ANTHRACITE CAPITAL INC
Form 10-Q
August 09, 2005

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the quarterly period ended June 30, 2005

OR

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

For the transition period from: ________ to ________

Commission File Number 001-13937

ANTHRACITE CAPITAL, INC.

(Exact name of registrant as specified in its charter)

Maryland	13-3978906
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
40 East 52nd Street, New York, New York	10022
(Address of principal executive offices)	(Zip Code)

(Registrant's telephone number including area code): (212) 810-3333

NOT APPLICABLE

(Former name, former address, and for new fiscal year; if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

(1) Yes X No__

(2) Yes X No__

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

(1) Yes X No__

As of August 9, 2005, 53,313,114 shares of common stock ($.001 par

value per share) were outstanding.

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Certain statements contained herein constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to future financial or business performance, strategies or expectations. Forward-looking statements are typically identified by words or phrases such as "trend," "opportunity," "pipeline," "believe," "comfortable,"

"expect," "anticipate," "current," "intention," "estimate," "position," "assume," "potential," "outlook," "continue," "remain," "maintain," "sustain," "seek," "achieve" and similar expressions, or future or conditional verbs such as "will," "would," "should," "could," "may" or similar expressions. Anthracite Capital, Inc. (the "Company") cautions that forward-looking statements are subject to numerous assumptions, risks and uncertainties, which change over time. Forward-looking statements speak only as of the date they are made, and the Company assumes no duty to and does not undertake to update forward-looking statements. Actual results could differ materially from those anticipated in forward-looking statements and future results could differ materially from historical performance.

In addition to factors previously disclosed in the Company's Securities and Exchange Commission (the "SEC") reports and those identified elsewhere in this report, the following factors, among others, could cause actual results to differ materially from forward-looking statements or historical performance:

(1) the introduction, withdrawal, success and timing of business initiatives and strategies;
(2) changes in political, economic or industry conditions, the interest rate environment or financial and capital markets, which could result in changes in the value of the Company's assets;
(3) the relative and absolute investment performance and operations of the Company's manager, BlackRock Financial Management, Inc. (the "Manager");
(4) the impact of increased competition;
(5) the impact of capital improvement projects;
(6) the impact of future acquisitions and divestitures;
(7) the unfavorable resolution of legal proceedings;
(8) the extent and timing of any share repurchases;
(9) the impact, extent and timing of technological changes and the adequacy of intellectual property protection;
(10) the impact of legislative and regulatory actions and reforms and regulatory, supervisory or enforcement actions of government agencies relating to the Company, the Manager or The PNC Financial Services Group, Inc. ("PNC Bank");
(11) terrorist activities, which may adversely affect the general economy, real estate, financial and capital markets, specific industries, and the Company and the Manager;
(12) the ability of the Manager to attract and retain highly talented professionals.
(13) fluctuations in foreign currency exchange rates; and
(14) the impact of changes to tax legislation and, generally, the tax position of the Company.

Forward-looking statements speak only as of the date they are made. The Company does not undertake, and specifically disclaims any obligation, to publicly release the result of any revisions which may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

Part I - FINANCIAL INFORMATION
Item 1. Interim Financial Statements

Anthracite Capital, Inc. and Subsidiaries
Condensed Consolidated Statements of Financial Condition
(in thousands, except per share data)

June 30, 2005
(Unaudited)

ASSETS		
Cash and cash equivalents		$13,2
Restricted cash equivalents		20,8
Securities available-for-sale, at estimated fair value:		
Subordinated commercial mortgage-backed securities ("CMBS")	$784,213	
Residential mortgage-backed securities ("RMBS")	121,544	
Investment grade securities	1,105,992	
Total securities available-for-sale		2,011,7
Commercial mortgage loan pools, at amortized cost		1,302,3
Securities held-for-trading, at estimated fair value		
CMBS	89,574	
RMBS	202,118	
Total securities held-for-trading		291,6
Commercial mortgage loans, net		221,9
Equity investment in the Carbon Capital Funds		60,4
Investments in real estate joint venture		
Other assets		42,1
Total Assets		$3,964,4
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Borrowings:		
Collateralized debt obligations ("CDOs")	$1,067,589	
Secured by pledge of subordinated CMBS	38,220	
Secured by pledge of other securities available-for-sale and restricted cash equivalents	603,390	
Secured by pledge of commercial mortgage loan pools	1,290,206	
Secured by pledge of securities held-for-trading	265,022	
Secured by pledge of commercial mortgage loans	94,396	
Total borrowings		$3,358,8
Payable for investments purchased		5,1
Distributions payable		15,8
Other liabilities		37,8
Total Liabilities		$3,417,6
Commitments and Contingencies		
Stockholders' Equity:		
Common Stock, par value $0.001 per share; 400,000 shares authorized; 53,305 shares issued and outstanding in 2005; 53,289 shares issued and outstanding in 2004		
9.375% Series C Preferred Stock, liquidation preference $57,500 in 2005 and 2004		55,4
Additional paid-in capital		579,1
Distributions in excess of earnings		(139,8
Accumulated other comprehensive income		52,1
Total Stockholders' Equity		546,8
Total Liabilities and Stockholders' Equity		$3,964,4

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

Anthracite Capital, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations (Unaudited)
(in thousands, except per share data)

	For the Three Months Ended June 30		For
	2005	2004	20
Income:			
Interest from securities available-for-sale	$34,203	$32,406	
Interest from commercial mortgage loans	4,937	1,979	
Interest from commercial mortgage loan pools	13,605	12,351	
Interest from securities held-for-trading	2,090	3,146	
Earnings from real estate joint ventures	-	542	
Earnings from equity investments	3,024	1,619	
Interest from cash and cash equivalents	266	103	
Total income	58,125	52,146	
Expenses:			
Interest	37,418	32,279	
Interest - securities held-for-trading	1,552	871	
Management fee	2,661	2,163	
General and administrative expense	938	633	
Total expenses	42,569	35,946	
Other gain (losses):			
Gain (loss) on sale of securities available-for-sale	47	(4,036)	
Loss on securities held-for-trading	(1,306)	(4,046)	
Foreign currency loss	(176)	(12)	
Loss on impairment of asset	(3,072)	-	
Total other losses	(4,507)	(8,094)	
Net income	11,049	8,106	
Dividends on preferred stock	1,348	1,775	
Cost to retire preferred stock in excess of carrying value	-	10,508	
Net income (loss) available to common stockholders	$9,701	$(4,177)	
Net income (loss) per common share, basic:	$0.18	$(0.08)	

Net income (loss) per common share, diluted:	$0.18	$(0.08)	
Dividend declared per share of Common Stock	$0.28	$0.28	
Weighted average number of shares outstanding:			
Basic	53,302	50,706	
Diluted	53,311	50,706	

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

Anthracite Capital, Inc. and Subsidiaries
Condensed Consolidated Statement of Changes in Stockholders' Equity (Unaudited)
For the Six Months Ended June 30, 2005
(in thousands)

	Common Stock, Par Value	Series C Preferred Stock	Additional Paid-In Capital	Distributions In Excess Of Earnings	Accumulated Other Comprehensiv Income
Balance at January 1, 2005	$53	$55,435	$578,919	$(134,075)	$13,406
Net income				26,765	
Unrealized loss on cash flow hedges					(8,538)
Reclassification adjustments from cash flow hedges included in net income					3,180
Change in net unrealized gain (loss) on securities available-for-sale, net of reclassification adjustment					44,084
Other Comprehensive income					
Comprehensive Income					
Dividends declared-common stock				(29,849)	
Dividends on preferred stock				(2,696)	
Issuance of common stock	-		184		
Balance at June 30, 2005	$53	$55,435	$579,103	$(139,855)	$52,132

Disclosure of reclassification adjustment:

Unrealized holding loss

Reclassification for realized gains previously recorded as unrealized

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

Anthracite Capital, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)
(in thousands)

	For the Six Months Ende June 30, 200
Cash flows from operating activities:	
Net income	$26,76
Adjustments to reconcile net income to net cash provided by (used in) operating activities:	
Net purchase of trading securities	(58,86
Net loss on securities	2,62
Earnings from real estate joint ventures and Carbon Capital Funds	(5,68
Distributions from real estate joint ventures and Carbon Capital Funds	2,76
Loss on impairment of assets	3,23
Amortization of collateralized debt obligation issuance costs	1,08
Premium amortization (discount accretion)	1,50
Unrealized net foreign currency (gain) loss	(1,25
Decrease (increase) in other assets	(2,29
Increase (decrease) in other liabilities	8,05
Net cash (used in) provided by operating activities	(22,06
Cash flows from investing activities:	
Purchase of securities available-for-sale	(223,08
Principal payments received on securities available-for-sale	28,50
Proceeds from sales of securities available-for-sale	
Purchase of commercial loan pools	
Repayments received from commercial mortgage loan pools	4,03
Funding of commercial mortgage loans	(30,26
Repayments received from commercial mortgage loans	70,58

Increase in restricted cash equivalents	(1,19
Return of capital from joint ventures and Carbon Capital Funds	16,65
Investment in Carbon Capital Funds	(12,35
Net payments under hedging securities	(1,72
Net cash (used in) provided by investing activities	(148,84
Cash flows from financing activities:	
Net increase in borrowings under reverse repurchase agreements and credit facilities	197,77
Repayments of borrowings secured by commercial mortgage loan pools	(4,62
Issuance of CDOs	
Repayments of CDOs	(37
Issuance costs for CDOs	
Proceeds from issuance of common stock, net of offering costs	18
Redemption of Series B Preferred Stock	
Dividends paid on common stock	(29,84
Dividends paid on preferred stock	(2,69
Net cash (used in) provided by financing activities	160,40
Net decrease in cash and cash equivalents	(10,50
Cash and cash equivalents, beginning of period	23,75
Cash and cash equivalents, end of period	$13,25
Supplemental disclosure of cash flow information:	
Interest paid	$49,60
Investments purchased not settled	$5,15
Investments sold not settled	$

Supplemental schedule of non-cash investing and financing activities:
Consolidation of the Controlling Class CMBS during the six months ended June 30, 2004:

Carrying value of assets acquired
Liabilities assumed

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

Anthracite Capital, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
(In thousands, except per shares and share data)

Note 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Anthracite Capital, Inc. and its subsidiaries (the "Company"), a Maryland corporation, is a real estate finance company that generates income based on the spread between the interest income on its commercial real estate securities and commercial real estate loans and the interest expense from borrowings used to finance its investments. The Company seeks to earn high returns on a risk-adjusted basis to support a consistent quarterly dividend. The Company has elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986 and, therefore, its income is largely exempt from corporate taxation. The Company commenced operations on March 24, 1998.

The Company's ongoing investment activities encompass two core investment activities:

1) Commercial Real Estate Securities
2) Commercial Real Estate Loans

The accompanying June 30, 2005 unaudited condensed consolidated financial statements have been prepared in conformity with the instructions to Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America ("GAAP") for complete financial statements. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and changes in cash flows have been made. These condensed consolidated financial statements should be read in conjunction with the annual audited financial statements and notes thereto included in the Company's annual report on Form 10-K for 2004 filed with the Securities and Exchange Commission.

In preparing the condensed consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the statements of financial condition and revenues and expenses for the periods covered. Actual results could differ from those estimates and assumptions. Significant estimates in the financial statements include the valuation of certain of the Company's mortgage-backed securities and certain other investments.

Recent Accounting Developments

In December 2004, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 123R, "Share-Based Payment." This statement is a revision to SFAS No. 123, "Accounting for Stock-Based Compensation" and supercedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." This statement establishes standards for the accounting for transactions in which an entity exchanges its

equity instruments for goods or services, primarily focusing on the accounting for transactions in which an entity obtains employee services in share-based payment transactions. Entities will be required to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). That cost will be recognized over the period during which an employee is required to provide service, the requisite service period (usually the vesting period), in exchange for the award. The grant-date fair value of employee share options and similar instruments will be estimated using option-pricing models. If an equity award is modified after the grant date, incremental compensation cost will be recognized in an amount equal to the excess of the fair value of the modified award over the fair value of the original award immediately before the modification. As amended by SEC Interpretive Release 33-8568, "Amendment to Rule 4-01(a) of Regulation S-X Regarding the Compliance Date for Statement of Financial Accounting Standards No. 123 (Revised 2004), Share Based Payment," this statement is effective as of the beginning of the first interim or annual reporting period of the Company's first fiscal year beginning after June 15, 2005. In accordance with the SFAS No. 123R, as amended, the Company will adopt SFAS No. 123R effective January 1, 2006. The Company has determined that this statement will not impact the Company's condensed consolidated financial statements, as there are no unvested options as of December 31, 2004 and the Company already applies the fair value method to all newly-issued options.

In March 2005, the FASB issued FASB Staff Position ("FSP") FIN 46(R)-5, "Implicit Variable Interests under FIN 46." FSP FIN 46(R)-5 states that a reporting entity should consider whether it holds an implicit variable interest in a variable interest entity (VIE) or in a potential VIE. If the aggregate of the explicit and implicit variable interests held by the reporting entity and its related parties would, if held by a single party, identify that party as the primary beneficiary, the party within the group most closely associated with the VIE should be deemed the primary beneficiary. The effective date of FSP FIN 46(R)-5 is the first reporting period beginning after March 31, 2005, with early application permitted for periods for which financial statements have not been issued. The adoption of FASB FIN 46(R)-5 is not expected to have a significant impact on the Company's financial statements.

In June 2005, the FASB issued Statement of Financial Accounting Standards No. 154, "Accounting Changes and Error Corrections" ("FAS 154"). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FAS No. 3, "Reporting Accounting Changes in Interim Financial Statements." FAS 154 requires that a voluntary change in accounting principle be applied retrospectively with all prior period financial statements presented on the new accounting principle. FAS 154 also requires that a change in method of depreciating or amortizing a long-lived nonfinancial asset be accounted for prospectively as a change in estimate, and correction of errors in previously issued financial statements should be termed a "restatement." FAS 154 is effective for accounting changes and correction of errors made in fiscal years beginning after December 15, 2005. The implementation of FAS 154 is not expected to have a material impact on the Company's condensed consolidated financial statements.

Reclassifications

Certain items previously reported have been reclassified to conform to the current presentation.

Note 2   NET INCOME PER SHARE

Net income per share is computed in accordance with SFAS No. 128, "Earnings Per Share." Basic income per share is calculated by dividing net income available

to common stockholders by the weighted average number of common shares outstanding during the period. Diluted income per share is calculated using the weighted average number of common shares outstanding during the period plus the additional dilutive effect, if any, of common stock equivalents. The dilutive effect of outstanding stock options is calculated using the treasury stock method, and the dilutive effect of preferred stock is calculated using the "if converted" method.

	For the Three Months Ended June 30, 2005	2004
Numerator:		
Net income (loss) available to common stockholders	$9,701	$(4,177)
Numerator for basic and diluted earnings per share	$9,701	$(4,177)
Denominator:		
Denominator for basic earnings per share-weighted average common shares outstanding	53,302,298	50,706,210
Dilutive effect of stock options	8,671	-
Denominator for diluted earnings per share--weighted average common shares outstanding and common share equivalents outstanding	53,310,969	50,706,210
Basic net income (loss) per weighted average common share:	$0.18	$(0.08)
Diluted net income (loss) per weighted average common share and common share equivalents:	$0.18	$(0.08)

Total anti-dilutive stock options excluded from the calculation of net income per share were 1,385,151 for the three and six months ended June 30, 2005. Total anti-dilutive stock options excluded from the calculation of net income (loss) per share were 1,423,351 and 1,385,651 for the three and six months ended June 30, 2004, respectively.

Note 3 SECURITIES AVAILABLE-FOR-SALE

The Company's securities available-for-sale are carried at estimated fair value. The amortized cost and estimated fair value of securities available-for-sale as of June 30, 2005 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain	U
CMBS:			
CMBS interest only securities ("IOs")	$114,460	$3,092	

Investment grade CMBS	464,470	21,651
Non-investment grade rated subordinated securities	682,063	83,391
Non-rated subordinated securities	4,616	1,533
Credit tenant leases	25,259	534
Investment grade REIT debt	297,766	15,740
Project loans	170,744	754
CDO investments	20,063	276
Total CMBS	1,779,441	126,971
Single-family RMBS:		
Agency adjustable rate securities	99,476	90
Residential CMOs	999	65
Hybrid adjustable rate mortgages ("ARMs")	21,714	-
Total RMBS	122,189	155
Total securities available-for-sale	$1,901,630	$127,126

As of June 30, 2005, an aggregate of $1,993,096 in estimated fair value of the Company's securities available-for-sale was pledged to secure its collateralized borrowings.

As of June 30, 2005, the anticipated weighted average yield to maturity based upon the amortized cost of the subordinated CMBS ("reported yield") was 10.8% per annum. The anticipated reported yield of the Company's other securities available-for-sale was 5.8%. The Company's anticipated yields on its subordinated CMBS and other securities available-for-sale are based upon a number of assumptions that are subject to certain business and economic uncertainties and contingencies. Examples of these include, among other things, the rate and timing of principal payments (including prepayments, repurchases, defaults, and liquidations and related expenses), the pass-through or coupon rate, and interest rate fluctuations. Additional factors that may affect the Company's anticipated yields to maturity on its Controlling Class CMBS (as hereafter defined) include interest payment shortfalls due to delinquencies on the underlying mortgage loans, and the timing and magnitude of credit losses on the mortgage loans underlying the Controlling Class CMBS that are a result of the general condition of the real estate market (including competition for tenants and their related credit quality) and changes in market rental rates. As these uncertainties and contingencies are difficult to predict and are subject to future events which may alter these assumptions, no assurance can be given that the anticipated yields to maturity, discussed above and elsewhere, will be achieved.

During the six months ended June 30, 2005, the Company realized a gain of $57 on securities available-for-sale. During the six months ended June 30, 2004, the Company sold securities available-for-sale for total proceeds of $280,936 resulting in a realized loss of $1,222.

The following table shows the Company's estimated fair value and gross unrealized losses, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2005.

	Less than 12 Months		12 Months or More	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
CMBS IOs	$49,950	$(2,082)	$2,716	$(349)
Investment grade CMBS	26,216	(487)	126,161	(3,744)
Non-investment grade rated subordinated securities	51,663	(1,713)	15,095	(4,256)
Credit tenant leases	-	-	16,047	(699)
Investment grade REIT debt	-	-	56,234	(786)
Project loans	17,702	(212)	662	(119)
CDO investments	14,700	(1,760)	-	-
Agency adjustable rate securities	-	-	11,307	(277)
ARMs	17,871	(302)	3,320	(221)
Total temporarily impaired securities	$178,102	$(6,556)	$231,542	$(10,451)

The temporary impairment of the available-for-sale securities results from the estimated fair value of the securities falling below the amortized cost basis. Management possesses both the intent and the ability to hold the securities until maturity, allowing for the anticipated recovery in estimated fair value of the securities held. As such, management does not believe any of the securities held are other-than-temporarily impaired at June 30, 2005.

As of June 30, 2005, the Company owns 18 different trusts where, through its investment in the lowest or non-rated subordinated CMBS of such trusts, the Company is in the first loss position. The Company considers the CMBS securities where it maintains the right to control the foreclosure/workout process on the underlying loans its controlling class CMBS ("Controlling Class"). The following table sets forth certain information relating to the aggregate principal balance and payment status of delinquent mortgage loans underlying the Controlling Class CMBS held by the Company as of June 30, 2005. The underlying collateral related to the Company's investment in commercial mortgage loan pools is also included in the table. See Note 4 of the consolidated financial statements, Commercial Mortgage Loan Pools, for a further description of the Company's investment in commercial mortgage loan pools.

	June 30, 2005	
	Principal	Number of Loans
Past due 30 days to 60 days	$44,578	12
Past due 61 days to 90 days	32,378	5
Past due 91 days or more	117,496	21
Real estate owned ("REO")	5,606	2

Foreclosure	3,631	1
Total delinquent	$203,689	41
Total principal balance	$21,294,624	

To the extent that the Company's expectation of realized losses on individual loans supporting the CMBS, if any, or such resolutions differ significantly from the Company's original loss estimates, it may be necessary to reduce the projected reported yield on the applicable CMBS investment to better reflect such investment's expected earnings net of expected losses, and write the investment down to its estimated fair value. While realized losses on individual loans may be higher or lower than original estimates, the Company currently believes its aggregate loss estimates and reported yields are appropriate on all investments.

Note 4 COMMERCIAL MORTGAGE LOAN POOLS

During the second quarter of 2004, the Company acquired subordinated CMBS in a trust establishing a Controlling Class interest. The Company negotiated for and obtained a greater degree of influence over the disposition of the commercial mortgage loans than is typically granted to the special servicer. As a result of this expanded influence, the trust was not a QSPE and FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" (revised December 2003) ("FIN 46R") required the Company to consolidate the net assets and results of operations of the trust.

The CMBS acquired by the Company had a par value of $41,495 with $13,890 not rated and the balance rated BBB- to B-. During the third quarter of 2004 the Company sold the BBB- rated security, which had the impact of increasing the borrowings for the commercial loan pool by $5,848. As of June 30, 2005, the CMBS owned by the Company have a par value of $35,495.

The debt associated with this trust is non-recourse to the Company, and is secured only by the commercial mortgage loan pools. The consolidation of this trust results in an increase in the Company's total debt to capital ratio from 3.81 to 6.14, but has no effect on the Company's recourse debt to capital ratio.

Approximately 45% of the par amount of the commercial mortgage loan pool is comprised of loans that are shadow rated A2 or better by Moody's Investors Service, Inc. and AA by Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. For income recognition purposes, the Company considers the investment grade and unrated commercial mortgage loans in the pool as single assets reflecting the credit assumptions made in establishing loss adjusted yields for Controlling Class securities. The Company has taken into account the credit quality of the underlying loans in formulating its loss assumptions. Credit losses assumed on the entire pool are 1.40% of the principal balance, or 2.53% of the unrated principal balance.

Over the life of the commercial mortgage loan pools, the Company reviews and updates its loss assumptions to determine the impact on expected cash flows to be collected. A decrease in estimated cash flows will reduce the amount of interest income recognized in future periods and may result in a loan loss reserve depending upon the severity of the cash flow reductions. An increase in estimated cash flows will first reduce the loan loss reserve and any additional cash will increase the amount of interest income recorded in future periods.

Note 5 SECURITIES HELD-FOR-TRADING

Securities classified as held-for-trading include investments that the Company intends to hold for a short period of time, usually less than one year. This classification generally includes highly liquid securities that the Company acquires to earn net interest income until the Company redeploys that capital into credit sensitive commercial real estate opportunities.

The Company's securities held-for-trading are carried at estimated fair value. At June 30, 2005, the Company's securities held-for-trading consisted of FNMA Mortgage Pools with an estimated fair value of $202,118 and CMBS with an estimated fair value of $89,574. The FNMA Mortgage Pools, and the underlying mortgages, bear interest at fixed rates for specified periods, generally three to seven years, after which the rates are periodically reset to market.

Note 6 IMPAIRMENTS - CMBS

In 2001, the Company adopted Emerging Issues Task Force Issue 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets" ("EITF 99-20"). The Company is required to update its estimated cash flows for securities subject to EITF 99-20. The Company compares the yields resulting from the updated cash flows to the current accrual yields. An impairment charge is required under EITF 99-20 if the updated yield is lower than the current accrual yield and the security has a market value less than its adjusted purchase price. The Company carries all these securities at their market value on its consolidated statement of financial condition.

During the first quarter of 2005, changes in prepayment assumptions caused the expected yield on one investment grade CMBS to decline by 1 basis point. As a result, the Company recorded a loss on impairment of the asset of $159. Based on current economic conditions, the Company believes the $159 will be repaid in full and the impairment charge will be reflected in income over the remaining life of the bond.

During the second quarter of 2005, the Company increased its underlying loan loss expectations on a 1998 vintage CMBS transaction resulting in a charge of $3,072 on one of the Company's below investment grade securities. This CMBS transaction has two underlying mortgage loans secured by assisted living facilities located in Texas that are performing below management's original expectations. The Company anticipates that these mortgage loans will be resolved in the third quarter of 2005. Based on management's current estimate of the amount recoverable from these resolutions, an impairment charge was recorded in the second quarter. The actual loss may be less than or exceed the amount recorded in the second quarter of 2005 depending upon the proceeds received upon final resolution.

Note 7 COMMON STOCK

On March 10, 2005, the Company declared dividends to its common stockholders of $0.28 per share, payable on May 2, 2005 to stockholders of record on March 31, 2005. For U.S. federal income tax purposes, the dividends are expected to be ordinary income to the Company's stockholders.

On May 24, 2005, the Company declared dividends to its common stockholders of $0.28 per share, payable on August 1, 2005 to stockholders of record on June 30, 2005. For U.S. federal income tax purposes, the dividends are expected to be ordinary income to the Company's stockholders.

During the first quarter of 2004, the Company suspended its Dividend

Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan") for all investments after March 26, 2004, and for all future investment dates. During the second quarter of 2004, the dividend reinvestment portion of the Dividend Reinvestment Plan was reinstated for all dividend payments made after August 2, 2004, and for all future dividend payment dates with a discount of 2%. During the second quarter of 2005, the optional cash purchase portion of the Dividend Reinvestment Plan was reinstated for all investment dates July 26, 2005 with a discount of 2% to the trailing 12-business day average provided the stock price remains above threshold levels established by the Company at the time.

For the six months ended June 30, 2005, the Company issued 16,230 shares of common stock of the Company, par value $0.001 per share (the "Common Stock"), under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately $184. For the six months ended June 30, 2004, the Company issued 1,077,102 shares of Common Stock under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately $12,606.

For the three and six months ended June 30, 2004, the Company issued 213,100 shares of Common Stock under a sale agency agreement with Brinson Patrick Securities Corporation. Net proceeds to the Company were approximately $2,299.

On June 30, 2004 the Company completed a follow-on offering of 2,100,000 shares of its Common Stock in an underwritten public offering. The net proceeds to the Company (after deducting underwriting fees and expenses) were approximately $23,184. The Company had granted the underwriters an option, exercisable for 30 days, to purchase up to 315,000 additional shares of Common Stock to cover over-allotments. This option was exercised on July 6, 2004 and resulted in net proceeds to the Company of approximately $3,478.

Note 8   PREFERRED STOCK

At the end of the first quarter of 2004, the Board of Directors approved the Company's decision to redeem its Series B Preferred Stock, $0.001 par value per share ("Series B Preferred Stock"). The second quarter of 2004 earnings includes a charge of $10,508 (or $0.21) per share for the redemption of the Company's Series B Preferred Stock. The Series B Preferred Stock was redeemed on May 6, 2004.

Note 9   TRANSACTIONS WITH AFFILIATES

The Company has a Management Agreement with the Manager, a majority owned indirect subsidiary of The PNC Financial Services Group, Inc. and the employer of certain directors and officers of the Company, under which the Manager manages the Company's day-to-day operations, subject to the direction and oversight of the Company's Board of Directors. On March 25, 2002, the Management Agreement was extended for one year through March 27, 2003, with the approval of the unaffiliated directors, on terms similar to the prior agreement with the following changes: (i) the incentive fee calculation would be based on GAAP earnings instead of funds from operations, (ii) the removal of the four-year period to value the Management Agreement in the event of termination and (iii) subsequent renewal periods of the Management Agreement would be for one year instead of two years. Houlihan Lokey Howard & Zukin Financial Advisors, Inc., a national investment banking and financial advisory firm, advised the Board in the 2002 renewal process.

On March 6, 2003, the unaffiliated directors approved an extension of the Management Agreement from its expiration of March 27, 2003 for one year through March 31, 2004. The terms of the renewed agreement were similar to the prior agreement except for the incentive fee calculation that would provide for a

rolling four-quarter high watermark rather than a quarterly calculation. In determining the rolling four-quarter high watermark, the Company would calculate the incentive fee based upon the current and prior three quarters' net income. The Manager would be paid an incentive fee in the current quarter if the Yearly Incentive Fee, as defined, was greater than what was paid to the Manager in the prior three quarters cumulatively. The Company phased in the rolling four-quarter high watermark commencing with the second quarter of 2003. Calculation of the incentive fee was based on GAAP earnings and adjusted to exclude special one-time events pursuant to changes in GAAP accounting pronouncements after discussion between the Manager and the unaffiliated directors. The incentive fee threshold did not change. The high watermark provided for the Manager to be paid 25% of the amount of earnings (calculated in accordance with GAAP) per share that exceeds the product of the adjusted issue price of the Company's Common Stock per share and the greater of 9.5% or 350 basis points over the ten-year Treasury note.

The Management Agreement was further extended for one year from March 31, 2004 through March 31, 2005. The base management fee was revised to equal 2% of the quarterly average total stockholders' equity for the applicable quarter. The incentive fee was revised to be 25% of the amount of earnings (calculated in accordance with GAAP) per share that exceeds the product of the adjusted issue price of the Company's Common Stock per share ($11.37 as of June 30, 2005) and the greater of 8.5% or 400 basis points over the ten-year Treasury note. On March 31, 2005, the Management Agreement was extended for one additional year through March 31, 2006. The terms of the extended agreement did not change.

For the three months ended March 31, 2004, the Company paid the Manager an annual base management fee equal to a percentage of the average invested assets of the Company as defined in the Management Agreement. The base management fee was equal to 1% per annum of the average invested assets rated less than BB- or not rated, 0.75% of average invested assets rated BB- to BB+, and 0.20% of average invested assets rated above BB+. During the third quarter of 2003, the Manager agreed to reduce the management fees by 20% from its calculated amount for the third and fourth quarters of 2003 and the first quarter of 2004. This revision resulted in $532 in savings to the Company for the three months ended March 31, 2004.

The Company incurred $2,661 and $5,240 in base management fees in accordance with the terms of the Management Agreement for the three and six months ended June 30, 2005, respectively, and $2,163 and $4,293 for the three and six months ended June 30, 2004, respectively. The Company did not incur incentive fees for the three and six months ended June 30, 2005 and 2004. As of June 30, 2005 and 2004, respectively, management fees of $2,519 and $2,021 are payable to the Manager. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of $40 and $80 for certain expenses incurred on behalf of the Company for the three and six months ended June 30, 2005, respectively, and $20 and $54 for the three and six months ended June 30, 2004, respectively, which are included in general and administrative expense on the accompanying consolidated statements of operations.

The Company has an administration agreement with the Manager. Under the terms of the administration agreement, the Manager provides financial reporting, audit coordination and accounting oversight services to the Company. The agreement can be cancelled upon 60-day written notice by either party. The Company pays the Manager a monthly administrative fee at an annual rate of 0.06% of the first $125 million of average net assets, 0.04% of the next $125 million of average net assets and 0.03% of average net assets in excess of $250 million subject to a minimum annual fee of $120. For the three and six months ended June 30, 2005, the Company paid administration fees of $52 and $103, respectively, and $45 and $89, for the three and six months ended June 30, 2004, respectively, which are included in general and administrative expense on

the accompanying consolidated statements of operations.

During 2001, the Company entered into a $50,000 commitment to acquire shares in Carbon Capital, Inc. ("Carbon I"), a private commercial real estate income opportunity fund managed by the Manager. The Carbon I investment period ended on July 12, 2004 and the Company's investment in Carbon I as of June 30, 2005 was $29,869. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon I. On June 30, 2005, the Company owned approximately 20% of the outstanding shares in Carbon I.

The Company is committed to purchase up to $100,000 of Carbon Capital II, Inc. ("Carbon II" and collectively with Carbon I, the "Carbon Capital Funds"), of which $29,311 has already been funded and $70,689 is the remaining commitment. As of June 30, 2005, the carrying value of the Company's investment in Carbon II was $30,603. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon II.

During 2000, the Company completed the acquisition of CORE Cap, Inc. At the time of the CORE Cap, Inc. acquisition, the Manager agreed to pay GMAC (CORE Cap, Inc.'s external advisor) $12,500 over a ten-year period ("Installment Payment") to purchase the right to manage the CORE Cap, Inc. assets under the existing management contract ("GMAC Contract"). The GMAC Contract had to be terminated in order to allow the Company to complete the merger, as the Company's management agreement with the Manager did not provide for multiple managers. As a result the Manager offered to buy-out the GMAC Contract as the Manager estimated it would receive incremental fees above and beyond the Installment Payment, and thus was willing to pay for, and separately negotiate, the termination of the GMAC Contract. Accordingly, the value of the Installment Payment was not considered in the Company's allocation of its purchase price to the net assets acquired in the acquisition of CORE Cap, Inc. The Company agreed that should the Management Agreement with its Manager be terminated, not renewed or not extended for any reason other than for cause, the Company would pay to the Manager an amount equal to the Installment Payment less the sum of all payments made by the Manager to GMAC. As of June 30, 2005, the Installment Payment would be $5,000 payable over five years. The Company does not accrue for this contingent liability.

Note 10 STOCK OPTIONS

On May 25, 2004, the Company granted stock options to each of its unaffiliated directors with an exercise price equal to the closing price of the Common Stock on the New York Stock Exchange on such date (or $11.81). The options vested immediately upon grant. The fair value of the options granted is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions.

	May 25, 2004
Estimated volatility	22.6%
Expected life	7 years
Risk-free interest rate	1.2%
Expected dividend yield	9.5%

The fair value of the options granted on May 25, 2004 was negligible. There were no options granted in 2005.

Note 11 BORROWINGS

Certain information with respect to the Company's collateralized borrowings at

June 30, 2005 is summarized as follows:

	Lines of Credit and Term Loans	Reverse Repurchase Agreements	Commercial Mortgage Loan Pools	Collate Debt Obl
Outstanding borrowings	$119,019	$888,712	$1,283,503	
Weighted average borrowing rate	4.60%	3.41%	3.96%	
Weighted average remaining maturity	595 days	22 days	2,660 days	
Estimated fair value of assets pledged	$182,819	$982,441	$1,302,303	

As of June 30, 2005, the Company's collateralized borrowings had the following remaining maturities:

	Lines of Credit	Reverse Repurchase Agreements	Commercial Mortgage Loan Pools	Collateralized Debt Obligations*
Within 30 days	$-	$888,712	$-	$-
31 to 59 days	-	-	-	-
60 days to less than 1 year	12,894	-	-	-
1 year to 3 years	106,125	-	-	-
3 years to 5 years	-	-	-	-
Over 5 years	-	-	1,283,503	1,067,589
	$119,019	$888,712	$1,283,503	$1,067,589

* Comprised of $405,779 of CDO debt with a weighted average remaining maturity of 6.78 years as of June 30, 2005, $292,988 of CDO debt with a weighted average remaining maturity of 7.20 years as of June 30, 2005, and $368,822 of CDO debt with a weighted average remaining maturity of 7.89 years as of June 30, 2005.

Under the lines of credit and the reverse repurchase agreements, the respective lender retains the right to mark the underlying collateral to estimated fair value. A reduction in the estimated fair value of its pledged assets will require the Company to provide additional collateral or fund margin calls. From time to time, the Company expects that it will be required to provide such additional collateral or fund margin calls.

Note 12 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company accounts for its derivative investments under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other

contracts and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at estimated fair value. If the derivative is designated as a fair value hedge, the changes in the estimated fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, the effective portions of change in the estimated fair value of the derivative are recorded in other comprehensive income ("OCI") and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the estimated fair value of cash flow hedges are recognized in earnings.

The Company uses interest rate swaps to manage exposure to variable cash flows on portions of its borrowings under reverse repurchase agreements and the floating rate debt of its CDOs and as trading derivatives intended to offset changes in estimated fair value related to securities held as trading assets. On the date in which the derivative contract is entered, the Company designates the derivative as either a cash flow hedge or a trading derivative.

On June 9, 2005, interest rate swaps with notional amounts of $43,000 that were classified as trading derivatives were re-designated as cash flow hedges of borrowings under reverse repurchase agreements. The reclassification was based on the Company's intent with respect to these derivatives with the principle objective of generating returns from other than short-term pricing differences.

As of June 30, 2005, the Company had interest rate swaps with notional amounts aggregating $1,352,628 designated as cash flow hedges of borrowings under reverse repurchase agreements and the floating rate debt of its CDOs. Cash flow hedges with an estimated fair value of $3,962 are included in other assets on the consolidated statement of financial condition and cash flow hedges with an estimated fair value of $25,606 are included in other liabilities on the consolidated statement of financial condition. For the six months ended June 30, 2005, the net change in the estimated fair value of the interest rate swaps was a decrease of $9,810, of which $(1,272) was deemed ineffective and is included as an increase of interest expense and $8,538 was recorded as a reduction of OCI. As of June 30, 2005, the $1,352,628 notional of swaps designated as cash flow hedges had a weighted average remaining term of 6.97 years.

As of June 30, 2005, the Company had interest rate swaps with notional amounts aggregating $356,445 designated as trading derivatives. Trading derivatives with an estimated fair value of $77 are included in other assets on the consolidated statement of financial condition and trading derivatives with an estimated fair value of $(862) are included in other liabilities on the consolidated statement of financial condition. For the six months ended June 30, 2005, the change in estimated fair value for these trading derivatives was a decrease of $1,749 and is included as an addition to loss on securities held-for-trading in the consolidated statements of operations. As of June 30, 2005, the $356,445 notional of swaps designated as trading derivatives had a weighted average remaining term of 7.49 years.

Occasionally, counterparties will require the Company or the Company will require counterparties to provide collateral for the interest rate swap agreements in the form of margin deposits. Net deposits are recorded as a component of either other assets or other liabilities. Should the counterparty fail to return deposits paid, the Company would be at risk for the estimated fair value of that asset. At June 30, 2005 and December 31, 2004, the balance of such net margin deposits owed to counterparties as collateral under these agreements totaled $5,876 and $4,680, respectively.

Additionally, the Company had a forward London Interbank Offered Rate ("LIBOR") cap with a notional amount of $85,000 and an estimated fair value at June 30,

2005 of $424 which is included in other assets, and the change in estimated fair value related to this derivative is included as a component of loss on securities held-for-trading in the consolidated statements of operations.

The U.S. dollar is considered the functional currency for the Company's international subsidiaries. Foreign currency transaction gain or losses are recognized in the period incurred and are included in other gain (loss) in the consolidated statement of operations. Foreign exchange contracts may be used to hedge the Company's net foreign investments. Gains and losses on foreign exchange contracts are included in other gain (loss) in the consolidated statement of operations. The Company recorded net foreign currency transaction loss of $12 and $344 for the six months ended June 30, 2004 and 2005, respectively. At June 30, 2005, the Company also had foreign currency forward commitments with an estimated fair value of $3,448 included in other assets on the consolidated statement of financial condition.

Note 13 SUBSEQUENT EVENTS

As previously disclosed in a Form 8-K filed August 1, 2005, on July 26, 2005, the Company issued $365,010 face amount of commercial mortgage related securities in a non-recourse financing ("CDO HY2"). $240,134 face amount of senior investment grade notes were issued and sold in a private placement. The Company retained the floating rate BBB- notes, the below investment grade notes and the preferred shares.

The total value of the underlying collateral portfolio is approximately $378,166 in aggregate principal balance, which will consist of approximately $330,281 in aggregate principal balance of CMBS and $47,885 in aggregate principal balance of unsecured debt issued by REITs. In addition, $100,000 will be deposited with the trustee for the purpose of purchasing additional collateral on or prior to April 26, 2006.

The Company will record the transaction as a financing for accounting purposes and will consolidate the assets, liabilities, income and expense of the CDO issuer. In the event of a sale of the BBB- floating rate security retained by the Company, CDO HY2 would be a qualifying special-purpose entity ("QSPE"). Accordingly, the Company would record the transaction as a sale for accounting purposes and would no longer consolidate the assets, liabilities, income and expense of the CDO issuer. If the transaction qualifies as a QSPE prior to the ramp being completed, the Company could experience a loss on the sale. If no securities were acquired for the ramp prior to sale treatment, the Company would incur a loss of approximately $32,000.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

All dollar figures expressed herein are expressed in thousands, except share or per share amounts or as otherwise noted.

I. General

Anthracite Capital, Inc. and subsidiaries (the "Company"), a Maryland corporation, is a real estate finance company that generates income based on the spread between the interest income on its commercial real estate securities and commercial real estate loans and the interest expense from borrowings to finance its investments. The Company's primary activity is investing in high yielding commercial real estate debt. The Company combines traditional real

estate underwriting and capital markets expertise to exploit the opportunities arising from the continuing integration of these two disciplines. The Company focuses on acquiring pools of performing loans in the form of commercial mortgage-backed securities ("CMBS"), issuing secured debt backed by CMBS and providing strategic capital for the commercial real estate industry in the form of mezzanine loan financing. The Company commenced operations on March 24, 1998.

The Company's common stock is traded on the New York Stock Exchange under the symbol "AHR". The Company's primary long-term objective is to distribute consistent dividends supported by earnings. The Company establishes its dividend by analyzing the long-term sustainability of earnings given existing market conditions and the current composition of its portfolio. This includes an analysis of the Company's credit loss assumptions, general level of interest rates and projected hedging costs.

The Company is managed by BlackRock Financial Management, Inc. (the "Manager"), a subsidiary of BlackRock, Inc., a publicly traded (NYSE: BLK) asset management company with approximately $414,400,000 of assets under management as of June 30, 2005. The Manager provides an operating platform that incorporates significant asset origination, risk management, and operational capabilities.

The Company's ongoing investment activities encompass two core investment activities:

1) Commercial Real Estate Securities
2) Commercial Real Estate Loans

The Company continues to maintain a positive, though controlled, exposure to both long- and short-term interest rates through its active hedging strategies. See "Item 3 - Quantitative and Qualitative Disclosures about Market Risk" for a discussion of interest rates and their effect on earnings and book value.

The commercial real estate securities portfolio provides diversification and high yields that are adjusted for anticipated losses over a period of time (typically, a ten-year weighted average life) and can be financed through the issuance of secured debt that matches the life of the investment. Commercial real estate loans provide attractive risk adjusted returns over shorter periods of time through strategic investments in specific property types or regions. The Company believes these portfolios can serve to provide stable earnings over time.

The following table illustrates the mix of the Company's asset types as of June 30, 2005 and December 31, 2004:

	Carrying Value as of			
	June 30, 2005		December 31, 2004	
	Amount	%	Amount	%
Commercial real estate securities	$1,979,779	50.9%	$1,628,519	44.8
Commercial mortgage loan pools	1,302,303	33.5	1,312,045	36.1
Commercial real estate loans(1)	282,461	7.3	325,350	8.9
Residential mortgage-backed securities	323,662	8.3	372,071	10.2
Total	$3,888,205	100.0%	$3,637,985	100.

(1) Includes the Company's investments in the Carbon Capital Funds at June 30, 2005 and December 31, 2004 and a real estate joint venture at December 31, 2004.

Commercial Real Estate Securities Portfolio Activity

The Company's commercial real estate securities include CMBS, investment grade real estate investment trusts ("REIT") debt and collateralized debt obligation ("CDO") investments. During the six months ended June 30, 2005, the Company's commercial real estate securities portfolio increased by approximately 22% from an estimated fair value of $1,628,519 at December 31, 2004, compared with $1,979,779 at June 30, 2005.

The Company's CDO offerings allow the Company to match fund its commercial real estate portfolio by issuing long-term debt to finance long-term assets and protects the Company from increases in short-term interest rates. The CDO debt is non-recourse to the Company; therefore, the Company's losses are limited to its equity investment in the CDO. As of June 30, 2005, over 79% of the estimated fair value of the Company's subordinated CMBS assets are match funded in the Company's CDOs.

The Company retained 100% of the equity of CDOs I, II and III and recorded the transactions on its consolidated financial statements as secured financing.

	Collateral as of June 30, 2005		Debt as of June 30, 2005	
	Adjusted Purchase Price	Loss Adjusted Yield	Adjusted Issue Price	Weighted Average Cost of Funds *
CDO I	$437,497	9.09%	$405,779	6.95%
CDO II	325,506	7.93%	292,988**	5.85%
CDO III	377,492	7.18%	368,822**	5.08%
Total **	$1,140,495	8.13%	$1,067,589	6.00%

* Weighted Average Cost of Funds is the current cost of funds plus hedging expenses.

** The Company chose not to sell $10,000 of par of CDO II debt rated BB and $13,069 of par of CDO III debt rated BB.

The following table details the par, estimated fair value, adjusted purchase price, and loss adjusted yield of the Company's commercial real estate securities outside of the CDOs as of June 30, 2005:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Adj Do Pr
Investment grade CMBS	$202,828	$209,558	103.32	$211,764	104
Investment grade REIT debt	70,885	71,191	100.43	70,938	100

CMBS rated BB+ to B	160,725	131,941	82.09	127,966	79
CMBS rated B- or lower	131,552	40,055	30.45	37,998	28
CDO investments	201,023	18,579	9.24	20,063	9
CMBS Interest Only securities ("IOs")	3,613,483	115,121	3.19	114,460	3
Project loans	159,255	171,167	107.48	170,744	107
Total	$4,539,751	$757,612	16.69	$753,933	16

The following table details the par, estimated fair value, adjusted purchase price and loss adjusted yield of the Company's commercial real estate securities outside of the CDOs as of December 31, 2004:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Adj Do Pr
Investment grade CMBS	$145,420	$146,467	100.72	$150,612	103
Investment grade REIT debt	43,885	43,291	98.65	44,274	100
CMBS rated BB+ to B	96,825	77,738	80.29	75,465	77
CMBS rated B- or lower	74,740	14,833	19.85	16,120	21
CDO investments	203,182	19,837	9.76	19,450	9
CMBS IOs	3,712,604	125,246	3.37	122,379	3
Project loans	23,082	23,649	102.46	24,092	104
Total	$4,299,738	$451,061	10.49	$452,392	10

Below Investment Grade CMBS and Underlying Loan Performance

The Company divides its below investment grade CMBS investment activity into two portfolios; Controlling Class CMBS and other below investment grade CMBS. The distinction between the two is in the rights the Company obtains with its investment in Controlling Class CMBS. Controlling Class rights allow the Company to control the workout and/or disposition of defaults that occur in the underlying loans. These securities absorb the first losses realized in the underlying loan pools. The coupon payment on the non-rated security can also be reduced for special servicer fees charged to the trust. The next highest rated security in the structure will then generally be downgraded to non-rated and become the first to absorb losses and expenses from that point on. The Company's other below investment grade CMBS have no rights associated with its ownership to control the workout and/or disposition of underlying loan defaults; however, these investments are not the first to absorb losses in the underlying pools.

During the second quarter of 2005, the Company acquired $139,552 of par of Controlling Class CMBS, $4,800 of par of other below investment grade CMBS, and $28,407 of other investment grade CMBS. The total par of the Company's other below investment grade CMBS at June 30, 2005 was $318,045; the average credit protection, or subordination level, of this portfolio is 4.85%. The total par of the Company's subordinated Controlling Class CMBS securities at June 30, 2005 was $725,135 and the total par of the loans underlying these securities was $21,294,624.

The Company's investment in its subordinated Controlling Class CMBS by credit rating category at June 30, 2005 is as follows:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Adjusted Dollar Price	Subordinatio Level
BB+	$137,135	$134,892	98.36	$118,088	86.11	6.20%
BB	93,724	85,116	90.82	76,926	82.08	4.44%
BB-	115,178	97,281	84.46	87,599	76.06	4.01%
B+	97,429	67,162	68.93	65,221	66.94	2.72%
B	150,117	93,871	62.53	89,542	59.65	2.67%
B-	26,764	15,624	58.38	15,633	58.41	1.30%
CCC	19,326	3,891	20.13	3,736	19.33	1.49%
NR	85,462	20,530	24.02	18,628	21.80	n/a
Total	$725,135	$518,367	71.49	$475,373	65.56	

The Company's investment in its subordinated Controlling Class CMBS by credit rating category at December 31, 2004 is as follows:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Adjusted Dollar Price	Subordinatio Level
BB+	$129,493	$122,294	94.44	$112,754	87.07	6.50%
BB	76,575	65,610	85.68	61,602	80.45	4.73%
BB-	118,144	91,919	77.80	90,307	76.44	4.16%
B+	61,604	40,409	65.59	40,951	66.48	2.88%
B	171,093	106,455	62.22	102,893	60.14	2.64%
B-	7,809	4,478	57.35	4,552	58.29	1.41%
CCC	19,326	4,360	22.56	6,573	34.01	1.38%
NR	47,605	5,984	12.57	4,996	10.49	n/a
Total	$631,649	$441,509	69.90	$424,628	67.23	

During the six months ended June 30, 2005, servicers reduced the par amount of the Company's Controlling Class CMBS in the amount of $4,562. Further delinquencies and losses may cause the par reductions to continue and cause the Company to conclude that a change in loss adjusted yield is required along with a write down of the adjusted purchase price through the income statement according to Emerging Issues Task Force Issue 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets" ("EITF 99-20"). Also during the six months ended June 30, 2005, the loan pools were paid down by $422,786. Pay down proceeds are distributed to the highest rated CMBS class first and reduce the percent of total underlying collateral represented by each rating category.

For all of the Company's Controlling Class securities, the Company assumes that a total of 1.73% of the original loan balance will not be recoverable. This estimate was developed based on an analysis of individual loan characteristics and prevailing market conditions at the time of origination. This loss estimate equates to cumulative expected defaults of approximately 5% over the life of the portfolio and an average assumed loss severity of 35% of the defaulted loan balance. All estimated workout expenses including special servicer fees are included in these assumptions. Actual results could differ materially from

these estimated results. See Item 3 -"Quantitative and Qualitative Disclosures About Market Risk" for a discussion of how differences between estimated and actual losses could affect Company earnings.

The Company monitors credit performance on a monthly basis and debt service coverage ratios on a quarterly basis. Using these and other statistics, the Company maintains watch lists for loans that are delinquent thirty days or more and for loans that are not delinquent but have issues that the Company's management believes require close monitoring.

During the second quarter of 2005, the Company increased its underlying loan loss expectations on a 1998 vintage CMBS transaction resulting in a charge of $3,072 on one of the Company's below investment grade securities. This CMBS transaction has two underlying mortgage loans secured by assisted living facilities located in Texas that are performing below management's original expectations. The Company anticipates that these mortgage loans will be resolved in the third quarter of 2005. Based on management's current estimate of the amount recoverable from these resolutions, an impairment charge was recorded in the second quarter. The actual loss may be less than or exceed the amount recorded in the second quarter of 2005 depending upon the proceeds received upon final resolution.

During the first quarter of 2005, changes in prepayment assumptions caused the expected yield on one investment grade CMBS to decline by 1 basis point. As a result, the Company recorded a loss on impairment of the asset of $159. Based on current economic conditions, the Company believes the $159 will be repaid in full and the impairment charge will be reflected in income over the remaining life of the bond.

The Company considers delinquency information from the Lehman Brothers Conduit Guide to be the most relevant benchmark to measure credit performance and market conditions applicable to its Controlling Class CMBS holdings. The year of issuance, or vintage year, is important, as older loan pools will tend to have more delinquencies than newly underwritten loans. The Company owns Controlling Class CMBS issued in 1998, 1999, 2001, 2002, 2003, 2004 and 2005. Comparable delinquency statistics referenced by vintage year as a percentage of par outstanding as of June 30, 2005 are shown in the table below:

Vintage Year	Underlying Collateral	Delinquencies Outstanding	Lehman Brothers Conduit Guide
1998	$6,378,835	2.30%	1.54%
1999	671,812	1.01%	2.31%
2001	888,737	3.95%	1.97%
2002	1,154,653	0.31%	0.70%
2003	2,139,830	0.48%	0.33%
2004	6,676,865	.02%	0.08%
2005	3,383,892	-%	-%
Total	$21,294,624	0.96%	0.71%*

* Weighted average based on current principal balance.

Morgan Stanley also tracks CMBS loan delinquencies for the specific CMBS transactions with more than $200,000 of collateral and that have been seasoned for at least one year. This seasoning criteria will generally adjust for the lower delinquencies that occur in newly originated collateral. As of June 30,

2005, the Morgan Stanley index indicated that delinquencies on 314 securitizations were 1.41%, and as of December 31, 2004, this same index indicated that delinquencies on 286 securitizations were 1.74%. See Item 3 - "Quantitative and Qualitative Disclosures About Market Risks" for a detailed discussion of how delinquencies and loan losses affect the Company.

Delinquencies on the Company's CMBS collateral as a percent of principal increased in line with expectations. The Company's aggregate delinquency experience is consistent with comparable data provided in the Lehman Brothers Conduit Guide.

Of the 41 delinquent loans shown on the chart in Note 3 of the consolidated financial statements, two loans were real estate owned and being marketed for sale, one loan was in foreclosure, and the remaining 38 loans were in some form of workout negotiations. Aggregate realized losses of $4,955 were realized during the six months ended June 30, 2005. This brings cumulative realized losses to $80,175, which is 19.3% of total estimated losses. These losses include special servicer and other workout expenses. This experience to date is in line with the Company's loss expectations. Realized losses and special servicer expenses are expected to increase on the underlying loans as the portfolio matures. Special servicer expenses are also expected to increase as the portfolio matures.

The Company manages its credit risk through disciplined underwriting, diversification, active monitoring of loan performance and exercise of its right to control the workout process for delinquent loans as early as possible. The Company maintains diversification of credit exposures through its underwriting process and can shift its focus in future investments by adjusting the mix of loans in subsequent acquisitions. The comparative profiles of the loans underlying the Company's CMBS by property type as of June 30, 2005 and December 31, 2004 are as follows:

	June 30, 2005 Exposure		December 31, 2004 Exposure	
Property Type	Loan Balance	% of Total	Loan Balance	% of Total
Retail	$7,028,370	33.0%	$6,026,472	32.4%
Multifamily	5,537,718	26.0	5,305,129	28.6
Office	5,771,970	27.1	4,617,616	24.9
Industrial	1,438,827	6.8	1,272,583	6.8
Lodging	1,048,898	4.9	915,369	4.9
Healthcare	322,557	1.5	327,832	1.8
Other	146,284	0.7	115,728	0.6
Total	$21,294,624	100%	$18,580,729	100%

As of June 30, 2005, the estimated fair value of the Company's holdings of subordinated Controlling Class CMBS is $42,995 higher than the adjusted cost for these securities which consists of a gross unrealized gain of $49,152 and a gross unrealized loss of $6,157. The adjusted purchase price of the Company's subordinated Controlling Class CMBS portfolio as of June 30, 2005 represents approximately 65.6% of its par amount. The estimated fair value of the Company's Controlling Class CMBS portfolio as of June 30, 2005 represents approximately 71.5% of its par amount. As the portfolio matures, the Company expects to recoup the $6,157 of unrealized loss, provided that the credit losses experienced are not greater than the credit losses assumed in the projected cash flow analysis. As of June 30, 2005, the Company believes there has been no material deterioration in the credit quality of its portfolio below current expectations.

As the portfolio matures and expected losses occur, subordination levels of the lower rated classes of a CMBS investment will be reduced. This may cause the lower rated classes to be downgraded, which would negatively affect their estimated fair value and therefore the Company's net asset value. Reduced estimated fair value would negatively affect the Company's ability to finance any such securities that are not financed through a CDO or similar matched funding vehicle. In some cases, securities held by the Company may be upgraded to reflect seasoning of the underlying collateral and thus would increase the estimated fair value of the securities. During the six months ended June 30, 2005, there were credit upgrades on three of the Company's Controlling Class CMBS and no credit downgrades.

The Company's income calculated in accordance with generally accepted accounting principles in the United States of America ("GAAP") for its CMBS is computed based upon a yield, which assumes credit losses will occur. The yield to compute the Company's taxable income does not assume there would be credit losses, as a loss can only be deducted for tax purposes when it has occurred. As a result, for the years 1998 through June 30, 2005, the Company's GAAP income accrued on its CMBS assets was approximately $39,704 lower than the taxable income accrued on the CMBS assets.

Commercial Real Estate Loan Activity

The Company's commercial real estate loan portfolio generally emphasizes larger transactions located in metropolitan markets, as compared to the typical loan in the CMBS portfolio.

The following table summarizes the Company's commercial real estate loan portfolio by property type as of June 30, 2005 and December 31, 2004:

	Book Value				Weighted Average Yield	
	June 30, 2005		December 31, 2004			
Property Type	Amount	%	Amount	Amount	2005	2004
Office	$ 79,580	35.8%	$88,311	33.5%	9.1%	9.2%
Residential	43,802	19.7	13,480	5.1	4.5	12.2
Retail	21,003	9.5	59,070	22.4	2.5	6.6
Hotel	77,603	35.0	102,645	39.0	7.8	7.8
Total	221,988	100.0%	$263,506	100.0%	8.6%	8.3%

During the six months ended June 30, 2005, the Company experienced repayments of $70,583 related to its U.S. dollar denominated commercial real estate loan portfolio.

Additionally, during the six months ended June 30, 2005, the Company purchased a commercial real estate loan secured by apartment buildings located throughout Germany. The loan is denominated in Euros and has a stated face of (euro)25,000. The acquisition of this loan brings total European commercial real estate loans to $49,935 as of June 30, 2005, up from $19,991 as of December 31, 2004. The Company finances these loans by borrowing in the applicable currency and hedging the un-financed portion. The carrying value and average yields on the Company's commercial real estate loans as of June 30,

2005 were as follows:

	Carrying Value	Average Yield	Average Spread to to 1-month USD LIBOR	Average Spread to to 3-month GBP LIBOR	Average Spread to to 3-month EURIBOR
Fixed Rate	$89,111	9.71%			
Floating Rate	82,885		5.48%		
Floating Rate	19,671			6.00%	
Floating Rate	30,264				4.00%
	$221,931				

Recent Events

As previously disclosed in a Form 8-K filed August 1, 2005, on July 26, 2005, the Company issued $365,010 face amount of commercial mortgage related securities in a non-recourse financing ("CDO HY2"). $240,134 face amount of senior investment grade notes were issued and sold in a private placement. The Company retained the floating rate BBB- notes, the below investment grade notes and the preferred shares.

The total value of the underlying collateral portfolio is approximately $378,166 in aggregate principal balance, which will consist of approximately $330,281 in aggregate principal balance of CMBS and $47,885 in aggregate principal balance of unsecured debt issued by REITs. In addition, $100,000 will be deposited with the trustee for the purpose of purchasing additional collateral on or prior to April 26, 2006.

The Company will record the transaction as a financing for accounting purposes and will consolidate the assets, liabilities, income and expense of the CDO issuer. In the event of a sale of the BBB- floating rate security retained by the Company, CDO HY2 would be a qualifying special-purpose entity ("QSPE"). Accordingly, the Company would record the transaction as a sale for accounting purposes and would no longer consolidate the assets, liabilities, income and expense of the CDO issuer. If the transaction qualifies as a QSPE prior to the ramp being completed, the Company could experience a loss on the sale. If no securities were acquired for the ramp prior to sale treatment, the Company would incur a loss of approximately $32,000.

Critical Accounting Estimates

Management's discussion and analysis of financial condition and results of operations are based on the amounts reported in the Company's consolidated financial statements. These financial statements are prepared in accordance with GAAP. In preparing the financial statements, management is required to make various judgments, estimates and assumptions that affect the reported amounts. Changes in these estimates and assumptions could have a material effect on the Company's consolidated financial statements. The following is a summary of the Company's accounting policies that are the most affected by management judgments, estimates and assumptions:

Securities Available-for-sale

The Company has designated certain investments in mortgage-backed securities, mortgage-related securities and certain other securities as available-for-sale. Securities available-for-sale are carried at estimated fair value with the net unrealized gains or losses reported as a component of accumulated other comprehensive income (loss) in stockholders' equity. Many of these investments are relatively illiquid, and management must estimate their values. In making these estimates, management generally utilizes market prices provided by dealers who make markets in these securities, but may, under certain circumstances, adjust these valuations based on management's judgment. Changes in the valuations do not affect the Company's reported net income or cash flows, but impact stockholders' equity and, accordingly, book value per share.

Management must also assess whether unrealized losses on securities reflect a decline in value that is other than temporary, and, accordingly, write the impaired security down to its fair value, through earnings. Significant judgment by management is required in this analysis, which includes, but is not limited to, making assumptions regarding the collectability of the principal and interest, net of related expenses, on the underlying loans.

Income on these securities is recognized based upon a number of assumptions that are subject to uncertainties and contingencies. Examples of these assumptions include, among other things, the rate and timing of principal payments (including prepayments, repurchases, defaults and liquidations), the pass-through or coupon rate and interest rate fluctuations. Additional factors that may affect the Company's reported interest income on its mortgage securities include interest payment shortfalls due to delinquencies on the underlying mortgage loans, the timing and magnitude of credit losses on the mortgage loans underlying the securities that are a result of the general condition of the real estate market (including competition for tenants and their related credit quality) and changes in market rental rates. These uncertainties and contingencies are difficult to predict and are subject to future events that may alter the assumptions.

The Company recognizes interest income from its purchased beneficial interests in securitized financial interests ("beneficial interests") (other than beneficial interests of high credit quality, sufficiently collateralized to ensure that the possibility of credit loss is remote, or that cannot contractually be prepaid or otherwise settled in such a way that the Company would not recover substantially all of its recorded investment) in accordance with EITF 99-20. Accordingly, on a quarterly basis, when changes in estimated cash flows from the cash flows previously estimated occur due to actual prepayment and credit loss experience, the Company calculates a revised yield based on the current amortized cost of the investment (including any other-than-temporary impairments recognized to date) and the revised cash flows. The revised yield is then applied prospectively to recognize interest income.

For other mortgage-backed and related mortgage securities, the Company accounts for interest income under SFAS No. 91, "Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases" ("SFAS No. 91"), using the effective yield method which includes the amortization of discount or premium arising at the time of purchase and the stated or coupon interest payments.

Impairment - Securities

In accordance with SFAS No. 115, when the estimated fair value of the security classified as available-for-sale has been below amortized cost for a significant period of time and the Company concludes that it no longer has the ability or intent to hold the security for the period of time over which the Company expects the values to recover to amortized cost, the investment is

written down to its fair value. The resulting charge is included in income, and a new cost basis is established. Additionally, under EITF 99-20, when changes in estimated cash flows from the cash flows previously estimated occur due to actual prepayment and credit loss experience, and the present value of the revised cash flows using the current expected yield is less than the present value of the previously estimated remaining cash flows (adjusted for cash receipts during the intervening period), an other-than-temporary impairment is deemed to have occurred. Accordingly, the security is written down to fair value with the resulting change being included in income, and a new cost basis established. In both instances, the original discount or premium is written off when the new cost basis is established.

After taking into account the effect of an impairment charge, income is recognized under EITF 99-20 or SFAS No. 91, as applicable, using the market yield for the security used in establishing the write-down.

Mortgage Loans

The Company purchases and originates commercial mortgage loans to be held as long-term investments. The Company also has investments in private opportunity funds that invest in commercial mortgage loans and are managed by the Manager. Management must periodically evaluate each loan for possible impairment. Impairment is indicated when it is deemed probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan. If a loan was determined to be impaired, the Company would establish a reserve for probable losses and a corresponding charge to earnings. Given the nature of the Company's loan portfolio and the underlying commercial real estate collateral, significant judgment of management is required in determining impairment and the resulting loan loss allowance, which includes but is not limited to making assumptions regarding the value of the real estate that secures the mortgage loan. To date, the Company has determined that no loan loss allowances have been necessary on the loans in its portfolio or held by the opportunity funds.

Derivative Instruments

The Company utilizes various hedging instruments (derivatives) to hedge interest rate and foreign currency exposures or to modify the interest rate or foreign currency characteristics of related Company investments. All derivatives are carried at fair value, generally estimated by management based on valuations provided by the counterparty to the derivative contract. For accounting purposes, the Company's management must decide whether to designate these derivatives as either a hedge of an asset or liability, securities available-for-sale, securities held-for-trading, or foreign currency exposure. This designation decision affects the manner in which the changes in the fair value of the derivatives are reported.

II. Results of Operations

Net income for the three and six months ended June 30, 2005 was $9,701 or $0.18 per share (basic and diluted) and $24,069 or $0.45 per share (basic and diluted), respectively. Net income (loss) for the three and six months ended June 30, 2004 was $(4,177) or $(0.08) per share (basic and diluted) and $5,666 or $0.11 per share (basic and diluted), respectively. Net income increased to $0.45 per share for the six months ended June 30, 2005 as compared to $0.11 per share for the six months ended June 30, 2004.

Interest Income: The following tables set forth information regarding the total amount of income from certain of the Company's interest-earning assets.

	For the Three Months Ended June 30, 2005	2004
	Interest Income	Interest Income
Commercial real estate securities	$33,602	$30,166
Commercial mortgage loan pools	13,605	12,351
Commercial real estate loans	4,937	1,979
Residential mortgage-backed securities ("RMBS")	2,691	5,386
Cash and cash equivalents	266	103
Total interest income	$55,101	$49,985

	For the Six Months Ended June 30, 2005	2004
	Interest Income	Interest Income
Commercial real estate securities	$66,233	$59,352
Commercial mortgage loan pools	27,157	12,351
Commercial real estate loans	10,281	3,458
RMBS	5,571	12,103
Cash and cash equivalents	503	191
Total interest income	$109,745	$87,455

The following chart reconciles interest income and total income for the three and six months ended June 30, 2005 and 2004.

	For the Three Months Ended June 30, 2005	2004
Interest Income	$55,101	$49,985
Earnings from real estate joint ventures	-	542
Earnings from the Carbon Capital Funds	3,024	1,619
Total Income	58,125	$52,146

	For the Six Months Ended June 30, 2005	2004
Interest Income	$109,745	$87,455
Earnings from real estate joint ventures	59	$764
Earnings from the Carbon Capital Funds	5,629	2,991

Total Income	$115,433	$91,210

For the three and six months ended June 30, 2005, interest income from commercial real estate securities increased by $752 and $1,681 due to yield adjustments on the Company's CMBS IO portfolio computed in accordance with SFAS No. 91.

Interest Expense: The following table sets forth information regarding the total amount of interest expense from certain of the Company's collateralized borrowings and cash flow hedges. Information is based on daily average balances during the period.

	For the Three Months Ended June	
	2005	200
	Interest Expense	Inter Expe
Reverse repurchase agreements	$5,111	$2
Commercial mortgage loan pools	12,732	11
Lines of credit and term loan	1,949	
CDO liabilities	16,018	15
Cash flow hedges	1,626	3
Total	$37,436	$33

	For the Six Months Ended June	
	2005	200
	Interest Expense	Inter Expe
Reverse repurchase agreements	$9,199	$5
Commercial mortgage loan pools	25,509	11
Lines of credit and term loan	3,801	1
CDO liabilities	31,766	26
Cash flow hedges	3,926	7
Total	$74,201	$53

The foregoing interest expense amounts for the three and six months ended June 30, 2005, respectively, do not include a $1,534 and $1,273 addition to interest expense related to hedge ineffectiveness. The foregoing interest expense amounts for the three and six months ended June 30, 2004, respectively, do not include a $(467) and $506 of interest expense related to hedge ineffectiveness. See Note 12 of the consolidated financial statements, Derivative Instruments, for a further description of the Company's hedge ineffectiveness.

Net Interest Margin and Net Interest Spread from the Portfolio: The Company considers its portfolio to consist of securities available-for-sale, securities

held-for-trading, commercial mortgage loans, and cash and cash equivalents because these assets relate to its core strategy of acquiring and originating high yield loans and securities backed by commercial real estate, while at the same time maintaining a portfolio of investment grade securities to enhance the Company's liquidity.

Net interest margin from the portfolio is annualized net interest income divided by the average estimated fair value of interest-earning assets. Net interest income is total interest income less interest expense relating to collateralized borrowings. Net interest spread equals the yield on average assets for the period less the average cost of funds for the period. The yield on average assets is interest income divided by average amortized cost of interest earning assets. The average cost of funds is interest expense from the portfolio divided by average outstanding collateralized borrowings.

The following chart describes the interest income, interest expense, net interest margin and net interest spread for the Company's portfolio. The following interest income and interest expense amounts exclude income and expense related to real estate joint ventures, equity investments, hedge ineffectiveness, and the effect of the consolidation of the commercial mortgage loan pools.

	For the Three Months Ended June 30,	
	2005	2004
Interest income	$42,369	$38,037
Interest expense	$24,705	$21,669
Net interest margin	3.07%	3.05%
Net interest spread	2.05%	2.43%

Other Expenses: Expenses other than interest expense consist primarily of management fees and general and administrative expenses. Management fees paid to the Manager of $2,661 and $5,240 for the three and six months ended June 30, 2005, respectively, were solely base management fees. Management fees paid to the Manager of $2,163 and $4,293 for the three and six months ended June 30, 2004, respectively, were solely base management fees and were lower for the quarter ended March 31, 2004 as the Manager agreed to reduce the management fees by 20%. General and administrative expense of $938 and $1,757 for the three and six months ended June 30, 2005, respectively, and $633 and $1,235 for the three and six months ended June 30, 2004, respectively, were comprised of accounting agent fees, custodial agent fees, directors' fees, fees for professional services, and insurance premiums. General and administrative fees for the quarter ended June 30, 2005 rose primarily due to an increase in professional fees related to ongoing Sarbanes-Oxley Act compliance and additional costs associated with Company's expanding investment activities in Europe.

Other Gains (Losses): During the six months ended June 30, 2005 and 2004, the Company realized a gain (loss) of $57 and $(1,222), respectively, on securities available-for-sale. During the six months ended June 30, 2004, the Company sold a portion of its securities available-for-sale for total proceeds of $280,936, resulting in a realized loss of $1,222. The losses on securities held-for-trading were $1,306 and $4,046 for the three months ended June 30, 2005 and 2004, respectively, and $2,678 and $10,030 for the six months ended June 30, 2005 and 2004, respectively. Foreign currency losses were $176 and $12 for the three months ended June 30, 2005 and 2004, respectively, and $344 and $12 for the six months ended June 30, 2005 and 2004, respectively. The losses

on impairment of assets of $3,072 and $3,232 for the three and six months ended June 30, 2005, respectively, were related to the Company's write down of certain CMBS as required by EITF 99-20.

Dividends Declared: On May 24, 2005, the Company declared distributions to its stockholders of $0.28 per share, payable on August 1, 2005 to stockholders of record on June 30, 2005.

Changes in Financial Condition

Securities Available-for-sale: The Company's securities available-for-sale, which are carried at estimated fair value, included the following at June 30, 2005 and December 31, 2004:

Security Description	June 30,2005 Estimated Fair Value	Percentage	December 2004 Estim Fair Value
Commercial mortgage-backed securities:			
CMBS IOs	$115,121	5.7%	$12
Investment grade CMBS	481,890	24.0	38
Non-investment grade rated subordinated securities	759,485	37.8	75
Non-rated subordinated securities	6,149	0.3	
Credit tenant leases	25,094	1.2	2
Investment grade REIT debt	312,720	15.5	28
Project loans	171,167	8.5	2
CDO investments	18,579	0.9	1
Total CMBS	1,890,205	93.9	1,62
Single-family RMBS:			
Agency adjustable rate securities	99,289	4.9	11
Residential CMOs	1,064	0.1	
Hybrid arms	21,191	1.1	2
Total RMBS	121,544	6.1	13
Total securities available-for-sale	$2,011,749	100.0%	$1,76

Borrowings: As of June 30, 2005 and December 31, 2004, the Company's debt consisted of line-of-credit borrowings, CDO debt, term loans and reverse repurchase agreements, collateralized by a pledge of most of the Company's securities available-for-sale, securities held-for-trading, and its commercial mortgage loans. The Company's financial flexibility is affected by its ability to renew or replace on a continuous basis its maturing short-term borrowings. As of June 30, 2005 and December 31, 2004, the Company has obtained financing in amounts and at interest rates consistent with the Company's short-term financing objectives.

Under the lines of credit, and the reverse repurchase agreements, the lender retains the right to mark the underlying collateral to estimated fair value. A

reduction in the estimated fair value of its pledged assets would require the Company to provide additional collateral or fund margin calls. From time to time, the Company expects that it will be required to provide such additional collateral or fund margin calls.

The following table sets forth information regarding the Company's collateralized borrowings:

	For the Six Months End June 30, 2005	
	June 30, 2005 Balance	Maximum Balance
CDO debt*	$1,067,589	$1,067,967
Commercial mortgage loan pools	1,283,503	1,294,058
Reverse repurchase agreements	888,712	888,712
Line of credit and term loan borrowings	119,019	166,555

* Disclosed as adjusted issue price. Total par of the Company's CDO debt as of June 30, 2005 was $1,080,595.

Hedging Instruments: From time to time, the Company may reduce its exposure to market interest rates by entering into various financial instruments that adjust portfolio duration. These financial instruments are intended to mitigate the effect of changes in interest rates on the estimated fair value of the Company's assets and the cost of borrowing.

Interest rate swap agreements as of June 30, 2005 and December 31, 2004 consisted of the following:

	As of June 30, 2005			
	Notional value	Estimated Fair Value	Unamortized Cost	Average R Term (
Cash flow hedges	$643,900	$(8,211)	-	5.
Trading swaps	133,000	(718)	-	7.
CDO cash flow hedges	708,728	(13,432)	-	8.
CDO timing swaps	223,445	(67)	-	7.

	As of December 31, 2004			
	Notional value	Estimated Fair Value	Unamortized Cost	Average R Term (
Cash flow hedges	$452,600	$253	-	5.
Trading swaps	16,000	(5)	-	1.
CDO cash flow hedges	718,120	(11,262)	-	8.
CDO timing swaps	223,445	145	-	8.

Capital Resources and Liquidity

Liquidity is a measurement of the Company's ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund investments, loan acquisition and lending activities and for other general business purposes. The primary sources of funds for liquidity consist of collateralized borrowings, principal and interest payments on and maturities of securities available-for-sale, securities held-for-trading and commercial mortgage loans, and proceeds from the maturity or sales thereof.

To the extent that the Company may become unable to maintain its borrowings at their current level due to changes in the financing markets for the Company's assets, the Company may be required to sell assets in order to achieve lower borrowing levels. In this event, the Company's level of net income would decline. The Company's principal strategies for mitigating this risk are to maintain portfolio leverage at levels it believes are sustainable and to diversify the sources and types of available borrowing and capital. The Company has utilized committed bank facilities and preferred stock offerings, and will consider resecuritization or other achievable term funding of existing assets.

During the first quarter of 2004, the Company suspended its Dividend Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan") for all investments after March 26, 2004, and for all future investment dates. During the second quarter of 2004, the dividend reinvestment portion of the Dividend Reinvestment Plan was reinstated for all dividend payments made after August 2, 2004, and for all future dividend payment dates with a discount of 2%. During the second quarter of 2005, the optional cash purchase portion of the Dividend Reinvestment Plan was reinstated for all investment dates after July 26, 2005 with a discount of 2% to the trailing 12-business day average provided the stock price remains above threshold levels established by the Company at the time.

For the six months ended June 30, 2004, the Company issued 1,077,102 shares of common stock of the Company, par value $0.001 per share (the "Common Stock") under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately $12,606.

For the three and six months ended June 30, 2004, the Company issued 213,100 shares of Common Stock under a sale agency agreement with Brinson Patrick Securities Corporation. Net proceeds to the Company were approximately $2,299.

On June 30, 2004 the Company completed a follow-on offering of 2,100,000 shares of its Common Stock in an underwritten public offering. The net proceeds to the Company (after deducting underwriting fees and expenses) were approximately $23,184. The Company had granted the underwriters an option, exercisable for 30 days, to purchase up to 315,000 additional shares of Common Stock to cover over-allotments. This option was exercised on July 6, 2004 and resulted in net proceeds to the Company of approximately $3,478.

As of June 30, 2005, $118,309 of the Company's $200,000 committed credit facility with Deutsche Bank, AG was available for future borrowings and $50,473 of the Company's $75,000 committed credit facility with Greenwich Capital, Inc. was available. The Company had outstanding borrowings of $12,800 under a $13,000 committed credit facility with Morgan Stanley Mortgage Capital, Inc.

The Company's committed credit facility with Greenwich Capital, Inc., scheduled to mature in July 2005, has been extended through July 2006, with the option for an additional one-year extension.

At June 30, 2005, the Company's collateralized borrowings had the following

remaining maturities:

	Lines of Credit	Reverse Repurchase Agreements	Collateralized Debt Obligations	Comme Mortga Po
Within 30 days	$-	$888,712	$-	
31 to 59 days	-	-	-	
60 days to less than 1 year	12,894	-	-	
1 year to 3 years	106,125	-	-	
3 year to 5 years		-	-	
Over 5 years		-	1,067,589	1,2
	$119,019	$888,712	$1,067,589	$1,2

* Comprised of $405,779 of CDO debt with a weighted average remaining maturity of 6.79 years as of June 30, 2005, $292,988 of CDO debt with a weighted average remaining maturity of 7.20 years as of June 30, 2005 and $368,822 of CDO debt with a weighted average remaining maturity of 7.89 years as of June 30, 2005.

The Company has no off-balance sheet financing arrangements.

The Company's operating activities (used) provided cash flows of $(22,064) and $9,884 during the six months ended June 30, 2005 and 2004, respectively, primarily through net income offset by purchases of trading securities.

The Company's investing activities (used) provided cash flows of $(148,848) and $52,321 during the six months ended June 30, 2005 and 2004, respectively, primarily from repayments received on securities and commercial mortgage loans, offset by purchases of securities available-for-sale and commercial mortgage loans.

The Company's financing activities provided (used) cash flows $160,408 and $(21,171) during the six months ended June 30, 2005 and 2004, respectively, primarily from increase (decrease) in borrowings and dividends paid, offset by issuance of collateralized debt obligation issuance in 2004.

The Company is subject to various covenants in its lines of credit, including maintaining a minimum net worth measured on GAAP of $305,000, a recourse debt-to-equity of 3.0 to 1, a minimum cash requirement based upon certain debt-to-equity ratios, a minimum recourse debt service coverage ratio of 1.75 and a minimum liquidity reserve of $10,000. For the quarter ended June 30, 2005, the Company did not maintain the minimum recourse debt service coverage ratio of 1.75. The Company's lenders agreed to waive this requirement for the quarter ended June 30, 2005. As of June 30, 2005, the Company was in compliance with all other covenants in its lines of credit.

The Company's ability to execute its business strategy depends to a significant degree on its ability to obtain additional capital. Factors which could affect the Company's access to the capital markets, or the costs of such capital, include changes in interest rates, general economic conditions and perception in the capital markets of the Company's business, covenants under the Company's current and future credit facilities, results of operations, leverage, financial conditions and business prospects. Consequently, there can be no assurance that the Company will be able to effectively fund future growth. Except as discussed herein, management is not aware of any other trends, events, commitments or uncertainties that may have a significant effect on

liquidity.

Contingent Liability

During 2000, the Company completed the acquisition of CORE Cap, Inc. At the time of the CORE Cap, Inc. acquisition, the Manager agreed to pay GMAC (CORE Cap, Inc.'s external advisor) $12,500 over a ten-year period ("Installment Payment") to purchase the right to manage the Core Cap, Inc. assets under the existing management contract ("GMAC Contract"). The GMAC Contract had to be terminated in order to allow the Company to complete the merger, as the Company's management agreement with the Manager did not provide for multiple managers. As a result the Manager offered to buy-out the GMAC Contract as the Manager estimated it would receive incremental fees above and beyond the Installment Payment, and thus was willing to pay for, and separately negotiate, the termination of the GMAC Contract. Accordingly, the value of the Installment Payment was not considered in the Company's allocation of its purchase price to the net assets acquired in the acquisition of CORE Cap, Inc. The Company agreed that should the Management Agreement with its Manager be terminated, not renewed or not extended for any reason other than for cause, the Company would pay to the Manager an amount equal to the Installment Payment less the sum of all payments made by the Manager to GMAC. As of June 30, 2005, the Installment Payment would be $5,000 payable over five years. The Company does not accrue for this contingent liability.

Transactions with Affiliates

The Company has a Management Agreement with the Manager, a majority owned indirect subsidiary of The PNC Financial Services Group, Inc. and the employer of certain directors and officers of the Company, under which the Manager manages the Company's day-to-day operations, subject to the direction and oversight of the Company's Board of Directors. On March 25, 2002, the Management Agreement was extended for one year through March 27, 2003, with the approval of the unaffiliated directors, on terms similar to the prior agreement with the following changes: (i) the incentive fee calculation would be based on GAAP earnings instead of funds from operations, (ii) the removal of the four-year period to value the Management Agreement in the event of termination and (iii) subsequent renewal periods of the Management Agreement would be for one year instead of two years. Houlihan Lokey Howard & Zukin Financial Advisors, Inc., a national investment banking and financial advisory firm, advised the Board in the 2002 renewal process.

On March 6, 2003, the unaffiliated directors approved an extension of the Management Agreement from its expiration of March 27, 2003 for one year through March 31, 2004. The terms of the renewed agreement were similar to the prior agreement except for the incentive fee calculation that would provide for a rolling four-quarter high watermark rather than a quarterly calculation. In determining the rolling four-quarter high watermark, the Company would calculate the incentive fee based upon the current and prior three quarters' net income. The Manager would be paid an incentive fee in the current quarter if the Yearly Incentive Fee, as defined, was greater than what was paid to the Manager in the prior three quarters cumulatively. The Company phased in the rolling four-quarter high watermark commencing with the second quarter of 2003. Calculation of the incentive fee was based on GAAP earnings and adjusted to exclude special one-time events pursuant to changes in GAAP accounting pronouncements after discussion between the Manager and the unaffiliated directors. The incentive fee threshold did not change. The high watermark provided for the Manager to be paid 25% of the amount of earnings (calculated in accordance with GAAP) per share that exceeds the product of the adjusted issue price of the Company's Common Stock per share and the greater of 9.5% or 350 basis points over the ten-year Treasury note.

The Management Agreement was further extended for one year from March 31, 2004

through March 31, 2005. The base management fee was revised to equal 2% of the quarterly average total stockholders' equity for the applicable quarter. The incentive fee was revised to be 25% of the amount of earnings (calculated in accordance with GAAP) per share that exceeds the product of the adjusted issue price of the Company's Common Stock per share ($11.37 as of December 31, 2004) and the greater of 8.5% or 400 basis points over the ten-year Treasury note. On March 31, 2005, the Management Agreement was extended for one additional year through March 31, 2006. The terms of the extended agreement did not change.

For the three months ended March 31, 2004, the Company paid the Manager an annual base management fee equal to a percentage of the average invested assets of the Company as defined in the Management Agreement. The base management fee was equal to 1% per annum of the average invested assets rated less than BB- or not rated, 0.75% of average invested assets rated BB- to BB+, and 0.20% of average invested assets rated above BB+. During the third quarter of 2003, the Manager agreed to reduce the management fees by 20% from its calculated amount for the third and fourth quarters of 2003 and the first quarter of 2004. This revision resulted in $532 in savings to the Company for the three months ended March 31, 2004.

The Company incurred $2,661 and $5,240 in base management fees in accordance with the terms of the Management Agreement for the three and six months ended June 30, 2005, respectively, and $2,163 and $4,293 for the three and six months ended June 30, 2004. The Company did not incur incentive fees for the three and six months ended June 30, 2005 and 2004. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of $40 and $80 for certain expenses incurred on behalf of the Company for the three and six months ended June 30, 2005, respectively, and $20 and $54 for the three and six months ended June 30, 2004, respectively, which are included in general and administrative expense on the accompanying consolidated statements of operations.

The Company has an administration agreement with the Manager. Under the terms of the administration agreement, the Manager provides financial reporting, audit coordination and accounting oversight services to the Company. The agreement can be cancelled upon 60-day written notice by either party. The Company pays the Manager a monthly administrative fee at an annual rate of 0.06% of the first $125 million of average net assets, 0.04% of the next $125 million of average net assets and 0.03% of average net assets in excess of $250 million subject to a minimum annual fee of $120. For the three and six months ended June 30, 2005, the Company paid administration fees of $52 and $103, respectively, and $45 and $89, for the three and six months ended June 30, 2004, respectively, which are included in general and administrative expense on the accompanying consolidated statements of operations.

During 2001, the Company entered into a $50,000 commitment to acquire shares in Carbon Capital, Inc. ("Carbon I"), a private commercial real estate income opportunity fund managed by the Manager. The Carbon I investment period ended on July 12, 2004 and the Company's investment in Carbon I as of June 30, 2005 was $29,869. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon I. On June 30, 2005, the Company owned approximately 20% of the outstanding shares in Carbon I.

The Company is committed to purchase up to $100,000 of Carbon Capital II, Inc. ("Carbon II" and collectively with Carbon I, the "Carbon Capital Funds"), of which $29,311 has already been funded and $70,689 is the remaining commitment. As of June 30, 2005, the carrying value of the Company's investment in Carbon II was $30,603. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon II.

REIT Status: The Company has elected to be taxed as a REIT and therefore must

comply with the provisions of the Internal Revenue Code with respect thereto. Accordingly, the Company generally will not be subject to U.S. federal income tax to the extent of its distributions to stockholders and as long as certain asset, income and stock ownership tests are met. The Company may, however, be subject to tax at corporate rates or at excise tax rates on net income or capital gains not distributed.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market Risk: Market risk includes the exposure to loss resulting from changes in interest rates, credit curve spreads, foreign currency exchange rates, commodity prices and equity prices. The primary market risks to which the Company is exposed are interest rate risk and credit curve risk. Interest rate risk is highly sensitive to many factors, including governmental, monetary and tax policies, domestic and international economic and political considerations and other factors beyond the control of the Company. Credit curve risk is highly sensitive to the dynamics of the markets for commercial mortgage securities and other loans and securities held by the Company. Excessive supply of these assets combined with reduced demand will cause the market to require a higher yield. This demand for higher yield will cause the market to use a higher spread over the U.S. Treasury securities yield curve, or other benchmark interest rates, to value these assets. Changes in the general level of the U.S. Treasury yield curve can have significant effects on the estimated fair value of the Company's portfolio.

The majority of the Company's assets are fixed rate securities valued based on a market credit spread to U.S. Treasuries. As U.S. Treasury securities are priced to a higher yield and/or the spread to U.S. Treasuries used to price the Company's assets is increased, the estimated fair value of the Company's portfolio may decline. Conversely, as U.S. Treasury securities are priced to a lower yield and/or the spread to U.S. Treasuries used to price the Company's assets is decreased, the estimated fair value of the Company's portfolio may increase. Changes in the estimated fair value of the Company's portfolio may affect the Company's net income or cash flow directly through their impact on unrealized gains or losses on securities held-for-trading or indirectly through their impact on the Company's ability to borrow. Changes in the level of the U.S. Treasury yield curve can also affect, among other things, the prepayment assumptions used to value certain of the Company's securities and the Company's ability to realize gains from the sale of such assets. In addition, changes in the general level of the LIBOR money market rates can affect the Company's net interest income. As of June 30, 2005, all of the Company's liabilities outside of the CDOs are floating rate based on a market spread to LIBOR. As the level of LIBOR increases or decreases, the Company's interest expense will move in the same direction.

The Company may utilize a variety of financial instruments, including interest rate swaps, caps, floors and other interest rate exchange contracts, in order to limit the effects of fluctuations in interest rates on its operations. The use of these types of derivatives to hedge interest-earning assets and/or interest-bearing liabilities carries certain risks, including the risk that losses on a hedge position will reduce the funds available for payments to holders of securities and that such losses may exceed the amount invested in such instruments. A hedge may not perform its intended purpose of offsetting losses or increased costs. Moreover, with respect to certain of the instruments used as hedges, the Company is exposed to the risk that the counterparties with which the Company trades may cease making markets and quoting prices in such instruments, which may render the Company unable to enter into an offsetting transaction with respect to an open position. If the Company anticipates that the income from any such hedging transaction will not be qualifying income for

REIT income purposes, the Company may conduct part or all of its hedging activities through a to-be-formed corporate subsidiary that is fully subject to federal corporate income taxation. The profitability of the Company may be adversely affected during any period as a result of changing interest rates.

The Company monitors and manages interest rate risk based on a method that takes into consideration the interest rate sensitivity of the Company's assets and liabilities, including its preferred stock. The Company's objective is to acquire assets and match fund the purchase so that interest rate risk associated with financing these assets is reduced or eliminated. The primary risks associated with acquiring and financing these assets are mark-to-market risk and short-term rate risk. Examples of these financing types include 30-day repurchase agreements and committed borrowing facilities. Certain secured financing arrangements provide for an advance rate based upon a percentage of the estimated fair value of the asset being financed. Market movements that cause asset values to decline would require a margin call or a cash payment to maintain the relationship between asset value and amount borrowed. A cash flow based CDO is an example of a secured financing vehicle that does not require a mark to market to establish or maintain a level of financing. When financed assets are subject to a mark to market margin call, the Company carefully monitors the interest rate sensitivity of those assets. The duration of the assets financed which are subject to a mark to market margin call was 1.32 years based on net asset value as of June 30, 2005.

The Company's reported book value incorporates the estimated fair value of the Company's interest bearing assets but it does not incorporate the estimated fair value of the Company's interest bearing fixed rate liabilities and preferred stock. The fixed rate liabilities and preferred stock will generally reduce the actual interest rate risk of the Company from a pure economic perspective even though changes in the estimated fair value of these liabilities are not reflected in the Company's book value. The fixed rate liabilities issued in CDO I, CDO II and CDO III reduce the Company's economic duration by 4.72 years. The Series C Preferred Stock reduces the Company's economic duration by approximately 0.32 years. The Company's GAAP book value is not reduced by the change in the estimated fair value of these liabilities and therefore is approximately 5.04 years longer than the economic duration. The Company's duration management strategy focuses on the economic risk and maintains economic duration within a band of 3.0 to 5.0 years. At June 30, 2005, economic duration for the Company's entire portfolio was 3.08 years. Earnings per share is analyzed using the assumptions that interest rates, as defined by the LIBOR curve, increase or decrease and that the yield curves of the LIBOR rate shocks will be parallel to each other. Estimated fair value in this scenario is calculated using the assumption that the U.S. Treasury yield curve remains constant even though changes in both long- and short-term interest rates can occur simultaneously.

Regarding the table below, all changes in income and are measured as percentage changes from the respective values calculated in the scenario labeled as "Base Case." The base interest rate scenario assumes interest rates as of June 30, 2005. Actual results could differ significantly from these estimates.

Projected Change In
Earnings Per Share
Given LIBOR Movements

Change in LIBOR, +/- Basis Points	Projected Change in Earnings per Share
-200	$0.042
-100	$0.021
-50	$0.011
Base Case	

+50	$(0.011)
+100	$(0.021)
+200	$(0.042)

Credit Risk: The Company's portfolios of commercial real estate assets are subject to a high degree of credit risk. Credit risk is the exposure to loss from loan defaults. Default rates are subject to a wide variety of factors, including, but not limited to, property performance, property management, supply/demand factors, construction trends, consumer behavior, regional economics, interest rates, the strength of the U.S. economy, and other factors beyond the control of the Company.

All loans are subject to a certain probability of default. Before acquiring a Controlling Class security, the Company will perform an analysis of the quality of all of the loans proposed. As a result of this analysis, loans with unacceptable risk profiles are either removed from the proposed pool or the Company receives a price adjustment. The Company underwrites its Controlling Class CMBS investments assuming the underlying loans will suffer a certain dollar amount of defaults and these defaults will lead to some level of realized losses. Loss adjusted yields are computed based on these assumptions and applied to each class of security supported by the cash flow on the underlying loans. The most significant variables affecting loss adjusted yields include, but are not limited to, the number of defaults, the severity of loss that occurs subsequent to a default and the timing of the actual loss. The different rating levels of CMBS will react differently to changes in these assumptions. The lowest rated securities (B- or lower) are generally more sensitive to changes in timing of actual losses. The higher rated securities (B or higher) are more sensitive to the severity of losses and timing of cashflows.

The Company generally assumes that all of the principal of a non-rated security and a significant portion, if not all, of CCC and a portion of B- rated securities will not be recoverable over time. The loss adjusted yields of these classes reflect that assumption; therefore, the timing of when the total loss of principal occurs is the most important assumption in determining value and interest income. The interest coupon generated by a security will cease when there is a total loss of its principal regardless of whether that principal is paid. Therefore, timing is of paramount importance because the longer the principal balance remains outstanding, the more interest coupon the holder receives; which results in a larger economic return. Alternatively, if principal is lost faster than originally assumed, there is less opportunity to receive interest coupon; which results in a lower or possibly negative return. Additional losses, which occur due to greater severity, will not have a significant effect as all principal is already assumed to be non-recoverable.

If actual principal losses on the underlying loans exceed assumptions, the higher rated securities will be affected more significantly as a loss of principal may not have been assumed. The Company generally assumes that all principal will be recovered by classes rated B or higher. The Company manages credit risk through the underwriting process, establishing loss assumptions and careful monitoring of loan performance. After the securities have been acquired, the Company monitors the performance of the loans, as well as external factors that may affect their value.

Factors that indicate a higher loss severity or acceleration of the timing of an expected loss will cause a reduction in the expected yield and therefore reduce the earnings of the Company. Furthermore, the Company may be required to write down a portion of the adjusted purchase price of the affected assets through its consolidated statements of operations.

For purposes of illustration, a doubling of the losses in the Company's Controlling Class CMBS, without a significant acceleration of those losses,

would reduce GAAP income going forward by approximately $0.32 per share of Common Stock per year and cause a significant write down at the time the loss assumption is changed. The amount of the write down depends on several factors, including which securities are most affected at the time of the write down, but is estimated to be in the range of $0.07 to $0.27 per share based on a doubling of expected losses. A significant acceleration of the timing of these losses would cause the Company's net income to decrease. The Company's exposure to a write down is mitigated by the fact that most of these assets are financed on a non-recourse basis in the Company's CDOs, where a significant portion of the risk of loss is transferred to the CDO bondholders. As of June 30, 2005, securities with a total estimated fair value of $1,234,193 are collateralizing the CDO borrowings of $1,083,093; therefore, the Company's preferred equity interest in the three CDOs is $151,100 ($2.83 per share). The CDO borrowings are not marked to market in accordance with GAAP even though their economic value will change in response to changes in interest rates and/or credit spreads.

Asset and Liability Management: Asset and liability management is concerned with the timing and magnitude of the re-pricing and/or maturing of assets and liabilities. It is the Company's objective to attempt to control risks associated with interest rate movements. In general, management's strategy is to match the term of the Company's liabilities as closely as possible with the expected holding period of the Company's assets. This is less important for those assets in the Company's portfolio considered liquid, as there is a very stable market for the financing of these securities.

Other methods for evaluating interest rate risk, such as interest rate sensitivity "gap" (defined as the difference between interest-earning assets and interest-bearing liabilities maturing or re-pricing within a given time period), are used but are considered of lesser significance in the daily management of the Company's portfolio. Management considers this relationship when reviewing the Company's hedging strategies. Because different types of assets and liabilities with the same or similar maturities react differently to changes in overall market rates or conditions, changes in interest rates may affect the Company's net interest income positively or negatively even if the Company were to be perfectly matched in each maturity category.

ITEM 4. CONTROLS AND PROCEDURES

Under the direction of the Company's Chief Executive Officer and Chief Financial Officer, the Company evaluated its disclosure controls and procedures and concluded that its disclosure controls and procedures were effective as of June 30, 2005.

No change in internal control over financial reporting occurred during the quarter ended June 30, 2005 that has materially affected, or is reasonably likely to materially affect, such internal control over financial reporting.

Part II - OTHER INFORMATION

Item 1. Legal Proceedings

At June 30, 2005 there were no pending legal proceedings of which the Company was a defendant or of which any of its properties were subject.

Item 2. Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Ma th Und
April 1, 2005 through April 30, 2005	-	-	-	
May 1 2005 through May 31. 2005	-	-	-	
June 1 2005 through June 30, 2005	-	-	-	
Total	-	-	-	

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

Exhibits

31.1 Certification of Chief Executive Officer

31.2 Certification of Chief Financial Officer

32.1 Section 1350 Certification of Chief Executive Officer and Chief Financial Officer

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ANTHRACITE CAPITAL, INC.

Dated: August 9, 2005

By: /s/ Christopher A. Milner
Name: Christopher A. Milner
Title: Chief Executive Officer

(duly authorized representative)

Dated: August 9, 2005

By: /s/ James J. Lillis

Name: James J. Lillis
Title: Chief Financial Officer

Exhibit 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Christopher A. Milner, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Anthracite Capital, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on

our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2005

/s/ Christopher A. Milner

Name: Christopher A. Milner
Title: Chief Executive Officer

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, James J. Lillis, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Anthracite Capital, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the

effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2005

/s/ James J. Lillis

Name: James J. Lillis
Title: Chief Financial Officer

Exhibit 32.1

Certification of CEO and CFO Pursuant to
18 U.S.C. Section 1350,
as Adopted Pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report on Form 10-Q of Anthracite Capital, Inc. (the "Company") for the quarter ending June 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Christopher A. Milner, as Chief Executive Officer of the Company, and James J. Lillis, as Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Christopher A. Milner

Name: Christopher A. Milner
Title: Chief Executive Officer
Date: August 9, 2005

/s/ James J. Lillis

Name: James J. Lillis

Title: Chief Financial Officer
Date: August 9, 2005

This certification accompanies the Report pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of ss. 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this certification required by ss. 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.