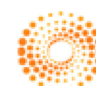

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Christopher J. Abate - *Redwood Trust, Inc. - CEO & Director*

Yes, we've -- we raised capital in January. At this point, we've -- consistent with what we said, I think on the last call, we feel like we're well-capitalized. We're much more focused today on growing our asset base than our capital base. So we're actively looking at different ways of -- or different forms of capital, I should say, whether it be converts or it be even potentially third-party money. 5 Arches runs a nice asset management platform. But there are certain things that we have the capability to source that don't necessarily meet our internal hurdle requirements, which have been going up. So I think the capital situation remains fluid. At this point, our goal is to continue to find ways to be efficient and look at some other forms before we look at equity. The one thing I will say and something that did drive our thinking in January is right back to that preservation line, and we were starting to push on our comfort level with leverage. We were approaching, I think at the time, close to 4x leverage, non-recourse leverage as a firm. So when it comes to the safeguards and running the business safely, we'll always think about, do we have the right mix of equity versus debt? But at this point, we feel really, really good about our capital position and our leverage.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

We have one more here from Stephen Laws before we go into break.

Stephen Albert Laws - *Raymond James & Associates, Inc., Research Division - Research Analyst*

Can you talk -- historically, you've really stayed away from recourse -- excuse me, recourse financing on permanent investments. Can you talk about the opportunities for non-recourse financing for the business purpose in non-QM and what you're seeing on that front?

Dashiell I. Robinson - *Redwood Trust, Inc. - President*

Sure. I can take that. So the non-QM securitization market has matured significantly. So we securitized our Choice loans for the first time in September of '17 and we've done 6 or 7 Choice transactions since then and the market acceptance there has -- has really become much more robust as folks have obviously gotten continuously comfortable with credit as well as the convexity and prepaid speeds of those sorts of borrowers. So that's maturing. The business purpose space, there's a lot of options, which we're exploring. We currently finance the investments that we have with more traditional repurchase facilities. But a couple of things have emerged there. We've talked on earnings calls before about the emergence of securitization markets, particularly for the shorter-term bridge loans. There was just another one completed this week. And so we're very optimistic about the opportunity to again, as I mentioned earlier, sort of allow for our brand to be portable to those new opportunities away from or in addition to jumbo and leverage that competency within BPL securitizations. The single-family rental loans have been securitized in rated form for a number of years. So that's a fairly efficient and well-known market. At this point, there's not a lot of volume, but there's methodologies and there's a pretty deep buyer base. The other element that's emerging is more sort of private opportunities. There's a significant amount, like I mentioned earlier, of private capital outside of the more public rated securitization markets that has an interest in taking exposure here, either as a whole loan owner or a financier. And so we're exploring that as well because what we're finding is that the cost of funds there, particularly when you net out the time of an expensive rate agency cost and things of that nature, is actually looking fairly compelling. So there's more to come there, but that's another sleeve, particularly within the business purpose lending space that we think can hopefully be helpful for us.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

Thank you. We're going to take a 5-minute break, and then we'll welcome you back at about 10 after 10.

(Break)

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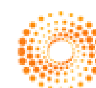

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PRESENTATION

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

Welcome back. I'd like to invite people back into the room. We're going to get started for our second session, starting with Bo, who's going to walk through our investment portfolio. And welcome people back on to the webcast as well.

So we're heading into our second session today. As I pointed out at the beginning, we're going to have Bo Stern, followed by Collin Cochrane. There are a couple of items on your tables and people have been asking me what is this little white cap that's on top of this notebook and this is a webcam cover. So you can do away with a post-it note that you put on top of your camera on your laptop and put that on there and you've got a little slider there. So that's what that is, if you would like to have it, it's pretty convenient. So Bo, I'm going to turn it over to you.

Shoshone A. Stern - *Redwood Trust, Inc. - CIO*

Thank you, Lisa. Welcome back from the break. My name is Bo Stern, I am the CIO of Redwood Trust. It's funny, because when I'm in the Bay Area, and I tell people I'm the CIO, I get a lot of blockchain questions and people asking me if I can help them with their network problems, and it doesn't go too well. But anyway, I'm excited to be here for the second time, it's our second annual Investor Day.

So despite what you see on TV and what you may be reading in the housing blogs, the housing market is not headed for impending doom. Though if you're a real estate agent, a homebuilder, a loan originator, it may feel that way. At Redwood, we aren't trying to sell homes, we aren't trying to build houses and we aren't originating loans. We're focused on making full cycle credit investments that provide long-term and durable cash flows. We think now it's -- we think now, obviously, it's still a great time to take credit investment -- to take risk on the credit investment side. Worked, great. There's been a lot of news on HPA and while undoubtedly HPA is slowing, credit has historically performed well, even with just 2% to 3% home price growth annually. The main driver of credit performance for our book is really the economy. When people have jobs, when wage growth is growing, people pay their mortgage bills. It's as simple as that. For the borrowers that we target, prime borrowers who are affluent and even just in general, people pay their mortgage bills first. It's one of the high, very high priorities. You can do without -- some people can do without their big-screen TVs, but you've got to live somewhere. So that's been, throughout history, that's been a tried and true mantra of ours.

We don't expect uniform performance across the country in terms of credit. Many of the previous hottest markets have been laggards recently. We think specific housing markets will require much closer inspection than in the recent past. Memories of the housing crisis have been slow to fade for mortgage investors. Even with the recent increase in LTVs and DTIs, today's underwriting box is far superior and tighter to previous pre-crisis days. Speculation levels and animal spirits are much lower in contrast to other asset classes, such as student loans and corporates. Riskier mortgages, like negative amortization loans, like subprime teasers, have disappeared. There's still a lot of good borrowers who can't get good mortgage rates today. That was part of our rationale for creating the Choice program. And from the results, which I'm happy to report, we have had 0 losses in the Choice program since inception. We've only had 4 losses in our post-crisis securitization Select platform as well. So credit has been fantastic.

Though delayed compared to previous generations, millennials are getting married, they are having kids. Increasingly, although maybe not fast enough for their parents, they are moving out of the basement and looking for their own homes. Due to nothing other than demographics, we expect the surge in housing formation to continue for the next couple of years. And specifically what I'm talking about, if you look at the chart in front of you, the line represents annual new households and the bars represent housing supply. I think one of the things that you'll notice is after the crisis, there's a large mismatch between those 2 numbers. If you look pre-crisis, even though in given years, they can be -- the series is quite volatile, pre-crisis, they average out to pretty close, which make sense. When you have new household formation, you need new housing units to be built. Post-crisis, there's been a permanent gap in that supply. That's been a big issue. This is really the tailwind at the housing credit investors' back. I'll do the math for you. The mismatch of about 4 million units over the last 8 to 9 years, in terms of household formation and what the U.S. has actually supplied in housing units. Unfortunately, we don't see that changing -- unfortunately for society, we don't see that changing anytime soon. The U.S. just isn't building enough housing units. As a result, vacancy rates are now at levels last seen in the 1970s. This includes ownership housing as well as rental housing. What's unique about the '70s and early '80s is that's when baby boomers were in their '20s and '30s, they were getting married, they were having kids. So you can see the effect of -- demographics has on -- it's, of course, indirect, but even on our investment portfolio today.

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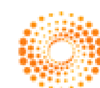

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As I mentioned, this is a huge tailwind at our back and forms the underlying thesis for a lot of our credit investments. Millennials aren't moving into the biggest houses on the block, nor in the most expensive Manhattan apartments Midtown. But homebuilders are still primarily building higher-priced homes. Since homebuilders aren't building cheap housing due to various reasons, regulation, our national immigration policies and other reasons, the housing shortage is most acute at the starter home level. We think this trend will continue. As a result, the strongest HPA growth has been the lowest-priced tier of housing. The strongest rental growth has been the lowest price point in apartments, both -- and single-family rentals. As I mentioned, we think that's going to continue and you'll see that come through in some of the investments that I'll talk about later, about how we're positioning the investment portfolio.

All right, the good stuff, the numbers. We're looking for investment opportunities where our capital is needed, meaningful and impactful. While we can be the 25th bidder on some commoditized investment, we add the most value to counterparties where they have few bidders, either because of complexity or illiquidity. For taking on this complexity and illiquidity, we get paid a yield premium. That's the whole -- that is the underlying thesis of the portfolio. Increasingly, these areas are away from jumbo prime, in areas that are, you can see up there, in bold and italicized. Each of the bold and italicized numbers represented 0 capital for us deployed 5 years ago. So if you do a quick tally, it's not only significant, it's close to 40% of the portfolio is in areas where we had 0 investment 5 years ago.

One question I get asked, we get asked a lot is, why now, why are you doing this now? And the reasons vary. Sometimes the product didn't exist 5 years ago. For example, CRT, that came into existence recently. Other times it's about finding the right partner, as Dash talked about with 5 Arches. Sometimes it's waiting for certain product maturity or the product to reach certain milestones. The reasons vary, but they all represent additional ways for us to take housing credit risks and we're excited about them. Just to be clear, while we still really like and love the jumbo fundamentals, the yields aren't what they used to be. As Chris alluded to, jumbo is graduating to its pre-crisis roots, becoming more commoditized. When something becomes more commoditized, the premium that you get paid for taking that risk decreases, and that's what we've seen with jumbo. If there was a market disruption and yields widened out, we would not hesitate to add aggressively.

I don't think people have seen this chart yet. This is a little different than what we've published in the Redwood Review. This is our most recent capital deployment, where we're going, which took the last 6 months of 2018. The largest slices are the fastest-growing part of the portfolio. We expect that they, along with single-family bridge, will continue to fuel portfolio growth in 2019. I'm going to just talk about a couple of these for a few minutes here. Multifamily has been an interesting path journey for us. So 3 years ago, we didn't have any multifamily. We went back to McLean to go talk to Freddie Mac, said, "Listen, we want to become investors. We ultimately want to buy your B-Pieces. We have a long track record with Sequoia, how do we do it?" We raised our hand, we want to get in line. They said, "No, no, no. It's not that easy. You have to lay out some plan for us and prove to us that you can be a good partner." So we said, "Okay." So 3 years ago, we started buying mezz pieces, and we've actually been one of the largest mezz -- multi-family mezz buyer that Freddie Mac has. We've gone back constantly and told them, "Look, we want to get -- we want closer to the credit." Doug talked about concentrated credit risk. That's what we want. So finally, this past year, we had a discussion with them. They said, "You know what, you guys exactly -- you laid out your plan and you have exactly adhered to it and we would love for you guys to start buying B-Pieces." So this 28% -- the 28% that we invested last year, the last 6 months, represents a mix of mezz as well as our first B-Pieces on the multifamily side. We've spent some time talking about RPL, that is represented a, almost a quarter of the investments for last year, sorry, last 6 months. This is another exciting area. Freddie Mac has various programs that we remain very active with, are one of the largest investors for this program. As I mentioned, I expect that will continue.

CRT is really interesting, it's one of the areas we're keeping our eyes open to. Obviously, as I'm sure everybody is aware, with all the noise out of Washington in terms of both a newly nominated FHFA director who has broad administrative powers to change the CRT program, as well as possible legislative changes in housing reform coming down the pipeline, this is an area where we can see significant change. On a side note, Fannie Mae late last year, restructured their CRT securities to make it much more REIT-friendly, in particular, down at the bottom of the capital structure. So that's a very exciting development. Freddie is a little behind, but they have indicated that by early second quarter, they'll be in the same place. Freddie has also started to sell what is essentially a first-loss piece on conforming credit. So CRT is rather unique, it's obviously much more public than some of these other opportunities. But it represents a really large size and it is easy to add exposure in that area very quickly.

We've talked about finding the right partner, and I had mentioned Freddie. Wherever Freddie sells credit risk, we try to get involved. That's been a great relationship and something that we hope to expand or continue to expand. By continuing to add investments that you see on this slide, we think we'll be able to scale and material increase -- materially increase the yields on the portfolio. If we execute properly, we expect that within

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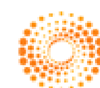

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the next 12 months, we can add 50 basis points to the normalized portfolio yield, over the next, as I mentioned, over the next year. We've constructed our portfolio to accept higher complexity, less liquidity and higher credit risk for lower leverage and specifically, less repo debt than our competitors. It's a trade-off that we've been making for 25 years and we expect through a full cycle, be confident will lead to attractive risk-adjusted returns and good performance relative to our peers. So with that, I'm going to turn it over to Collin Cochrane, our CFO. Collin?

Collin Lee Cochrane - *Redwood Trust, Inc. - CFO*

Good morning, everyone. My name is Collin Cochrane, I am Redwood's Chief Financial Officer. And today, I'm going to be discussing what we do to focus on delivering shareholder value. I'm going to start with a quick review of our 2018 financial results, and then I'm going to talk about some of the things that differentiate us from many of our peers. And then I'm going to finish by going through the areas that we're focused on to drive profitable growth moving forward.

So 2018 was a productive year for Redwood. Through portfolio optimization and the capital that we raised in July, we're able to achieve record capital deployment. And with strong earnings from our mortgage banking portfolio, we're able to drive a meaningful increase in core earnings. Our GAAP income was impacted by the volatility in the fourth quarter, but the impact of our portfolio and from the flattening of the yield curve throughout the year was much more moderate for us than it was for many of our competitors. If you look at the chart on the lower left, which shows book value total shareholder return, which I'm sure you're familiar with, and takes our dividend and the change in our book value, you can see that we strongly outperformed the rest of the sector. And we think this is one of the key metrics, that we focus on anyway, when we think about how mortgage REITs should be evaluated. I'm going to talk about that a little bit later.

So overall, we had a very productive year, with strong operational metrics that drove solid returns for shareholders.

So moving on, I'm going to review some of the things that makes us different and differentiates us from others in our sector. First, as others have talked about, we're the only mortgage REIT that is -- has a portfolio that's exclusively focused on residential credit and that now invests across the full housing spectrum. And additionally, being focused on credit risk, we try to minimize our interest rate risk, and we're generally much less sensitive to rate changes than many others in our sector. And in addition to our investment portfolio, we have our mortgage banking portfolio, which provides a diversified source of revenue and also allows us to create investments for our own portfolio.

And as Dash discussed, moving forward, once we add 5 Arches into the mix, similar to our mortgage banking portfolio, we'll have another platform that will deliver fee income and be able to produce investments for our portfolio as well, associated with business purpose loans.

The last thing I want to touch on here is how we make money and try to simplify it a little bit, because sometimes we hear from people that our business is complex. And obviously, there's aspects of it that when you get down into the weeds that can be complex. But at a very high level, we think about it in pretty simple terms. First, it's how we allocate our capital, the returns that we can generate on that capital and how efficiently we can run our business. As you see here, the majority of our capital is allocated to our investment portfolio. And in 2018, we generated a 10% return on equity here. That was obviously pretty significantly impacted by the volatility in the fourth quarter, but if you take out the impact from the fourth quarter, but you also take out the benefit from spread tightening throughout the rest of the year, so just eliminating all the market value adjustments, we would have generated about 11.5% return on this portfolio.

Moving down, we have our mortgage banking business, which last year, we allocated about $200 million to, and we saw very strong returns in this business. And then the corporate line item at the bottom, what's in this number essentially represents our corporate overhead. We take the direct operating expenses for each of our business segments, and those get allocated up into the lines up above, and we also take our corporate debt cost and that gets allocated to our investment portfolio and is reflected down in the ROE. So what we're left with here is really our overhead. And when you look at that as a percentage of equity, that represents a measure of our operating efficiency. And I'm going to talk a little bit more about this in a moment.

So moving on, another thing that differentiates us from our peers is our leverage profile. As others have talked about, in general, we run our business with lower overall leverage and with more longer-term debt. And for us, that's comprised of our borrowings from the Federal Home Loan Bank and also our convertible bonds. On the far left side of the chart, what we did here is break down the leverage in the different parts of our balance

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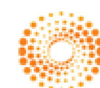

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sheet. On the far left, we have mortgage banking, and this does run at slightly higher leverage, but these are much more liquid loans and they move through our balance sheet much more quickly. When we move over to the portfolio side, and that's really the 2 bars in green there, the majority of our capital is allocated to our securities portfolio, and that's where we do use some repo debt, but we generally try to use that much more judiciously, and when you see in the chart here, we actually have that portfolio less than 1x levered. And while we do have a bit higher leverage on our FHLB portfolio, that is longer-term debt, with about 7 years term. And so it's a much lower risk profile. And the remainder of our debt is comprised of our corporate convertible bonds.

The last thing I want to touch on a little bit that differentiates us is the book value TSR. As I mentioned earlier, we think that this is the key metric to look at when evaluating the performance of mortgage REITs. And in the chart, the green bar shows the average dividend yield over the last 5 years and the blue bars represent the 5-year book value TSR. And as I'm sure you're aware, our dividend yield is a bit lower than others in our sector, and we attribute this primarily to the fact that we use lower leverage and the fact that we generate a meaningful amount of income at our TRS, which we're able to retain and reinvest.

And while companies can generally generate higher returns with higher leverage, this also contributes to more book value volatility. And TSR -- book value TSR capture these changes, whether that book value volatility runs through the P&L, which it does for us, or if it runs through the balance sheet, which it does for many others in our sector. And so as the chart shows, when you combine the dividends with the changes in the book value, we've actually outperformed our peers over the long term.

So next, I'm going to spend a little time going over some of the areas that we're focused on that are key to us growing profitability into the future. First is deploying more capital into portfolio investments at accretive returns, improving our mortgage banking capital efficiency and finally, scaling our business to unlock operating leverage and drive profitability.

So I'll start with opportunities in the investment portfolio. A moment ago, Bo went through the investment portfolio in detail and highlighted where we've been deploying capital recently and where we see future opportunities. He also outlined some of the return ranges for these opportunities, which in general are above our current weighted average yield in our portfolio, and in some cases, meaningfully higher. And as such, as we continue to deploy capital into these new opportunities, we expect to see our weighted average returns increase, which is obviously going to benefit our bottom line.

And in the table here, we framed out the benefit that we could expect to see from raising the weighted average portfolio yield 50 basis points. And this level of improvement, as Bo mentioned, is something we think we can achieve this year as we continue to optimize the portfolio and believe it can continue to improve further into the future. So based on our current capital base, we estimate that this could benefit EPS by approximately $0.10 per share annually. And since interest income is a stable source of income that is earned at our REIT, as it grows, it can support higher dividends. And this table shows we have recently seen economic net interest income rise throughout the year as we've been optimizing our portfolio. And as I said, we expect this to continue to rise as we deploy additional capital into these new opportunities.

Moving on to mortgage banking. Here, as I mentioned, we're most focused on how we can utilize capital most efficiently in this business. What we're looking at is ways that we can turn capital more quickly or essentially run the same amount of volume through the business with a lower amount of capital. What we can then do is take that excess capital, redeploy it into our investment portfolio and then generate an overall higher return. And the chart runs through the math here, but in this scenario, if we're able to allocate about $50 million over, this could benefit in $0.06 of incremental earnings per share.

As we mentioned in the fourth quarter Redwood Review, at the end of the year, we actually adjusted our capital allocation to mortgage banking from about $200 million down to $170 million, and we expect to do further allocation into our investment portfolio in the near term.

The last thing I would like to touch on is operating efficiency. During 2018, we added resources that we believe put us in a position to scale the business profitably and manage significantly more capital as we move forward. We like to think about our operating expenses in 2 different buckets. First is expenses associated with our operating platforms and that is our mortgage banking business currently, and then going forward, that will also include 5 Arches. And those expenses can be more variable as they're driven by volume. And when you compare us to others in our sector,

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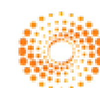

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the fact that we're running an operating business, those amounts generally are higher than when you look at the other bucket, which is our corporate overhead and the amount of overhead we are required to manage our investment portfolio.

So moving forward, we expect that our corporate overhead and our cost to run our investment portfolio should be able to remain relatively stable. And as we increase capital, the relative reduction to our operating expenses will accrue to the bottom line. And as the table shows here, we've already begun to see some improvement in this ratio late in 2018, and we expect to see further improvement from our capital raise that happened in January.

So in conclusion, we remain focused on delivering shareholder value through our unique platform that gives investors the opportunity to invest in residential mortgage credit through a platform with lower relative leverage, lower inherent volatility and diversified income streams. And as we continue to diversify our investments across the full housing spectrum, the new opportunities to deploy capital into higher-returning investments should drive higher returns and support higher dividends. And additionally, the new operating efficiencies in our mortgage banking business should drive higher turns on capital. And finally, we'll -- excuse me, continue to seek scale prudently to leverage our operating infrastructure if we believe it'll be accretive to investors.

So that concludes my presentation, and next up, we have Carlene Graham and Jon Groesbeck, who are both Managing Directors in our mortgage banking business. Thank you very much.

Jonathan Groesbeck

Good morning. My name is Jon Groesbeck. I manage Business Development for Redwood Trust, particularly as it relates to the conduit. So I manage -- overall view of the 180-plus sellers that sell to us. With me today is Carlene Graham, Managing Director and Head of all Pre-purchased Operations at Redwood. So she facilitates it all, so basically, you're the boss.

Carlene Graham

Hello.

Jonathan Groesbeck

And I have the real pleasure to have with us today David Hrobon. David is the President and CEO of Wintrust Mortgage. Wintrust Mortgage is a division of Barrington National Bank. It's 1 of 15 affiliate banks totaling around $31 billion, which is part of the Wintrust financial services company, a publically traded firm, headquarters in the Chicago area.

David has been with Wintrust since 1994 in some major key roles, and he assumed the role of President and CEO in 2007. One of the things I know very well about David is that he likes to do the right thing. And in 2017, Wintrust Mortgage made $40 million of below-market mortgage financing available for affordable housing. They did that in partnership with Habitat for Humanity in the Chicago area. David is also very involved in the MBA. He sits on one of the national governing boards. And then one of the biggest things that really is his passion is mPower, which is a program sponsored by the MBA. It really is all about promoting gender equity, equity in pay, equity in advancement for women in mortgage finance. In 2014, David received an award. It was the Chicago -- Who's Who in the Chicago real estate business, an award given to him in 2014. He was a graduate of Ohio Wesleyan college, a big Ohio State fan. And David, could you just tell everybody a little bit more about Wintrust and your involvement in mPower?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Sure. Thank you, Jon. As you mentioned, Wintrust is a community-based bank or financial services company headquartered in Chicago. Our retail banking business, our footprint is really Northeast Illinois, Southeast Wisconsin and the northwest tip of Indiana. But the rest of our financial services

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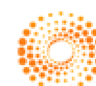

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products are nationwide in scope, including the mortgage business. Thanks for the shout out to mPower. For those of you who don't know, it was stood up about 3 years ago by Marcia Davies, who's the COO of the National Mortgage Bankers Association, really sort of emulated or it was formed out of the #MeToo movement. And she and I ran into each other just down the street here at a conference 2.5 years ago at JPMorgan Chase and we got into the conversation about mPower and what she was doing and what it stood for and why. And I was able to share with her a number of things that we've done as well and have been for a number of years and why it was important to us as an organization. And one thing led to another and she's invited me to sort of travel with her in the mPower group to talk about, as you say, ways to get to gender equity, equal opportunities for women, equal representation and certainly, most importantly, equal compensation. And there are some things that are obvious and there are some things that aren't obvious about both the opportunities and things that have stood in the way. And it's been a learning experience for us and we're looking to do more. We've just sort of scratched the surface, so to speak.

Carlene Graham

David, thank you for joining us. What's special about the relationship between Redwood and Wintrust?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Yes, it's a great question. I think the short answer is that I think that we share a number of the same core values as organizations, and we're aligned. But it sort of is deeper than that. And I think we started our relationship in 2011. And we've been in the business a long time and we came through the housing recession and weren't unscathed by it. So we were very cautious about the products that we originated and the vendors and investors that we worked with. And so while I know that you did your due diligence in evaluating us, we did the same. We're very cautious about the products that we wanted to originate. I think if you look back historically and you look at the trend summaries for homeownership rate, not only domestically but internationally in developed countries, you find this equilibrium around 67%. At the end of the housing recession, we went -- or prior to it, as you know, we were almost 70%. And so it was overheated. We've dropped down to just over 64% and climbing our way back. And we knew that certainly, there seemed to be pent-up opportunity to expand homeownership.

But having said that, probably the thing which is most obvious that we learned, and I say most obvious and it should have been obvious, is that there are clearly people out there that have an interest of the American dream. They're seduced by the opportunity of having a home, and there's toxic products out there that can enable them to do that, without either the emotional or physical capabilities of repaying that mortgage. And we learned that through the housing recession.

So the thing that really has become special for us about Redwood is that we think you guys have been always disciplined around doing the right thing and creating products that are available to the near-missed folks that are missing out on homeownership opportunity who are prepared and can show and illustrate not only the ability, but also the intent to repay their mortgage. And that's the reason why for us that the relationship is special. And it started with conversations and becoming a relationship, if you will, and I would tell you that it's turned into a partnership. And that's special for us. We've had an opportunity to co-create some unique products together, and that has helped our organization a bunch.

Carlene Graham

Thank you. What's unique about Redwood as it pertains to some of your other non-bank or banking investors?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Well, the cliché answer is the people. But it's true. When you look at the individuals that we get to interact with on a daily basis, bright, well-intentioned folks that are committed to doing the right thing and providing opportunities. And I know that we're not your only customer, but you help us to feel like we are.

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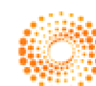

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Carlene Graham

We sure try to.

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

And it feels that way for us. And those are the things that make the relationship special from our perspective.

Jonathan Groesbeck

David, looking at 2019, what do you see as the biggest challenges facing a retail originator in the mortgage banking business like yourself? And maybe the mortgage banking business in general?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

There's a number of things, but the first one that comes to mind for me is the cost to originate a loan. I mean, these are statistics that are pretty publicly well-known, but prior to the housing recession, the cost to originate a retail loan and turn including commission expense was about $3,900, compliments of some of the regulatory environment that we live in, rising cost of salaries, benefits expenses and regulatory oversight, we had a high-water mark of nearly $9,000 at the tail end of last year. And that's unsustainable. And as an industry, there has been a race to leverage and utilize technology to find ways to bring that cost origination down. And many years ago, I worked for one of the largest mortgage companies in the country and we brought in BCG to do a consulting assignment. It was almost a year long. They talked with us about this very same topic, and this was in the late '80s. And they came back and they said 3 things to us. One, the #1 cost to originate a loan is people expense and that was pretty obvious. The second one was facilities-related expense and that also was under the obvious explanation. But the third one really opened our eyes, and it was the cost that it takes from time to originate a loan to the time that you get the loan approved. And the reason for it is that the longer you take, the more challenges that will occur, borrower will go out and take on additional debt, which will make them now not qualified. The lower that the customer satisfaction will be, the less likely they are to refer you to others. And also your employees, the less satisfied they are, your higher your turnover will be, your higher onboarding of new talent and training them. And so we've been focused on bringing the cycle time to originate a loan down, not only for customer engagement and employee experience, but also to be able to improve our cost to originate a loan. And so that is our biggest challenge as an industry right now. Technology hasn't been there, but it is today. And when you look at robotic process automation, you look at artificial intelligence, you look at a number of the ways that we can, as long as we can get adoption and utilization rate amongst our employees, we really have an opportunity to bring it down. I don't know that we're going to cut it in half anytime soon, but that is our challenge. And to the extent that Redwood can help us by utilizing technology that we adopt to not only fulfill those loans, but also to deliver them to you, will be paramount. Because it is a race in the industry right now to find a way to shorten the cycle time. Historically, it was 60 days to get a loan from application to funding. It's going to 45 days. It's now at 30 days. Technology that we now utilize, unless there are fiction points or challenges with some aspect of the loan, we can get a loan from application to clear to close in 8 or 9 days. But the technology is coming forward very quickly and there's going to be more of that to come.

Carlene Graham

As Redwood's one of largest and most valued relationships, going all the way back to 2011, what advice do you give us to ensure that we maintain our leadership position in the whole loan world?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Well, in some ways, it's stay the course. The things that got you here that we so very much appreciate, the credit discipline, the counterparty discipline, your approach towards being, I think, open to innovation, where those opportunities exist, where we're going to be able to do the right thing for missing opportunities. The things that we see today in the forward-looking, in the next 12 to 24 months, we have some ideas what that

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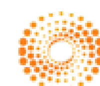

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looks like. And some of them have been shared earlier today about the challenges in new construction and being able to create some products that enable us to serve that portion of the community better than we have in the past. But there's going to be new ideas. There's going to be new challenges that will be 36, 48 months out. And so continuing to partner with your lenders and letting us help co-create some things in the way forward, I think, will be critical.

Carlene Graham

And what are some of the intangibles that we should stay focused on, that we should remain focused on?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Again, I think I would repeat. The intangibles about making sure that you're asking the tough questions, that you're looking for opportunities, avoiding what I will call yield chasing. The folks out there that are today in the non-QM space that seem to have forgotten what 2007 was all about, that are rushing towards alt and reduced documentation loan programs. That's not what I'm talking about in terms of finding ways to shorten the cycle time. It's not to short-circuit the risk evaluation of the credit profile, but avoid those temptations, continue to partner with your folks and continue to be good leaders in the industry for us.

Carlene Graham

Thank you.

Jonathan Groesbeck

David, I have to congratulate you. In the time I've known you, you've turned Wintrust Mortgage into a 4-plus billion dollar originator. You are now, I believe, servicing $8 billion to over 40,000 clients. What is the advantage of being part of a division of a bank versus being in independent mortgage right now?

David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Yes, we're a concentrated organization from our retail banking footprint in the Chicagoland area. As the CEO of the holding company likes to say, inside Chicago, Wintrust is a name you might recognize, but outside of that, you say Wintrust and you're likely to answer, "With your what hurts?" And you say, "No, it's your Wintrust." And so it's not a name that has a lot of brand recognition outside of our footprint. But inside the footprint, there's an opportunity for us to deepen our relationship with the customers that our organization has worked hard to develop. Between retail banking, commercial lending, niche lending, mortgage lending, wealth services, there's over 1 million folks that transact with the Wintrust brand on a daily, weekly and monthly basis. And our opportunity to be able to have an origination platform that then services their loan and provides them all the tools that they need is critical for us. And that's what we're looking to do, is deepen our relationship within the footprint with the customers that recognize the Wintrust name.

Jonathan Groesbeck

Well, David, as we're kind of running into the end of our time, I would -- one thing is that if the Cubs can win another World Series, you've got the big Wintrust sign over at the Wrigley Field. So congratulations on grabbing that. I want to thank you for making the trip out here from Chicago, for being just an incredibly good friend to the firm. Your firm has done fabulous. We love working with you. And really, just very happy to have you as part of the Redwood Trust family. So I really appreciate you taking this time today.

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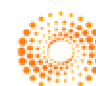

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David Hrobon - *Wintrust Mortgage Corporation - Former President and CEO*

Well, thank you for having me and also the shout out for the Cubs. They had a couple of good years of run, and we joked with them that it wasn't until they put the Wintrust sign out in left field that they started winning. And they rolled their eyes at us, but we're sticking with the story, so.

Jonathan Groesbeck

Great. I think you can take credit for that. And now, we'll turn it over to Lisa Hartman for more question-and-answers.

Carlene Graham

Thank you.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

I'll invite Bo and Collin back up and open it up for another brief Q&A session before we go into our final break.

QUESTIONS AND ANSWERS

Unidentified Analyst

So like you guys on the last earnings talked about potentially taking the dividend up over time. Can you just -- is it because there's more investment income that's driving that or there's more comfort on it or can you just walk through your thought process there?

Collin Lee Cochrane - *Redwood Trust, Inc. - CFO*

I'm going to have to step back. Can everyone hear me okay without a mic? Can you -- Okay.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

I got you, Collin.

Collin Lee Cochrane - *Redwood Trust, Inc. - CFO*

Yes, I think what I alluded to in my presentation is that we're doing things by allocating more capital into the investment portfolio and focusing on generating higher returns that we think will ultimately be able to support a higher dividend. So I think that's something that we are working towards. We did increase our dividend last year for the first time in quite a while, and we're hoping that by doing the things that I talked about, that we're going to put ourselves in a position to be able to raise it further in the future. So that's definitely something that we are focused on.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

Steve Delaney.

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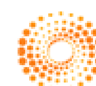

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Steven Cole Delaney - *JMP Securities LLC, Research Division - MD, Director of Specialty Finance Research and Senior Research Analyst*

Steve Delaney, JMP Securities. You've got a wonderful trade that you've had on for several years now with the Federal Home Loan Bank with, I think, about $2 billion of borrowings, I guess it is, and a little more than that in loans. Can you talk a little bit about that relationship? And I think you've got some -- it's sunsetting for everyone else, I think you've got some extended term, but just how do you view that on a long-term basis?

Shoshone A. Stern - *Redwood Trust, Inc. - CIO*

Well, first off, we wish we could do a lot more and we're looking for ways to try to help make that happen. But the distinction, and Collin talked about leverage, and I talked about leverage, recourse leverage. The real distinction there and why we like it so much is, no offense to a couple of people in this room, but we're not facing Wall Street in terms of getting cheap capital. We're facing a government entity that promises capital for 10 years at sub-LIBOR rates. So that's really the first thing that really makes the transaction happen. Putting that aside, we've spent a lot of time talking about counterparties. And then you look at the counterparty and they have a, not only an incentive, but a mandate to try to help liquidity in the housing market, whether that's for banks, insurance companies and just membership in general. So when you put both of those together, we would -- it's just an extremely attractive transaction for us. And we would allocate significantly more capital there if we could. So a lot of time and effort and work that we've been spending is to try to see if that can happen. Obviously, some legislation got introduced, I think it was last year, last year. We'll have to see where that goes. We're looking at other potential opportunities. Nothing firm yet, but we have every incentive and we'll try as hard as we can to stay in the system.

Unidentified Analyst

Thank you. In terms of having less capital in the mortgage banking, what is actually allowing you to do that? Is that better financing, shorter timelines, just rightsizing of the business?

Shoshone A. Stern - *Redwood Trust, Inc. - CIO*

It's a combination of things. The big driver, though, is really the process and improvements that we have internally. If we can hold on to loans before disposition, if we can cut that time by 10%, by 20%, that has a really big impact in terms of how much capital we have to hold for the business. Most of the capital that we hold for the business is actually unutilized throughout most of the cycle. Because if you think about it, we hold capital typically for the most that we're going to have in a given month or a given period. And we buy loans every day, then we eventually securitize or sell, our accumulated loans drops off. And then we start the process again. And so we're holding for a much larger amount of loans than, frankly, on average that we actually hold. So anything that we can do to get those loans both in the door and out the door faster is really beneficial on the capital front.

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

That's all the time we have for this particular Q&A session. We'll take another short break and then welcome you back in about 7 minutes, and then we'll have our final session.

(Break)

PRESENTATION

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

We're going to welcome everybody back and have a seat and we'll get started on our next session. Welcome back. We're starting our next session. All right. And welcome back for those of you on the webcast. And for those of you in the room, if you hadn't noticed, there is Wi-Fi cards on your

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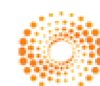

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table. So if you were looking for that and didn't notice that, that information is there. And not to make an Oprah moment every time that I announce things that are on the table, but I noticed that we do have some power banks that if you'd like to take those, they're in the white boxes, if you're wondering what's in there. So I welcome Sasha up to go through our next session on how we are moving the company forward through our organizational capability through our human capital.

Sasha G. Macomber - *Redwood Trust, Inc. - MD & Chief Human Resource Officer*

Good morning. I'm Sasha Macomber. I head up Human Resources here at Redwood Trust, and I'm excited to talk to you today about how we're building organizational capability, sustainability and shareholder returns through our people and our human capital practices. At Redwood, we're committed to best-in-class human capital practices that result in positive impacts for our shareholders, our company, our people and the communities in which we do business. We place a great emphasis on our culture at Redwood, because at the end of the day, we recognize that a strong culture results in stronger employee performance, morale, retention, lower turnover and ultimately, results for the organization. And I'm going to talk to you today about some of the programs and practices that are important to us, as well as some of our talent that we're very proud of. I think that Doug spoke earlier to talent, as did Chris. We're incredibly proud of our people at Redwood. We've been able to attract and retain truly best-in-class people to lead our business channels as well as similarly talented people who run back office functions and keep the business moving on a day-to-day basis. We have rigorous recruiting practices and standards, and we really have attracted the best and the brightest over time.

Diversity is also very important to us at Redwood. We recognize that diversity is important for a strong culture, but also it's good for business. The more diversity we have on our teams, the greater creativity, innovation, different perspectives in the room help us avoid group think, and they also mitigate risk for the organization. And when we think about diversity, we're really looking at it across a spectrum of age, gender, ethnicity, but also diversity of thought, diversity of perspectives and experiences that we have in the room and national origin. And I know that David spoke earlier to the work that he's doing with mPower. We are equally invested in empowering and elevating our women leaders at Redwood. We actually have terrific women leadership at all levels within the organization. We have active mentorship from our board and our executive team. We have a newly launched women's employee resource group, mentoring women together in the organization, and we are doing some good work there that we're proud of.

Also, I want to talk about how we're developing our talent, both for today and for the future. We have a wonderful history, as Rick spoke about, with internal promotion and succession planning. Many people in the room today from Redwood have had various roles within the organization and have progressed through their careers. And we've focused on a couple of important areas. One is strategic workforce planning. So we're looking both at our talent needs for today and for tomorrow, assessing gaps and ensuring that we're doing what we need to today to build our talent base for future needs. And we also focus on career experiences. We want to make sure that we're creating experiences for our people that build skill over time. We have validated programs and methodologies, really best-in-class training programs that we're rolling out. And then finally, our leadership development within the organization is very personalized. It's customized for our leaders that are emerging and in role. There's a lot of executive hands-on mentorship and coaching, as well as external resources that we utilize.

We talked about people. I'm going to spend a few minutes on our culture. Doug spoke to the importance of culture when he and George founded the organization, and that's really something that we have sustained over time. We invest in our culture because at the end of the day, a strong, healthy culture results in returns for the company. And we want to create a great place where people enjoy coming to work, but also where they're performing at their best. And over the last year, we've spent quite a bit of time talking about our culture and really articulating what's important to us as an organization and there are a few key themes here. We're definitely a growth-oriented firm. We're looking to grow in a sustainable way. We are passion and results driven. We've talked a lot about the quality of the work that we do and the quality of our people. That comes through loud and clear within the organization.

We're also empowered and inclusive in our ways of working together. We are a flat, non-hierarchical and very collaborative environment at Redwood. We also strive to be unified across our offices and functions. We have 3 different locations now with the acquisition of 5 Arches, and it's never been so important that our culture is consistent, especially as we consider future M&A activity.

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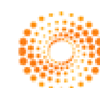

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Comfortable taking informed risks. We spoke about our risk management framework. We're very thoughtful in how we make decisions as an organization, but we also want to be able to respond to the market when it's relevant. And then finally, we're invested in accountable people practices. Our people are our greatest asset at Redwood and we want to ensure that we're investing in their future growth and development.

I want to talk about community. That's so important to us at Redwood. Giving back to the communities where we do business has been historically just a key factor in our culture. We have a unique employee-driven foundation that makes recommendations for charitable giving. They also raise funds within the organization. They drive our volunteerism efforts, and they have executive sponsorship, but they're entirely employee-driven. I love the photos behind me. I recognize Carlene, and I believe this is Dash with a pitchfork at one of our recent volunteer days. So we really do get out there and get involved in our communities.

And I'd like to end by speaking about our core values. Our core values at Redwood drive how we show up and do our work together every day. They are a set of beliefs that guide how we work together. And as we've talked today as well quite a bit about values, we understand that values drive our behavior and behavior is, at the end of the day, what really drives our results.

We have 6 core values. Growth is the first value. We define growth as profitable growth. We don't want to grow for growth's sake. It's really important that we're making the right moves around growth.

Our next value is results. We define results by doing work that has the biggest impact for our shareholders, the company and for our people.

Our next value is integrity. Integrity shows up at every level with every individual in the organization. It's so important to us that we're reliable, credible and that we do what we say we're going to do.

I've talked a lot about passion. We define passion as intellectual passion at Redwood. It is a complex business. We have very, very smart people that come to the table. I think we love nothing more than getting together and solving a really tough problem.

I've spoken about change. We think of change as being agile. Our ability to reinvent ourselves in tandem with the market is one of the reasons why we're around 25 years, and we look to continue to change and evolve over the next 25 years.

And with relationships, a core value for us. It's the reason we're here together in this room today. We understand that at Redwood, we're only as strong as our relationships and we take them very seriously.

Thank you. I'd like to welcome up Blake Eger, she is going to lead a conversation on housing.

Blake Eger

Thank you, Sasha. Hi, everyone. I'm Blake Eger, Managing Director on the Investments team at Redwood, focused on our strategic initiatives. I'm really excited to be moderating today's panel on housing reform with our distinguished guests.

Let me introduce everybody for a minute. Seated closest to me is Armando Falcon, CEO of Falcon Capital Advisors, a management consulting firm based in Washington, D.C. Before that, he served 6 years regulating Fannie Mae and Freddie Mac as the director of OFHEO, the predecessor to the FHFA. He also spent 8 years as counsel to the House Committee on Banking and Financial Services.

Next to him is Chrissi Johnson, Vice President for Federal Policy and External Affairs at Quicken Loans. In this role, she coordinates the company's position on federal public policy issues. Before joining Quicken, Chrissi served as Chief of Staff of the Division of External Affairs at the CFPB. Prior to that, Chrissi was Director of Scheduling for Elizabeth Warren's senate campaign and also worked with Senator Al Franken and President Barack Obama's presidential campaign.

Last but not least, we have Michael Bright, the newly installed President and CEO of Structured Finance Industry Group, SFIG, a trade association in D.C. that represents the securitization industry. Michael was previously the President of Ginnie Mae. He has been in D.C. for 10 years, working

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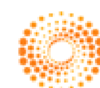

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not only at Ginnie Mae, but as a staffer to Senator Bob Corker, as an author at the Milken Institute as an -- and as an analyst at the OCC. He began his career trading mortgage derivatives for Countrywide's servicing hedge in California and then at Wachovia's investment bank in Charlotte.

Let's jump into the topics at hand, notably mortgage finance and housing reform. We'd like to walk through some of the major discussion topics occurring in Washington right now. Michael, do you want to kick us off?

Michael Bright - *Structured Finance Industry Group, Inc - President & CEO*

Yes, sure. I'm happy to give you an update on where things are and how we've gotten here. It is going to be a difficult, a little bit of a challenge. We have 18 minutes and the clock is ticking, you want to talk about housing finance reform. Since starting on housing finance reform, I have been seeing a therapist on a regular basis and the 30-minute sessions go too quickly. So I don't know how we're going to get through this.

But progress has been made. I do think that a lot of us, people in Washington, in the press, market participants, sort of on occasion bemoan the lack of a legislative solution, or when are we going to get to this last unfinished piece of business.

And I've given a lot of thought as to why has it played out the way it has. And I think the biggest thing that makes sense to me is if you compare sort of Dodd-Frank with this housing finance reform thing, the financial crisis happened, it's been 10 years. In the Dodd-Frank space, a law was passed very quickly. A whole bunch of regs were then written and then regs were recalibrated. A law was passed to recalibrate some of the regs and there's been all this kind of progress. In housing finance reform, none of that has really happened structurally.

And I think the reason is that for Congress, passing a bunch of new rules, just saying, "There are going to be new rules for this exact same market, we're just going to have a whole bunch of new rules," that's something that they can do.

They're quite good at writing a bunch of very vague rules and then having the regulator turn the vague rules into something, even on complicated topics.

Quickly, the housing finance reform thing, it became and has become a financial restructuring exercise. So when I joined Senator Corker's office in late 2010 and started working on this issue in 2011, the mandate, and this was broadly, I mean, this was conservatives, progressives, centrists, everybody. There was this sort of, "We don't want to have these 2 GSEs. There's a problem with that model, something's fundamentally sort of broken. Come up with something that's better." And it took a lot of work and brain damage, and we really tried very hard, but that's a structural reform conversation. And if you're a Senator or a member of Congress and you're coming from a meeting on Syria and then a meeting on health care, yada, yada, and now you're going to sit down and you're going to talk about bond guarantors and issuers and the CSP, like this is a very difficult thing.

So at a macro level, that's kind of why I think 10 years on, there hasn't been a law passed. Now real quickly, though, the thing that I am proud of and I -- and what I think doesn't get enough attention is that there has been an evolution. There have been reforms that have been taking place. And Congress actually has been doing a decent job of overseeing that process. So despite the fact that a law has not been passed, the hearings have been substantive. The FHFA, along with the enterprises, have made some changes, not enough. And there's a lot more to be done. And at the end of the day, Congress is going to have to put on its big adult pants and pass a law, but over the last 10 years, there have been hearings where Congress kind of set the 4 corners of the debate of what's acceptable for end state. FHFA has been evolving it, Fannie and Freddie have been evolving it, and now we're at this moment where I think everyone's ready to take another step and really shrink that footprint.

And so if we're -- if it's a baseball metaphor, we're probably in the seventh inning, early top of the seventh is maybe how I feel. And I think that more progress has actually been made than people give credit for.

So I could talk for a long time on this.

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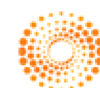

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Blake Eger

Well, let's see if Armando could shed some light maybe on some of the recent headlines we've seen.

Armando Falcon

Sure, sure. I wonder if we'll be going to extra innings, Mike, right? The way this is...

Michael Bright - *Structured Finance Industry Group, Inc - President & CEO*

They stop serving beers at 7:00, too. This is going to get rough.

Armando Falcon

Right. So yes, so bringing this forward, we've got -- we're going to have a new Head of the Federal Housing Finance Agency, right? Mark Calabria has been nominated. He's had a hearing. It looked like it might take until the summer or the fall to get him confirmed, but there have been recent developments and now there's some urgency around his confirmation for the job. There's even some speculation that it might get confirmed as soon as the end of this month or early April. We'll see how that turns out. But what does that mean for reform, to have a new director and Mark as the head of the agency? Well, I think a lot of people are anticipating the potential for some sweeping overhauls of FHFA and Mark, working in tandem with Treasury, to drive some final endgame for Fannie and Freddie and the future of the government's role in that sector of the housing finance system.

Mark was certainly questioned during his confirmation hearing about his past statements regarding housing finance reform and the mortgage market. It was him speaking as an academic, and he made that clear to the committee. What's also -- what's important to understand about him taking over the agency is the agency has a clear mission that's established in the agency's charter. The mission of this agency is to ensure the safety and soundness of Fannie Mae and Freddie Mac at its core. It's not a platform for a director to come in and make sweeping changes to the housing finance system. It's safety and soundness, just like a bank regulator is. And so Mark won't have a lot of latitude to just come in and try to restructure the entire housing finance sector. That's the role of policymakers in Washington, like Treasury, like Congress. But nevertheless, the agency under Mark's leadership will have a lot of tools available to it in order to try to assist policymakers in moving towards an endgame strategy. And that's -- I think that's what we're going to see about to kick off here later this year.

Senator Crapo has introduced an outline of his vision for housing finance reform. And he's working on organizing hearings around what he has put out there. And it's important -- it's not just so much the content of what he put out there, but just the fact that he put something out there and he's going to have hearings on and try to get discussion and debate generated around what's the endgame, what do we do? That's a big step forward. That's a contribution towards, moving towards an endgame.

He sets up a system of guarantors that will be competitors to Fannie Mae and Freddie Mac. And using Ginnie Mae as a platform, which, Mike, you probably had a hand in this, using Ginnie Mae as a platform for conveying the explicit government guarantee on this new system that is in Crapo's bill.

So a lot of good progress making -- moving forward. I think there's more we'll about that in the second half, but let me stop there.

Blake Eger

Thanks, Armando. Chrissi, as coming from the largest retail lender in the country, what are some of the issues that Quicken's focused on, some of the under-the-radar issues that you might be positioning for?

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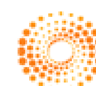

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Chrissi Johnson

Sure. Well, first, thank you for having me here today. We really value our partnership with Redwood. So this is a great opportunity to work with groups like yours who are credible and reliable and have that great reputation and really provide the space for these conversations. It's also great to be between these 2, who really have -- and a part of these conversations. Like Michael said, for 10 years, because most people have GSE fatigue at this point and don't want to talk about it anymore. So this is our year. I believe it. Not so popular these days, but this is our year.

So thanks for the plug, too, about Quicken being the largest retail lender. We are, and that's exciting. Now we're a year in with that title. And not -- I think it's worth noting, too, that it's a precedent that we are the first -- it's the first time that a non-depository has taken that title. So we like to say that we're a FinTech company that does mortgages, which I think is relevant to the GSE conversation, because we really pride ourselves on the technology and innovation, leveraging that technology and innovation to really provide the best product to our partner -- to clients, to our partners and really lead in this space. And it's for that reason, and you'll get into this a little bit later, that any discussion around reform is important to us. So we're talking about those standards that create that space for innovation, that safety for innovation and technology.

But I want to -- you had asked about some of the under-the-radar things that I really wanted to touch on, because I feel like a lot of times, we talk about GSE reform, but I like to talk about GSE reform-plus.

So I know this is shocking, but in Washington, there isn't always a lot of collaboration or coordination between the agencies. They're not always talking to each other, but there are some pretty specific interdependencies with what happens with the decisions that are made at Treasury and FHFA, and for example, CFPB and Dodd-Frank and specifically, QM and the QM patch. So there is a statute in Dodd-Frank says that when the GSEs, either by January 2021 or when the GSEs are pulled out of conservatorship that, that patch will expire.

For those of you who don't know what the patch is, that is the part of QM that was added in to make sure that the 43% to 50% debt-to-income ratio, DTI, would still be considered qualified mortgage at Fannie and Freddie. So that's about 30% of the current market at Fannie and Freddie. So the moment that those GSEs, that footprint decreases, that means that patch expires.

And I want people to start thinking about that, because I think that's relevant to the conversation here. We need to talk about where those loans are going to go. Is FHA, Ginnie going to be ready for that type of volume? What does that mean for the market that wants to compete and come into that space? And what does it means for our future clients and borrowers? The millennials, we are finally growing up, I hear, and we are going to be coming in as the most diverse group in history. So coming from communities that have -- that traditionally have been served FHA, also with the highest student debt that we've ever seen. So this debt-to-income ratio, this DTI, is very relevant for those clients. And those are the people we want to serve, those are the people we care about. So as we're talking about this, I do want to keep plugging and pushing on that across the industry, across consumer groups, across government, that importance of the dependencies from GSE reform to QM reform to FHA reform and altogether bringing in that private market.

Blake Eger

Thanks, Chrissi. Well, there's certainly a lot of questions that remain outstanding, but the core of the discussion seems centered on reduced role of government. How do -- in your best estimation, what do all of these conversations mean for both mortgage finance going forward and what sorts of platforms will emerge as the likely winners? Chrissi, can you tell us what sort of partners Quicken would want in a new world post-housing reform? What skill sets you view as most important moving forward?

Chrissi Johnson

Sure. I'm sitting between these 2 ballers and they don't have notes, but I have notes and I'm going to use them. But as I mentioned before, we are the -- a big agency lender because of the certainty of the process that leads to execution for us. So for better or worse, GSE -- the GSEs have been able to provide that certainty for us. That doesn't mean that that's the only answer, but that is the reality right now. There is a difference of 20-some days between agency and non-agency loans closing for us. So that makes a difference. It's that speed, it's that -- what we can depend on, because

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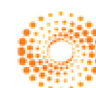

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we -- that predictability moving forward. We can, because of that predictability, that provides us the space to innovate, because we can then really like go ham out on those technologies that make us the leader, that make us different from everybody else.

So because of that, I really want to focus on, you had asked what type of characteristics would be important for partners moving forward, and I think any type of partnership that we would consider, I -- and I think Redwood has already indicated that they can be a leader in this space. But bringing comfort to buyers through that market-wide process or standard that could be agreed upon by the industry, supported by the government, help to efficiently identify errors so that we can fix it and move forward. That's another thing that's important to us. And increase our ease of execution through that technology and innovation. Currently, that standard and certainty is provided by the GSEs, but the private market wants to get there, game on. Let's do it, let's have these conversations. And I'm certain that any potential partner that would be interested in exploring these technologies, we would want to be a key contributor and part of that conversation.

Blake Eger

Great. Thank you. Michael, how do you see a reduced role of government play out for private capital participants?

Michael Bright - *Structured Finance Industry Group, Inc - President & CEO*

Yes, well, first off, Chrissi does make a very good point on the GSE plus and specifically the QM thing. So I'm testifying -- was just invited to testify at the end of March on this topic to Senator Crapo's committee, because he put this outline out. And I sat down, there -- the ask from him was to opine on the outline for reform that he put on. And I sat down and started to write this testimony earlier this week. And I suddenly found myself really just talking about QM. And I think the reason for that is that QM is definitely this trap and the patch specifically is this trap that does make it difficult for private capital to come in, or at least allow Fannie and Freddie to dominate that market. But you want to be, of course, very careful with how you do that, because you don't want to pull the rug out and move on. But the QM patch thing is a deed that's coming in 2021, and I do not think that the CFPB is going to extend it. So we really need to have people starting to think about what replaces it. And I think what I'm going to advocate for in this testimony is that there just needs to be a process, an automated underwriting process, that doesn't have a hard DTI cap, but that maybe -- but that also isn't just controlled by a company. So that a regulator can actually control an AUS system, maybe that looks like DU or LP, but it can be out for public comment on some level and so we can actually have a deemed legal safe harbor from liability, from the ability to repay rules, in a little bit more of an appropriate manner. So that's a very good point that you make, and it really does play in a lot to what private capital can do.

The next thing I'm going to say, with all due respect to Howard, who is my -- the Chairman of SFIG's board, whom I love and have a great deal of respect for, I don't know what Chris Abate has been doing, but everyone loves him in Washington. And when I -- this is not planned, I'm telling you. So when I took this job, and a lot of people in Washington are kind of like, "What is SFIG? What do you do?" And I sort of try and explain it and they're confused. And I'm like, "Well, you know, and Chris Abate is our incoming Chairman." And they're like, "Oh, that's great. Hey, look forward to working with you." And I'm kind of like, "I've worked with Chris over the last few years. I don't -- he's fine, but..."

Blake Eger

Come on, Michael.

Michael Bright - *Structured Finance Industry Group, Inc - President & CEO*

Okay. So SFIG is leveraging Chris's credibility, but for Redwood, I think what that means is that there's some desperation in Washington for private capital to figure out how to innovate a little bit and to add some value in the system and to say this isn't necessarily going through a GSE, but there is private capital behind it and we're solving these public policy problems. And I think you definitely, on a business level, have the real infrastructure to do it. But you are on -- for a variety of reasons, you're on the right side of public policymakers. And so I think that everyone is kind of looking to this institution to kind of help us figure out how private capital can play a bigger role. I wasn't going to use those terms, private capital, in this

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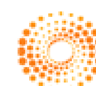

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testimony, probably 20 times. And that just kind of is the way it evolved and the way it came out when I started putting words on a page. And there is definitely appetite to have private capital come in, coupled with a little bit of anxiety over, now if we're in the government and there's private capital, we're relinquishing some control. And the last time that happened, we're not sure we understand exactly -- or we don't love how it played out. We're not fully understanding exactly why. So we'll get there, but we're nervous about it. And Chris and Redwood, apparently, are -- have credibility in helping to solve this. So that's going to be part of the conversation.

Armando Falcon

I think, yes, Chris and the team at Redwood have spent years of shoe leather just building brands in Washington and being thought leaders. I mean, it was -- people from Redwood have testified many times before Congress, as you know. They restarted the PLS market after the financial crisis. And I think that ties in a little bit to where we go from here. So let me get into that a little bit.

Blake Eger

You took the question from me, Armando.

Armando Falcon

Okay, good. So the way I think things might play out, and this could be wrong, but I think it's clear that it's going to be hard to pass legislation to -- that's been proven true to figure out what happens to Fannie and Freddie and the government's role in that market.

We seem to be moving towards a path that became more clear over the last few years as the likely -- the way to get this done. And it's for the administration, whatever administration was in power, to use the regulatory powers that they have through the regulators and other policy tools at the administration's disposal, to start moving towards a path of a resolution of Fannie and Freddie, whatever that may be, and have Congress play the role of filling in the gaps where there wasn't regulatory power. But you -- I think you sort of -- you might see that coming out where the administration will come out with a plan for how they see this endgame taking place and what the role of the administration will be using their existing powers and advising Congress along the way, and Congress understanding what they need to do to fill in the gaps. And so as this plays out, I think there are a couple of overriding themes that there seems to be a lot of consensus on, that Michael talked about some of those, private capital going to the mortgage market. I think one of the others is competition in the Fannie and Freddie space. Now there were efforts through regulatory tools to try to generate that competition in the past. The g-fees, Ed DeMarco talked about g-fees going up in order to try to level the playing field on pricing and execution for competitors, i.e., Redwood. Redwood is a jumbo, known as a jumbo lender, but that's because they can't compete with Fannie and Freddie in that conforming mortgage market. But Redwood, I think, has been a competitor knocking at the door for many years in this space. And so if the desire is to bring in that competition, reduce their footprint and bring in competition to Fannie and Freddie, how do you do that? Well, they tried to do it through the g-fees, that didn't quite work out for a variety of other reasons. And now you see in Senator Crapo's bill outline, a hard -- he doesn't have a number yet, but hard market share caps for Fannie and Freddie. I don't know where those might get set, 25% each, but that's going to open up -- let's say it is that, that's going to open up 50% of that conforming mortgage market to competitors. And I think who's better positioned to fill that void as a guarantor than someone like Redwood, that's already got the same platform? I think that's where there seems to be huge potential going forward as policymakers decide the future of Fannie and Freddie and what happens in that space.

Blake Eger

Thank you. Thank you to our panelists. That concludes our time for today. I turn over the stage to Matt Tomiak.

Matthew Tomiak

Is this live? Everybody hear me? Great. You guys mind -- I'm going to sit. I'm going to sit. I don't -- I generally -- I like talking to people. I don't like talking at people, so now we're all sitting, we're all talking. So the good part about going at the end of the day is everybody's tired and not really

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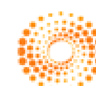

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listening. The bad part about going at the end of the day is everybody's already said everything you were going to say. I'd say the good thing for me in that role is what I do at Redwood is really listening. So I guess I should go back and introduce myself.

I'm Matt Tomiak. I work in the Denver office. Jason Moutray and myself administer the Sequoia bond issuance program. So we're really the bridge between the sellers that sell us loans, who you talk to and heard earlier, and the buyers that buy bonds at the other end, as well as buy whole loans from us on the other end.

So it's kind of a simple job. I hear the concerns of bond buyers, what people want to purchase, what people want to do. And I look at sellers and I hear their needs, and we try and bridge the gap between the 2. And also in that, we really try and reach past to what the consumer is looking for at the end of the day. I think it's a realization and a humbleness at Redwood that has made this program so successful. Chris talked earlier about building market standards. We've heard from Armando about the respect that we carry in D.C., which is a really nice thing to hear. But I think a lot of that all comes from the fact that we realize we have shareholders, a lot of you are here today, and we're out there for you. But at the same time, we realized the universe doesn't focus on us. At the end of the day, the consumer doesn't buy a home because they want to produce a loan, because we're looking for a certain rate of return in order to create leveraged securities on the other end. That's not where things start. At the end of the day, we're looking for really product, a product that can serve a consumer on the other end and proper leverage and a proper return for the AAA buyers that finance us.

When we sell risk on the other end, we don't ever really truly sell all of the risk. We're looking to create investments for ourselves first and foremost. And if you look at where -- we talked to one of the founders earlier and look where everything started, it was to create assets for ourselves, but it's really evolved since then. And I think it's important, as I mentioned, listening. I think it's important to listen to the people who started things and talk about where we started, where we are now, and also listen what are the demands in the marketplace? Where people -- where do people want us to go? Where is there opportunity? And that really comes not by forcing yourself in, but really listening and thinking about where can I insert myself at that point in time to really add value in the process?

Chris started the entire day off with the statement of every time a mortgage loan, a non-agency mortgage loan, transfers hands in the markets, we want to participate and earn a fee. And I think that might sound ambitious at first, and I think it would be very ambitious if our goal was to go out and say every time 2 people try and come together to make a trade, we're going to stick our hand in the middle. It's really the opposite, the way that we're going to try and come at this. And that really is, if we can insert value, people are going to look for us to enter the center of the trade. And I think we're doing that now. When I say -- I'm going to explain to you all how I see us doing that now. And I think it'll become pretty clear how we're looking to continue doing that in the future. So currently, you heard from our seller partners at Wintrust earlier. I think they did a great job praising us. And I spend a lot of time on the road listening to sellers and that's what I hear again and again. Consumer transactions are difficult. These are individual people, buying a home is an emotional experience. There's a lot on the line for people there. Serving each one of them, especially the jumbo borrower, the agency borrower, the FHA borrower, talking about a lot simpler profile, maybe in some instances, a less qualified consumer. But it's much more difficult to underwrite consumer when you're talking about the jumbo borrower. There's much more sophisticated financials involved. Every one of them is really a snowflake. It's a hard transaction. We see very difficult on one side and then you look at bond investors, especially AAA bond investors, the yields aren't massive on that side of the house. They're looking for a very simple, very homogenous investment. Somebody needs to stand in the middle and take what is very, very hard, funnel it through and then put it out the other side for financing in a very, very simple, homogenous fashion.

We heard earlier, effectively from our friends at Quicken, the GSEs are really providing that for them in the agency space, which has allowed for innovation on the front end. We really try and provide that in the jumbo space to the best of our ability. They are different business models. One is a government-backed and government-sponsored entity; the other one represents full private capital. But we're really looking to bridge the gap there.

Looking at what we've done so far. I look at the standardization and the markets standards we've create both at Sequoia and the Choice brands. I'd like to think on a daily basis, it's not that we're geniuses in moving forward, I think it's that we take one step at a time. Select was really a product of its environment. The securitizations just post-crisis, there wasn't a ton of investor trust out there. People needed a safe product. They needed an alternative to a bank loan product. Mortgage lenders needed an outlet at that point in time. We stepped in and filled that dual void. Simple transactions, simple standards. Since then, we've simplified even more. We froze our AAA enhancement at 5%. We leave money on the table when

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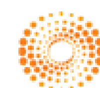

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we do that. Now people don't -- might not necessarily want to hear that, but it's for a very good reason, because it makes it simple to do the next transaction. I'm not worried about the trade in front of me, I'm worried about the next trade and the next trade after that. We're worried about buying mortgage loans the next (inaudible). Choice was a very simple evolution from there. We looked around the market, Select was becoming more commoditized. It was really going to its cheapest investment financing source. We try and be that source. We believe we're that source, as Chris had mentioned, amongst securitizers. But at the end of the day, we're not a bank, we're not an insurance company, so we have to be thoughtful about where we participate, and again, thoughtful about where we add value. The Choice product, and we looked around the market at really what was available to consumers at that point in time. I remember looking at rate sheets and rate grids and I saw a 90% LTV loan to a consumer with 10x the amount of value of the home in reserves who had a very good reason they were taking a 90% LTV with a 8.5% interest rate and the current rate was 3.5%. And I was like, well, this doesn't make any sense on a risk-return basis, and I think we can do a lot better than this.

So we started looking at the market of what was there. We started talking to our seller partners and everyone saw there was going -- eventually going to be a rise in interest rates. I think there's going to be a rise in interest rates. I don't know at this point in time. But in that environment, refis were going to go away. It was going to become a purchase money market. How do you fill that void in production for our seller partners and keep their businesses going? Choice was an obvious move for us at that point in time. So again, it's looking at what's around you and taking the simple answer next. We've since -- Choice has become a market standard. We're very proud of what we've done there. The securitizations are all very standardized. I think my #1 comment from investors when I first meet them to talk about -- to talk about investing in the bonds and the program, I'll run through the program attributes. We talk about everything. We go into everything in depth. And my answer -- the response is constantly, that's it? Like everyone can't believe, like, that's it. Our non-QM is really simple. As mentioned earlier by a couple people, QM and non-QM are loan designations. It's how the consumer's qualified. I think the phrase has been bastardized in the market for several reasons. There's a connotation that it's non-prime. There's a connotation that non-QM really means that the borrower is not qualified. It's the furthest from the truth. The borrower is qualified. It doesn't qualify for a regulatory exception, that's what we're talking about here. And that's the loan we're providing on our side, the financing for the loan that we're providing on our side.

So I think in moving forward, again, this goes to listening. I heard on the panel just before I spoke just now, was there's a call in D.C. for private capital to enter. I think this is, again, where Redwood excels. We're willing to go first. If you look at the first securitization post-crisis, the first expanded transaction, the 120-day stop advance is something we didn't innovate. We heard from investors that they would want a protection like this. We put it in the transaction. It was difficult, we went first, not everybody agreed with it. Since then, it's become a market standard. We're not afraid to put our money where our mouth is and go first.

So I've been on the road since Sunday, talking to a lot of bond investors about a potential new program that we've been working on, I think Chris alluded to earlier in the day today. It's, again, a simple program. What we're hearing is smaller insurance companies, smaller banks want to start participating in whole loans. Whole loans are very difficult. If you look at trading whole loans, everybody wants the due diligence on the loan, despite the fact that it was underwritten by the originator, completely re-underwritten by us, re-underwritten by a third-party. When the loan trades hands again, they're going to want to look at the whole loan all over again. To the extent they want to move the loan after that, they're going to look at it again. Every time a loan changes hands, we're basically setting money on fire on behalf of the industry. We're wasting the consumers' money, because at the end of the day, that's reflected in the initial interest rate. We're also wasting investors' money in the whole loans in that we're burning their yields, re-checking the checker of the checker of the checker. So what we're really looking for at this point in time, is there a simpler way for people to participate and invest in whole loans, without the licensing of owning whole loans, without controlling the servicing, without owning the MSR, without creating all of the hassle, is there a easier way to participate? And I simply look at this as a easy evolution. We started with securities for ourselves. We saw that wasn't always easy. We started looking at that point in time for a whole loan execution so that we could provide a consistent outlet for Wintrust, Quicken, our various other originator partners. And now we're really looking for what is the third channel and what is that going to be from there. So we're very excited to talk to you guys all about that in the future. It's 0.00 on the clock. I don't know if I get tasered after this, but I'm going to give it back to Chris, who's going to have some closing remarks for everybody. Thank you, all.

Christopher J. Abate - *Redwood Trust, Inc. - CEO & Director*

I'm going to keep this brief. I've noticed most of the investment bankers left when the bar wasn't open, so we're a few people short. So before everybody else leaves, we'll make this quick. Thank you guys for coming. Hopefully, you feel like I've surrounded myself with smarter people than me. I think we've got a tremendous management team. We've got a tremendous and loyal shareholder base, which we sincerely appreciate. And

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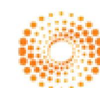

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there is just a lot of exciting things going on at Redwood. We try to keep it short and punchy for you guys, keep everything on schedule, but by all means, we can wrap up with some Q&A, or always follow up with one of us, we're happy to take your questions offline. But thank you guys so much for a great morning and a great Investor Day.

So to yourselves, a round of applause.

QUESTIONS AND ANSWERS

Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

We'll take 1 or 2 questions, if we have any. Thank you. Yes, yes. Open for the...

Unidentified Analyst

So the question is, do you think GSE reform will get -- could get done without congressional involvement? And then do you think it'll get -- could get done this year or next?

Michael Bright - *Structured Finance Industry Group, Inc - President & CEO*

I think it depends on what you define as reform. So if reform means the end of the conservatorships, maybe that's one metric of looking at it. I think Mnuchin and Craig are very determined to do that. The challenge is that there's 18 months left -- 19 months until this whole place turns into a pumpkin and public policy decisions are not going to be made. And there's a whole lot of wood to chop between now and then. And I don't think that they can get the end of conservatorship or even really lock in the idea that there's going to be an end of conservatorship before the end of this term. So what'll end up starting to happen is the likelihood of administrative end of the conservatorship will be tethered to the poll numbers. And if Trump administration is reelected, then it definitely will happen in the second term. If not, then it definitely won't happen, because I don't think any Democrat is going to re-IPO the company. So that's kind of my view of the next 2 years.

Armando Falcon

I agree with Mike. It depends on what you think of as the reform. Even without legislation, if the administration were to pull Fannie and Freddie out of conservatorship, they won't have dealt with, I think, some of the key issues. You might see the administration try to pull them out of conservatorship and say, well, we're going to require higher capital levels, there's risk-sharing transactions in place so they're less risky and other reforms have kind of been put in place. But there are other key reforms that they just won't be able to do. And I -- the key ones I think about are ownership and governance structures. What made Fannie and Freddie have such serious problems going back to the accounting scandals, it wasn't the lack of capital. There were other issues at the companies. And those kind of issues that center on the ownership and governance just won't be handled with the end of the conservatorships. So I think you absolutely do need congressional involvement in the long-term endgame on what happens to Fannie and Freddie, you really do need Congress to play a part in this. But it looks like Congress probably won't get involved until they see something happening on the administrative end through the administration's actions. Chrissi, do you have anything to add or you...?

Chrissi Johnson

I generally agree. There needs to be a trigger for Congress to take any action. And I think that, that is the administrative route that they're looking at. I think that's why there's a sense of urgency with pushing Mark's confirmation through right now and even Otting getting a little over his skis in his alluding to a plan, the plan that is yet to be seen. But I know Treasury, like he said, like Michael said, Craig and Mnuchin are actively engaged on this issue. And if they can move forward, I think that is the necessary trigger to make Congress act.

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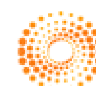

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Lisa Hartman - *Redwood Trust, Inc. - Senior VP & Head of IR*

All right. I'll invite everyone to lunch.

Christopher J. Abate - *Redwood Trust, Inc. - CEO & Director*

Thank you, guys, very much. We have lunch in the other room. Please help yourselves. Thank you.

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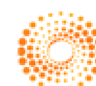

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