ANTHRACITE CAPITAL INC
Form 10-Q
November 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 September 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 __

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

(1) Yes __ No X

As of November 9, 2005, 55,799,661 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.

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Part I - FINANCIAL INFORMATION
Item 1. Financial Statements

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

		September 30, 2005 (Unaudited)
ASSETS		
Cash and cash equivalents		$63,030
Restricted cash equivalents		89,038
Securities available-for-sale, at estimated fair value:		
Subordinated commercial mortgage-backed securities ("CMBS")	$806,924	
Residential mortgage-backed securities ("RMBS")	109,754	
Investment grade securities	1,176,588	
Total securities available-for-sale		2,093,266
Securities held-for-trading, at estimated fair value		
CMBS	87,213	
RMBS	181,700	
Total securities held-for-trading		268,913
Commercial mortgage loans, net		294,077
Commercial mortgage loan pools, at amortized cost		1,297,029
Equity investment in the Carbon Capital Funds		59,325
Investments in real estate joint venture		-
Other assets		74,904
Total Assets		$4,239,582
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Borrowings:		
Collateralized debt obligations ("CDOs")	$1,306,851	
Secured by pledge of subordinated CMBS	2,496	
Secured by pledge of other securities available-for-sale and restricted cash equivalents	571,780	
Secured by pledge of securities held-for-trading	172,575	
Secured by pledge of commercial mortgage loans	126,868	
Secured by pledge of commercial mortgage loan pools	1,278,965	
Junior subordinated notes to subsidiary trust issuing preferred securities	77,380	
Total borrowings		$3,536,915
Payable for investments purchased		87,829
Distributions payable		16,442
Other liabilities		25,910
Total Liabilities		$3,667,096

Commitments and Contingencies	
Stockholders' Equity:	
Common Stock, par value $0.001 per share; 400,000 shares authorized; 55,511 shares issued and outstanding in 2005; 53,289 shares issued and outstanding in 2004	56
9.375% Series C Preferred Stock, liquidation preference $57,500 in 2005 and 2004	55,435
Additional paid-in capital	603,839
Distributions in excess of earnings	(140,331)
Accumulated other comprehensive income	53,487
Total Stockholders' Equity	572,486
Total Liabilities and Stockholders' Equity	$4,239,582

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

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

	For the Three Months Ended September 30,		For
	2005	2004	
Income:			
Interest from securities available-for-sale	$35,480	$33,611	$
Interest from commercial mortgage loans	5,362	2,979	
Interest from commercial mortgage loan pools	13,460	13,715	
Interest from securities held-for-trading	3,797	2,738	
Earnings from real estate joint ventures	-	165	
Earnings from Carbon Capital Funds	2,870	1,979	
Interest from cash and cash equivalents	969	165	
Other income	-	742	
Total income	61,938	56,094	
Expenses:			
Interest	40,940	36,343	
Interest - securities held-for-trading	1,864	1,016	
Management fee	2,799	2,212	
General and administrative expense	933	886	
Total expenses	46,536	40,457	

Other gain (losses):			
Gain on sale of securities available-for-sale	31	2,081	
Gain (loss) on securities held-for-trading	897	(1,103)	
Foreign currency gain (loss)	87	(114)	
Loss on impairment of assets	-	-	
Total other gain (loss)	1,015	864	
Net income	16,417	16,501	
Dividends on preferred stock	1,348	1,348	
Cost to retire preferred stock in excess of carrying value	-	-	
Net income available to common stockholders	$15,069	$15,153	
Net income per common share, basic:	$0.28	$0.28	
Net income per common share, diluted:	$0.28	$0.28	
Dividend declared per share of Common Stock	$0.28	$0.28	
Weighted average number of shares outstanding:			
Basic	54,115	53,212	
Diluted	54,124	53,221	

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

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

	Common Stock, Par Value	Series C Preferred Stock	Additional Paid-In Capital	Distributions In Excess Of Earnings	Accumulate Other Comprehensi Income
Balance at January 1, 2005	$53	$55,435	$578,919	$(134,075)	$13,406
Net income				43,181	
Unrealized gain on cash flow hedges					21,018

Reclassification of losses from cash flow hedges included in net income					4,622
Change in net unrealized gain on securities available-for-sale, net of reclassification adjustment					14,441
Other comprehensive income					
Comprehensive income					
Dividends declared-common stock				(45,393)	
Dividends declared - preferred stock				(4,044)	
Issuance of common stock	3		24,920		
Balance at September 30, 2005	$56	$55,435	$603,839	$(140,331)	$53,487

Disclosure of reclassification adjustment:

Unrealized holding gain
Reclassification for realized gains previously recorded as unrealized

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

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

	For the Nin Months Ende September 30,
Cash flows from operating activities:	
Net income	$43,18
Adjustments to reconcile net income to net cash provided by operating activities:	
Net (purchase) sale of trading securities	(37,77
Net loss on securities	1,69

Earnings from subsidiary trust	(
Earnings from Carbon Capital Funds and real estate joint ventures	(8,55
Distributions from Carbon Capital Funds and real estate joint ventures	5,51
Loss on impairment of assets	3,23
Amortization of collateralized debt obligation issuance costs	1,74
Amortization of junior subordinated notes issuance costs	
Discount accretion	(64
Unrealized net foreign currency gain	1,22
Increase in other assets	1,82
Decrease in other liabilities	(6,18
Net cash provided by operating activities	5,25
Cash flows from investing activities:	
Purchase of securities available-for-sale	(321,80
Principal payments received on securities available-for-sale	55,08
Proceeds from sales of securities available-for-sale	2,63
Purchase of securities related to consolidated variable interest entity	
Sale of securities related to consolidated variable interest entity	
Repayments received from commercial mortgage loan pools	5,89
Funding of commercial mortgage loans	(83,51
Repayments received from commercial mortgage loans	82,97
Increase in restricted cash equivalents	(69,35
Return of capital from Carbon Capital Funds and joint ventures	26,86
Investment in Carbon Capital Funds	(12,35
Investment in subsidiary trust	(2,38
Net cash used in investing activities	(315,96
Cash flows from financing activities:	
Net increase in borrowings under reverse repurchase agreements and credit facilities	70,79
(Repayments) borrowings secured by commercial mortgage loan pools	(5,89
Issuance of CDOs	239,66

Repayments of CDOs	(77
Issuance costs for CDOs	(5,02

Issuance of junior subordinated notes to subsidiary trust	77,38
Issuance costs of junior subordinated notes	(2,25
Proceeds from issuance of common stock, net of offering costs	24,92
Redemption of Series B Preferred Stock	
Dividends paid on common stock	(44,77
Dividends paid on preferred stock	(4,04
Net cash provided by financing activities	349,99
Net increase (decrease) in cash and cash equivalents	39,27
Cash and cash equivalents, beginning of period	23,75
Cash and cash equivalents, end of period	$63,03
Supplemental disclosure of cash flow information:	
Interest paid	$78,68
Investments purchased not settled	$87,82
Investments sold not settled	$

Supplemental schedule of non-cash investing and financing activities:
Consolidation of variable interest entity during the nine months ended September 30, 2004:

Carrying value of assets acquired
Liabilities assumed

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

Anthracite Capital, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
(Dollar amounts in thousands, except share and per share data)

Note 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Anthracite Capital, Inc., a Maryland corporation, and its subsidiaries (the "Company") is a real estate finance company that primarily 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 primarily encompass two core investment activities:

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

The accompanying September 30, 2005 unaudited 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 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 the year ended December 31, 2004 filed with the Securities and Exchange Commission (the "SEC").

In preparing the 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 ("FASB") issued SFAS No. 123R, Share-Based Payment. This statement is a revision to SFAS No. 123, Accounting for Stock-Based Compensation, and superceded Accounting Principles Board ("APB") 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 (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 Rule 4-01(a) of Regulation S-X promulgated by the SEC, this statement is effective as of the beginning of the first interim or annual reporting period of the Company's first fiscal year beginning on or after December 15, 2005. The Company will adopt SFAS No. 123R, as amended, effective January 1, 2006. The Company has determined that this statement will not impact the Company's consolidated financial statements, as there are no unvested options as of September 30, 2005 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 was the first reporting period beginning after March 31, 2005. The adoption of FSP FIN 46(R)-5 did not have a significant impact on the Company's consolidated financial statements.

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

	For the Three Months Ended September 30, 2005	2004
Numerator:		
Net income available to common stockholders	$15,069	$15,153
Numerator for basic and diluted earnings per share	$15,069	$15,153
Denominator:		
Denominator for basic earnings per share-weighted average common shares outstanding	54,114,955	53,212,226
Dilutive effect of stock options	9,391	8,282
Denominator for diluted earnings per share--weighted average common shares outstanding and common share equivalents outstanding	54,124,346	53,220,508
Basic net income per weighted average common share:	$0.28	$0.28
Diluted net income per weighted average common share and common share equivalents:	$0.28	$0.28

Total anti-dilutive stock options excluded from the calculation of net income per share were 1,380,151 and 1,375,151 for the three and nine months ended September 30, 2005, respectively. Total anti-dilutive stock options excluded from the calculation of net income per share were 1,407,443 for the three and nine months ended September 30, 2004.

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 September 30, 2005 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain
CMBS:		
CMBS interest only securities ("IOs")	$109,465	$2,232
Investment grade CMBS	512,080	22,190
Non-investment grade rated subordinated securities	699,158	65,534
Non-rated subordinated securities	26,179	2,420
Credit tenant leases	25,129	530
Investment grade REIT debt	297,675	11,037
Project loans	214,197	67
CDO investments	17,247	1,725
Total CMBS	1,901,130	105,735
Single-family RMBS:		
Agency adjustable rate securities	93,271	25
Residential CMOs	783	56
Hybrid adjustable rate mortgages ("ARMs")	17,041	0
Total RMBS	111,095	81
Total securities available-for-sale	$2,012,225	$105,816

As of September 30, 2005, an aggregate of $2,092,907 in estimated fair value of the Company's securities available-for-sale was pledged to secure its collateralized borrowings.

During the nine months ended September 30, 2005, the Company sold a portion of its securities available-for-sale for total proceeds of $2,636 resulting in a realized gain of $88. During the nine months ended September 30, 2004, the Company sold a portion of its securities available-for-sale for total proceeds of $318,273 resulting in a realized gain of $857.

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 September 30, 2005.

Less than 12 Months		12 Months or More	
Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses

CMBS IOs	$60,176	$(2,669)	$1,087	$(254)	$
Investment grade CMBS	118,675	(1,635)	122,654	(6,936)	2
Non-investment grade rated subordinated securities	108,436	(2,177)	18,620	(3,158)	1
Non-rated subordinated securities	13,759	(4)	-	-	
Credit tenant leases	-	-	15,985	(692)	
Investment grade REIT debt	34,612	(274)	72,271	(2,173)	1
Project loans	181,918	(3,082)	18,235	(299)	2
Agency adjustable rate securities	78,677	(760)	11,182	(270)	
Hybrid ARMs	16,648	(392)	-	-	
Total temporarily impaired securities	$612,901	$(10,993)	$260,034	$(13,782)	$8

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 September 30, 2005.

As of September 30, 2005, the anticipated weighted average yield to maturity based upon the amortized cost of the subordinated CMBS ("reported yield") was 10.9% per annum. The anticipated reported yield of the Company's other securities available-for-sale was 5.9%. 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 in Note 5 of the consolidated financial statements) 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.

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Note 4 SECURITIES HELD-FOR-TRADING

The Company's securities held-for-trading are carried at estimated fair value. At September 30, 2005, the Company's securities held-for-trading consisted of FNMA Mortgage Pools with an estimated fair value of $181,700 and CMBS with an estimated fair value of $87,213. 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 5 VARIABLE INTEREST ENTITIES

The Company's ownership of the subordinated classes of CMBS from a single issuer gives it the right to control the foreclosure/workout process on the underlying loans ("Controlling Class CMBS"). FIN 46(R)-5 has certain scope exceptions, one of which provides that an enterprise that holds a variable interest in a qualifying special-purpose entity ("QSPE") does not consolidate that entity unless that enterprise has the unilateral ability to cause the entity to liquidate. SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities ("SFAS No. 140") provides the requirements for an entity to be considered a QSPE. To maintain the QSPE exception, the trust must continue to meet the QSPE criteria both initially and in subsequent periods. A trust's QSPE status can be impacted in future periods by activities by its transferor(s) or other involved parties, including the manner in which certain servicing activities are performed. To the extent its CMBS investments were issued by a trust that meets the requirements to be considered a QSPE, the Company records the investments at the purchase price paid. To the extent the underlying trusts are not QSPEs the Company follows the guidance set forth in FIN 46(R)-5 as the trusts would be considered VIEs.

The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the QSPE criteria. However, there is uncertainty with respect to QSPE treatment due to ongoing review by accounting standard setters, potential actions by various parties involved with the QSPE, as discussed above, as well as varying and evolving interpretations of the QSPE criteria under SFAS No. 140. Additionally, the standard setters continue to review the FIN 46(R)-5 provisions related to the computations used to determine the primary beneficiary of a VIE. Future guidance from the standard setters may require the Company to consolidate CMBS trusts in which the Company has invested.

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The table below details the purchase date, face amount of the Company's Controlling Class CMBS and the face amount of the respective issuance:

Controlling Class Securities	Purchase Date	Par Held by the Company	Total CMBS Issued
Unconsolidated			
CMAC 1998-C1	Jul-98	$47,786	$1,192,239
CMAC 1998-C2	Sep-98	83,858	2,891,309
DLJCM 1998-CG1	Jun-98	65,747	1,564,253
GMAC 1998-C1	Apr-98	24,737	1,438,000
LBCMT 1998-C1	May-98	129,681	1,727,818
PNCMA 1999-CM1	Nov-99	18,059	760,414
CSFB 2001-CK6	Dec-01	48,115	939,182
LBUBS 2002-C2	Oct-04	32,357	1,210,453
CSFB 2003-CPN1	Feb-03	39,759	1,006,389
GECMC 2003-C2	Jul-03	38,450	1,183,080
BACM 2004-1	Mar-04	27,925	1,327,183
BACM 2004-3	Jul-04	23,103	1,180,168
BACM 2004-6	Dec-04	47,015	956,589
GMACC 2004-C2	Aug-04	22,177	933,735

JPMCC 2004-PNC1	Jun-04	31,949	1,097,416
BACM 2005-2	Jun-05	66,721	1,608,844
BACM 2005-5	Sep-05	78,494	1,962,338
GECMC 2005-C3	Aug-05	68,774	2,116,111
MTMT 2005-MCP1	Jul-05	72,831	1,737,993
Total Unconsolidated		$967,541	$26,833,516
Consolidated			
LBUBS 2004-C2	Apr-04	35,495	1,237,113
Total Consolidated		$35,495	$1,237,113
Total Controlling Class CMBS		$1,003,036	$28,070,629

The Company's maximum exposure to loss as a result of its investment in these VIEs totaled $670,795 and $479,636 as of September 30, 2005 and December 31, 2004, respectively.

The financing structures that the Company offers to its borrowers on certain of its commercial mortgage loans involve the creation of entities that could be deemed VIEs and, therefore, could be subject to FIN 46R. Management has evaluated these entities and has concluded that none of them are VIEs that are subject to consolidation under FIN 46(R)-5.

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Note 6 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.

Approximately 45% of the par amount of the commercial mortgage loan pool is comprised of investment grade loans and the remaining 55% are unrated. 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 7 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 updates its estimated cash flows for securities subject to EITF 99-20 on a quarterly basis. 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. 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 were performing below management's original expectations. The two underlying

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mortgage loans were resolved in the fourth quarter of 2005 with lower than expected loss severities. The effect of the improved loss severity will be recognized over the remaining life of the security in the form of an increased yield.

Note 8 AFFECT OF HURRICANES ON BELOW INVESTMENT GRADE CMBS

During the third quarter of 2005, four properties which are security for mortgages in four separate CMBS transactions were severely damaged by Hurricane Katrina. The outstanding loan balances on these four properties is $24,089. Based on the Company's on-site review of the damages incurred and information available to date, the Company believes that the properties have adequate insurance coverage and the cash flows related to the four CMBS transactions should not be adversely affected. As a result, the Company has not adjusted the carrying value or the loss adjusted yields for the four CMBS transactions that include the damaged properties. However, the determinations relating to the following factors are ongoing: how the insurance companies involved will address damage with respect to wind versus flooding; what the level of deductibles will be, which is dependent upon the category determinations; and the financial resources of the insurers. In addition, the Company expects that properties underlying its CMBS transactions were affected by Hurricane Wilma during the fourth quarter of 2005. However, due to limited access and availability of information at this time, the Company has not been able to determine what affect, if any, there will be on the cash flows related to its CMBS transactions. The Company will continue to monitor the situation and will make any necessary adjustments as additional information becomes available.

Note 9 COMMON STOCK

On August 18, 2005, the Company completed a follow-on offering of 1,725,000 shares of its common stock, par value $0.001 per share ("Common Stock"), at a price of $11.59, which included a 15% over-allotment option exercised by the underwriter. Net proceeds (after deducting underwriting fees and expenses) were $19,199.

On June 30, 2004, the Company completed a follow-on offering of 2,415,000 shares of its Common Stock, at a price of $11.50, which included a 15% over-allotment option exercised by the underwriter. Net proceeds (after deducting underwriting fees and expenses) were $26,662.

During the first quarter of 2004, the Company suspended its Dividend Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan") for all investment dates after March 26, 2004. 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 nine months ended September 30, 2005, the Company issued 497,188 shares of its Common Stock under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately $5,743. For the nine months ended September 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 nine months ended September 30, 2004, the Company issued 253,800 shares of Common Stock under a sale agency agreement with Brinson Patrick Securities Corporation. Net proceeds to the Company were approximately $2,761.

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.

On September 14, 2005, the Company declared dividends to its common stockholders of $0.28 per share, payable on October 31, 2005 to stockholders of record on September 30, 2005. For U.S. federal income tax purposes, the dividends are expected to be ordinary income to the Company's stockholders.

Note 10 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 11 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 September 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 $2,799 and $8,039 in base management fees in accordance with the terms of the Management Agreement for the three and nine months ended September 30, 2005, respectively, and $2,212 and $6,505 for the three and nine months ended September 30, 2004, respectively. The Company did not incur incentive fees for the three and nine months ended September 30, 2005 and 2004. As of September 30, 2005 and 2004, respectively, management fees of $2,668 and $2,070 are payable to the Manager. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of $40 and $120 for certain expenses incurred on

behalf of the Company for the three and nine months ended September 30, 2005, respectively, and $15 and $45 for the three and nine months ended September 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 $125,000 of average net assets, 0.04% of the next $125,000 of average net assets and 0.03% of average net assets in excess of $250,000 subject to a minimum annual fee of $120. For the three and nine months ended September 30, 2005, the Company paid administration fees of $53 and $156, respectively, and $43 and $129, for the three and nine months ended September 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 September 30, 2005 was $19,096. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon I. On September 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 shares of Carbon Capital II, Inc., a private commercial real estate income opportunity fund managed by the Manager ("Carbon II" and collectively with Carbon I, the "Carbon Capital Funds"), of which $38,258 has already been funded and $61,742 is the remaining commitment. As of September 30, 2005, the carrying value of the Company's investment in Carbon II was $40,229. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon II. On September 30, 2005, the Company owned approximately 20% of the outstanding shares 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

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sum of all payments made by the Manager to GMAC. As of September 30, 2005, the Installment Payment would be $5,000 payable over five years. The Company does not accrue for this contingent liability.

Note 12 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 13 BORROWINGS

Certain information with respect to the Company's collateralized borrowings at September 30, 2005 is summarized as follows:

	Lines of Credit and Term Loans	Reverse Repurchase Agreements	Commercial Mortgage Loan Pools	Collate Debt Obl
Outstanding borrowings	$195,067	$679,425	$1,278,192	$1,
Weighted average borrowing rate	4.98%	3.85%	3.97%	
Weighted average remaining maturity	1.49 years	22 days	7.04 years	7.3

Estimated fair value of assets pledged	$296,487	$718,967	$1,297,029	$1,

As of September 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	$12,900	$679,425	$-	$-
31 to 59 days	-	-	-	-
60 days to less than 1 year	76,579	-	-	-
1 year to 3 years	105,588	-	-	-
3 years to 5 years	-	-	-	-
Over 5 years	-	-	1,278,192	1,306,851
	$195,067	$679,425	$1,278,192	$1,306,851

* As of September 30, 2005, collateralized debt obligations are comprised of $405,992 of CDO debt with a weighted average remaining maturity of 6.54 years, $292,900 of CDO debt with a weighted average remaining maturity of 6.94 years, $368,347 of CDO debt with a weighted average remaining maturity of 7.64 years, and $239,612 of CDO debt with a weighted average remaining maturity of 8.61 years.

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.

On September 26, 2005, the Company issued $75,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust I, a Delaware statutory trust (the "Trust"). The trust preferred securities have a thirty-year term ending October 30, 2035 with interest at a fixed rate of 7.497% for the first ten years and at a floating rate of three-month London Interbank Offered Rate for U.S. dollar deposits ("LIBOR") plus 2.9% thereafter. The trust preferred securities can be redeemed at par beginning in October 2010.

The Trust issued $2,380 aggregate liquidation amount of common securities, representing 100% of the voting common stock of the Trust to the Company for a purchase price of $2,380. The Trust used the proceeds from the sale of the trust preferred securities and the common securities to purchase the Company's junior subordinated notes. The terms of the junior subordinated notes match the

terms of the trust preferred securities. The notes are subordinate and junior in right of payment to all present and future senior indebtedness and certain other of our financial obligations. The Company realized net proceeds from this offering of approximately $72,740.

The Company's interest in the Trust is accounted for using the equity method and the assets and liabilities of the Trust are not consolidated into the Company's financial statements. Interest on the junior subordinated notes is included in interest expense on our consolidated income statements while the $2,380 of common securities are included as a component of other assets on the Company's consolidated statement of financial condition.

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Note 14 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 consolidated statement of financial condition 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 September 30, 2005, the Company had interest rate swaps with notional amounts aggregating $1,202,868 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 $21,020 are included in other assets on the consolidated statement of financial condition and cash flow hedges with an estimated fair value of $10,256 are included in other liabilities on the consolidated statement of financial condition. For the nine months ended September 30, 2005, the net change in the estimated fair value of the interest rate swaps was an increase of $19,352, of which $1,666 was deemed ineffective and is included as an increase of interest expense and $21,018 was recorded as an addition to OCI. As of September 30, 2005, the $1,202,868 notional of swaps designated as cash flow hedges had a weighted average remaining term of 8.09 years.

As of September 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 $2,866 are included in other assets on the consolidated statement of financial condition and trading derivatives with an estimated fair value of $116 are included in other liabilities on the consolidated statement of financial condition. For the nine months ended September 30, 2005, the change in estimated fair value for these trading derivatives was an increase of $1,785 and is included as a reduction of loss on securities held-for-trading in the consolidated statements of operations. As of September 30, 2005, the $356,445 notional of swaps designated as trading derivatives had a weighted average remaining term of 7.24 years.

Additionally, the Company had a forward LIBOR cap with a notional amount of $85,000 and an estimated fair value at September 30, 2005 of $1,423 which is included in other assets, and the change in estimated fair value related to this derivative is included as a component of gain (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 gains or losses are recognized in the period incurred and are included in other gain (loss) in the consolidated statement of operations. Foreign currency forward commitments may be used to hedge the Company's net foreign investments. Gains and losses on foreign currency forward commitments are included in other gain (loss) in the consolidated statement of operations. The Company recorded net foreign currency transaction loss of $257 and $126 for the nine months ended September 30, 2005 and 2004, respectively. At September 30, 2005, the Company also had foreign currency forward commitments with an estimated fair value of $482 included in other liabilities on the consolidated statement of financial condition.

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 September 30, 2005 and December 31, 2004, the balance of such net margin deposits owed to counterparties as collateral under these agreements totaled $200 and $4,680, respectively.

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., a Maryland corporation, and subsidiaries (the "Company") is a real estate finance company that generates income based primarily 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 $427,800,000 of assets under management as of September 30, 2005. The Manager provides an operating platform that incorporates significant asset origination, risk management, and operational capabilities.

The Company's ongoing investment activities primarily 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.

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

	Carrying Value as of			
	September 30, 2005		December 31, 2004	
	Amount	%	Amount	%
Commercial real estate securities	$2,070,725	51.6%	$1,628,519	44.8
Commercial mortgage loan pools	1,297,029	32.3	1,312,045	36.1

Commercial real estate loans(1)	353,402	8.8	325,350	8.9
Residential mortgage-backed securities	291,454	7.3	372,071	10.2
Total	$4,012,610	100.0%	$3,637,985	100.0

(1) Includes the Company's investments in the Carbon Capital Funds at September 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 nine months ended September 30, 2005, the Company's commercial real estate securities portfolio increased by approximately 27% from an estimated fair value of $1,628,519 at December 31, 2004, compared with $2,070,725 at September 30, 2005.

As of September 30, 2005, $1,506,820 of the Company's $2,070,725 commercial real estate securities portfolios are financed using CDOs. 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 protect 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.

The Company retained 100% of the equity of CDOs I, II, III and HY2 and recorded the transactions on its consolidated financial statements as secured financing.

	Collateral as of September 30, 2005		Debt as of September 30, 2005		
	Adjusted Purchase Price	Loss Adjusted Yield	Adjusted Issue Price	Weighted Average Cost of Funds *	S
CDO I	$439,065	9.13%	$405,992	6.99%	2
CDO II	326,165	7.93%	292,900**	6.30%	1
CDO III	377,642	7.20%	368,347**	5.05%	2
CDO HY2	319,472	8.54%	239,612	5.38%	3
Total **	$1,462,344	8.24%	$1,306,851	6.00%	2

* 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, $13,069 of par of CDO III debt rated BB, $9,376 of CDO HY2 debt rated BBB-, $58,000 of CDO HY2 debt rated BB, and $57,500 of CDO HY2 debt rate B.

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 September 30, 2005:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Adjusted Dollar Pric
Investment grade CMBS	$145,139	$149,882	103.27	$156,905	108.11
Investment grade REIT debt	23,000	21,901	95.22	22,823	99.23
CMBS rated BB+ to B	43,530	39,858	91.56	40,649	93.38
CMBS rated B- or lower	48,789	13,635	27.95	13,108	26.87
CDO investments	197,536	18,972	9.60	17,247	8.73
CMBS Interest Only securities ("IOs")	3,565,559	108,774	3.05	109,465	3.07
Project loans	200,869	210,884	104.99	214,197	106.64
Total	$4,224,422	$563,906	13.35	$574,394	13.60

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	Adjusted Dollar Pri
Investment grade CMBS	$145,420	$146,467	100.72	$150,612	103.57
Investment grade REIT debt	43,885	43,291	98.65	44,274	100.89
CMBS rated BB+ to B	96,825	77,738	80.29	75,465	77.94
CMBS rated B- or lower	74,740	14,833	19.85	16,120	21.57
CDO investments	203,182	19,837	9.76	19,450	9.57
CMBS IOs	3,712,604	125,246	3.37	122,379	3.30
Project loans	23,082	23,649	102.46	24,092	104.38
Total	$4,299,738	$451,061	10.49	$452,392	10.52

Affect of Hurricanes on Below Investment Grade CMBS

During the third quarter of 2005, four properties which are security for mortgages in four separate CMBS transactions were severely damaged by Hurricane Katrina. The outstanding loan balances on these four properties is $24,089.

Based on the Company's on-site review of the damages incurred and information available to date, the Company believes that the properties have adequate insurance coverage and the cash flows related to the four CMBS transactions should not be adversely affected. As a result, the Company has not adjusted the carrying value or the loss adjusted yields for the four CMBS transactions that include the damaged properties. However, the determinations relating to the following factors are ongoing: how the insurance companies involved will address damage with respect to wind versus flooding; what the level of deductibles will be, which is dependent upon the category determinations; and the financial resources of the insurers. In addition, the Company expects that properties underlying its CMBS transactions were affected by Hurricane Wilma during the fourth quarter of 2005. However, due to limited access and availability of information at this time, the Company has not been able to determine what affect, if any, there will be on the cash flows related to its CMBS transactions. The Company will continue to monitor the situation and will make any necessary adjustments as additional information becomes available.

Real Estate Credit Profile of Below Investment Grade CMBS

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. As of September 30, 2005, the Company owns 20 different trusts where, through its investment in the lowest or non-rated subordinated CMBS of such trusts, the Company is in the first loss

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position. These securities absorb the first losses realized in the underlying loan pools. The coupon payment on these securities can also be reduced for special servicer fees charged to the trust as well as the effect of realized losses. As losses are realized, 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 nine months ended September 30, 2005, the Company acquired $265,583 of par of Controlling Class CMBS and $10,100 of par of other below investment grade CMBS. The total par of the Company's other below investment grade CMBS at September 30, 2005 was $257,284; the average credit protection, or subordination level, of this portfolio is 4.87%. The total par of the Company's subordinated Controlling Class CMBS securities at September 30, 2005 was $872,364 and the total par of the loans underlying these securities was $25,109,561. As of September 30, 2005, over 93% of the estimated fair value of the Company's subordinated CMBS assets are match funded in the Company's CDOs.

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

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Adjusted Dollar Price	Subordinatio Level

BB+	$157,336	$149,956	95.31	$136,022	86.45	5.94%
BB	113,924	99,932	87.72	94,245	82.73	4.19%
BB-	130,664	107,461	82.24	99,454	76.11	3.93%
B+	102,527	71,868	70.10	69,138	67.43	2.71%
B	160,505	102,393	63.79	96,840	60.33	2.73%
B-	42,059	24,713	58.76	24,917	59.24	1.28%
CCC	19,326	3,721	19.26	3,894	20.15	1.38%
NR	146,024	42,601	29.17	40,200	27.53	n/a
Total	$872,365	$602,645	69.08	$564,710	64.73	

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	Subordination 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 nine months ended September 30, 2005, servicers reduced the par amount of the Company's Controlling Class CMBS in the amount of $4,437. 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 nine months ended September 30, 2005, the loan pools were paid down by $562,888. 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 1.62% 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.

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 were performing below management's original expectations. The two underlying mortgage loans were resolved in the fourth quarter of 2005 with lower than expected loss severities. The effect of the improved loss severity will be recognized over the remaining life of the security in the form of an increased yield.

During the first quarter of 2005, changes in prepayment assumptions caused the expected yield on one investment grade CMBS to decline. 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 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.

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 September 30, 2005 are shown in the table below:

Vintage Year	Underlying Collateral	Delinquencies Outstanding	Lehman Brothers Conduit Guide
1998	$6,187,664	1.80%	1.37%
1999	659,863	2.45%	2.14%
2001	884,874	4.38%	1.98%
2002	1,166,080	0.31%	0.75%
2003	2,128,162	0.50%	0.37%
2004	6,663,107	0.11%	0.12%
2005	7,419,811	-%	-%
Total	$25,109,561	0.75%	0.56%*

* 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 September

30, 2005, the Morgan Stanley index indicated that delinquencies on 324 securitizations were 1.27%, 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 Risk" 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.

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 September 30, 2005. The underlying collateral related to the Company's investment in commercial mortgage loan pools is also included in the table. See Note 6 of the consolidated financial statements, Commercial Mortgage Loan Pools, for a further description of the Company's investment in commercial mortgage loan pools.

	September 30, 2005		
	Principal	Number of Loans	% of Collateral
Past due 30 days to 60 days	$37,672	9	0.15%
Past due 61 days to 90 days	47,191	9	0.19%
Past due 91 days or more	92,487	16	0.37%
Real estate owned ("REO")	6,757	3	0.03%
Foreclosure	3,630	1	0.01%
Total delinquent	$187,737	38	0.75%
Total principal balance	$25,109,561		

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.

Aggregate realized losses of $10,731 were realized during the nine months ended September 30, 2005. This brings cumulative realized losses to $85,707, which is 18.8% of the Company's 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 September 30, 2005 and December 31, 2004 are as follows:

	September 30, 2005 Exposure		December 31, 2004 Exposure	
Property Type	Loan Balance	% of Total	Loan Balance	% of Total
Retail	$7,909,426	31.5%	$6,026,472	32.4%
Multifamily	6,331,296	25.2	5,305,129	28.6
Office	7,442,318	29.6	4,617,616	24.9
Industrial	1,682,667	6.7	1,272,583	6.8
Lodging	1,262,323	5.1	915,369	4.9
Healthcare	319,855	1.3	327,832	1.8
Other	161,676	0.6	115,728	0.6
Total	$25,109,561	100%	$18,580,729	100%

As of September 30, 2005, the estimated fair value of the Company's holdings of subordinated Controlling Class CMBS is $37,935 higher than the adjusted cost for these securities which consists of a gross unrealized gain of $45,172 and a gross unrealized loss of $7,237. The adjusted purchase price of the Company's subordinated Controlling Class CMBS portfolio as of September 30, 2005 represents approximately 65% of its par amount. The estimated fair value of the Company's subordinated Controlling Class CMBS portfolio as of September 30, 2005 represents approximately 69% of its par amount. As the portfolio matures, the Company expects to recoup the $7,237 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 September 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 nine months ended September 30, 2005, there were credit upgrades on four 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 September 30, 2005, the Company's GAAP income accrued on its CMBS assets was approximately $36,721 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 September 30, 2005 and December 31, 2004:

	Carrying Value				Weighted Average Yield	
	September 30, 2005		December 31, 2004			
Property Type	Amount	%	Amount	%	2005	2004
Office	$78,606	26.7%	$88,311	33.5%	9.7%	9.2%
Residential	43,612	14.8	13,480	5.1	8.0	12.2
Storage	32,957	11.2	-	-	9.1	-
Retail	20,962	7.1	59,070	22.4	9.8	6.6
Communication Tower	20,000	6.8	-	-	8.9	-
Hotel	97,940	33.4	102,645	39.0	8.9	7.8
Total	$294,077	100.0%	$263,506	100.0%	9.0%	8.3%

During the nine months ended September 30, 2005, the Company purchased $116,401 of commercial real estate loans, including a 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 $49,823 as of September 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. During the nine months ended September 30, 2005, the Company experienced repayments of $82,971 related to its U.S. dollar denominated commercial real estate loan portfolio.

The carrying value and average yields on the Company's commercial real estate

loans as of September 30, 2005 were as follows:

	Carrying Value	Book Value	Book Value (Local Currency)	Average Yield	Averag Spread t 1-month U LIBOR
Fixed Rate	$120,902	$122,042		9.54%	
Floating Rate	123,961	124,098			5.29%
Floating Rate	19,082	19,600	(pound)11,082		
Floating Rate	30,132	30,223	(euro)25,041		
	$294,077	$295,963			

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, Accounting for Certain Investments in Debt and Equity Securities ("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.

Variable interest entities

The consolidated financial statements include the financial statements of the Company and its subsidiaries, which are wholly-owned or controlled by the Company or entities which are variable interest entities ("VIEs") in which the Company is the primary beneficiary under FASB Interpretation No. 46, Consolidation of Variable Interest Entities (revised December 2003) ("FIN 46R"). FIN 46R requires a VIE to be consolidated by its primary beneficiary. The primary beneficiary is the party that absorbs the majority of the VIE's anticipated losses and/or the majority of the expected returns. The Company has evaluated its investments for potential variable interests by evaluating the sufficiency of the entities equity investment at risk to absorb losses. All significant inter-company balances and transactions have been eliminated in consolidation.

The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the qualifying special-purpose entity ("QSPE") criteria. However, there is uncertainty with respect to QSPE treatment due to ongoing review by accounting standard setters, potential actions by various parties involved with the QSPE, as well as varying and evolving interpretations of the QSPE criteria under SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities ("SFAS 140"). Additionally, the standard setters continue to review the FIN 46R provisions related to the computations used to determine the primary beneficiary of a VIE. Future guidance from the standard setters may require the Company to consolidate CMBS trusts in which the Company has invested.

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 Carbon Capital Funds (as defined under Transactions with Affiliates, below).

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 available to common stockholders for the three and nine months ended September 30, 2005 was $15,069 or $0.28 per share (basic and diluted) and $39,137 or $0.73 per share (basic and diluted), respectively. Net income available to common stockholders for the three and nine months ended September 30, 2004 was $15,153 or $0.28 per share (basic and diluted) and $20,819 or $0.41 per share (basic and diluted), respectively. Net income available to common stockholders increased to $0.73 per share for the nine months ended September 30, 2005 as compared to $0.41 per share for the nine months ended September 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 September 30,		
	2005	2004	A
Commercial real estate securities	$37,009	$32,408	$4
Commercial mortgage loan pools	13,460	13,715	
Commercial real estate loans	5,362	2,979	2
Residential mortgage-backed securities ("RMBS")	2,268	3,941	(1
Cash and cash equivalents	969	165	
Total interest income	$59,068	$53,208	$5

	For the Nine Months Ended September 30,		
	2005	2004	Amo
Commercial real estate securities	$103,242	$92,073	$11
Commercial mortgage loan pools	40,617	26,066	14
Commercial real estate loans	15,643	6,437	9
RMBS	7,839	15,731	(7
Cash and cash equivalents	1,471	356	1
Total interest income	$168,812	$140,663	$28

The following table reconciles interest income and total income for the three and nine months ended September 30, 2005 and 2004.

	For the Three Months Ended September 30, 2005	2004
Interest Income	$59,068	$53,208
Earnings from real estate joint ventures	-	165
Earnings from the Carbon Capital Funds	2,870	1,979
Other Income	-	742
Total Income	$61,938	$56,094

	For the Nine Months Ended September 30, 2005	2004
Interest Income	$168,812	$140,663
Earnings from real estate joint ventures	59	929
Earnings from the Carbon Capital Funds	8,499	4,970
Other income	-	742
Total Income	$177,370	$147,304

For the three months ended September 30, 2005, interest income increased $5,860, or 11%, from the same three month period in 2004. The Company continued to increase its investments in commercial real estate assets, while RMBS investments declined as the Company completed the repositioning of its portfolio into commercial real estate assets. For the nine months ended September 30, 2005, interest income increased $28,149, or 20%, from the same nine month period in 2004. The consolidation of a VIE that included commercial mortgage loan pools contributed $14,551 to the increase. In addition, commercial real estate securities increased $11,169, or 12.4%, and commercial real estate loans increased $9,206, 143.0% from the same period of 2004 as the Company continued to increase its investments in commercial real estate assets.

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Interest Expense: The following table sets forth information regarding the total amount of interest expense from certain of the Company's borrowings and cash flow hedges.

	For the Three Months Ended September 30, 2005	2004	Variance Amount	
Collateralized debt obligations	$18,758	$16,162	$2,596	

Commercial real estate securities	5,371	1,945	3,426
Commercial mortgage loan pools*	12,760	12,706	54
Commercial real estate loans	1,273	424	849
RMBS	2,594	1,673	921
Junior subordinated notes - net	66	-	66
Cash flow hedges	1,588	3,825	(2,237)
Hedge ineffectiveness**	394	624	(230)
Total Interest Expense	$42,804	$37,359	$5,445

	For the Nine Months Ended September 30,		Variance
	2005	2004	Amount
Collateralized debt obligations	$50,523	$43,007	$7,516
Commercial real estate securities	11,334	5,086	6,248
Commercial mortgage loan pools*	38,285	24,678	13,607
Commercial real estate loans	3,771	718	3,153
RMBS	7,119	5,159	1,960
Junior subordinated notes - net	66	-	66
Cash flow hedges	5,514	11,604	(6,090)
Hedge ineffectiveness**	1,666	1,130	536
Total Interest Expense	$118,278	$91,382	$26,896

* Includes $62 and $79 of interest expense for the three and nine months ended September 30, 2005 respectively, and $60 and $84 for the three and nine months ended September 20, 2004, respectiv from short-term financings of securities related to the consolidation of commercial mortgage lo

**See Note 14 of the consolidated financial statements, Derivative Instruments and Hedging Activi for a further description of the Company's hedge ineffectiveness.

For the three months ended September 30, 2005, interest expense increased $5,445, or 14.6%, from the same three month period in 2004. Hedging expenses not related to the CDOs decreased $2,237, or 58.5%, from 2004 levels. This decrease is due to the removal of interest rate swaps upon issuance of fixed rate liabilities in connection with CDO HY1 and CDO HY2. The increase in expense related to CDOs of $2,596, or 16.1%, from the same three month period in 2004 is primarily attributable to the additional fixed rate liabilities issued in connection with CDO HY1 and CDO HY2. The financing of additional

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commercial real estate securities and commercial real estate loans increased interest expense $3,426 and $849, respectively, for the same three month period of 2004.

For the nine months ended September 30, 2005, interest expense increased $26,896 or 29.4%, from the same nine month period in 2004. The consolidation of a VIE that finances commercial mortgage loan pools contributed $13,607 to the increase. The VIE was consolidated for nine months of 2005 and for six months of 2004 as the entity was acquired in April 2004. Hedging expense not related to CDOs decreased $6,090, or 52.5%, from 2004 levels. The decrease is due to the removal of interest rate swaps upon the issuance of fixed rate liabilities in connection with CDOs HY1 and CDO HY2. The increase in interest expense related to CDOs of $7,516, or 17.5%, from the same nine month period in 2004, is primarily attributable to the issuance of CDO HY1 and CDO HY2. The financing of additional commercial real estate securities and commercial real estate

loans increased interest expense by $6,248 and $3,165, respectively, from the same nine month period of 2004.

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 hedge ineffectiveness, and the gross-up effect of the consolidation of a VIE that includes commercial mortgage loan pools. The Company believes interest income and expense excluding the effects of these items better reflects the Company's net interest margin and net interest spread from the portfolio.

	For the Three Months Ended September 30,	
	2005	2004
Interest income	$46,370	$41,539
Interest expense	$29,712	$24,202
Net interest margin	2.82%	3.08%
Net interest spread	2.24%	2.32%

Other Expenses: Expenses other than interest expense consist primarily of management fees and general and administrative expenses. Management fees paid to the Manager of $2,799 and $8,039 for the three and nine months ended September 30, 2005, respectively, were solely base management

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fees. Management fees paid to the Manager of $2,212 and $6,505 for the three and nine months ended September 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 $933 and $2,691 for the three and nine months ended September 30, 2005, respectively, and $886 and $2,120 for the three and nine months ended September 30, 2004, respectively, were comprised of administration fees, accounting agent fees, custodial agent fees, directors' fees, fees for professional services, and insurance premiums. General and administrative expenses for the nine months ended September 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): Gains on securities available-for-sale were $31 and $2,081 for the three months ended September 30, 2005 and 2004, respectively,

and $88 and $857 for the nine months ended September 30, 2005 and 2004, respectively. Gains (losses) on securities held-for-trading were $897 and $(1,103) for the three months ended September 30, 2005 and 2004, respectively, and $(1,781) and $(11,133) for the nine months ended September 30, 2005 and 2004, respectively. Foreign currency gains (losses) were $87 and $(114) for the three months ended September 30, 2005 and 2004, respectively, and $(257) and $(126) for the nine months ended September 30, 2005 and 2004, respectively. The losses on impairment of assets of $0 and $3,231 for the three and nine months ended September 30, 2005, respectively, were related to the Company's write down of certain CMBS as required by EITF 99-20.

Dividends Declared: On September 14, 2005, the Company declared distributions to its stockholders of $0.28 per share, payable on October 31, 2005 to stockholders of record on September 30, 2005.

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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 September 30, 2005 and December 31, 2004:

Security Description	September 30, 2005 Estimated Fair Value	Percentage	December 31, 2004 Estimated Fair Value
Commercial mortgage-backed securities:			
CMBS IOs	$108,774	4.6%	$125,246
Investment grade CMBS	525,699	23.1	389,813
Non-investment grade rated subordinated securities	759,357	34.4	753,388
Non-rated subordinated securities	28,595	1.8	5,994
Credit tenant leases	24,967	1.1	25,251
Investment grade REIT debt	306,265	12.9	285,341
Project loans	210,883	11.7	23,650
CDO investments	18,972	0.8	19,837
Total CMBS	1,983,512	90.4	1,628,520
Single-family RMBS:			
Agency adjustable rate securities	92,266	5.5	112,139
Residential CMOs	839	-	1,408
Hybrid adjustable rate mortgages	16,649	4.1	25,606
Total RMBS	109,754	9.6	139,153
Total securities available-for-sale	$2,093,266	100.0%	$1,767,673

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Borrowings: As of September 30, 2005 and December 31, 2004, the Company's debt consisted of line-of-credit borrowings, CDO debt, junior subordinated notes, 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 September 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.

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

	For the Nine Months Ended September 30, 2005		
	September 30, 2005 Balance	Maximum Balance	Range of Maturitie
CDO debt*	$1,306,851	$1,306,963	6.5 to 9.8 yea
Commercial mortgage loan pools	1,278,192	1,294,051	3.3 to 13.2 ye
Reverse repurchase agreements	679,425	888,712	17 to 23 day
Line of credit and term loan borrowings	195,067	350,554	25 days to 2.22
Junior subordinated notes	77,380	77,380	30 years**

* Disclosed as adjusted issue price. Total par of the Company's CDO debt as of September 30, 200 $1,320,090.
** The junior subordinated notes can be redeemed at par beginning in October 2010.

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 hedging instruments as of September 30, 2005 and December 31, 2004 consisted of the following:

	As of September 30, 2005			
	Notional Value	Estimated Fair Value	Unamortized Cost	Average Term (
Cash flow hedges	$337,850	$4,066	$-	
Trading swaps	133,000	2,782	-	
CDO cash flow hedges	865,018	6,698	-	
CDO timing swaps	223,445	(33)	-	
CDO LIBOR cap	85,000	1,423	1,407	

	As of December 31, 2004			
	Notional Value	Estimated Fair Value	Unamortized Cost	Average Term (
Cash flow hedges	$452,600	$253	$-	
Trading swaps	16,000	(5)	-	
CDO cash flow hedges	718,120	(11,262)	-	
CDO timing swaps	223,445	145	-	
CDO LIBOR cap	85,000	694	1,407	

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.

On September 26, 2005, the Company issued $75,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust I, a Delaware statutory trust (the "Trust"). The trust preferred securities have a thirty-year term ending October 30, 2035 with interest at a fixed rate of 7.497% for the first ten years and at a floating rate of three-month LIBOR plus 2.9% thereafter. The trust preferred securities can be redeemed at par beginning in October 2010.

For the nine months ended September 30, 2005, the Company issued 497,188 shares of its Common Stock, par value $0.001 per share (the "Common Stock"), under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately $5,743.

On August 18, 2005, the Company completed a secondary stock offering of 1,725,000 shares at a price of $11.59, which included a 15% over-allotment option exercised by the underwriter. Net proceeds were $19,199.

On July 26, 2005, the Company closed CDO HY2 and issued non-recourse liabilities with a face amount of $365,010. Senior investment grade notes with a face amount of $240,134 were issued and sold in a private placement. The Company retained the floating rate BBB- note, the below investment grade notes and the preferred shares. The CDO HY2 transaction provides match-funding for a portfolio of commercial mortgage-backed securities and unsecured real estate investment trust debt with a total par of $478,050. CDO HY2 included a $100,000 ramp facility that was fully funded on October 13, 2005. Since July 26, 2005, the $100,000 ramp facility has been invested at short-term money market rates.

For the nine months ended September 30, 2004, the Company issued 1,077,102 shares of its Common Stock under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately $12,606.

For the three and nine months ended September 30, 2004, the Company issued 253,800 shares of Common Stock under a sale agency agreement with Brinson Patrick Securities Corporation. Net proceeds

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to the Company were approximately $2,761.

On June 30, 2004, the Company completed a follow-on offering of 2,415,000 shares of its Common Stock, at a price of $11.50, which included a 15% over-allotment option exercised by the underwriter. Net proceeds to the Company were approximately $26,662.

During the first quarter of 2004, the Company suspended its Dividend Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan") for all investment dates after March 26, 2004. 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.

As of September 30, 2005, $50,266 of the Company's $200,000 committed credit facility with Deutsche Bank, AG was available for future borrowings and $57,467 of the Company's $75,000 committed credit facility with Greenwich Capital, Inc. was available. The Company had outstanding borrowings of $27,800 under a 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 September 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	$12,900	$679,425	$-	$-
31 to 59 days	-	-	-	-
60 days to less than 1 year	76,579	-	-	-
1 year to 3 years	105,588	-	-	-
3 years to 5 years	-	-	-	-
Over 5 years	-	-	1,278,192	1,306,851
	$195,067	$679,425	$1,278,192	$1,306,851

* As of September 30, 2005, collateralized debt obligations are comprised of $405,992 of CDO debt with a weighted average remaining maturity of 6.54 years, $292,900 of CDO debt with a weighted average remaining maturity of 6.94 years, $368,347 of CDO debt with a weighted average remaining maturity of 7.64 years, and $239,612 of CDO debt with a weighted average remaining maturity of 8.61 years.

The Company has no off-balance sheet financing arrangements.

Cash provided by operating activities is net income adjusted for certain non-cash items and changes in

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assets and liabilities including the Company's trading securities. Operating activities provided cash flows of $5,250 and $91,143 during the nine months ended September 30, 2005 and 2004, respectively. The decline of $85,893, or 94%, is primarily attributable to the sale of $46,319 of securities held-for-trading during 2004 and purchases of $37,777 of securities held-for-trading in 2005.

The Company's investing cash flow consists primarily of the purchase, sale, and repayments on securities activities available for sale, commercial loan pools, commercial mortgage loans and equity investments. The Company's investing activities used cash flows of $315,967 and $101,652 during the nine months ended September 30, 2005 and 2004, respectively. In 2004, investing cash flow used was partially offset by sales of securities available for sale in 2004.

Financing cash flows consist primarily of borrowings, CDO and junior subordinated note issuances, common and preferred stock offerings offset by dividends on common and preferred stock and repayments of borrowings. The Company's financing activities provided cash flows $349,992 and $4,967 during the nine months ended September 30, 2005 and 2004, respectively. The increase in financing cash flows in 2005 was primarily attributable to CDO HY2 which provided for proceeds of $239,660, the common stock offering which provided net proceeds of $19,199 and issuance of junior subordinated notes to the subsidiary Trust for proceeds of $77,380. In 2004, the Company redeemed its Series B Preferred Stock which used $43,931 of financing cash flows. This was partially offset by a common stock offering which provided for net proceeds of $26,662.

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. As of September 30, 2005, the Company was in compliance with all 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 September 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

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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 $2,799 and $8,039 in base management fees in accordance with the terms of the Management Agreement for the three and nine months ended September 30, 2005, respectively, and $2,212 and $6,505 for the three and nine months ended September 30, 2004. The Company did not incur incentive fees for the three and nine months ended September 30, 2005 and 2004. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of $40 and $120 for certain expenses incurred on behalf of the Company for the three and nine months ended September 30, 2005, respectively, and $15 and $45 for the three and nine months ended September 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 $125,000 of average net assets, 0.04% of the next $125,000 of average net assets and 0.03% of average net assets in excess of $250,000 subject to a minimum annual fee of $120. For the three and nine months ended September 30, 2005, the Company paid administration fees of $53 and $156, respectively, and $ 43 and $129, for the three and nine months ended September 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 September 30, 2005 was $19,096. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon I. On September 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 shares of Carbon Capital II, Inc., a private commercial real estate income opportunity fund managed by the Manager ("Carbon II" and collectively with Carbon I, the "Carbon Capital

Funds"), of which $38,258 has already been funded and $61,742 is the remaining commitment. As of September 30, 2005, the carrying value of the Company's investment in Carbon II was $40,229. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon II. On September 30, 2005, the Company owned approximately 20% of the outstanding shares 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 September 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 rising interest rates. 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

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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 under 30-day repurchase agreements and committed borrowing facilities are mark-to-market risk and short-term rate risk. 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 1.66 years based on net asset value as of September 30, 2005. This means that a 100 basis point increase in interest rates would cause a margin call of approximately $9,000.

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 reported book value. The Company focuses on economic risk in managing its sensitivity to interest rates and maintains an economic duration within a band of 3.0 to 5.0 years. At September 30, 2005, economic duration for the Company's entire portfolio was 3.28 years. This implies that for each 100 basis points of change in interest rates the Company's economic value will change by approximately 3.28%. At September 30, 2005 the Company estimates its economic value, or net asset value of its common stock to be $478,776.

A reconciliation of the economic duration of the Company to the duration of the reported book value of the Company's common stock is as follows:

Duration - GAAP book value at September 30, 2005	9.71
Less:	
Duration contribution of CDO I liabilities	(1.62)
Duration contribution of CDO II liabilities	(1.42)
Duration contribution of CDO III liabilities	(1.32)
Duration contribution of CDO HY2 liabilities	(1.34)
Duration contribution of Series C Preferred Stock	(0.22)
Duration contribution of Junior subordinated notes	(0.51)
Economic duration at September 30, 2005	3.28

The reported book value of the Company's common stock is $9.31 per share. As indicated in the table above a 100 basis point change in interest rates will change reported book value by approximately 9.2%. Also, as indicated above, approximately $9,000 of that change would be required to meet margin calls in the event rates rise by 100 basis points.

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 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 September 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	$0.03
-100	$0.02
-50	$0.01
Base Case	
+50	$(0.01)
+100	$(0.02)
+200	$(0.03)

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

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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 cash flows.

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.

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 reportable income going forward by approximately $0.27 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 $0.01 to $0.21 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 September 30, 2005, securities with a total estimated fair value of $1,559,909 are collateralizing the CDO borrowings of $1,367,856; therefore, the Company's preferred equity interest in the three CDOs is $192,053 ($3.46 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 by issuing CDOs. 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 September 30, 2005.

No change in internal control over financial reporting occurred during the quarter ended September 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 September 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. Unregistered Sales of Equity Securities and Use of Proceeds

	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
July 1, 2005 through July 31, 2005	-	-	-	
August 1 2005 through August 31, 2005	-	-	-	
September 1 2005 through September 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

Exhibit No.	Description
10.1	Junior Subordinated Indenture, dated as of September 26, 2005, between Anthracite Capital, Inc. and Wells Fargo Bank,

	National Association, as trustee
10.2	Amended and Restated Trust Agreement, dated as of September 26, 2005, among Anthracite Capital, Inc., as depositor, Wells Fargo Bank, National Association, as

	property trustee, Wells Fargo Delaware Trust Company, as Delaware trustee, and the Administrative Trustees Named Therein
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: November 9, 2005

By: /s/ Christopher A. Milner

Name: Christopher A. Milner
Title: Chief Executive Officer
(duly authorized representative)

Dated: November 9, 2005

By: /s/ James J. Lillis

Name: James J. Lillis
Title: Chief Financial Officer