



November 7, 2011

Via E-Mail (rule-comments@sec.gov)
Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE Washington, D.C. 20549-1090

Re: Companies Engaged in the Business of Acquiring Mortgages and Mortgage-Related Instruments - Commission File No. S7-34-11

Dear Ms. Murphy:

Hatteras Financial Corp. (“Hatteras”) is pleased to respond to the request for comments by the Securities and Exchange Commission (“SEC”) in Investment Company Act Release No. 29778 (August 31, 2011), 76 FR 55300 (Sept. 7, 2011) (the “Concept Release”), seeking comments on questions concerning the interpretation of Section 3(c)(5)(C) of the Investment Company Act of 1940, as amended (the “Investment Company Act”).

We are a member of the National Association of Real Estate Investment Trusts (“NAREIT”) and participated in the discussions among NAREIT and many of its members leading to the November 7, 2011 comment letter on behalf of residential mortgage REITs submitted by NAREIT in response to the Concept Release (the “NAREIT Comment Letter”).

The purpose of this letter is to:

- inform the SEC about our business and address certain of the questions and concerns raised in the Concept Release;
- advise the SEC that restricting or reversing the Section 3(c)(5)(c) exclusion as it pertains to whole-pool agency securities would negatively impact our company, our shareholders and residential mortgage financing in the U.S.; and
- confirm our support for the views expressed in the NAREIT Residential Comment Letter.

We believe that we, and companies like us, are a vital source of financing to the U.S. single family housing market. Congress clearly intended to exclude companies such as ours that acquire and invest in mortgages from regulation as an investment company under the Investment Company Act. We rely on the Section 3(c)(5)(c) exclusion and particularly from the staff’s

current no-action interpretation with respect to whole-pool agency securities. We have no difficulty satisfying the exclusion requirements as they currently stand and do not believe there is any confusion or uncertainty related to our use of the exclusion.

We further believe our management practices, the positive results we have attained for our shareholders, existing regulation, transparent disclosure and market constraints demonstrate that additional regulation of our industry is not needed to protect investors. To the contrary, amending the Section 3(c)(5)(c) exclusion, as it applies to us, would effectively end our participation in acquiring and holding agency securities. It would not only deny investors the opportunity to invest in a distinct and attractive asset class, but would also decrease liquidity and capital formation in the residential mortgage market, increasing costs to the substantial majority of Americans that borrow to acquire their family homes.

We hope the information that follows will provide you with clarity about our business practices as well as how we provide investors and homeowners with important options to achieve their goals. In return, we ask that the SEC act quickly to eliminate the market confusion caused by the Concept Release.

Our Company

Hatteras Financial Corp. is a residential mortgage real estate investment trust (“REIT”) that invests primarily in what the SEC and the industry refer to as “agency securities,” which are single-family residential mortgage pass-through securities guaranteed or issued by a U.S. Government agency, such as the Government National Mortgage Association (Ginnie Mae), or by a U.S. Government-sponsored entity such as the Federal National Mortgage Association, (Fannie Mae), and the Federal Home Loan Mortgage Corporation (Freddie Mac). We commenced operations in November of 2007 after raising private equity capital and completed an initial public offering in April of 2008. Our stock is listed on the New York Stock Exchange and trades under the symbol “HTS.” To date, we have raised equity capital of \$1.9 billion and have a market capitalization of approximately \$2.0 billion. As of September 30, 2011 we had total assets of \$18.4 billion, including approximately \$17.6 billion in agency securities.

We are organized and qualify as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”) and operate fully and comfortably within the restrictions applicable to REITs under the Code. We chose this form of tax entity as it is efficient and well understood by the investor community; enables us to acquire and invest in mortgages; and to effectively finance these investments. REITs are an integral participant in the mortgage market and our business activities are proven, supported, and monitored by other market participants, including banks, mortgage originators, broker-dealers, secondary market makers, financing providers, institutional and individual investors, equity research analysts and other service providers.

Our Business

We are in the business of investing our capital in the U.S. residential mortgage market to generate attractive risk-adjusted returns for our shareholders. Almost all of our investments are in agency securities. This is primarily a reflection of the U.S. mortgage industry, which is

dominated by U.S. Government-sponsored entities, with agency securities currently accounting for more than 90% of all mortgage production. Our investment strategy also reflects economic conditions including the fragile housing market, financing availability and investor preference.

We work on a daily basis with originators and sellers of mortgages to help them determine the rates and terms of the residential mortgage loans they originate. The majority of agency securities we own were purchased directly from or in cooperation with the originators of the mortgages, with whom we work to specify the composition of mortgages to be included in a pool (geography, loan size, etc.). Our focus is mortgage loans with short effective durations and predictable prepayment characteristics. We invest in both adjustable-rate mortgages (“ARMs”), hybrid ARMs, and fixed-rate mortgages.

ARMs are mortgages that have floating interest rates that reset on a specific time schedule, such as monthly, quarterly or annually, based on a specified index, typically the London Interbank Offered Rate. Hybrid ARMs are ARMs have interest rates that are fixed for an initial period (typically three, five, or seven) and then reset annually thereafter to an increment over a pre-determined interest rate index. Both fixed and adjustable-rate mortgages are important components of the overall mortgage market by offering borrowers options to fit the needs of their individual situations.

We serve an important role in financing U.S. homeowners, with our investors being ultimate financiers of the residential mortgage market. We estimate that since our inception we have provided first-mortgage financing to more than 100,000 homeowners across the United States.

Our principal goal for investors is to generate an attractive net income for distribution through regular quarterly dividends from the difference between the interest income on our investment portfolio and the interest costs of our borrowings and hedging activities and other expenses. In general, our strategy is to manage interest rate risk associated with our agency securities while trying to significantly mitigate exposure to credit risk.

We invest in agency securities we believe are likely to generate long-term attractive risk-adjusted returns on capital invested, after considering (i) the amount and nature of anticipated cash flows received, (ii) our ability to borrow against them, (iii) the capital requirements resulting from the purchase and financing of them, and (iv) the costs of financing, hedging, and managing the portfolio. Within this long-term view, we believe the most effective way to provide consistent returns is through disciplined asset/liability management. We focus on both the assets and liabilities to effectively manage the interest rate risk inherent in the agency securities and the financing of our investments.

To finance our agency securities investments, we borrow using repurchase agreements (also referred to as “repo”). The repo market is a long-established, \$4 trillion lending market common to our business and often used to finance investment in agency securities. We generally borrow, using our agency securities as collateral, using repurchase agreements for terms ranging from 30 days up to three years. Our debt-to-equity ratio, generally referred to as leverage in the financial industry, is an indication of our management of interest rate risk. At September 30,

2011 our debt-to-equity ratio was 7.9:1 and has generally ranged between 6:1 and 9:1 in recent periods, reflecting economic uncertainty and our concerns about potential interest rate volatility. The terms of our financing, including the amount of leverage, is driven by market forces. Most prominently, our repo lenders require “haircuts,” a margin requirement which is the percentage amount by which our collateral value must exceed the amount of the repurchase loan secured by the collateral, to provide for the lenders a liquidity cushion. This haircut reflects lenders’ view of us, our collateral, and the potential volatility in market prices for our collateral. Our repo lenders conduct thorough credit analysis on our operations, review our leverage on at least a quarterly basis and determine our availability to their repo books based on our credit, liquidity and leverage profile.

Managing our financing is an important aspect of our business. To own and leverage any agency security, we must be able to fund lender margin calls as often as needed, sometimes as often as daily. A lender will issue a margin call to us when the value of the collateral they hold drops below a certain threshold. This may occur because of a price drop or a decrease in principal balance due to mortgage repayments. We maintain a cushion of unencumbered agency securities, short-term investments and cash and cash equivalents with which to meet these margin calls. We refer to this cushion as our liquidity position. Our liquidity position is based on experience and models of possible price movements of our assets under normal and abnormal circumstances. Our desired leverage is a result of our liquidity target.

Lastly, our leverage is determined in some part by our investors. Investors have differing risk tolerances and measure and compare risk profiles of the financial companies in which they invest. As our growth and long-term success is tied to our ability to access the capital markets, we are very conscious of how investors react to various levels of risk. We hear these comments not only through our stock price, but also at our quarterly conference calls and investor conferences which we attend.

We are proud of the results of our four years of operations. We have a paid a dividend every quarter to date, with an average yield of 15.65%. We have managed a company that has given our investors an attractive risk-adjusted return on investment during what has been unquestionably a very volatile time in the financial markets. We have always viewed our company as an appropriate diversification investment that increases average portfolio return and gives investors access to a portion of the real estate market which otherwise would be unavailable to them.

Our Disclosure

As a publicly-reporting entity, we are required to make comprehensive and accurate disclosure of our business pursuant to regulations put forth by the SEC. Through our quarterly and annual reports, we make clear plain English disclosure about a multitude of matters concerning our business, including the following:

- How we use leverage by margining our agency securities and how our repo facilities function.

- Our leverage levels, including average daily repo agreement amounts during each reporting period, repo agreement amounts at period end, our highest and lowest repurchase balances during the period and the weighted average margin requirement at period end. We also disclose the typical frequency at which we receive margin calls from our lenders and the amount of agency securities, short-term investments and cash and cash equivalents available at period end to satisfy margin calls (our liquidity position described above).
- The risks associated with using leverage, and the effect of interest rate changes on our business.
- Detailed information about our agency securities, including the percentage mix of the type of agency securities, time until interest rate reset and amortized cost of our agency securities.
- That our business is primarily the ownership and financing of agency securities.
- That we operate our business in a manner to avoid regulation as an investment company under the Investment Company Act.

We believe our investors are well informed about our use of debt and the associated risks and that we provide detailed information about our leverage and repo facilities.

Responses to Specific Concerns and Questions in the Concept Release

Although the Release asks many specific questions, the general questions seem to be:

- What companies should be covered by this exemption?
- Should the exemption be tightened or expanded?
- Should companies that qualify for the exemption be further regulated?

While it is not our intention to speculate on the full range of intentions of Congress in its lawmaking, we believe that it clearly determined real estate and real estate mortgage and related investments should be treated differently than investments in corporate stocks and bonds. As such, Congress legislated that companies primarily investing in real estate and mortgage investments should be excluded from the Investment Company Act.

The Concept Release requested comment on the appropriateness of the 55%/45% test for determining an issuer's primary engagement for purposes of Section 3(c)(5)(c). We support NAREIT in the proposition that there be no change to the 55% test for purposes of determining whether a company is primarily engaged in the business of purchasing or otherwise acquiring mortgage and other liens on and interests in real estate. We note that our business is acquiring

and owning whole agency securities and that approximately 96.5%, 97.4%, 98.5% and 97.9% of our real estate assets consisted of whole-pool agency securities at December 31, 2008, December 31, 2009, December 31, 2010, and September 30, 2011, respectively. As such, we do not believe there is any confusion about our exemption and the 55% test, compared to a moderately lower or higher percentage test, is not particularly relevant to our current operations.

The Concept Release further stated concerns about an “evolution of mortgage pools” and “new and complex mortgage related instruments.” We believe that the rules implementing the Section 3(c)(5)(c) exclusion should provide flexibility for companies to invest in a range of mortgage assets and that such flexibility is important to the long-term support of the housing market. We would encourage the SEC to consider expanding the definition of the exclusion to encompass more flexibility to allow mortgage REITs to adapt with the evolution of mortgage finance and to continue to support the fragile recovery in the housing market.

The Concept Release expressed concerns about abuses of the type the Investment Company Act was intended to address, including abuses relating to commingling and misappropriation of assets, extensive leveraging and overreaching by insiders. In this regard, we refer you to the observations in the NAREIT Comment Letter that publicly-traded REITs are subject to substantial regulation, including regulation of assets and income under the Code relating to qualification as a REIT, to the public reporting requirements of the Securities Exchange Act of 1934, the requirements of the Sarbanes-Oxley Act of 2002 and the requirements of the New York Stock Exchange. We note that, among other matters:

- Our financial position, results of operations and asset valuation are regularly audited and reviewed by our independent auditor.
- A majority of our board of directors consists of independent directors within the meaning of rules established by the New York Stock Exchange, and our board meets at least quarterly and meets regularly in executive session without any members of our management or manager present.
- We provide a process by which shareholders may directly contact our independent directors.
- We have a lead independent director and have adopted a charter of the lead director that provides the lead director with the responsibility, among others, to approve meeting agenda items.
- Our manager manages our business subject to the direction and oversight of our board of directors and must manage our business in conformity with policies and investment guidelines (including leverage levels) approved by a majority of our independent directors and monitored by our board of directors. One of the policies adopted by our board of directors is that our investments are limited to agency securities.

- We have had no affiliate transactions described by Item 404 of Regulation S-K this year or in the last fiscal year, other than as a result of our external management relationship.
- We have adopted (i) a code of business conduct and ethics that applies to all of our employees and directors, (ii) a whistleblower policy by which individuals can report suspected violations of the laws and rules that govern the reporting of our financial performance or any complaint or concern regarding our accounting, internal accounting controls, or auditing matters, or any concerns regarding any questionable accounting or auditing matters; and (iii) corporate governance guidelines that address responsibilities, composition and meeting process for our board of directors. We have made copies of these documents available to our investors.

Consequences of Restricting the Section 3(c)(5)(c) Exclusion

Changing in the Section 3(c)(5)(c) exclusion would harm our business and the investors who provide our capital. We relied on the exclusion and the SEC staff's interpretations when we raised our initial private capital in 2007, when we affected our initial public offering in 2008 and each time we raised additional capital in a subsequent public offering. Since November 2007, we have consummated eight offerings raising approximately \$1.9 billion in gross proceeds in reliance on the Section 3(c)(5)(c) exclusion and the SEC's long-standing no-action positions that whole-pool agency securities are qualifying assets. If we become subject to the Investment Company Act, and particularly Section 18(f)(1), we will be prohibited from employing appropriate leverage and will be unable to generate sufficient interest income to provide our shareholders with a favorable return on their investment.

Moreover, restricting the 3(c)(5)(c) exclusion would adversely affect not just us but also mortgage rates, home owners, real estate prices, and ultimately the U.S. economy. We believe the Concept Release negatively affected capital formation and the perception of capital formation and resulted in lower agency security prices. While the impact of the announcement was muted by actions by the Federal Reserve, we would expect the consequence of further regulation or restrictions to be more transparent through higher mortgage rates to borrowers.

We applaud the SEC's inclusion of capital formation in this discussion. It has been made clear by Congress and the executive administration that private capital needs to return in a significant fashion to the mortgage market. Due to the financial crisis in the U.S. in general, and the shutdown of the mortgage securitization market in particular, private capital involved in supporting mortgages has gone from more than 50% to less than 10% in the last four years. In order for that market to return to health, significant additional private capital will need to be encouraged into the market. Regulation that "changes the rules after the game has started," will negatively impact capital formation supporting the mortgage market.

We believe the Section 3(c)(5)(c) exclusion for mortgage investment pools served a critical purpose during the financial crisis of 2007 and 2008. The conservatorship of the Fannie Mae and Freddie Mac enabled the U.S. Government to support the U.S. residential mortgage

markets and likely prevented a more severe disruption to the mortgage industry. During the crisis, confidence in financial institutions waned, as many such institutions bore excessive leverage and owned illiquid and distressed loans and other investments that prevented investors from assessing the true value of these institutions. As a result, many financial institutions had significant difficulty accessing the capital markets and were generally deleveraging their balance sheets through the net disposition of assets. During this period, agency mortgage REITs accessed the capital markets and deployed the proceeds into the mortgage market, which served to significantly reduce volatility. As an example and as discussed above, we were formed and raised our initial capital in 2007 and completed an initial public offering in 2008 during the height of the crisis.

Conclusion

The mortgage REIT business model that relies on the exclusion has been proven over several decades. The business model is subject to numerous regulations, including the REIT restrictions of the Code, the public reporting requirements of the Securities Exchange Act of 1934, the requirements of the Sarbanes-Oxley Act of 2002 and the requirements of the New York Stock Exchange. The investor community seems comfortable with the current structure, and we are not aware of any confusion regarding our exclusion under Section 3(c)(5)(c). These conditions have resulted in significant institutional and individual investor interest and investment in the sector.

We are proud of the important role we play as a specialist in acquiring and holding mortgage securities, and we believe that our participation, and the participation of our public residential mortgage REIT peers, helps reduce the cost of home ownership to the substantial majority of Americans that borrow to acquire their family homes. We further believe that our common stock is an appropriate and desired medium for mutual funds, hedge funds, pension funds, high-net worth investors and other retail investors to invest into the residential mortgage market. Residential mortgages REITs are a distinct asset class that has produced attractive returns over time, and it would be difficult for most investors to invest in the mortgage market with the efficiency and expertise that we are able to provide them.

The ample public disclosure we make pursuant to existing regulation provides the market with sufficient information to properly evaluate our company, whether by investors, short sellers or lenders. For example, our lenders evaluate our creditworthiness on a regular basis and are comfortable with our operations and disclosure. Our stock price is affected at all times by the market including its evaluation of our investments, financing, management, management fees, and affiliate transactions, and our ability to raise capital requires our operations and disclosure are acceptable to potential investors. We host quarterly earnings calls during which we provide management's insight into our financial condition and operations, and during which analysts and shareholders may raise questions directly to us. Our shareholders, particularly our institutional shareholders, are vocal about their concerns, and we have endeavored to be responsive. Our primary mandate is to deliver a transparent and attractive risk-adjusted return for our investors, which we take seriously. We attempt to mitigate the effect of uncertainties when they arise so our investors are able to make clear and informed investment decisions without the overhang of the unknown.

We believe amending the Section 3(c)(5)(c) exclusion as it applies to us is unwarranted and detrimental to our business, our shareholders and ultimately the homeowner. We encourage the SEC to consider the position we present here and to provide clarity to the market surrounding this issue as soon as possible.

Sincerely,

Hatteras Financial Corp.

By: /s/ Michael R. Hough

Title: Chairman and Chief Executive Officer