Ellington Financial LLC
Form S-11/A
November 03, 2009
Table of Contents

As filed with the Securities and Exchange Commission on November 3, 2009

Registration No. 333-160562

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Pre-Effective Amendment No. 3

to

Form S-11

FOR REGISTRATION UNDER THE SECURITIES ACT OF 1933

OF CERTAIN REAL ESTATE COMPANIES

Ellington Financial LLC

(Exact name of registrant as specified in its governing instruments)

53 Forest Avenue

Old Greenwich, Connecticut 06870

(203) 698-1200

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Laurence Penn

Chief Executive Officer

53 Forest Avenue

Old Greenwich, Connecticut 06870

(203) 698-1200

(Name, address, including zip code, and telephone number, including area code, of agent for service)

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Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this Registration Statement.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box. ¨

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	x (Do not check if a smaller reporting company)	Smaller reporting company	¨

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this prospectus is not complete and may be changed. Neither we nor the selling shareholders named in this prospectus may sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and neither we nor the selling shareholders are soliciting an offer to buy these securities in any state where an offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED NOVEMBER 3, 2009

Shares

Ellington Financial LLC

Common Shares Representing Limited Liability Company Interests

This is the initial public offering of common shares of Ellington Financial LLC. We are selling common shares representing limited liability company interests, which we refer to as common shares.

The selling shareholders named in this prospectus are offering 1,130,000 common shares. We will not receive any proceeds from the sale of the common shares in this offering by the selling shareholders named in this prospectus.

Ellington Financial LLC is a specialty finance company that specializes in acquiring and managing mortgage-related assets, including residential mortgage-backed securities backed by prime jumbo, Alt-A and subprime residential mortgage loans, residential mortgage-backed securities for which the principal and interest payments are guaranteed by a U.S. Government agency or a U.S. Government-sponsored entity and mortgage-related derivatives, as well as corporate debt and equity securities and derivatives. We are externally managed and advised by Ellington Financial Management LLC, or our Manager, an affiliate of Ellington Management Group, L.L.C.

Prior to this offering, there has been no public market for our common shares. The initial public offering price of the common shares is expected to be between $ and $ per share. Our common shares have been approved for listing on the New York Stock Exchange under the symbol EFC.

Concurrent with the closing of this offering, we will sell to EMG Holdings, L.P., an affiliate of our Manager, in a separate private placement, approximately common shares at a price per share equal to the initial public offering price per share. EMG Holdings, L.P. has committed to purchase in the concurrent private placement no less than the greater of (i) common shares and (ii) the lesser of common shares and the number of shares sufficient for our Manager and certain of its affiliates to own, in aggregate, % of our outstanding common shares immediately after completion of this offering and the concurrent private placement, excluding any shares sold pursuant to the underwriters exercise of their over-allotment option.

The underwriters have an option to purchase a maximum of additional shares to cover over-allotments of shares.

Investing in our common shares involves risks. See Risk Factors on page 23.

	Price to Public	Underwriting Discounts and Commissions	Proceeds to Issuer	Proceeds to Selling Shareholders

Per Share	$	$	$	$
Total	$	$	$	$

Delivery of the common shares will be made on or about , 2009.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Credit Suisse **Deutsche Bank Securities**

FBR Capital Markets **Keefe, Bruyette & Woods**

Cantor Fitzgerald & Co. **Fox-Pitt Kelton Cochran Caronia Waller**

The date of this prospectus is , 2009

TABLE OF CONTENTS

You should rely only on the information contained in this document. We have not authorized anyone to provide you with information that is different. This document may only be used where it is legal to sell these securities. The information in this document may only be accurate as of the date of this document.

Dealer Prospectus Delivery Obligation

Until , all dealers that effect transactions in these securities, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealer s obligation to deliver a prospectus when acting as an underwriter and with respect to unsold allotments or subscriptions.

SUMMARY

This summary highlights information contained elsewhere in this prospectus. It is not complete and may not contain all of the information that you should consider before making an investment in our common shares. You should read carefully the more detailed information set forth under Risk Factors and the other information included in this prospectus. Except where the context suggests otherwise, EFC, we, us and our refer to Ellington Financial LLC and its subsidiaries, our Manager refers to Ellington Financial Management LLC, our external manager, Manager Group refers collectively to our Manager, EMG Holdings, L.P., VC Investments L.L.C. and a trust for which Michael Vranos is settlor, and Ellington refers to Ellington Management Group, L.L.C. and its affiliated investment advisory firms, including our Manager. In certain instances, references to our Manager and services to be provided to us by our Manager may also include services provided by Ellington and its other affiliates from time to time. Unless indicated otherwise, the information in this prospectus assumes (i) the common shares to be sold in this offering will be sold at $ per share, which is the mid-point of the price range set forth on the front cover of this prospectus, (ii) the concurrent private placement to EMG Holdings, L.P., an affiliate of our Manager, of common shares at $ per share and (iii) no exercise of the underwriters over-allotment option described on the cover page of this prospectus.

Our Company

Ellington Financial LLC is a specialty finance company formed in August 2007 that specializes in acquiring and managing mortgaged-related assets. Our primary objective is to generate attractive, risk-adjusted total returns for our shareholders by making investments that we believe compensate us appropriately for the risks associated with them. We seek to attain this objective by utilizing an opportunistic strategy. Our targeted assets currently include:

- residential mortgage-backed securities, or RMBS, backed by prime jumbo, Alternative A-paper, or Alt-A, and subprime residential mortgage loans, or non-Agency RMBS;
- RMBS for which the principal and interest payments are guaranteed by a U.S. Government agency or a U.S. Government-sponsored entity, or Agency RMBS;
- mortgage-related derivatives; and
- derivatives on corporate debt and equity securities.

We also may opportunistically acquire and manage other types of mortgage-related assets and financial assets, such as residential whole mortgage loans, commercial mortgage-backed securities, or CMBS, and commercial mortgages or other commercial real estate debt, asset-backed securities, or ABS, backed by consumer and commercial assets and non-mortgage-related derivatives. As of June 30, 2009, we had an aggregate portfolio of RMBS with a net value of approximately $460.0 million, derivatives contracts with a net value of approximately $117.6 million and total shareholders equity of approximately $284.1 million.

The members of our management team are Michael Vranos, founder and Chief Executive Officer of Ellington, who serves as our Co-Chief Investment Officer, Laurence Penn, Vice Chairman of Ellington, who serves as our Chief Executive Officer and President, Mark Tecotzky, a Managing Director of Ellington, who serves as our Co-Chief Investment Officer, Lisa Mumford, who serves as our dedicated Chief Financial Officer, Paul Saltzman, General Counsel of Ellington, who serves as our Secretary, and Eric Bothwell, a Managing Director of Ellington, who serves as our Chief Operating Officer. Each of these individuals is an officer of our Manager. We currently do not have any employees.

Table of Contents

Our Manager and Ellington

We are externally managed and advised by our Manager, an affiliate of Ellington, pursuant to a management agreement. Our Manager was formed solely to serve as our manager and does not have any other clients. In addition, our Manager currently does not have any employees and instead relies on the employees of Ellington to perform its obligations to us. Ellington is a private investment management firm and registered investment advisor with a 14-year history of investing in a broad spectrum of mortgage-backed securities, or MBS, and related derivatives.

Our Manager is responsible for administering our business activities and day-to-day operations and, pursuant to a services agreement between our Manager and Ellington, relies on the resources of Ellington to support our operations. See Certain Relationships and Related Party Transactions Services Agreement for a description of the terms of the services agreement between our Manager and Ellington. Ellington has established portfolio management resources for each of our targeted asset classes and an established infrastructure supporting those resources. Through our relationship with our Manager, we benefit from Ellington s highly analytical investment processes, broad-based deal flow, extensive relationships in the financial community, financial and capital structuring skills, investment surveillance database and operational expertise. Ellington s analytic approach to the investment process involves collection of substantial amounts of data regarding historical performance of MBS collateral and MBS market transactions. Ellington analyzes this data to identify possible trends and develops financial models used to support the investment and risk management process. In addition, throughout Ellington s 14-year history of investing in MBS and related derivatives, it has developed strong relationships with a wide range of dealers and other market participants that provide Ellington access to a broad range of trading opportunities and market information. In addition, our Manager provides us with access to a wide variety of asset acquisition and disposition opportunities and information that assist us in making asset management decisions across our targeted asset classes, which we believe provides us with a significant competitive advantage. We also benefit from Ellington s finance, accounting, operational, legal, compliance and administrative functions.

As of June 30, 2009, Ellington employed over 100 employees and, including our company, various hedge funds, and various private accounts, had net assets under management of approximately $2.2 billion, in addition to approximately $578.0 million of net assets under management in certain hedge funds that have not been actively making new investments but rather have been returning capital to investors. In addition, Ellington, through its affiliates, manages collateralized debt obligations, or CDOs, collateralized by MBS or ABS and a traditional managed account.

Our Manager has an investment and risk management committee that advises and consults with our senior management team with respect to, among other things, our investment policies, portfolio holdings, financing and hedging strategies and investment guidelines. The members of the investment and risk management committee include Messrs. Vranos, Penn, Tecotzky and Bothwell.

Our Strategy

We utilize an opportunistic strategy to seek to provide investors with attractive, risk-adjusted total returns by:

- taking advantage of opportunities in the residential mortgage market by purchasing investment grade and non-investment grade non-Agency RMBS, including senior and subordinated securities;

- acquiring Agency RMBS on a more leveraged basis in order to take advantage of opportunities in that market sector and assist us in maintaining our exclusion from regulation as an investment company under the Investment Company Act of 1940, as amended, or the Investment Company Act;

- opportunistically entering into and managing a portfolio of mortgage-related derivatives;

Table of Contents

opportunistically acquiring and managing other mortgage-related and financial assets, such as residential whole mortgage loans, CMBS, commercial mortgages or other commercial real estate debt, ABS backed by consumer and commercial assets and non-mortgage-related derivatives; and

opportunistically mitigating our credit and interest rate risk by using a variety of hedging instruments.

Our strategy is adaptable to changing market environments, subject to compliance with the income and other tests that will allow us to continue to be treated as a partnership for U.S. federal income tax purposes and to maintain our exclusion from regulation as an investment company under the Investment Company Act. As a result, although we focus on the assets described above, our acquisition and management decisions depend on prevailing market conditions and our targeted asset classes may vary over time in response to market conditions. To effect our strategy, we may engage in a high degree of trading volume. Our Manager is authorized to follow very broad investment guidelines and, as a result, we cannot predict our portfolio composition. We may change our strategy and policies without a vote of our shareholders. Moreover, although our independent directors periodically review our investment guidelines and our portfolio, they generally do not review our proposed asset acquisitions or asset management decisions.

Ellington s investment philosophy revolves around the pursuit of value across various types of MBS and related assets. Ellington seeks investments across a wide range of MBS sectors without any restriction as to ratings, structure or position in the capital structure. Over time and through market cycles, opportunities will present themselves in varying sectors and in varying forms. In current markets, for example, the liquidation of portfolios of MBS from structured vehicles and from distressed financial institutions have been significant sources of asset acquisition opportunities. By rotating between sectors of the MBS markets and adjusting the extent to which it hedges, Ellington believes that it is able to capitalize on the disparities between these sectors as well as on overall trends in the marketplace, and therefore provide better and more consistent returns for its investors. Disparities between MBS sectors vary from time to time and are driven by a combination of factors. For example, as various MBS sectors fall in and out of favor, the relative yields that the market demands for those sectors may vary. In addition, Ellington s performance projections for certain sectors may differ from those of other market participants and such disparities will naturally cause us, from time to time, to gravitate towards certain sectors and away from others. Disparities between MBS sectors may also be driven by differences in collateral performance (for example, seasoned subprime collateral may perform better than more recent subprime collateral) and in the structure of particular investments (for example, in the timing of cash flow or the level of credit enhancement), and our Manager may believe that other market participants are overestimating or underestimating the value of these differences. Furthermore, we believe that risk management, including opportunistic portfolio hedging and prudent financing and liquidity management, is essential for consistent generation of attractive, risk-adjusted total returns across market cycles.

Ellington s continued emphasis on and development of proprietary MBS credit, interest rate and prepayment models, as well as other proprietary research and analytics, underscores the importance it places on a disciplined and often analytical approach to fixed income investing, especially in MBS. Our Manager uses Ellington s proprietary models to identify attractive assets, value these assets, monitor and forecast the performance of these assets, and opportunistically hedge our credit and interest rate risk. We leverage these skills and resources to seek to meet our objectives.

We believe that our Manager is uniquely qualified to implement our strategy. Our strategy is consistent with Ellington s investment approach, which is based on its distinctive strengths in sourcing, analyzing, trading and hedging complex MBS. Furthermore, we believe that Ellington s extensive experience in buying, selling, analyzing and structuring fixed income securities, coupled with its broad access to market information and trading flows, provides us with a steady flow of opportunities to acquire assets with favorable trade executions.

Table of Contents

Our Targeted Asset Classes

Our targeted asset classes currently include:

Asset Class	Principal Assets
Non-Agency RMBS	RMBS backed by prime jumbo[1], Alt-A[2] and subprime mortgages[3] RMBS backed by fixed rate mortgages, adjustable rate mortgages, or ARMs, Option-ARMs, Negative amortization ARMs, or Neg-Am ARMs, and Hybrid ARMs RMBS backed by first lien and second lien mortgages Investment grade and non-investment grade securities Senior and subordinated securities Interest only securities, or IOs, principal only securities, or POs, inverse interest only securities, or IIOs, and inverse floaters
Agency RMBS	Whole pool pass-through certificates To-Be-Announced, or TBA, mortgage pass-through certificates
Mortgage-Related Derivatives	Credit default swaps on individual RMBS, on the ABX and CMBX indices and on other mortgage-related indices Other mortgage-related derivatives
Corporate Debt and Equity Securities and Derivatives	Credit default swaps on corporations or on corporate indices Corporate debt or equity securities Options or total return swaps on corporate equity or on corporate equity indices
Other	Residential whole mortgage loans CMBS Commercial mortgages and other commercial real estate debt ABS Other non-mortgage-related derivatives

(1) Prime jumbo mortgage loans are mortgage loans that have principal amounts that are greater than the conforming loan limits for the Federal National Mortgage Association, or Fannie Mae, and the Federal Home Loan Mortgage Company, or Freddie Mac, but are otherwise within typical Fannie Mae and Freddie Mac guidelines.

Table of Contents

(2) Alt-A mortgage loans generally have income verification and/or employment verification standards that are weaker than those standards employed in prime underwriting. Additionally, Alt-A mortgage loans are more frequently collateralized by non-primary residences than prime loans. The credit quality of Alt-A borrowers generally exceeds the credit quality of subprime borrowers.
(3) Subprime mortgage loans are loans that are originated using underwriting standards that are less restrictive than those used for other first and junior lien mortgage loan origination programs, such as the programs of Fannie Mae and Freddie Mac. These lower standards permit loans to be made to borrowers having low credit scores and/or imperfect or impaired credit histories (including outstanding judgments or prior bankruptcies), loans with no income disclosure or verification and loans with high loan-to-value ratios.

Our Portfolio

As of June 30, 2009, our RMBS portfolio consisted of the following assets:

Asset Class	Amortized Cost Basis	Estimated Fair Value	Estimated Fair Value as a Percentage of Total Shareholders Equity
Non-Agency RMBS	$ 225,592,234	$ 188,002,122	66%
Agency RMBS	267,228,145	272,046,314	96%
Total	$ 492,820,379	$ 460,048,436	162%

As of June 30, 2009, our derivatives portfolio consisted substantially of the following derivatives:

Asset Class	Notional Amount	Estimated Fair Value	Estimated Fair Value as a Percentage of Total Shareholders Equity
Long positions using credit default swaps on RMBS(1)	$ 15,977,810	$ (10,911,356)	(4)%
Short positions using credit default swaps on RMBS and on RMBS and CMBS indices(2)	(175,779,400)	127,686,902	45 %
Short positions using credit default swaps on corporate bonds and corporate bond indices	(48,625,000)	5,440,874	2 %
Short positions in interest rate swaps(3)	(100,000,000)	(4,140,602)	(1)%
Total		$ 118,075,818	42 %

(1) Long positions using credit default swaps represent transactions where we sold credit protection to a counterparty.
(2) Short positions using credit default swaps represent transactions where we purchased credit protection from a counterparty.
(3) For short positions in interest rate swaps, a fixed rate is being paid and a floating rate is being received.

As of June 30, 2009, a small portion of our portfolio consisted of depreciated futures, long and short positions in total return swaps and other swaps. As of June 30, 2009, the fair value of our long and short positions in total return swaps and other swaps was $(427,459).

As of June 30, 2009, in addition to our RMBS portfolio and our derivatives portfolio, a small portion of our investment portfolio consisted of put options purchased and trade claims with a fair value of $5.4 million.

Our Performance

Notwithstanding the difficult market conditions in which we have operated since our inception in August 2007, we have delivered a positive total return on our capital over that period. As of June 30, 2009, our book value per common share was $23.87. For companies such as ours that employ an investment company basis of accounting, book value and net asset value are the same. Entities utilizing investment company accounting carry investments at fair value. The total return on our common shares based on change in book value per share since inception and for the six month period ended June 30, 2009, was 24.52% and 23.87%, respectively. Total return on our common shares excludes shares held by our Manager. See Description of Shares Manager s Shares, for a detailed description of how shares held by our Manager were treated prior to July 1, 2009.

Table of Contents

The following table shows our book value per outstanding common share as of our inception date and as of the end of each fiscal quarter thereafter, the quarterly total return for each such quarter and the cumulative total return as of the end of each such quarter:

	Book Value(1)	Quarterly Total Return(1)(2)	Cumulative Total Return(1)(2)
Inception (August 17, 2007)	$ 19.17		
September 30, 2007	$ 19.10	(0.37)%	(0.37)%
December 31, 2007	$ 19.35	1.31%	0.94%
March 31, 2008	$ 18.96	(2.02)%	(1.10)%
June 30, 2008	$ 20.28	6.96%	5.79%
September 30, 2008	$ 20.47	0.94%	6.78%
December 31, 2008	$ 19.27	(5.86)%	0.52%
March 31, 2009(3)	$ 20.83	8.10%	8.66%
June 30, 2009(4)	$ 23.87	14.59%	24.52%

(1) Amounts exclude common shares issuable upon conversion of outstanding LTIP units. As of June 30, 2009, we had 11,901,533 common shares outstanding and 381,250 LTIP units outstanding (which are convertible into common shares on a one-to-one basis).
(2) Returns are calculated based on the sum of the changes in book value per share plus distributions per share. As of June 30, 2009, we had not paid any distributions on our common shares.
(3) Returns include the effect of share repurchases during the quarter. Because we repurchased common shares during the quarter at a discount to our book value per common share and subsequently canceled the repurchased shares, the share repurchases were accretive to our quarter-end book value per common share. Had this accretive benefit not been included, total return for the first quarter of 2009 would have been 6.26% and cumulative total return would have been 6.83%.
(4) Returns include the effect of share repurchases during the quarter. Because we repurchased common shares during the quarter at a discount to our book value per common share and subsequently canceled the repurchased shares, the share repurchases were accretive to our quarter-end book value per common share. Had this accretive benefit not been included, total return for the second quarter of 2009 would have been 14.11% and cumulative total return would have been 21.54%.

As of August 31, 2009, our book value per common share was approximately $. The change in our book value per common share as compared to June 30, 2009, resulted primarily from net realized and unrealized gains (losses) on investments. Our results can fluctuate from month to month depending on a variety of factors, some of which are beyond our control and/or are difficult to predict, including, without limitation, changes in interest rates, changes in default rates and prepayment speeds, and other changes in market conditions and economic trends. Therefore, you should not assume that our performance (as measured by the change in our book value per share) for the two month period ended August 31, 2009 is indicative of what our performance is likely to be for the three month period ended September 30, 2009, and we cannot assure you that our performance for the full three month period or in future periods will be consistent with our performance for the two month period ended August 31, 2009 or consistent with our performance in recent periods. The estimated book value per common share as of August 31, 2009 that is referenced above does not reflect the impact on our book value of the $1.50 dividend that was paid on September 15, 2009 to shareholders of record as of September 1, 2009.

We believe that our performance is attributable to the experience and expertise of our Manager. We further believe that our strategy of being flexible with respect to the sectors of the non-Agency RMBS market in which we acquire assets and the level of credit exposure taken in our portfolio combined with selective hedging of credit risk in our portfolio has been effective in these difficult markets. Given the substantial declines in the mortgage markets during the last two years, as evidenced by the decline in the 2006-2 AAA ABX index from approximately 91.75 as of August 17, 2007 to approximately 36.00 as of August 31, 2009, we believe that we have performed well relative to the broader mortgage market.

The 2006-2 AAA ABX index, an index widely used and cited by investors and market participants tracking the subprime non-Agency RMBS market, is composed of 20 credit default swaps referencing mortgage-backed securities, originally rated AAA by Standard & Poor s, Inc., or Standard & Poor s, and Aaa by Moody s Investors

Table of Contents

Service, Inc., or Moody s, issued during the first six months of 2006 and backed by subprime mortgage loans originated in late 2005 and early 2006. Subject to certain selection criteria, these transactions represent some of the largest subprime mortgage securitizations completed during the first six months of 2006. Given that monthly subprime loan origination peaked in the last six months of 2005 and that monthly subprime non-Agency RMBS issuance peaked in late 2005 and early 2006, we believe that the performance of this index since our inception is a representative measure of the performance of the subprime non-Agency RMBS market over the same period.

All performance data provided is historical and is not indicative of future results, and there can be no assurance that these or comparable results will be achieved or that performance objectives will be achieved.

Our Hedging Strategy

In addition to utilizing derivatives to generate profits outright, we utilize derivatives and other hedging instruments to opportunistically hedge our credit and interest rate risk. For example, we enter into short positions using credit default swaps to protect against adverse credit events with respect to an underlying credit instrument (which may be a single debt instrument, a basket of debt instruments, or an issuer of a series of debt instruments). We also enter into short positions in interest rate swaps to offset the potential adverse effects that changes in interest rates will have on the value of our assets and our financing costs. We also enter into derivative contracts for hedging purposes referencing the unsecured corporate credit, or the equity of corporations. See Our Portfolio, for a description of our short derivatives positions, most of which were entered into for hedging purposes.

Our Financing Strategy

We finance our assets with what we believe to be a prudent amount of leverage, the level of which varies from time to time based upon the particular characteristics of our portfolio, availability of financing and market conditions. Our borrowings currently consist solely of reverse repurchase agreements, or reverse repos. Currently, the great majority of our reverse repo borrowings are collateralized by Agency RMBS; however, should the prospects for stable and reliable reverse repo financing for non-Agency RMBS continue to improve, we would expect to increase our reverse repo borrowings that are collateralized by non-Agency RMBS. While the proceeds of our reverse repo financings are generally used to finance the assets subject to the repo, our financing arrangements do not restrict our ability to use the proceeds from these arrangements to support our other liquidity needs. Our reverse repo arrangements are typically documented under the standard form Master Repurchase Agreement published by the Securities Industry and Financial Market Association (formerly The Bond Market Association), or SIFMA, with the ability for both parties to request margin. Given daily market volatility, we and our repo counterparties are required to post additional margin collateral to each other from time to time as part of the normal course of our business. Our reverse repo financing counterparties generally have the right to determine the value of the underlying collateral for margining purposes, subject to the terms and conditions of our agreement with the counterparty, including in certain cases our right to dispute the counterparty s valuation determination. As of June 30, 2009, we had approximately $352.1 million outstanding on reverse repos with four counterparties. These borrowings were the only debt financings we had outstanding as of June 30, 2009, and, given that we had approximately $284.1 million of shareholders equity as of June 30, 2009, our debt-to-equity ratio was 1.24 to 1. Our debt-to-equity ratio does not account for liabilities other than debt financings. As of June 30, 2009, the remaining terms on our reverse repos ranged between 6 and 71 days.

We may utilize other types of borrowings in the future, including term facilities or other more complex financing structures. Additionally, we may also take advantage of available borrowings, if any, under new programs established by the U.S. Government such as the Term Asset Loan Facility, or TALF, to finance our assets. We also may raise capital by issuing unsecured debt, preferred or common shares, or trust preferred securities.

Our use of leverage, especially in order to increase the amount of assets supported by our capital base, may have the effect of increasing losses when these assets underperform. Our investment policies require no minimum or maximum leverage and our Manager s investment and risk management committee will have the discretion, without the need for further approval by our board of directors, to change both our overall leverage and the leverage used for individual asset classes. Because our strategy is flexible, dynamic and opportunistic, our overall leverage will vary over time. As a result, we do not have a targeted debt-to-equity ratio.

Our Competitive Strengths

Experienced and Cohesive Management Team. We believe that the extensive experience of our officers and the officers and employees of Ellington and our Manager provides us with expertise across all of our targeted asset classes. Certain of our officers were founding principals of Ellington and have worked together in the mortgage securities business for over 14 years. Among the members of our management team are the former heads of RMBS origination and trading, whole loan MBS origination and trading and fixed income research and quantitative systems at Kidder Peabody. Our Chief Executive Officer, Mr. Penn, was one of the founding principals of Ellington and worked for 10 years at Lehman Brothers where he co-headed the Lehman Brothers trading desk for collateralized mortgage obligations, or CMOs.

Access to Leading Investment Advisor. We benefit substantially from our relationship with our Manager and Ellington through our access to Ellington s investment ideas, proprietary research, models and analytics, trading and structuring expertise, risk management, and asset-sourcing capabilities. We believe this relationship provides us with unique access to attractive opportunities and market information that enhances our ability to make decisions regarding our targeted asset classes, which we believe is a significant competitive advantage. We believe that Ellington possesses the essential elements necessary to successfully acquire and manage RMBS and our other targeted asset classes: portfolio management experience across multiple market cycles, asset selection, trading and hedging expertise, broad asset sourcing capabilities, and sophisticated risk management systems and analytical tools.

As of June 30, 2009, Ellington employed over 100 employees, including 14 principals with an average of over 20 years of industry experience; its Chief Executive Officer and three Vice Chairmen have an average of over 24 years of industry experience. Ellington and its senior management have a long history managing a broad range of asset classes and sectors and extensive experience as a leader in buying, selling, analyzing, and structuring MBS and ABS. As of June 30, 2009, Ellington, including our company, various hedge funds, and various private accounts, had net assets under management of approximately $2.2 billion, in addition to approximately $578.0 million of net assets under management in certain hedge funds that have not been actively making new investments but rather have been returning capital to investors. In addition, Ellington, through its affiliates, manages CDOs collateralized by MBS or ABS and a traditional managed account.

Sophisticated Platform and Analytical Capabilities. We benefit from Ellington s proprietary analytical models and infrastructure, which have been developed as a result of many years of experience as a significant participant in our target markets. Ellington s risk management process emphasizes the quantitative assessment of credit risk, interest rate risk and prepayment risk, both on a security-by-security and portfolio basis. This is only possible with sophisticated quantitative tools and methodologies that are the foundation of Ellington s investment technique and asset surveillance. Analyzing RMBS credit risk and prepayment risk, in particular, necessitates the development and continuous refinement of sophisticated statistics-based computer models. We believe that these skills and range of resources, together with Ellington s experience investing and leveraging large pools of capital in complex mortgage and derivative instruments through various economic and business cycles, are critical for us to meet our objectives. We believe that Ellington s proprietary models and modeling capabilities provide it with a competitive advantage over most other market participants.

Strong Relationships and Deal Flow. Acquiring our targeted assets is a highly competitive process, and our Manager competes with many other investment managers and companies for attractive opportunities in these areas. We believe that the strengths of Ellington in this regard give us a competitive advantage. We capitalize on the proprietary deal-sourcing opportunities that Ellington brings to us as a result of its investment experience in our targeted asset classes and extensive network of contacts in the financial community.

Table of Contents

Ellington currently sources many of its and our assets through its well-developed relationships with a large and diverse group of financial intermediaries. Ellington has extensive contacts throughout the market and experience dealing with investment banks, lenders and other major market participants, as well as a thorough knowledge of the characteristics and location of the product inventory in the fixed income markets.

Alignment of Interests between Our Manager, the Manager Group and Our Investors. As of November 2, 2009, the Manager Group owned 1,794,004 of our common shares, excluding LTIP units, representing approximately 15.0% of our common shares outstanding as of that date. EMG Holdings, L.P., an affiliate of our Manager, has committed to purchase in a concurrent private placement at a price per share equal to the initial public offering price per share, no less than the greater of (i) common shares and (ii) the lesser of common shares and the number of common shares sufficient for the Manager Group to own, in aggregate, % of our outstanding common shares immediately after completion of this offering and the concurrent private placement, excluding any shares sold pursuant to the underwriters exercise of their over-allotment option. Subject to these conditions, assuming we sell the number of shares set forth on the cover of this prospectus, EMG Holdings, L.P. will purchase common shares from us in the concurrent private placement. Upon completion of this offering and the concurrent private placement to EMG Holdings, L.P., the Manager Group will own an aggregate of common shares representing approximately % of our outstanding common shares, excluding LTIP units, at that time. Our directors and executive officers and the Manager Group have indicated that they intend to enter into lock-up agreements covering of our common shares, including vested LTIP units and the common shares purchased by EMG Holdings, L.P. in the concurrent private placement. In addition, our Manager receives at least 10.0% of its incentive fee under our management agreement in the form of EFC common shares. Our Manager has agreed not to sell any of the common shares it receives as part of its incentive fee prior to one year after the date such shares are issued. To date, the Manager Group has not sold any of our common shares.

Summary Risk Factors

An investment in our common shares involves various risks. You should consider carefully the risks listed below and those risks under Risk Factors before purchasing common shares.

- Difficult conditions in the mortgage and residential real estate markets have caused and may cause us to experience losses and these conditions may persist for the foreseeable future.

- No assurance can be given that the actions taken by the U.S. Government, including the Federal Reserve and the Treasury, and other governmental and regulatory bodies, for the purpose of stabilizing the financial and credit markets will achieve their intended effect, or will benefit our business, and further government or market developments could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

- The federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government, may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

- Mortgage loan modification programs and future legislative action may adversely affect the value of, and the returns on, our targeted assets.

- The principal and interest payments on our non-Agency RMBS are not guaranteed by any entity, including any government entity or government-sponsored entity, or GSE, and, therefore, are subject to increased risks, including credit risk.

- We rely on analytical models and other data to analyze potential asset acquisition and disposition opportunities and to manage our portfolio. Such models and other data may be incorrect, misleading or

Table of Contents

incomplete, which could cause us to purchase assets that do not meet our expectations or to make asset management decisions that are not in line with our strategy.

Valuations of some of our assets are inherently uncertain, may be based on estimates, may fluctuate over short periods of time and may differ from the values that would have been used if a ready market for these assets existed. As a result, the values of some of our assets are uncertain.

Prepayment rates can change, adversely affecting the performance of our assets.

We leverage certain of our assets, which may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Interest rate mismatches between our assets and any borrowings used to fund purchases of our assets may reduce our income during periods of changing interest rates.

Our lenders may require us to provide additional collateral, especially when the market values for our assets decline, which may restrict us from leveraging our assets as fully as desired, force us to liquidate assets, reduce our liquidity, and materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Hedging against credit events and interest rate changes and other risks may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We are dependent on our Manager and certain key personnel of Ellington that are provided to us through our Manager and may not find a suitable replacement if our Manager terminates the management agreement or such key personnel are no longer available to us.

The base management fee payable to our Manager is payable regardless of the performance of our portfolio, which may reduce its incentive to devote the time and effort to seeking profitable opportunities for our portfolio.

Our Manager s incentive fee may induce our Manager to acquire certain assets, including speculative or high risk assets, or to acquire assets with increased leverage, which could increase the risk to our portfolio.

We compete with Ellington s other accounts for access to Ellington.

We and other Ellington accounts may compete for opportunities to acquire assets, which are allocated in accordance with Ellington s investment allocation policies.

There are conflicts of interest in our relationships with our Manager and Ellington, which could result in decisions that are not in the best interests of our shareholders.

There may not be an active market for our common shares, which may cause our common shares to trade at a discount to the initial offering price and make it difficult to sell the common shares you purchase.

The market price and trading volume of our common shares may be volatile following this offering.

Future sales of our common shares could have an adverse effect on our share price.

Our shareholders may not receive distributions or distributions may not grow over time.

Investing in our common shares involves a high degree of risk.

If we were required to register as an investment company under the Investment Company Act, we would be subject to the restrictions imposed by the Investment Company Act, which would require us to make material changes to our strategy.

If we fail to satisfy the qualifying income exception under the tax rules for publicly traded partnerships, all of our income will be subject to an entity-level tax.

The Internal Revenue Service, or IRS, Schedules K-1 we will provide will be significantly more complicated than the IRS Forms 1099 provided by real estate investment trusts, or REITs, and regular corporations, and holders of our common shares may be required to request an extension of time to file their tax returns.

Table of Contents

Our Formation and Structure

We were formed as a Delaware limited liability company in July 2007 and completed our initial capitalization in August 2007. We have a holding company structure and conduct most of our business through various subsidiaries. The following chart illustrates our organizational structure immediately prior to the completion of this offering and the concurrent private placement to EMG Holdings, L.P., an affiliate of our Manager.

(1) EMG Holdings, L.P. is a holding company that owns interests in our Manager, Ellington, and other Ellington affiliates. VC Investments L.L.C. is the general partner of EMG Holdings, L.P., and is also the managing member of our Manager and Ellington, and as such controls each of these three entities. The limited partners of EMG Holdings L.P. include Mr. Vranos and certain other Ellington principals.

(2) Michael Vranos, our Co-Chief Investment Officer, beneficially owns a controlling interest in VC Investments L.L.C.

Table of Contents

(3) Includes 1,258,783 common shares held by EMG Holdings, L.P., but excludes LTIP units held by EMG Holdings, L.P.
(4) Includes 35,221 common shares held by Ellington Financial Management LLC, but excludes LTIP units held by Ellington Financial Management LLC.
(5) This entity has established a wholly-owned subsidiary for the purpose of utilizing TALF financing for asset purchases. See Management s Discussion and Analysis of Financial Condition and Results of Operations Trends and Recent Market Developments.
(6) Our assets generally include cash, cash equivalents, shares of EF Mortgage LLC and shares of EF Securities LLC. EF Mortgage LLC s assets generally include Agency whole pool pass-through certificates and shares of EF CMO LLC. EF CMO LLC s assets generally include non-Agency CMOs. EF Securities LLC s assets generally include any targeted assets that are not cash, cash equivalents, Agency whole pool pass-through certificates, or CMOs; however EF Securities LLC s assets may also include cash and certain CMOs. Although the foregoing reflects recent and current allocations of assets among our subsidiaries, as well as our expectations for our allocations in the near term, we may choose to allocate assets among our subsidiaries in a different manner going forward.

Conflicts of Interest; Equitable Allocation of Opportunities

Ellington manages, and expects to continue to manage, other funds, accounts and vehicles that have strategies that are similar to, or that overlap with, our strategy. As of June 30, 2009, Ellington managed various funds, accounts and vehicles that have strategies that are similar to, or that overlap with, our strategy, that have aggregate net assets of approximately $1.9 billion (excluding our assets and excluding the assets of certain hedge funds that have not been actively making new investments but rather have been returning capital to investors). Ellington makes available to our Manager all opportunities to acquire assets that it determines, in its reasonable and good faith judgment, based on our objectives, policies and strategies, and other relevant factors, are appropriate for us in accordance with Ellington s written investment allocation procedures and policies, subject to the exception that we might not participate in each such opportunity, but will on an overall basis equitably participate with Ellington s other accounts in all such opportunities. Ellington s investment and risk management committee and its compliance committee (headed by its Chief Compliance Officer) are responsible for monitoring the administration of, and facilitating compliance with, Ellington s investment allocation procedures and policies.

Because many of our targeted assets are typically available only in specified quantities and because many of our targeted assets are also targeted assets for other Ellington accounts, Ellington often is not able to buy as much of any given asset as required to satisfy the needs of all its accounts. In these cases, Ellington s investment allocation procedures and policies typically allocate such assets to multiple accounts in proportion to their needs and available capital. As a result, accounts in start-up mode are given priority. The policies permit departure from such proportional allocation when such allocation would result in an inefficiently small amount of the security being purchased for an account. In that case, the policy allows for a protocol of allocating assets so that, on an overall basis, each account is treated equitably.

Other policies of Ellington that our Manager will apply to the management of our company include controls for cross transactions (transactions between Ellington-managed accounts), principal transactions (transactions between Ellington and an Ellington-managed account), investments in other Ellington accounts and split price executions. To date we have not entered into any cross transactions with other Ellington-managed accounts, principal transactions with Ellington or invested in other Ellington accounts. See Business Conflicts of Interest; Equitable Allocation of Opportunities for a more detailed description of these types of transactions and the policies of Ellington and our Manager that govern these types of transactions.

Our executive officers and the officers and employees of our Manager are also officers and employees of Ellington, and, with the exception of those officers that are dedicated to us, we compete with other Ellington accounts for access to these individuals.

The management agreement with our Manager does not restrict the ability of its officers and employees from engaging in other business ventures of any nature, whether or not such ventures are competitive with our business.

Table of Contents

Our Management Agreement

We entered into a management agreement with our Manager upon our inception in August 2007. The management agreement, which was amended and restated effective July 1, 2009, has a current term that expires on December 31, 2011, and will be automatically renewed for successive one-year terms thereafter unless notice of non-renewal is delivered by either party to the other party at least 180 days prior to the expiration of the then current term. Pursuant to the management agreement, our Manager implements our strategy and manages our assets and our day-to-day business and operations and performs certain services for us, subject to oversight by our board of directors. Our Manager is responsible for, among other duties, determining criteria, in conjunction with our board of directors, for sourcing, analyzing and executing asset purchases, asset sales and financings and performing asset management duties.

The following table summarizes the fees and expense reimbursements and other amounts that we pay to our Manager and its affiliates.

Type	Description	Payment
Base management fee	We pay a base management fee of 1.50% per annum of our shareholders equity (calculated in accordance with GAAP) as of the end of each fiscal quarter (before calculations related to base management fees and incentive fees with respect to such quarter). Shareholders equity will be adjusted to exclude one-time events pursuant to changes in GAAP, as well as non-cash charges after discussion between our Manager and our independent directors and approval by a majority of our independent directors in the case of non-cash charges.	Quarterly in arrears in cash
Incentive fee	In addition to the base management fees, with respect to each fiscal quarter we pay an incentive fee equal to the excess, if any, of (i) the product of (A) 25% and (B) the excess of (1) our Adjusted Net Income (described below) for the Incentive Calculation Period (which means such fiscal quarter and the immediately preceding three fiscal quarters (but excluding any fiscal quarters prior to July 1, 2009)) over (2) the sum of the Hurdle Amounts (described below) for the Incentive Calculation Period, over (ii) the sum of the incentive fees already paid or payable for each fiscal quarter in the Incentive Calculation Period preceding such fiscal quarter.	Quarterly in arrears in a combination of common shares and cash, provided that at least 10% of any quarterly payment will be made in EFC common shares
	Adjusted Net Income for the Incentive Calculation Period means our net increase in shareholders equity from operations (or such equivalent GAAP measure based on the basis of presentation of our consolidated financial statements) for such period, after all base management fees but before any incentives fees for such period, and excluding any non-cash equity compensation expenses for such period, as reduced by any Loss Carryforward (as described below) remaining as of the end of the fiscal quarter preceding the Incentive Calculation Period. Adjusted Net Income will be adjusted to exclude one-time events pursuant to changes in GAAP, as well as non-cash charges after discussion between our	
	Manager and our independent directors and approval by a majority of our independent directors in the case of non-cash charges.	

Type	Description	Payment
	The Loss Carryforward as of the end of any fiscal quarter is calculated by determining the excess, if any, of (1) the Loss Carryforward as of the end of the immediately preceding fiscal quarter over (2) our net increase in shareholders equity from operations (expressed as a positive number) or net decrease in shareholders equity from operations (expressed as a negative number) for such fiscal quarter (or such equivalent GAAP measures as may be appropriate depending on the basis of presentation of our consolidated financial statements), as the case may be, calculated in accordance with GAAP, adjusted to exclude one-time events pursuant to changes in GAAP, as well as non-cash charges after discussion between our Manager and our independent directors and approval by a majority of our independent directors in the case of non-cash charges.	
	For purposes of calculating the incentive fee, the Hurdle Amount means, with respect to any fiscal quarter, the product of (i) one-fourth of the greater of (A) 9% and (B) 3% plus the ten-year Treasury rate for such fiscal quarter (determined as provided in the management agreement), (ii) the sum of (A) the weighted average gross proceeds per share of all of our common share issuances (excluding issuances of our common shares (a) as equity incentive awards, (b) to our Manager as part of its base management fees or incentive fees and (c) to our Manager or any of its affiliates in privately negotiated transactions) up to the end of such fiscal quarter (with each such issuance weighted by both the number of shares issued in such issuance and the number of days that such issued shares were outstanding during such fiscal quarter) and (B) the result obtained by dividing (I) retained earnings attributable to our common shares at the beginning of such fiscal quarter by (II) the average number of our common shares outstanding for each day during such fiscal quarter, and (iii) the average number of our common shares and LTIP units outstanding for each day during such fiscal quarter.	
Expense reimbursement	We reimburse our Manager for certain expenses directly related to our operations incurred by our Manager on our behalf or for our benefit, including legal, accounting and other services provided by outside professionals, as well as the costs associated with a dedicated Chief Financial Officer and a dedicated in-house counsel, and, if provided by our Manager, a dedicated controller.	Quarterly in cash

Operating and Regulatory Structure

Tax Requirements

We believe that we have been organized and have operated so that we have qualified, and will continue to qualify, to be treated for U.S. federal income tax purposes as a partnership and not as an association or a publicly traded partnership taxable as a corporation. In general, an entity that is treated as a partnership for U.S. federal income tax purposes is not subject to U.S. federal income tax at the entity level. Consequently, as a holder of our common shares, you will be required to take into account your allocable share of items of our income, gain, loss, deduction and credit for our taxable year ending within or with your taxable year, regardless of whether we make cash distributions on a current basis with which to pay any resulting tax. We believe that we are treated, and will continue to be treated, as a publicly traded partnership. Publicly traded partnerships are generally treated as partnerships for U.S. federal income tax purposes as long as they satisfy certain income and other tests on an ongoing basis. We believe that we have satisfied and will continue to satisfy those requirements and that we have been and will continue to be treated as a partnership for U.S. federal income tax purposes.

Investment Company Act Exclusions

Most of our business is conducted through various wholly-owned or majority-owned subsidiaries in a manner such that neither we nor our subsidiaries are subject to regulation under the Investment Company Act. Under Section 3(a)(1) of the Investment Company Act, a company is deemed to be an investment company if:

- it is, or holds itself out as being, engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting or trading in securities (Section 3(a)(1)(A)); or

- it is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and does own or proposes to acquire investment securities having a value exceeding 40% of the value of its total assets (excluding U.S. Government securities and cash) on an unconsolidated basis, or the 40% Test. Investment securities excludes U.S. Government securities and securities of majority-owned subsidiaries that are not themselves investment companies and are not relying on the exception from the definition of investment company for private funds under Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

We believe we will not be considered an investment company under Section 3(a)(1)(A) of the Investment Company Act because we will not engage primarily or hold ourself out as being engaged primarily in the business of investing, reinvesting or trading in securities. Rather, through wholly owned or majority-owned subsidiaries, we will be primarily engaged in the non-investment company businesses of these subsidiaries.

The 40% Test limits the types of businesses in which we may engage either directly or through our subsidiaries. Our wholly-owned subsidiary, EF Mortgage LLC, relies on the exclusion provided by Section 3(c)(5)(C) under the Investment Company Act. It, in turn, has a wholly-owned subsidiary, EF CMO LLC, which invests in mortgage-related securities and relies on Section 3(c)(7) of the Investment Company Act. EF Mortgage LLC treats its investment in EF CMO LLC as a real estate-related asset for purposes of its own exclusion under Section 3(c)(5)(C). Our other wholly-owned subsidiary, EF Securities LLC, owns securities, including various kinds of mortgage-related securities and relies on the exemption provided by Section 3(c)(7) of the Investment Company Act; therefore, we treat securities that we own and that were issued by EF Securities LLC as investment securities and are required to keep the value of these securities, together with any other investment securities we own, below 40% of our total assets (excluding U.S. Government securities and cash) on an unconsolidated basis. Any subsidiaries we may form in the future may not be majority-owned or wholly-owned by us or might rely on the exemption provided by Section 3(c)(1) or 3(c)(7) of the Investment Company Act, in which case we would treat securities that we own and that were issued by these types of subsidiaries as investment securities and be required to keep the value of these securities (together with the value of our investment in EF Securities LLC and any other investment securities we own) below 40% of our total assets (excluding U.S. Government securities and cash) on an unconsolidated basis.

Section 3(c)(5)(C), the Investment Company Act exclusion upon which EF Mortgage LLC relies, is designed for entities primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate. This exclusion generally requires that at least 55% of the entity s assets consist of qualifying real estate assets and at least 80% of the entity s assets consist of either qualifying real estate assets or real estate-related assets. Qualifying real estate assets for this purpose include mortgage

Table of Contents

loans, whole pool Agency pass-through certificates and other assets that the SEC staff has determined in various no-action letters are the functional equivalent of mortgage loans for the purposes of the Investment Company Act. We intend to treat as real estate-related assets RMBS that do not satisfy the conditions set forth in those SEC staff no-action letters. In classifying the assets held by EF Mortgage LLC as qualifying real estate assets or real estate-related assets, we also will rely on any other guidance published by the SEC staff or on our analyses (in consultation with outside counsel) of guidance published with respect to other types of assets to determine which assets are qualifying real estate assets and real estate-related assets.

Both the 40% Test and the requirements of the Section 3(c)(5)(C) exclusion limit the types of businesses in which we may engage and the types of assets we may hold, as well as the timing of sales and purchases of assets.

There can be no assurance that the laws and regulations governing the Investment Company Act status of companies similar to ours, or the guidance from the Division of Investment Management of the SEC regarding the treatment of assets as qualifying real estate assets or real estate-related assets, will not change in a manner that adversely affects our operations. To the extent that the SEC staff provides more specific guidance regarding any of the matters bearing upon our exemption from the need to register under the Investment Company Act, we may be required to adjust our strategy accordingly. Any additional guidance from the SEC staff could provide additional flexibility to us, or it could further inhibit our ability to pursue the strategies that we have chosen. Furthermore, although we intend to monitor the assets of EF Mortgage LLC regularly, there can be no assurance that EF Mortgage LLC will be able to maintain this exclusion from registration. In that case, our investment in EF Mortgage LLC would be classified as an investment security, and we might not be able to maintain our overall exclusion from registering as an investment company under the Investment Company Act.

If we or our subsidiaries were required to register as an investment company under the Investment Company Act, we would become subject to substantial regulation with respect to our capital structure (including our ability to use leverage), management, operations, transactions with affiliated persons (as defined in the Investment Company Act), and portfolio composition, including restrictions with respect to diversification and industry concentration and other matters. Compliance with the restrictions imposed by the Investment Company Act would require us to make material changes to our strategy which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders. Accordingly, to avoid that result, we may be required to adjust our strategy, which could limit our ability to make certain investments or require us to sell assets in a manner, at a price or at a time that we otherwise would not have chosen. This could negatively affect the value of our common shares, the sustainability of our business model and our ability to make distributions.

Investment Advisers Act of 1940

Both Ellington and our Manager are registered as investment advisers under the Investment Advisers Act of 1940, as amended, or the Advisers Act, and are subject to the regulatory oversight of the Investment Management Division of the SEC.

Distribution Policy

The declaration of distributions to our shareholders and the amount of such distributions are at the discretion of our board of directors. Our present intention is to make quarterly and special distributions to our common shareholders so that at least 50% of our net income attributable to our common shares each calendar year has been distributed prior to April of the subsequent calendar year, subject to adjustments for changes in common shares outstanding. In setting the level of shareholder distributions, our board of directors takes into account, among other things, our earnings, our financial condition, our working capital needs and new investment opportunities. Our ability to make distributions is subject to certain restrictions under the Delaware Limited Liability Company Act, or the Delaware LLC Act. Under the Delaware LLC Act, a limited liability company

Table of Contents

generally is not permitted to make a distribution if, after giving effect to the distribution, the liabilities of the company will exceed the value of the company s assets. In addition, it is possible that some of our future financing arrangements could contain provisions restricting our ability to make distributions. Shareholders generally will be subject to U.S. federal income tax (and any applicable state and local taxes) on their respective allocable shares of our net taxable income regardless of the timing or amount of distributions we make to our shareholders. On August 7, 2009, our board of directors authorized our first distribution to our shareholders of $1.50 per share for the quarter ended June 30, 2009. The distribution was paid on September 15, 2009 to our shareholders of record as of September 1, 2009. The distribution represented approximately 36.7% of our net income for the first six months of the 2009 fiscal year. We cannot assure you that we will make any future distributions to our shareholders and this distribution is not intended to be indicative of the amount and timing of future distributions, if any.

Lock-up Agreements

Our directors and executive officers and the Manager Group have indicated that they intend to enter into lock-up agreements covering a period of 180 days after the date of this prospectus with respect to our common shares held by them. The number of shares, including vested LTIP units, that will be subject to lock-up agreements covering a period of 180 days after the date of this prospectus is , including the common shares purchased by EMG Holdings, L.P. in the concurrent private placement. One Ellington-managed hedge fund, which owns 120,000 of our common shares, will be subject to a lock-up agreement covering a period of 60 days after the date of this prospectus. Two other Ellington-managed hedge funds, which collectively own 1,130,000 of our common shares, are selling shareholders named in this prospectus and do not at the present time intend to be subject to lock-up agreements in the event the number of shares offered by such selling shareholders is reduced. In addition, unaffiliated shareholders that beneficially hold common shares have entered into lock-up agreements covering a period of 60 days after the date of this prospectus.

Our Corporate Information

Our principal executive offices are located at 53 Forest Avenue, Old Greenwich, CT 06870. Our telephone number is (203) 698-1200. Our internet address is www.ellingtonfinancial.com. Our internet web site, and the information contained therein or connected thereto, does not constitute part of this prospectus.

Table of Contents

The Offering

Common shares offered by us	common shares (plus up to an additional common shares that we may issue and sell upon the exercise of the underwriters over-allotment option)
Common shares offered by selling shareholders	1,130,000
Shares outstanding after this offering and the concurrent private placement	common shares(1)
Use of proceeds	The net proceeds from this offering, after deducting underwriting discounts and commissions and estimated offering expenses, will be approximately $ million (or approximately $ million if the underwriters fully exercise their over-allotment option). We expect to use a substantial portion of the net proceeds of this offering and the concurrent private placement to acquire our targeted assets within six months after the closing of this offering and the concurrent private placement. We expect to use the balance of the net proceeds of this offering and the concurrent private placement, if any, for working capital and general corporate purposes. Pending such uses, we may invest the net proceeds from this offering and the concurrent private placement in interest-bearing, short-term investments, including money market accounts. See Use of Proceeds.
Distribution policy	Our present intention is to make quarterly and special distributions to our common shareholders so that at least 50% of our net income attributable to our common shares each calendar year has been distributed prior to April of the subsequent calendar year, subject to adjustments for changes in common shares outstanding. The declaration of distributions to our shareholders and the amount of such distributions are at the discretion of our board of directors. In setting the level of shareholder distributions, our board of directors takes into account, among other things, our earnings, our financial condition, our working capital needs and new opportunities. See Distribution Policy.
Ownership and transfer restrictions	We may own interests in real estate investment trusts, or REITs. Due to limitations on the concentration of ownership of REITs that are imposed by the Internal Revenue Code of 1986, as amended, or the Code, our operating agreement generally prohibits any holder of our common shares from directly or indirectly owning more than 9.8% of the aggregate value or number (whichever is more restrictive) of our outstanding shares. Our board of directors has granted an exemption from this limitation to Ellington, certain affiliated entities of Ellington and certain non-affiliated entities, subject to certain terms and conditions. In addition, our operating agreement contains various other restrictions on the ownership and transfer of our common shares.
Risk Factors	See Risk Factors and other information included in this prospectus for a discussion of factors you should carefully consider before deciding to invest in the common shares.
Proposed New York Stock Exchange Symbol	EFC

(1) The number of common shares outstanding after this offering includes (i) 12,500,000 common shares issued in our August 2007 private offering, (ii) 50 common shares issued in connection with the formation of our company, (iii) 43,954 common shares issued to our Manager as part of the incentive fees we have paid to our Manager, (iv) 3,750 common shares that have been issued in connection with LTIP unit conversions, (v) common shares being offered in this offering and (vi) shares to be sold to EMG Holdings, L.P. in a concurrent private placement. The number of common shares outstanding after this offering and the concurrent private placement (i) excludes 375,000 common shares which are issuable upon conversion of 375,000 LTIP units that were issued to our Manager and 7,500 common shares which are issuable upon conversion of 7,500 LTIP units that were issued to our independent directors to date and (ii) reflects the repurchase by us of 608,500 of our common shares. The number of common shares outstanding after the offering and the concurrent private placement also excludes up to an additional common shares that we may issue and sell upon the exercise of the underwriters over-allotment option.

Table of Contents

Summary Consolidated Financial Information

The following table presents summary consolidated financial information as of June 30, 2009, as of December 31, 2008 and 2007, for the six month periods ended June 30, 2009 and 2008, for the year ended December 31, 2008 and for the period from August 17, 2007 (commencement of operations) to December 31, 2007. The summary consolidated financial information as of June 30, 2009 and for the six month periods ended June 30, 2009 and 2008 have been derived from our unaudited consolidated financial statements included elsewhere in this prospectus. The summary consolidated financial information presented below as of December 31, 2008 and 2007, for the year ended December 31, 2008 and for the period from August 17, 2007 (commencement of operations) to December 31, 2007, have been derived from our audited consolidated financial statements included elsewhere in this prospectus. These unaudited consolidated financial statements have been prepared on substantially the same basis as our audited consolidated financial statements and include all adjustments that we consider necessary for a fair presentation of our consolidated financial position and results of operations for the periods presented therein. These results are not necessarily indicative of our results for the full fiscal year. Similarly, because we only operated our business for a portion of the year ended December 31, 2007, we do not believe that a comparison of our operating results for the year ended December 31, 2008 to the period from August 17, 2007 (commencement of operations) to December 31, 2007 is indicative of the trends in our performance.

Since the information presented below is only a summary and does not provide all of the information contained in our historical consolidated financial statements included elsewhere in this prospectus, including the related notes, you should read it in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations, and our historical consolidated financial statements, including the related notes, included elsewhere in this prospectus.

	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008	Year Ended December 31, 2008	Period from August 17, 2007 (commencement of operations) to December 31, 2007
Net Investment Income:				
Interest Income	$ 22,934,130	$ 12,924,980	$ 29,914,585	$ 5,898,720
Expenses:				
Base management fee	1,958,546	1,822,210	3,721,121	1,355,912
Incentive fee	8,407,373	1,771,026	1,771,026	
Share-based LTIP expense	1,823,000	1,312,430	2,389,436	906,973
Interest expense	1,012,021	1,698,267	6,189,887	
Professional fees	1,057,927	405,500	1,524,060	658,185
Other expenses	837,227	662,435	1,494,115	625,117
Total expenses	15,096,094	7,671,868	17,089,645	3,546,187
Net Investment Income	7,838,036	5,253,112	12,824,940	2,352,533
Net Realized and Unrealized Gain (Loss) on Investments and Financial Derivatives:				
Net realized gain (loss) on:				
Investments	(21,463,442)	(278,335)	(5,075,879)	1,753,849
Financial derivatives	20,743,064	6,015,766	63,598,153	
Net realized gain (loss)	(720,378)	5,737,431	58,522,274	1,753,849

Table of Contents

	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008	Year Ended December 31, 2008	Period from August 17, 2007 (commencement of operations) to December 31, 2007
Change in net unrealized gain (loss) on:				
Investments	$ 50,776,288	$ (32,865,988)	$ (79,180,278)	$ (651,290)
Financial derivatives	(7,532,030)	32,871,545	5,410,419	(130,122)
Change in net unrealized gain (loss)	43,244,258	5,557	(73,769,859)	(781,412)
Net Realized and Unrealized Gain (Loss) on Investments and Financial Derivatives	42,523,880	5,742,988	(15,247,585)	972,437
Net Increase (Decrease) in Shareholders Equity Resulting from Operations	$ 50,361,916	$ 10,996,100	$ (2,422,645)	$ 3,324,970

	As of June 30, 2009	As of December 31, 2008	As of December 31, 2007
Consolidated Balance Sheet Data:			
Cash and cash equivalents	$ 73,858,758	$ 61,400,254	$ 61,705,104
Investments at fair value	565,680,650	429,884,006	180,657,979
Financial derivatives at fair value (appreciated)	133,195,918	141,690,748	
Total assets	922,759,150	699,976,080	243,494,998
Investments sold short at fair value	100,239,532	38,421,032	
Reverse repos	352,098,700	260,534,000	
Financial derivatives at fair value (depreciated)	15,547,559	17,304,903	130,122
Total liabilities	638,614,617	458,898,436	1,668,105
Shareholders equity	284,144,533	241,077,644	241,826,893
Shareholders equity per common share	$ 23.87	$ 19.27	$ 19.35

20

Table of Contents

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements under Summary, Risk Factors, Management s Discussion and Analysis of Financial Condition and Results of Operations, Distribution Policy, Business and other statements included elsewhere in this prospectus constitute forward-looking statements. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. In some cases, you can identify forward-looking statements by terms such as anticipate, believe, could, estimate, expect, intend, may, plan, goal, objective, potential, project, should, will and would or the negative of these te terminology.

The forward-looking statements are based on our beliefs, assumptions and expectations of our future performance, taking into account information currently in our possession. These beliefs, assumptions and expectations may change as a result of many possible events or factors, not all of which are known to us or are within our control. If a change occurs, the performance of our portfolio and our business, financial condition, liquidity and results of operations may vary materially from those expressed, anticipated or contemplated in our forward-looking statements. You should carefully consider these risks before you invest in our common shares, along with the following factors that could cause actual results to vary from our forward-looking statements:

- the effect of the Federal Reserve s and the Treasury s recent actions and programs, including the Treasury s plan to buy Agency RMBS, the TALF, and the Public-Private Investment Program, or PPIP, on the liquidity of the capital markets and the impact and timing of any further programs or regulations implemented by the U.S. Government or its agencies;
- the federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government;
- the volatility of our target markets, especially the markets for non-Agency RMBS and of the market value of our common shares;
- increased rates of default and/or decreased recovery rates on our assets;
- mortgage loan modification programs and future legislative action;
- the degree to which our hedging strategies may or may not protect us from, or expose us to, credit or interest rate risk;
- changes in our business and strategy;
- availability, terms and deployment of capital;
- our projected financial and operating results;
- changes in interest rates and interest rate mismatches between our assets and related borrowings;
- our ability to maintain existing financing agreements, obtain future financing arrangements and the terms of such arrangements;

our ability to effectively deploy the proceeds raised in this offering and the concurrent private placement;

changes in economic conditions generally and the real estate and debt securities markets specifically;

legislative or regulatory changes (including tax law changes and changes to laws governing the regulation of investment companies);

availability of qualified personnel;

estimates relating to our future distributions to our shareholders;

Table of Contents

changes in our industry;

increased prepayments of the mortgages and other loans underlying our RMBS or other ABS;

availability of opportunities in real estate-related and other assets;

the degree and nature of our competition; and

changes to generally accepted accounting principles, or GAAP.

Table of Contents

RISK FACTORS

Investing in our common shares involves a high degree of risk. Before making an investment decision, you should carefully consider the following risk factors and all other information contained in this prospectus.

If any of the following risks occurs, our business, financial condition or results of operation could be materially and adversely affected. If this were to happen, we may be unable to make distributions to our shareholders, the market value of our common shares could decline significantly, and you may lose some or all of your investment. In connection with the forward-looking statements that appear in this prospectus, you should also carefully review the cautionary statements referred to under Special Note Regarding Forward-Looking Statements.

Risks Related To Our Business

Difficult conditions in the mortgage and residential real estate markets have caused and may cause us to experience losses and these conditions may persist for the foreseeable future.

Our business is materially affected by conditions in the residential mortgage market, the residential real estate market, the financial markets and the economy generally. Concerns about the residential mortgage market and a declining real estate market, as well as inflation, energy costs, geopolitical issues and the availability and cost of credit have contributed to increased volatility and diminished expectations for the economy and markets going forward. The residential mortgage market has been severely affected by changes in the lending landscape, the severity of which was largely unanticipated by the markets. There is no assurance that this market has stabilized or that it will not worsen.

For now (and for the foreseeable future), homeowner access to residential mortgage loans has been substantially limited. While the limitation on financing was initially in the subprime mortgage market, it also materially affected the prime jumbo and Alt-A mortgage market, with lending standards having become significantly more stringent than in recent periods and many product types being severely curtailed or eliminated. This financing limitation has had an impact on new demand for homes, has compressed home ownership rates and is weighing heavily on home price performance. There is a strong correlation between home price growth rates and mortgage loan delinquencies. Furthermore, investor perception of the risks associated with RMBS, residential mortgage loans, real estate-related securities and various other assets that we acquire has been negatively impacted by the continued adverse developments in the broader residential mortgage market, which has caused the values of these assets to experience high volatility. The further deterioration of the mortgage market and investor perception of the risks associated with RMBS, residential mortgage loans, real estate-related securities and various other assets that we acquire may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

No assurance can be given that the actions taken by the U.S. Government, including the Federal Reserve and the Treasury, and other governmental and regulatory bodies, for the purpose of stabilizing the financial and credit markets will achieve their intended effect, or will benefit our business, and further government or market developments could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

In response to the issues affecting the banking system and financial and housing markets, the U.S. Government, including the Federal Reserve and the Treasury, and other governmental and regulatory bodies, have taken a number of initiatives intended to bolster the banking system and the financial and housing markets. For a description of some of these initiatives, see Management s Discussion and Analysis of Financial Condition and Results of Operations Trends and Recent Market Developments.

The effects of the actions taken by the U.S. Government and governmental entities and regulatory bodies remain uncertain. Furthermore, the scope and nature of these and other actions are unknown and will continue to

Table of Contents

evolve. No assurance can be given that these initiatives will have the intended beneficial impact on the banking system, financial market or housing market. To the extent the markets do not respond favorably to these initiatives or if these initiatives do not function as intended, the pricing, supply, liquidity and value of our assets and the availability of financing on attractive terms may be materially adversely affected and our business may not receive the intended positive impact from these actions. There can also be no assurance that we will be eligible to participate in programs established by the U.S. Government and other governmental and regulatory bodies, or if we are eligible, that we will be able to utilize them successfully or at all. In addition, because the programs are designed, in part, to stimulate the market for certain of our targeted assets, the establishment of these programs may result in increased competition for our targeted assets. In addition, the U.S. Government and other governmental and regulatory bodies have taken or are considering taking other actions to address the financial crisis. We cannot predict whether or when such actions may occur, and such actions could have a material adverse impact on our business, results of operations and financial condition and our ability to make distributions to our shareholders.

The federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government, may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

The payments we receive on our Agency RMBS depend upon a steady stream of payments on the underlying mortgages and such payments are guaranteed by Fannie Mae, Freddie Mac or Ginnie Mae. Fannie Mae and Freddie Mac are GSEs but their guarantees are not backed by the full faith and credit of the United States. Ginnie Mae is part of a U.S. Government agency and its guarantees are backed by the full faith and credit of the United States.

In response to the deteriorating financial condition of Fannie Mae and Freddie Mac and the recent credit market disruption, the United States Congress and the Treasury undertook a series of actions to stabilize these GSEs and the financial markets generally, including the enactment of the Housing and Economic Recovery Act of 2008, or the HERA, on July 30, 2008. These actions include steps taken by the Treasury to capitalize and provide financing to Fannie Mae and Freddie Mac and an agreement to purchase direct obligations and Agency RMBS issued or guaranteed by Fannie Mae or Freddie Mac. See also Management s Discussion and Analysis of Financial Condition and Results of Operations Trends and Recent Market Developments.

Shortly after Fannie Mae and Freddie Mac were placed in federal conservatorship, the Secretary of the Treasury, in announcing the actions, noted that the guarantee structure of Fannie Mae and Freddie Mac required examination and that changes in the structures of the entities were necessary to reduce risk to the financial system. The future roles of Fannie Mae and Freddie Mac could be significantly reduced and the nature of their guarantees could be considerably limited relative to historical measurements or even eliminated. Under this conservatorship, Fannie Mae and Freddie Mac are required to reduce the amount of mortgage loans they own or for which they provide guarantees on Agency RMBS. Moreover, any changes to the nature of the guarantees provided by, or laws affecting, Fannie Mae and Freddie Mac could materially adversely affect the credit quality of the guarantees, could increase the risk of loss on purchases of Agency RMBS issued by these GSEs and could have broad adverse market implications for the Agency RMBS they currently guarantee. Any action that affects the credit quality of the guarantees provided by Fannie Mae and Freddie Mac could materially adversely affect the value of our Agency RMBS.

The Treasury could also stop providing financial support to Fannie Mae and Freddie Mac in the future. The Treasury s authority to purchase Agency RMBS and to provide financial support to Fannie Mae and Freddie Mac under the HERA expires on December 31, 2009. If Fannie Mae or Freddie Mac were eliminated, or their structures were to change radically or the U.S. Government significantly reduced its support for them, we may be unable or significantly limited in our ability to acquire Agency RMBS, which would drastically reduce the amount and type of Agency RMBS available for purchase which, in turn, could materially adversely affect our ability to maintain our exclusion from regulation as an investment company under the Investment Company Act.

Mortgage loan modification programs and future legislative action may adversely affect the value of, and the returns on, our targeted assets.

In the second half of 2008, the U.S. Government, through the Federal Housing Authority, or FHA, and the Federal Deposit Insurance Corporation, or FDIC, commenced implementation of programs designed to provide homeowners with assistance in avoiding residential mortgage loan foreclosures. The programs involve, among other things, the modification of mortgage loans to reduce the principal amount of the loans or the rate of interest payable on the loans, or to extend the payment terms of the loans. It is likely that loan modifications would result in interest rate reductions or principal reductions on the mortgage loans that back our RMBS. However, it is also likely that loan modifications would result in increased prepayments on some RMBS. See Prepayment rates can change, adversely affecting the performance of our assets, for information relating to the impact of prepayments on our business.

In addition, members of Congress have indicated support for additional legislative relief for homeowners, including an amendment of the bankruptcy laws to permit the modification of mortgage loans in bankruptcy proceedings. Under such an amendment, the mortgage servicer would have the authority to modify mortgage loans that are in default, or for which default is reasonably foreseeable, if such modifications are in the best interests of the holders of the related RMBS and such modifications are done in accordance with the terms of the relevant agreements. A significant number of loan modifications could result in a significant reduction in cash flows to the holders of the related RMBS on an ongoing basis.

These loan modification programs, as well as future legislative or regulatory actions, including amendments to the bankruptcy laws, that result in the modification of outstanding mortgage loans may adversely affect the value of, and the returns on, our assets which, in turn, could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

The increasing number of proposed federal, state and local laws may increase our risk of liability with respect to certain mortgage loans and could increase our cost of doing business.

Congress and various state and local legislatures are considering, and in the future may consider, legislation, which, among other provisions, would permit limited assignee liability for certain violations in the mortgage loan origination process, and would allow judicial modification of loan principal in the event of personal bankruptcy. We cannot predict whether or in what form Congress or the various state and local legislatures may enact legislation affecting our business or whether any such legislation will require us to change our practices or make changes in our portfolio in the future. These changes, if required, could materially adversely affect our business, results of operations and financial condition and our ability to make distributions to our shareholders, particularly if we make such changes in response to new or amended laws, regulations or ordinances in any state where we acquire a significant portion of our mortgage loans, or if such changes result in us being held responsible for any violations in the mortgage loan origination process.

The principal and interest payments on our non-Agency RMBS are not guaranteed by any entity, including any government entity or GSE, and, therefore, are subject to increased risks, including credit risk.

Our portfolio includes non-Agency RMBS which are backed by residential mortgage loans that do not conform to the Fannie Mae or Freddie Mac underwriting guidelines, including subprime, Alt-A and prime jumbo mortgage loans. See Business Our Targeted Asset Classes, for a detailed description of our assets. Consequently, the principal and interest on non-Agency RMBS, unlike those on Agency RMBS, are not guaranteed by GSEs such as Fannie Mae and Freddie Mac or, in the case of Ginnie Mae, the U.S. Government.

Table of Contents

Non-Agency RMBS are subject to many of the risks of the respective underlying mortgage loans. Residential mortgage loans are typically secured by single-family residential property and are subject to risks of delinquency and foreclosure and risks of loss. The ability of a borrower to repay a loan secured by a residential property is dependent upon the income or assets of the borrower. A number of factors, including a general economic downturn, acts of God, terrorism, social unrest and civil disturbances, may impair borrowers abilities to repay their mortgage loans. The ability of a borrower to repay these mortgage loans is dependent upon his or her income or assets.

In the event of defaults under mortgage loans backing any of our non-Agency RMBS, we will bear a risk of loss of principal to the extent of any deficiency between the value of the collateral and the principal and accrued interest of the mortgage loan. Additionally, in the event of the bankruptcy of a mortgage loan borrower, the mortgage loan to such borrower will be deemed to be secured only to the extent of the value of the underlying collateral at the time of bankruptcy (as determined by the bankruptcy court), and the lien securing the mortgage loan will be subject to the avoidance powers of the bankruptcy trustee or debtor-in-possession to the extent the lien is unenforceable under state law. Foreclosure of a mortgage loan can be an expensive and lengthy process which could have a substantial negative effect on our anticipated return on the foreclosed mortgage loan. If borrowers default on the mortgage loans backing our non-Agency RMBS and we are unable to recover any resulting loss through the foreclosure process, our business, financial condition and results of operations and our ability to make distributions to our shareholders could be materially adversely affected.

We rely on analytical models and other data to analyze potential asset acquisition and disposition opportunities and to manage our portfolio. Such models and other data may be incorrect, misleading or incomplete, which could cause us to purchase assets that do not meet our expectations or to make asset management decisions that are not in line with our strategy.

Our Manager relies on Ellington s analytical models (both proprietary and third-party models), and information and data supplied by third parties. These models and data may be used to value assets or potential asset acquisitions and dispositions and also in connection with our asset management activities. If Ellington s models and data prove to be incorrect, misleading or incomplete, any decisions made in reliance thereon could expose us to potential risks. Our Manager s reliance on Ellington s models and data may induce it to purchase certain assets at prices that are too high, to sell certain other assets at prices that are too low, or to miss favorable opportunities altogether. Similarly, any hedging activities that are based on faulty models and data may prove to be unsuccessful.

Some of the risks of relying on analytical models and third-party data include the following:

- collateral cash flows and/or liability structures may be incorrectly modeled in all or only certain scenarios, or may be modeled based on simplifying assumptions that lead to errors;

- information about collateral may be incorrect, incomplete or misleading;

- collateral or RMBS historical performance (such as historical prepayments, defaults, cash flows, etc.) may be incorrectly reported, or subject to interpretation (e.g. different RMBS issuers may report delinquency statistics based on different definitions of what constitutes a delinquent loan); and

- collateral or RMBS information may be outdated, in which case the models may contain incorrect assumptions as to what has occurred since the date information was last updated.

Some models, such as prepayment models or mortgage default models, may be predictive in nature. The use of predictive models has inherent risks. For example, such models may incorrectly forecast future behavior, leading to potential losses. In addition, the predictive models used by our Manager may differ substantially from those models used by other market participants, with the result that valuations based on these predictive models may be substantially higher or lower for certain assets than actual market prices. Furthermore, because predictive models are usually constructed based on historical data supplied by third parties, the success of relying on such

Table of Contents

models may depend heavily on the accuracy and reliability of the supplied historical data, and, in the case of predicting performance in scenarios with little or no historical precedent (such as extreme broad-based declines in home prices, or deep economic recessions or depressions), such models must employ greater degrees of extrapolation, and are therefore more speculative and of more limited reliability.

All valuation models rely on correct market data inputs. If incorrect market data is entered into even a well-founded valuation model, the resulting valuations will be incorrect. However, even if market data is inputted correctly, model prices will often differ substantially from market prices, especially for securities with complex characteristics or whose values are particularly sensitive to various factors. If our market data inputs are incorrect or our model prices differ substantially from market prices, our business, financial condition and results of operations and our ability to make distributions to our shareholders could be materially adversely affected.

Valuations of some of our assets are inherently uncertain, may be based on estimates, may fluctuate over short periods of time and may differ from the values that would have been used if a ready market for these assets existed. As a result, the values of some of our assets are uncertain.

The values of some of the assets in our portfolio are not readily determinable. We value these assets quarterly at fair value, as determined in good faith by our Manager, subject to the oversight of the valuation sub-committee of the Manager s investment and risk management committee as well as the oversight of the independent members of our board of directors, and changes in the fair value of our assets directly impact our net income. Because such valuations are inherently uncertain, may fluctuate over short periods of time and may be based on estimates, our Manager s determinations of fair value may differ from the values that would have been used if a ready market for these assets existed or from the prices at which trades occur. Furthermore, we do not obtain third party valuations for all of our assets. Our Manager s determination of fair value has a material impact on our net earnings through recording unrealized appreciation or depreciation of investments.

While in many cases our Manager s determination of the fair value of our assets is based on valuations provided by third-party dealers and pricing services, our Manager can and does value assets based upon its judgment and such valuations may differ from those provided by third-party dealers and pricing services. Valuations of certain assets are often difficult to obtain or are unreliable. In general, dealers and pricing services heavily disclaim their valuations. Additionally, dealers may claim to furnish valuations only as an accommodation and without special compensation, and so they may disclaim any and all liability for any direct, incidental, or consequential damages arising out of any inaccuracy or incompleteness in valuations, including any act of negligence or breach of any warranty. Depending on the complexity and illiquidity of an asset, valuations of the same asset can vary substantially from one dealer or pricing service to another. Higher valuations of our assets have the effect of increasing the amount of base management fees and incentive fees we pay to our Manager. Therefore, conflicts of interest exist because our Manager is involved in the determination of the fair value of our assets. The valuation process has been particularly difficult recently as market events have made valuations of certain assets more difficult and unpredictable and the disparity of valuations provided by third-party dealers has widened.

Our business, financial condition and results of operations and our ability to make distributions to our shareholders could be materially adversely affected if our Manager s fair value determinations of these assets were materially higher than the values that would exist if a ready market existed for these assets.

We depend on third-party service providers, including mortgage servicers, for a variety of services related to our non-Agency RMBS, and we intend to utilize third-party service providers if we acquire pools of whole mortgage loans. We are, therefore, subject to the risks associated with third-party service providers.

We depend on a variety of services provided by third-party service providers related to our non-Agency RMBS, and we will depend on similar services should we acquire pools of whole mortgage loans. We rely on the mortgage servicers who service the mortgage loans backing our non-Agency RMBS to, among other things, collect principal and interest payments on the underlying mortgages and perform loss mitigation services. Our mortgage servicers and other service providers to our non-Agency RMBS, such as trustees, bond insurance providers and custodians, may not perform in a manner that promotes our interests. In addition, recent legislation intended to reduce or prevent foreclosures through, among other things, loan modifications may reduce the value of mortgage loans backing our non-Agency RMBS or whole mortgage loans that we acquire, and mortgage servicers may be incentivized by the federal government to pursue such loan modifications, as well as forbearance plans and other actions intended to prevent foreclosure, even if such loan modifications and other actions are not in the best interest of the holder of the mortgage loan. In addition to the recent legislation that creates financial incentives for mortgage loan servicers to modify loans and take other actions that are intended to prevent foreclosures, legislation has recently been adopted that creates a safe harbor from liability to creditors for servicers that undertake loan modifications and other actions that are intended to prevent foreclosures. As a result of these recent legislative actions, the mortgage loan servicers on which we rely may not perform in our best interests or up to our expectations. If our third-party service providers do not perform as expected, our business, financial condition and results of operations and ability to make distributions to our shareholders may be materially adversely affected.

We rely on mortgage servicers for our loss mitigation efforts, and we also may engage in our own loss mitigation efforts with respect to whole mortgage loans we may purchase. Such loss mitigation efforts may be unsuccessful or not cost effective.

Both default frequency and default severity of mortgage loans is highly dependent on the quality of the mortgage servicer. We depend on the loss mitigation efforts of mortgage servicers and in some cases special servicers, which are mortgage servicers who specialize in servicing non-performing loans. If mortgage servicers are not vigilant in encouraging borrowers to make their monthly payments, the borrowers are far less likely to make those payments. In addition, if we purchase pools of whole mortgage loans, we may engage in our own loss mitigation efforts in addition to the efforts of the mortgage servicers, including more hands-on mortgage servicer oversight and management, borrower refinancing solicitations, as well as other efforts. Our and our mortgage servicers loss mitigation efforts may be unsuccessful in limiting delinquencies, defaults and losses, or may not be cost effective, which may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

To the extent that due diligence is conducted on potential assets, especially non-Agency RMBS or pools of whole mortgage loans, such due diligence may not reveal all of the risks associated with such assets and may not reveal other weaknesses in such assets, which could lead to losses.

Before acquiring non-Agency RMBS or pools of whole mortgage loans, our Manager may decide to conduct (either directly or using third parties) certain due diligence. Such due diligence may include (i) an assessment of the strengths and weaknesses of the originators or services of the related mortgage loans, (ii) a review of all or merely a subset of the related individual mortgage loans in order to, among other things, assess the accuracy or reasonableness of certain loan-level information, and to estimate current loan-to-value ratios by obtaining updated property appraisals or otherwise, or (iii) other reviews that our Manager may deem appropriate to conduct. There can be no assurance that our Manager will conduct any specific level of due diligence, or that, among other things, our Manager s due diligence processes will uncover all relevant facts or that any purchase will be successful, which could result in losses on these assets, which, in turn, could adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Our assets include subordinated and lower-rated securities that generally have greater risks of loss than senior and higher-rated securities.

Certain securities that we acquire are deemed by rating companies to have substantial vulnerability to default in payment of interest and/or principal. Other securities we acquire have the lowest quality ratings or are unrated. Many RMBS or ABS that we acquire are subordinated in cash flow priority to other more senior securities of the same securitization. The risks of defaults on the underlying mortgages or assets are severely

Table of Contents

magnified in subordinated securities. Certain subordinated securities (first loss securities) absorb all losses from default before any other class of securities is at risk. Such securities therefore possess some of the attributes typically associated with equity securities. Also, the risk of declining real estate values, in particular, is amplified in subordinated RMBS, as are the risks associated with possible changes in the market s perception of the entity issuing or guaranteeing them, or by changes in government regulations and tax policies. Accordingly, these securities may experience significant price and performance volatility relative to more senior securities and they are subject to greater risk of loss than more senior securities which, if realized, could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Prepayment rates can change, adversely affecting the performance of our assets.

The frequency at which prepayments (including both voluntary prepayments by the borrowers and liquidations due to defaults and foreclosures) occur on mortgage loans underlying RMBS is affected by a variety of factors, including the prevailing level of interest rates as well as economic, demographic, tax, social, legal, and other factors. Generally, borrowers tend to prepay their mortgages when prevailing mortgage rates fall below the interest rates on their mortgage loans. Many of the mortgage loans underlying our existing RMBS were originated in a relatively higher interest rate environment than currently in effect and, thus, could be prepaid if borrowers are eligible for refinancings.

In general, premium securities (securities whose market values exceed their principal or par amounts) are adversely affected by faster-than-anticipated prepayments because the above-market coupon that such premium securities carry will be earned for a shorter period of time. Generally, discount securities (securities whose principal or par amounts exceed their market values) are adversely affected by slower-than-anticipated prepayments. Since many RMBS will be discount securities when interest rates are high, and will be premium securities when interest rates are low, these RMBS may be adversely affected by changes in prepayments in any interest rate environment.

The adverse effects of prepayments may impact us in various ways. First, particular investments may experience outright losses, as in the case of IOs and IIOs in an environment of faster actual or anticipated prepayments. Second, particular investments may under-perform relative to any hedges that our Manager may have constructed for these assets, resulting in a loss to us. In particular, prepayments (at par) may limit the potential upside of many RMBS to their principal or par amounts, whereas their corresponding hedges often have the potential for unlimited loss. Furthermore, to the extent that faster prepayment rates are due to lower interest rates, the principal payments received from prepayments will tend to be reinvested in lower-yielding assets, which may reduce our income in the long run. Therefore, if actual prepayment rates differ from anticipated prepayment rates our business, financial condition and results of operations and ability to make distributions to our shareholders could be materially adversely affected.

Changes in interest rates could negatively affect the value of our assets, and increase the risk of default on our assets.

Currently, our assets primarily consist of RMBS. Most RMBS, especially most fixed-rate RMBS and most RMBS backed by fixed-rate mortgage loans, decline in value when long-term interest rates increase. Even in the case of Agency RMBS, the guarantees provided by GSEs do not protect us from declines in market value caused by changes in interest rates. In the case of RMBS backed by ARMs, increases in interest rates can lead to increases in delinquencies and defaults as borrowers become less able to make their mortgage payments following interest payment resets. At the same time, an increase in short-term interest rates would increase the amount of interest owed on our reverse repos.

RMBS backed by ARMs are typically subject to periodic and lifetime interest rate caps. Periodic interest rate caps limit the amount an interest rate can increase during any given period. Lifetime interest rate caps limit

Table of Contents

the amount an interest rate can increase over the life of the security. Our borrowings typically are not subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, the interest rates paid on our borrowings could increase without limitation while interest rate caps could limit the interest rates on our RMBS backed by ARMs. This problem is magnified for RMBS backed by ARMs and hybrid ARMs that are not fully indexed. Further, some RMBS backed by ARMs and hybrid ARMs may be subject to periodic payment caps that result in a portion of the interest being deferred and added to the principal outstanding. As a result, the payments we receive on RMBS backed by ARMs and hybrid ARMs may be lower than the related debt service costs. These factors could have a material adverse effect on our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Residential whole mortgage loans, including subprime residential mortgage loans and non-performing and sub-performing residential mortgage loans, are subject to increased risks.

We may acquire and manage pools of residential whole mortgage loans. Residential whole mortgage loans, including subprime mortgage loans and non-performing and sub-performing mortgage loans, are subject to increased risks of loss. Unlike Agency RMBS, whole mortgage loans generally are not guaranteed by the U.S. Government or any GSE, though in some cases they may benefit from private mortgage insurance. Additionally, by directly acquiring whole mortgage loans, we do not receive the structural credit enhancements that benefit senior tranches of RMBS. A whole mortgage loan is directly exposed to losses resulting from default. Therefore, the value of the underlying property, the creditworthiness and financial position of the borrower and the priority and enforceability of the lien will significantly impact the value of such mortgage. In the event of a foreclosure, we may assume direct ownership of the underlying real estate. The liquidation proceeds upon sale of such real estate may not be sufficient to recover our cost basis in the loan, and any costs or delays involved in the foreclosure or liquidation process may increase losses.

Whole mortgage loans are also subject to special hazard risk (property damage caused by hazards, such as earthquakes or environmental hazards, not covered by standard property insurance policies), and to bankruptcy risk (reduction in a borrower s mortgage debt by a bankruptcy court). In addition, claims may be assessed against us on account of our position as mortgage holder or property owner, including assignee liability, responsibility for tax payments, environmental hazards and other liabilities. In some cases, these liabilities may be recourse liabilities or may otherwise lead to losses in excess of the purchase price of the related mortgage or property.

Commercial mortgage loans are subject to risks of delinquency and foreclosure and risks of loss that may be greater than similar risks associated with residential mortgage loans.

We may acquire CMBS backed by commercial mortgage loans or directly acquire commercial mortgage loans. Commercial mortgage loans are secured by multifamily or commercial property and are subject to risks of delinquency and foreclosure and risks of loss that are greater than similar risks associated with residential mortgage loans. The ability of a borrower to repay a loan secured by an income-producing property typically is dependent primarily upon the successful operation of such property rather than upon the existence of independent income or assets of the borrower. If the net operating income of the property is reduced, the borrower s ability to repay the loan may be impaired. If we incur losses on CMBS, or commercial mortgage loans, our business, financial condition and results of operations and our ability to make distributions to our shareholders may be materially adversely affected.

Our real estate assets are subject to risks particular to real property.

We own assets secured by real estate and may own real estate directly in the future, either through direct acquisitions or upon a default of mortgage loans. Real estate assets are subject to various risks, including:

acts of God, including earthquakes, floods and other natural disasters, which may result in uninsured losses;

Table of Contents

- acts of war or terrorism, including the consequences of terrorist attacks, such as those that occurred on September 11, 2001;
- adverse changes in national and local economic and market conditions;
- changes in governmental laws and regulations, fiscal policies and zoning ordinances and the related costs of compliance with laws and regulations, fiscal policies and ordinances;
- costs of remediation and liabilities associated with environmental conditions such as indoor mold; and
- the potential for uninsured or under-insured property losses.

The occurrence of any of the foregoing or similar events may reduce our return from an affected property or asset and, consequently, materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

If we acquire and subsequently re-sell any whole mortgage loans, we may be required to repurchase such loans or indemnify investors if we breach representations and warranties.

If we acquire and subsequently re-sell any whole mortgage loans, we would generally be required to make customary representations and warranties about such loans to the loan purchaser. Our residential mortgage loan sale agreements and terms of any securitizations into which we sell loans will generally require us to repurchase or substitute loans in the event we breach a representation or warranty given to the loan purchaser. In addition, we may be required to repurchase loans as a result of borrower fraud or in the event of early payment default on a mortgage loan. The remedies available to a purchaser of mortgage loans are generally broader than those available to us against an originating broker or correspondent. Repurchased loans are typically worth only a fraction of the original price. Significant repurchase activity could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We engage in short selling transactions, which may subject us to additional risks.

Many of our hedging transactions, and occasionally our investment transactions, are short sales. Short selling involves selling securities that are not owned and typically borrowing the same securities for delivery to the purchaser, with an obligation to repurchase the borrowed securities at a later date. Short selling allows the investor to profit from declines in market prices to the extent such declines exceed the transaction costs and the costs of borrowing the securities. A short sale may create the risk of an unlimited loss, in that the price of the underlying security might theoretically increase without limit, thus increasing the cost of repurchasing the securities. There can be no assurance that securities sold short will be available for repurchase or borrowing. Repurchasing securities to close out a short position can itself cause the price of the securities to rise further, thereby exacerbating the loss.

We leverage certain of our assets, which may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We currently leverage certain of our assets through borrowings under reverse repos. The degree of leverage we employ may increase substantially in the future. Leverage can enhance our potential returns but can also exacerbate losses. Market conditions could cause our financing costs to increase relative to the income earned from our assets. To the extent that we cannot meet our debt service obligations, we risk the loss of some or all of our assets to forced liquidation in order to satisfy our debt obligations.

If our financing costs increase relative to the income earned from our assets or we are unable to satisfy our debt service obligations, our business, financial condition and results of operations and our ability to make distributions to our shareholders may be materially adversely affected.

Table of Contents

Our access to financing sources, which may not be available on favorable terms, or at all, especially in light of current market conditions, may be limited, and this may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We depend upon the availability of adequate capital and financing sources to fund our operations. However, as previously discussed, the capital and credit markets recently experienced unprecedented levels of volatility and disruption which exerted downward pressure on stock prices and credit capacity for lenders. If these levels of market volatility and disruption recur, it could materially adversely affect one or more of our lenders and could cause one or more of our lenders to be unwilling or unable to provide us with financing, or to increase the costs of that financing, or to become insolvent, as was the case with Lehman Brothers. Moreover, we are currently party to reverse repos of a short duration and there can be no assurance that we will be able to roll over these borrowings on favorable terms, if at all. In the event we are unable to roll over our reverse repos, it may be more difficult for us to obtain debt financing on favorable terms or at all. In addition, if regulatory capital requirements imposed on our lenders change, they may be required to limit, or increase the cost of, financing they provide to us. In general, this could potentially increase our financing costs and reduce our liquidity or require us to sell assets at an inopportune time or price. Under current market conditions, securitizations are generally unavailable, which has also limited borrowings under warehouse facilities and other credit facilities that are intended to be refinanced by such securitizations. Consequently, depending on market conditions at the relevant time, we may have to rely on additional equity issuances to meet our capital and financing needs, which may be dilutive to our shareholders, or we may have to rely on less efficient forms of debt financing that consume a larger portion of our cash flow from operations, thereby reducing funds available for our operations, future business opportunities, cash distributions to our shareholders and other purposes. We cannot assure you that we will have access to such equity or debt capital on favorable terms (including, without limitation, cost and term) at the desired times, or at all, which may cause us to curtail our asset acquisition activities and/or dispose of assets, which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Interest rate mismatches between our assets and any borrowings used to fund purchases of our assets may reduce our income during periods of changing interest rates.

Some of our assets are fixed-rate securities or have a fixed rate component (such as hybrid ARMs). This means that the interest we earn on these assets will not vary over time based upon changes in a short-term interest rate index. Although the interest we earn on our RMBS backed by ARMs generally will adjust for changing interest rates, the interest rate adjustments may not occur as quickly as the interest rate adjustments to any related reverse repos. Therefore, to the extent we finance our assets with reverse repos or other types of floating rate debt, the interest rate indices and repricing terms of our assets and their funding sources will create an interest rate mismatch between our assets and liabilities. Additionally, our RMBS backed by ARMs will generally be subject to interest rate caps, which potentially could cause such RMBS to acquire many of the characteristics of fixed-rate securities if interest rates were to rise above the cap levels. The use of interest rate hedges also will introduce the risk of other interest rate mismatches and exposures, as will the use of other financing techniques. During periods of changing interest rates, these mismatches could cause our business, financial condition and results of operations and ability to make distributions to our shareholders to be materially adversely affected.

Our lenders may require us to provide additional collateral, especially when the market values for our assets decline, which may restrict us from leveraging our assets as fully as desired, force us to liquidate assets, reduce our liquidity, and materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Our reverse repos allow the lenders, to varying degrees, to determine an updated market value of the collateral to reflect current market conditions. If the market value of the collateral declines in value, we may be required by the lender to provide additional collateral or pay down a portion of the funds advanced on minimal notice, which is known as a margin call. Posting additional collateral will reduce our liquidity and limit our

Table of Contents

ability to leverage our assets. Additionally, in order to satisfy a margin call, we may be required to liquidate assets at a disadvantageous time, which could cause us to incur further losses and adversely affect our results of operations, financial condition, and may impair our ability to make distributions. We receive margin calls from our lenders from time to time in the ordinary course of business similar to other entities in the specialty finance business. In the event we do not have sufficient liquidity to satisfy these margin calls, lending institutions can accelerate our indebtedness, increase our borrowing rates, liquidate our collateral and terminate our ability to borrow. A significant increase in margin calls could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders, and could increase our risk of insolvency.

Further, lenders may require us to maintain a certain amount of cash that is not invested or to set aside non-leveraged assets sufficient to maintain a specified liquidity position which would allow us to satisfy our collateral obligations. As a result, we may not be able to leverage our portfolio as fully as we would prefer, which could reduce our return on equity. In the event that we are unable to meet these collateral maintenance obligations, then, as described above, our financial condition could deteriorate rapidly.

Our rights under our reverse repos are subject to the effects of the bankruptcy laws in the event of the bankruptcy or insolvency of us or our lenders.

In the event of our insolvency or bankruptcy, certain reverse repos may qualify for special treatment under the U.S. Bankruptcy Code, the effect of which, among other things, would be to allow the lender to avoid the automatic stay provisions of the U.S. Bankruptcy Code and to foreclose on and/or liquidate the collateral pledged under such agreements without delay. In the event of the insolvency or bankruptcy of a lender during the term of a reverse repo, the lender may be permitted, under applicable insolvency laws, to repudiate the contract, and our claim against the lender for damages may be treated simply as an unsecured creditor. In addition, if the lender is a broker or dealer subject to the Securities Investor Protection Act of 1970, or an insured depository institution subject to the Federal Deposit Insurance Act, our ability to exercise our rights to recover our securities under a reverse repo or to be compensated for any damages resulting from the lenders insolvency may be further limited by those statutes. These claims would be subject to significant delay and costs to us and, if and when received, may be substantially less than the damages we actually incur.

There is no assurance that we will be able to obtain any TALF loans or remain eligible as a TALF borrower, and the terms and conditions of the TALF may change, which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We may consider financing certain assets with borrowings to the extent available to us under the TALF. The TALF is operated by the Federal Reserve Bank of New York. The Federal Reserve Bank of New York has complete discretion regarding the extension of credit under the TALF and is under no obligation to make any loans to us. Depending on the demand for TALF loans and the general state of the credit markets, the Federal Reserve and the Treasury may decide to modify the terms and conditions of the TALF, including asset and borrower eligibility, at any time. Any such modifications may adversely affect the market value of any of our assets financed under the TALF or our ability to obtain additional TALF financing. If the TALF is prematurely discontinued or reduced while our assets financed under the TALF are still outstanding, there may be no market for these assets and the market value of these assets would be adversely affected.

The application of the eligibility rules under the TALF also remain unclear. If for any reason we are deemed not to be eligible to participate in the TALF, we may not be eligible to obtain TALF loans and all of our outstanding TALF loans will become immediately due and payable with full recourse under the TALF program rules.

Table of Contents

In addition to the foregoing, assets to be used as collateral for TALF loans must meet strict eligibility criteria with respect to characteristics such as issuance date and credit rating. These restrictions may limit the availability of eligible assets, and we may be unable to acquire sufficient amounts of assets to obtain financing under the TALF consistent with our strategy which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Downgrades of legacy CMBS or changes in the rating methodology and assumptions for future CMBS issuances may decrease the availability of the TALF to finance CMBS.

On May 26, 2009, S&P, which rates a substantial majority of CMBS issuances, issued a request for comment regarding its proposed changes to its methodology and assumptions for rating CMBS, and in so doing indicated that it is likely that the proposed changes, which represent a significant change to the criteria for rating high investment-grade classes, will prompt a considerable amount of downgrades in recently issued (2005-2008 vintage) CMBS. The current TALF guidelines issued by the Federal Reserve Bank of New York indicate that in order to be eligible for the TALF, legacy CMBS must not have a rating below the highest investment-grade rating category from any TALF CMBS-eligible rating agency, which includes S&P. Other rating agencies may take similar actions with regard to their ratings of CMBS. As a result, downgrades of legacy CMBS or a decrease in the amount or availability of new issue CMBS resulting from such a change to the rating criteria may limit substantially the availability of the TALF to finance CMBS.

Our ability to transfer assets purchased using the TALF funding, to the extent available to us, would be restricted, which would limit our ability to trade or otherwise dispose of our assets as we may desire.

Our assets purchased using the TALF funding will be pledged to the Federal Reserve Bank of New York as collateral for the TALF loans. If we sell or transfer any of these assets, we must either repay the related TALF loan or obtain the consent of the Federal Reserve Bank of New York to assign our obligations under the related TALF loan to the applicable assignee. The Federal Reserve Bank of New York in its discretion may restrict or prevent us from assigning our loan obligations to a third party and will not consent to any assignments after the termination date for making new loans. These restrictions may limit our ability to trade or otherwise dispose of our assets pledged as collateral for TALF funding, and may adversely affect our ability to take advantage of favorable market conditions to trade or otherwise dispose of our assets as we may desire.

In accessing the TALF, we will be dependent on the activities of our primary dealers.

To obtain TALF loans, a TALF borrower must execute a customer agreement with at least one primary dealer which will act on its behalf under the agreement with the Federal Reserve Bank of New York. In addition to submitting aggregate loan request amounts on behalf of its customers in the form and manner specified by the Federal Reserve Bank of New York, primary dealers are also responsible for distributing principal and interest after receipt thereof from The Bank of New York Mellon, as custodian for the TALF. Once funds or collateral are transferred to a primary dealer or at the direction of a primary dealer, neither the custodian nor the Federal Reserve Bank of New York has any obligation to account for whether the funds or collateral are transferred to the borrower. We will therefore be exposed to bankruptcy risk of our primary dealers.

Under certain conditions, we may be required to provide full recourse for TALF loans or to make indemnification payments, which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders and we could incur a loss.

To participate in the TALF, a TALF borrower must execute a customer agreement with a primary dealer authorizing it to act as its agent under the TALF and to act on its behalf under the agreement with the Federal Reserve Bank of New York and with The Bank of New York Mellon as administrator and as the Federal Reserve Bank of New York s custodian of the collateral. Under such agreements, the TALF borrower will be required to represent to the primary dealer and to the Federal Reserve Bank of New York that, among other things, it is an

Table of Contents

eligible borrower and that the collateral that it pledges meets the TALF eligibility criteria. The Federal Reserve Bank of New York will have full recourse to such TALF borrower for repayment of the loan for any breach of these representations and may have full recourse to such TALF borrower for repayment of a TALF loan if the eligibility criteria for collateral under the TALF are considered continuing requirements and the pledged collateral no longer satisfies such criteria. In addition, a TALF borrower will be required to indemnify its primary dealers for certain breaches under the customer agreements and to indemnify the Federal Reserve Bank of New York and its custodian for certain breaches under the agreement with the Federal Reserve Bank of New York. Payments made to satisfy such full recourse requirements and indemnities could have a material adverse effect on our business, financial condition and results of operations and our ability to make distributions to our shareholders.

The terms and conditions of the Legacy Loans Program established under PPIP have not been finalized and there is no assurance that the final terms will enable us to participate in the Legacy Loans Program in a manner consistent with our investment strategy or benefit from the Legacy Loans Program.

Investors in the Legacy Loans Program must be pre-qualified by the FDIC. It is likely that the FDIC will have broad discretion regarding the qualification of investors in the Legacy Loans Program and is under no obligation to approve our participation even if we meet all of the applicable criteria. While the Treasury and the FDIC have released a summary of preliminary terms and conditions for the PPIP, including the Legacy Loans Program, they have not released the final terms and conditions governing these programs. The preliminary terms and conditions do not address the specific terms and conditions relating to, among other things: the FDIC-guaranteed debt to be issued by participants in the Legacy Loans Program and the warrants that the Treasury will receive under the Legacy Loans Program if it makes an equity investment in a Public-Private Investment Fund, or PPIF. The FDIC has indicated that Legacy Loans PPIFs will be subject to government loan modification program requirements. In addition, the Treasury and FDIC have reserved the right to modify the proposed terms of the PPIP, including the Legacy Loans Program. Because the Legacy Loans Program is still being developed and the details of the program are still emerging, it is not possible for us to predict how this program will impact our business. If and when the final terms and conditions are released, there is no assurance that we will benefit from this program or that the final terms will enable us to participate in the Legacy Loans Program in a manner that is consistent with our strategy, or at all.

Governmental regulation of participants in U.S. Government programs could materially adversely affect our ability to participate in such programs and may impose various restrictions on our business or on our investors.

The U.S. Government may from time to time establish or change requirements applicable to participants in the various programs that have been established by the U.S. Government, such as the TALF and PPIP. Furthermore, the U.S. Government may seek to modify the requirements applicable to participants in such programs after their initial participation. There can be no assurance that the U.S. Congress or regulatory bodies will not seek such modifications or impose new restrictions and/or taxes and penalties on participants in such programs, possibly even with retroactive effect. Even without action taken by the U.S. Congress or regulatory bodies, if a perception develops that there is or could be a Congressional or regulatory focus on participants in the various U.S. Government programs, market participants may become apprehensive or refuse to participate in such programs. If this were to occur, the intended benefits of such programs may not materialize, which could significantly diminish the value of our assets. While it is not possible for us to predict what types of new laws or regulations could be imposed on us or how they may affect us or our investors, it may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Table of Contents

Some of our lending and derivative counterparties may cease doing business with us or may become insolvent, which would adversely affect our ability to obtain financing readily or on favorable terms and enter into derivatives or may expose us to losses on our derivatives.

The ongoing downturn in the economy and stress within the financial industry may cause some of our lenders and the counterparties to our derivative positions to cease doing business with us, or to become insolvent, as was the case with Lehman Brothers. In the event one or more of our lenders cease doing business with us or becomes insolvent, it may be more difficult for us to obtain additional debt financing on favorable terms or at all. We also are exposed to the risk of loss associated with the insolvency of our lending and derivatives counterparties, including the risk that we may incur significant costs in attempting to recover any collateral held with such counterparties and the risk that we may not be able to recover such collateral in a timely manner or at all. Any of these events could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Hedging against credit events and interest rate changes and other risks may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We opportunistically pursue various hedging strategies to seek to reduce our exposure to losses from adverse credit events and other factors. Hedging against a decline in the values of our portfolio positions does not prevent losses if the values of such positions decline, or eliminate the possibility of fluctuations in the value of our portfolio. Hedging transactions generally will limit the opportunity for gain if the values of our portfolio positions should increase. Further, certain hedging transactions could result in our experiencing significant losses. Moreover, at any point in time we may choose not to hedge all or a portion of these risks, and we generally will not hedge those risks that we believe are appropriate for us to take at such time, or that we believe would be impractical or prohibitively expensive to hedge. Even if we do choose to hedge certain risks, for a variety of reasons we generally will not seek to establish a perfect correlation between our hedging instruments and the risks being hedged. Any such imperfect correlation may prevent us from achieving the intended hedge and expose us to risk of loss. Our hedging activity will vary in scope based on the composition of our portfolio, our market views, and changing market conditions, including the level and volatility of interest rates. When we do choose to hedge, hedging may fail to protect or could materially adversely affect us because, among other things:

- our Manager may fail to correctly assess the degree of correlation between the performance of the instruments used in the hedging strategy and the performance of the assets in the portfolio being hedged;
- our Manager may fail to recalculate, re-adjust and execute hedges in an efficient and timely manner;
- the hedging transactions may actually result in poorer over-all performance for us than if we had not engaged in the hedging transactions;
- credit hedging can be expensive, particularly when the market is forecasting future credit deterioration and when markets are more illiquid;
- interest rate hedging can be expensive, particularly during periods of volatile interest rates;
- available hedges may not correspond directly with the risks for which protection is sought;
- the durations of the hedges may not match the durations of the related assets or liabilities being hedged;
- many hedges are structured as over-the-counter contracts with counterparties whose creditworthiness is not guaranteed, raising the possibility that the hedging counterparty may default on their payment obligations; and

- to the extent that the creditworthiness of a hedging counterparty deteriorates, it may be difficult or impossible to terminate or assign any hedging transactions with such counterparty.

For these and other reasons, our hedging activity may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Table of Contents

Hedging instruments and other derivatives, including credit default swaps, often are not traded on regulated exchanges, guaranteed by or regulated by any U.S. or foreign governmental authorities and involve risks and costs that could result in material losses.

Hedging instruments and other derivatives, including credit default swaps, involve risk because they often are not traded on regulated exchanges and are not guaranteed by or regulated by any U.S. or foreign governmental authorities. Consequently, there are no requirements with respect to record keeping, financial responsibility or segregation of customer funds and compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. Our Manager is not restricted from dealing with any particular counterparty or from concentrating any or all of its transactions with one counterparty. Furthermore, our Manager has only a limited internal credit function to evaluate the creditworthiness of its counterparties, mainly relying on its experience with such counterparties and their general reputation as participants in these markets. The business failure of a hedging counterparty with whom we enter into a hedging transaction will most likely result in a default under the hedging agreement. Default by a party with whom we enter into a hedging transaction, such as occurred with Lehman Brothers, may result in losses and may force us to re-initiate similar hedges with other counterparties at the then-prevailing market levels. Generally we will seek to reserve the right to terminate our hedging transactions upon a counterparty s insolvency, but absent an actual insolvency, we may not be able to terminate a hedging transaction without the consent of the hedging counterparty, and we may not be able to assign or otherwise dispose of a hedging transaction to another counterparty without the consent of both the original hedging counterparty and the potential assignee. If we terminate a hedging transaction, we may not be able to enter into a replacement contract in order to cover our risk. There can be no assurance that a liquid secondary market will exist for hedging instruments purchased or sold, and therefore we may be required to maintain any hedging position until exercise or expiration, which could materially adversely affect our business, financial condition and results of operations.

The U.S. Commodity Futures Trading Commission and certain commodity exchanges have established limits referred to as speculative position limits or position limits on the maximum net long or net short position which any person or group of persons may hold or control in particular futures and options. Limits on trading in options contracts also have been established by the various options exchanges. It is possible that trading decisions may have to be modified and that positions held may have to be liquidated in order to avoid exceeding such limits. Such modification or liquidation, if required, could materially adversely affect our business, financial condition and results of operation and our ability to make distributions to our shareholders.

In light of recent events, significant public pressure exists for increased regulatory oversight of derivative transactions, including credit default swaps. Any actions taken by regulators could constrain our strategy and could increase our costs; either of which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We may change our asset acquisition strategy, hedging strategy and, asset allocation and operational and management policies without shareholder consent, which may result in the purchase of riskier assets and materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We may change our asset acquisition strategy, hedging strategy and asset allocation and operational and management policies at any time without the consent of our shareholders, which could result in our purchasing assets or entering into hedging transactions that are different from, and possibly riskier than, the assets and hedging transactions described in this prospectus. A change in our asset acquisition or hedging strategy may increase our exposure to real estate values, interest rates and other factors. A change in our asset allocation could result in us purchasing assets in classes different from those described in this prospectus. Our board of directors determines our operational policies and may amend or revise our policies, including those with respect to our acquisitions, growth, operations, indebtedness, capitalization and distributions or approve transactions that deviate from these policies without a vote of, or notice to, our shareholders. Operational policy changes could materially adversely affect our business, financial condition and results of operations and ability to make distributions to our shareholders.

Table of Contents

A portion of the net proceeds from this offering and the concurrent private placement will most likely be invested in more liquid, lower-yielding assets, which is likely to produce an initial return on your investment that may be lower than when the net proceeds from this offering and the concurrent private placement are fully invested in assets meeting our objectives.

We expect to take up to six months to fully deploy the net proceeds from this offering and the concurrent private placement in a portfolio satisfying our general objectives and policies, subject to the availability of appropriate opportunities to acquire assets. However, there can be no assurance that sufficient suitable opportunities will be available to adhere to this time frame. As a result, the initial return on your investment may be lower than when our portfolio is fully invested in assets meeting our long-term investment objectives and policies.

Until appropriate assets can be identified and purchased, our Manager may invest the net proceeds of this offering and the concurrent private placement in interest-bearing, short-term investments, including money market accounts. These investments are expected to provide a lower net return than we will seek to achieve from our targeted assets.

We may not realize income or gains from our assets.

We acquire assets to generate both current income and capital appreciation. The assets we acquire may, however, not appreciate in value and, in fact, may decline in value, and the debt securities we purchase may default on interest or principal payments. Accordingly, we may not be able to realize income or gains from our acquired assets. Any gains that we do realize may not be sufficient to offset any other losses we experience. Any income that we realize may not be sufficient to offset our expenses.

We or Ellington or its affiliates may be subject to adverse legislative or regulatory changes and to regulatory inquiries or proceedings.

At any time, laws or regulations that impact our business, or the administrative interpretations of those laws or regulations, may be amended. In addition, the markets for MBS and derivatives, including credit default swaps, have been the subject of intense legislative, regulatory and other scrutiny in recent months. We cannot predict when or if any new law, regulation or administrative interpretation, or any amendment to any existing law, regulation or administrative interpretation, will be adopted or promulgated or will become effective. Additionally, revisions in these laws, regulations or administrative interpretations could cause us to change our portfolio. We could be adversely affected by any change in, or any new, law, regulation or administrative interpretation.

Moreover, we cannot predict when or if any industry-wide or company-specific regulatory inquiries or proceedings will be initiated in which we and/or our Manager and Ellington will be involved. For example, in the last several years, as described below and also under Business-Legal Proceedings, Ellington and its affiliates have received, and we expect in the future may receive, inquiries and requests for documents and information from various federal, state and foreign regulators, including the following:

In June 2007, Ellington received an informal inquiry from the SEC requesting documents and other information relating to trading in credit default swaps on the ABX indices. Ellington provided documents to the SEC staff in August 2007 and Ellington has had no communication with the SEC on the matter since that time.

In November 2006, Ellington received a request from the SEC that it produce documents relating to trading of collateralized mortgage obligations, or CMOs, between Ellington and a third party broker-dealer as well as individuals associated with that broker-dealer, and Ellington produced documents to the SEC consistent with that request. In July 2007, Ellington received a subpoena from the SEC requesting documents relating to trading in CMOs by these individuals and firms they were affiliated with, including that broker-dealer. Ellington responded to that subpoena in August 2007, and has had no communication with the SEC on the matter since that time. In

May 2009, the SEC filed a complaint against certain former employees of that broker-dealer, alleging fraud in their marketing of CMOs to their clients, and stated that its investigation is ongoing.

In August 2007, Ellington received a subpoena from the New York Attorney General, or the NYAG, requesting documents and other information from Ellington about its and its affiliates mortgage loan servicing activities. Ellington informed the NYAG that it did not engage in mortgage loan servicing. Ellington subsequently received subpoenas for documents and information relating to Ellington s residual or equity interests in mortgage securitization trusts; communications with and information received from mortgage servicers relating to these trusts and their underlying mortgage loans; and trading in bonds of these trusts and related credit default swaps, and for documents and other information relating to communications with and information received from one of its vendors, which had performed asset surveillance for Ellington on these trusts. Ellington completed its response to the NYAG subpoenas in June 2008 and has had no communication with the NYAG since that time.

In March 2008, Ellington received a subpoena from the SEC requesting documents and other information relating primarily to CDOs underwritten during 2007 and 2008 by a particular investment bank and for which Ellington acted as collateral manager. Ellington provided an initial response to the subpoena in April 2008 and finished its production in May 2009. Ellington has had no communication with the SEC on the matter since that time.

In August 2009, Ellington and one of its affiliates received subpoenas from the SEC seeking documents and information regarding certain structuring, sales and marketing practices in the CDO market. The subpoenas seek documents and details regarding CDOs in which Ellington or its affiliates participated during 2006 and 2007. Ellington intends to cooperate fully with both of these subpoenas.

Information relating to legal proceedings and regulatory inquiries is also discussed under Business-Legal Proceedings. We can give no assurances that regulatory inquiries such as those discussed above will not result in investigations of Ellington or its affiliates or enforcement actions, fines or penalties or the assertion of private litigation claims against Ellington or its affiliates. In the event regulatory investigations such as those discussed above were to result in investigations, enforcement actions, fines, penalties or the assertion of private litigation claims against Ellington or its affiliates, our Manager s ability to perform its obligations to us under the management agreement between us and our Manager, or Ellington s ability to perform its obligations to our Manager under the services agreement between Ellington and our Manager, could be adversely impacted, which could in turn have a material adverse effect on our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We operate in a highly competitive market.

Our profitability depends, in large part, on our ability to acquire targeted assets at favorable prices. We compete with a number of entities when acquiring our targeted assets, including mortgage REITs, financial companies, public and private funds, commercial and investment banks and residential and commercial finance companies. We may also compete with (i) the Federal Reserve and the Treasury to the extent they purchase assets in our targeted asset classes and (ii) companies that partner with and/or receive financing from the U.S. Government, including TALF and PPIP participants. Many of our competitors are substantially larger and have considerably greater access to capital and other resources than we do. Furthermore, new companies with significant amounts of capital have recently been formed or have raised additional capital, and may continue to be formed and raise additional capital in the future, and these companies may have objectives that overlap with ours, which may create competition for assets we wish to acquire. Some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of assets to acquire and establish more relationships than us. Furthermore, competition for assets in our targeted asset classes may lead to the price of such assets increasing, which may further limit our ability to generate desired returns. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations.

Table of Contents

We are highly dependent on information systems and system failures could significantly disrupt our business, which may, in turn, materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Our business is highly dependent on communications and information systems. Any failure or interruption of our systems could cause delays or other problems in our securities trading activities, including RMBS trading activities, which could materially adversely affect on our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Lack of diversification in the number of assets we acquire would increase our dependence on relatively few individual assets.

Our management objectives and policies do not place a limit on the size of the amount of capital used to support, or the exposure to (by any other measure), any individual asset or any group of assets with similar characteristics or risks. As a result, our portfolio may be concentrated in a small number of assets or may be otherwise undiversified, increasing the risk of loss and the magnitude of potential losses to us and our shareholders if one or more of these assets perform poorly.

For example, our portfolio of mortgage-related assets may at times be concentrated in certain property types that are subject to higher risk of foreclosure, or secured by properties concentrated in a limited number of geographic locations. To the extent that our portfolio is concentrated in any one region or type of security, downturns relating generally to such region or type of security may result in defaults on a number of our assets within a short time period, which may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

The lack of liquidity in our assets may materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Many of our assets are structured as private placements. As such, they may be subject to legal and other restrictions on resale, transfer, pledge or other disposition or will otherwise be less liquid than publicly-traded securities. Other assets of ours, while publicly issued, have limited liquidity on account of their complexity, turbulent market conditions or other factors. Illiquid assets typically experience greater price volatility, because a ready market does not exist, and they can be more difficult to value. The illiquidity of our assets may make it difficult for us to sell such assets if the need arises or to vary our portfolio in response to changes in economic and other conditions. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our assets. We may also face other restrictions on our ability to liquidate any assets for which we or our Manager has or could be attributed with material non-public information. If we are unable to sell our assets at favorable prices or at all, it could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders

We may allocate the net proceeds from this offering and the concurrent private placement to acquiring assets with which you may not agree or for purposes that are different in range or focus than those contemplated in this prospectus.

We will have significant flexibility in using the net proceeds of this offering and the concurrent private placement and may use the net proceeds from this offering and the concurrent private placement to acquire assets with which you may not agree or for purposes that are different in range or focus than those contemplated in this prospectus or those in which we have historically invested. The failure of our Manager to apply these proceeds effectively could result in unfavorable returns, and could cause a material adverse effect on our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Table of Contents

In addition, prior to the time we have fully deployed the net proceeds of this offering and the concurrent private placement, we may fund distributions to our shareholders out of such net proceeds, which would reduce the amount of cash we have available for acquiring assets and other purposes. The use of our net proceeds for such distributions could be dilutive to our financial results and may constitute a return of capital to our investors, which would have the effect of reducing each shareholder s basis in its common shares.

We could be subject to liability for potential violations of predatory lending laws, which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

Various federal, state and local laws have been enacted that are designed to discourage predatory lending practices. The federal Home Ownership and Equity Protection Act of 1994, or HOEPA, prohibits inclusion of certain provisions in residential mortgage loans that have mortgage rates or origination costs in excess of prescribed levels and requires that borrowers be given certain disclosures prior to origination. Some states have enacted, or may enact, similar laws or regulations, which in some cases impose restrictions and requirements greater than those in HOEPA. In addition, under the anti-predatory lending laws of some states, the origination of certain residential mortgage loans, including loans that are not classified as high cost loans under applicable law, must satisfy a net tangible benefits test with respect to the related borrower. This test may be highly subjective and open to interpretation. As a result, a court may determine that a residential mortgage loan, for example, does not meet the test even if the related originator reasonably believed that the test was satisfied. Failure of residential mortgage loan originators or servicers to comply with these laws, to the extent any of their residential mortgage loans become part of our mortgaged-related assets, could subject us, as an assignee or purchaser to the related residential mortgage loans, to monetary penalties and could result in the borrowers rescinding the affected residential mortgage loans. Lawsuits have been brought in various states making claims against assignees or purchasers of high cost loans for violations of state law. Named defendants in these cases have included numerous participants within the secondary mortgage market. If the loans are found to have been originated in violation of predatory or abusive lending laws, we could incur losses, which could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our shareholders.

We may be exposed to environmental liabilities with respect to properties to which we take title.

In the course of our business, we may take title to real estate, and, if we do take title, we could be subject to environmental liabilities with respect to these properties. In such a circumstance, we may be held liable to a governmental entity or to third parties for property damage, personal injury, investigation, and clean-up costs incurred by these parties in connection with environmental contamination, or may be required to investigate or clean up hazardous or toxic substances, or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. In addition, the presence of hazardous substances may adversely affect an owner s ability to sell real estate or borrow using real estate as collateral. To the extent that an owner of an underlying property becomes liable for removal costs, the ability of the owner to make debt payments may be reduced, which in turn may materially adversely affect the value of the relevant mortgage-related assets held by us.

Risks Related to our Relationship with our Manager and Ellington

We are dependent on our Manager and certain key personnel of Ellington that are provided to us through our Manager and may not find a suitable replacement if our Manager terminates the management agreement or such key personnel are no longer available to us.

We do not have any employees of our own. Our officers are employees of Ellington or one or more of its affiliates. We have no separate facilities and are completely reliant on our Manager, which has significant discretion as to the implementatio