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ANTHRACITE CAPITAL INC  
Form 10-Q  
May 10, 2004

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 March 31, 2004

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) 409-3333  
-----

NOT APPLICABLE  
-----

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

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

(1) Yes X No

- -

(2) Yes X No

- -

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

(1) Yes X No

- -

As of May 7, 2004, 50,572,055 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

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"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 Anthracite 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 press release, 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;
- (4) the impact of increased competition;
- (5) the impact of capital improvement projects;
- (6) the impact of future acquisitions or 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, BlackRock Financial Management, Inc. (the "Manager") or The PNC Financial Services Group, Inc. ("PNC Bank");
- (11) terrorist activities, which may adversely affect the general economy, real estate, financial and capital markets, specific industries, and the Company and the Manager;
- (12) the ability of the Manager to attract and retain highly talented professionals; (13) fluctuations in foreign currency exchange rates; and (14) the impact of changes to tax legislation and, generally, the tax position of the Company.

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

Part I - FINANCIAL INFORMATION  
Item 1. Interim Financial Statements

Anthracite Capital, Inc. and Subsidiaries

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Consolidated Statements of Financial Condition  
(in thousands, except per share data)

	March 31, 2004
	----- (Unaudited)
<b>ASSETS</b>	
Cash and cash equivalents	\$ 17,264
Restricted cash equivalents	15,389
Securities available-for-sale, at fair value:	
Subordinated commercial mortgage-backed securities ("CMBS")	\$ 751,872
Residential mortgage backed securities ("RMBS")	367,029
Investment grade securities	720,764
	-----
Total securities available-for-sale	1,839,665
Securities held-for-trading, at fair value	341,075
Commercial mortgage loan pools	1,222,103
Commercial mortgage loans, net	81,292
Equity investment in Carbon Capital, Inc.	33,159
Investments in real estate joint ventures	7,813
Receivable for investments sold	100,662
Other assets	48,666
	-----
Total Assets	\$3,707,088
	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>	
<b>Liabilities:</b>	
<b>Borrowings:</b>	
Collateralized debt obligations ("CDOs")	\$1,057,522
Secured by pledge of subordinated CMBS	17,653
Secured by pledge of other securities available-for-sale and restricted cash equivalents	449,940
Secured by pledge of securities held-for-trading	315,399
Secured by pledge of investments in real estate joint ventures	-
Secured by pledge of commercial mortgage loans	7,430
	-----
Total borrowings	\$1,847,944
Obligation of REMIC Trust	1,199,034
Securities sold, not yet settled	101,234
Payable for investments purchased	49,301
Distributions payable	15,059
Other liabilities	48,451
	-----
Total Liabilities	\$3,261,023
	-----
<b>Commitments and Contingencies</b>	
<b>Stockholders' Equity:</b>	
Common Stock, par value \$0.001 per share; 400,000 shares authorized;	
50,572 shares issued and outstanding in 2004;	
49,464 shares issued and outstanding in 2003	51
10% Series B Preferred Stock, liquidation preference \$43,931 in 2004 and \$43,942 in 2003	33,422
9.375% Series C Preferred Stock, liquidation preference \$57,500 in 2004 and 2003	55,435
Additional paid-in capital	549,199
Distributions in excess of earnings	(105,952)

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Accumulated other comprehensive loss	(86,090)
	-----
Total Stockholders' Equity	446,065
	-----
Total Liabilities and Stockholders' Equity	\$3,707,088
	=====

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

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

	For the Three Months Ended March 31, 2004	For th Months March 3
	-----	-----
<b>Income:</b>		
Interest from securities available-for-sale	\$32,726	
Interest from commercial mortgage loans	1,479	
Interest from securities held-for-trading	3,177	
Earnings from real estate joint ventures	222	
Earnings from equity investment	1,372	
Interest from cash and cash equivalents	88	
	-----	
Total income	39,064	
	-----	
<b>Expenses:</b>		
Interest	20,091	
Interest - securities held-for-trading	782	
Management fee	2,130	
General and administrative expense	602	
	-----	
Total expenses	23,605	
	-----	
<b>Other gain (losses):</b>		
Gain on sale of securities available-for-sale	2,813	
Loss on securities held-for-trading	(5,983)	
	-----	
Total other loss	(3,170)	
	-----	
Net income	12,289	
	-----	
Dividends on preferred stock	2,446	
	-----	
Net income available to common stockholders	\$ 9,843	
	=====	

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Net income per common share, basic:	\$ 0.20
=====	
Net income per common share, diluted:	\$ 0.20
=====	
Weighted average number of shares outstanding:	
Basic	49,837
Diluted	49,846

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 Three Months Ended March 31, 2004  
(in thousands)

	Common Stock, Par Value	Series B Preferred Stock	Series C Preferred Stock	Additional Paid-In Capital	Distributions In Excess Of Earnings	Accum Ot Compre L
Balance at January 1, 2004	\$49	\$33,431	\$55,435	\$536,333	\$(101,635)	\$(1
Net income					12,289	
Unrealized loss on cash flow hedges						(
Reclassification adjustments from cash flow hedges included in net income						
Change in net unrealized gain (loss) on securities available-for-sale, net of reclassification adjustment						
Other Comprehensive income						
Comprehensive Income						
Dividends declared-common stock					(14,160)	
Dividends on preferred stock					(2,446)	
Conversion of Series B preferred stock to common stock	-	(9)		9		
Issuance of common stock	2			12,857		
-----						

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Balance at March 31, 2004	\$51	\$33,422	\$55,435	\$549,199	\$(105,952)	\$ (
=====						
Disclosure of reclassification adjustment:						
Unrealized holding loss						
Reclassification for realized gains previously recorded as unrealized						

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

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

	For the Three Months Ended March 31, 20
	-----
Cash flows from operating activities:	
Net income	\$12,289
Adjustments to reconcile net income to net cash (used in) provided by operating activities:	
Net (purchase) sale of trading securities	(33,332)
Net loss on sale of securities	3,170
Discount accretion	(961)
Equity in earnings in excess of distributions from Carbon Capital, Inc.	(317)
Decrease in other assets	2,502
Increase in other liabilities	4,876
Net cash (used in) provided by operating activities	----- (11,773) -----
Cash flows from investing activities:	
Purchase of securities available-for-sale	(117,479)
Funding of commercial mortgage loans	(19,961)

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Repayments received from commercial mortgage loans	120
(Increase) decrease in restricted cash equivalents	(2,544)
Principal payments received on securities available-for-sale	22,419
Distributions from joint ventures in excess of earnings	10
Investment in Carbon Capital, Inc.	(4,349)
Proceeds from sales of securities available-for-sale	111,790
Net payments under hedging securities	(2,740)
Net cash used in investing activities	(12,734)
Cash flows from financing activities:	
Net increase (decrease) in borrowings	24,403
Proceeds from issuance of common stock, net of offering costs	12,860
Dividends paid on common stock	(13,851)
Dividends paid on preferred stock	(2,446)
Net cash provided by (used in) financing activities	20,966
Net decrease in cash and cash equivalents	(3,541)
Cash and cash equivalents, beginning of period	20,805
Cash and cash equivalents, end of period	\$17,264
Supplemental disclosure of cash flow information:	
Interest paid	\$20,661
Investments purchased not settled	\$49,301
Investments sold not settled	\$ (572)

Supplemental schedule of non-cash investing and financing activities: The Company purchased the Controlling Class securities of a REMIC trust during the Three months ended March 31, 2004:

Carrying value of assets acquired	\$ 1,222,103
Liabilities assumed	1,199,034

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



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

### Note 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Anthracite Capital, Inc. (the "Company"), a Maryland corporation, is a real estate finance company that generates income based on the spread between the interest income on its mortgage loans and securities investments 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 core investment activities focus on (i) investing in below investment grade CMBS where the Company has the right to control the foreclosure/workout process on the underlying loans, and (ii) originating high yield commercial real estate loans. The Company also manages excess liquidity with a portfolio of investment grade real estate related securities. This portfolio is being reduced over time.

The accompanying March 31, 2004 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. 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 2003 filed with the Securities and Exchange Commission.

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.

### Note 2 NET INCOME PER SHARE

Net income per share is computed in accordance with Statements of Financial Accounting Standards ("SFAS") No. 128, "Earnings Per Share." Basic income per share is calculated by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted income per share is calculated using the weighted average number of common shares outstanding during the period plus the additional dilutive effect, if any, of common stock equivalents. The dilutive effect of outstanding stock options is calculated using the treasury stock method, and the dilutive effect of preferred stock is calculated using the "if converted" method.

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For the  
Months E  
March 31,

Numerator:

Net income available to common stockholders	\$
	-----
Numerator for basic earnings per share	\$
	-----
Numerator for diluted earnings per share	\$
	=====

Denominator:

Denominator for basic earnings per share--weighted average common shares Outstanding	
Dilutive effect of stock options	
	-----
Denominator for diluted earnings per share--weighted average common shares outstanding and common share equivalents outstanding	
	=====

Basic net income per weighted average common share: \$

Diluted net income per weighted average common share and common share  
equivalents: -----

Total anti-dilutive stock options and warrants excluded from the calculation of net income per share were 1,385,651 and 1,407,442 for the three months ended March 31, 2004 and 2003, respectively.

Note 3            SECURITIES AVAILABLE-FOR-SALE

The Company's securities available-for-sale are carried at estimated fair value. The amortized cost and estimated fair value of securities available-for-sale as of March 31, 2004 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain
-----		
CMBS:		
CMBS interest only securities ("IOs")	\$ 87,858	\$ 3,956
Investment grade CMBS	330,823	13,818
Non-investment grade rated subordinated securities	765,914	32,866
Non-rated subordinated securities	27,250	5,002

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Credit tenant lease	25,803	569
Investment grade REIT debt	238,436	22,635
	-----	-----
Total CMBS	1,476,084	78,846
	-----	-----
Single-family residential mortgage-backed securities (RMBS):		
Agency adjustable rate securities	150,760	618
Agency fixed rate securities	187,492	129
Residential CMOs	2,855	89
Hybrid adjustable rate mortgages ("ARMs")	6,050	-
Project Loans	20,468	833
	-----	-----
Total RMBS	367,625	1,669
	-----	-----
Total securities available-for-sale	\$ 1,843,709	\$ 80,515
	=====	=====

As of March 31, 2004, an aggregate of \$1,742,364 in estimated fair value of the Company's securities available-for-sale was pledged to secure its collateralized borrowings.

As of March 31, 2004, the anticipated weighted average yield to maturity based upon the amortized cost of the subordinated CMBS ("reported yield") was 9.6% per annum. The anticipated reported yield of the Company's investment grade securities available-for-sale was 5.3%. The Company's reported yields on its subordinated CMBS and investment grade 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), the pass-through or coupon rate, and interest rate fluctuations. Additional factors that may affect the Company's anticipated yields to maturity on its subordinated CMBS 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 subordinated 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.

The following table shows the Company's 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 March 31, 2004.

	Less than 12 Months		12 Months or More	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	-----	-----	-----	-----
Non-investment grade rated subordinated securities	\$280,591	\$ (16,715)	\$442,442	\$ (26,166)

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Agency fixed rate securities	\$185,460	\$ (2,032)	-	-
Hybrid ARMS	\$5,999	\$ (51)	-	-
-----				
Total temporarily impaired securities	\$472,050	\$ (18,798)	\$442,442	\$ (26,166)
=====				

The temporary impairment of the available-for-sale securities results from the 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 fair value of the securities held. As such, management does not believe any of the securities held are other-than-temporarily impaired at March 31, 2004.

The following table sets forth certain information relating to the aggregate principal balance and payment status of delinquent mortgage loans underlying the subordinated CMBS held by the Company as of March 31, 2004:

	March 31, 2004	
	Principal	Number of Loans
-----		
Past due 30 days to 60 days	\$6,057	3
Past due 60 days to 90 days	9,909	4
Past due 90 days or more	113,909	12
Real estate owned ("REO")	6,237	2
Total delinquent	\$136,112	21
Total principal balance	\$12,556,284	2,251
-----		

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 fair value. While realized losses on individual loans may be higher or lower than original estimates, the Company currently believes its aggregate loss estimates and reported yields are appropriate on all investments.

Note 4 COMMERCIAL MORTGAGE LOAN POOLS

As of March 31, 2004, the Company owns eleven different trusts where the Company through its investment in subordinated CMBS of such trusts is in the first loss

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position ("Controlling Class"). In March 2004, the Company committed to acquire \$41,495 par value of the Controlling Class interests in a CMBS transaction. The securities that comprise the Controlling Class interests were acquired for a dollar price of 55.6% of par, or \$23,069. The total par amount of underlying loans in this transaction is \$1,234,613 which have a carrying value of \$1,222,103. A CMBS real estate mortgage investment conduit ("REMIC") trust will typically issue securities with a par amount equal to the par value of the underlying loans. As noted, the Company acquired \$41,495 of par value of these securities; other third party investors will acquire the remaining \$1,193,118 of securities. During the negotiations for the purchase of these Controlling Class interests, the Company was able to obtain a greater degree of control for the special servicer in the process of disposing of or working out defaulted loans. As a result of this added discretion, FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46R") requires the Company to consolidate the net assets and results of operations of the issuing REMIC trust.

Typically, the Company records securities purchased at their market price, and the securities appear as assets on the Company's consolidated statement of financial condition. For this CMBS transaction, the Company included on its consolidated statement of financial condition all of the underlying loans shown as commercial mortgage loan pools at cost. The CMBS securities to be issued to third parties by the REMIC trust are shown as an offsetting liability ("obligation of REMIC trust"). The net effect on the Company's consolidated statement of financial condition at March 31, 2004 from the consolidation of the net assets of the REMIC trust is equivalent to the cost of the Controlling Class interests acquired of \$23,069.

The liability resulting from this transaction is non-recourse to Anthracite, and is secured only by the commercial mortgage loan pools. This accounting treatment increases the Company's debt to capital ratio from 4.6:1 to 6.8:1. The Company received authorization from its lenders to permit debt to capital ratios in excess of existing covenants. For income recognition purposes, the loans will carry their own yields and the Company will establish a loss reserve consistent with the credit assumptions made in establishing loss adjusted yields for Controlling Class securities.

### Note 5                    SECURITIES HELD-FOR-TRADING

Securities held-for-trading reflect short-term trading strategies, which the Company employs from time to time, designed to generate economic and taxable gains based on short-term differences in pricing. As part of its trading strategies, the Company may acquire long or short positions in U.S. Treasury or agency securities, forward commitments to purchase such securities, financial futures contracts and other fixed income or fixed income derivative securities.

The Company's securities held-for-trading are carried at estimated fair value. At March 31, 2004, the Company's securities held-for-trading consisted of FNMA Mortgage Pools with an estimated fair value of \$341,075, and a forward commitment with an estimated fair value of \$101,234. 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.

For the three months ended March 31, 2004, losses on securities held-for-trading in the consolidated statement of operations of \$5,983 are largely attributable to the Company's continued repositioning and reduction of the RMBS portfolio and associated hedges. The Company's longstanding policy has been to maintain limits on the exposure of the Company's equity to changes in long-term rates as well as the exposure of earnings to changes in short-term funding rates.

The Company's trading strategies are subject to the risk of unanticipated

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changes in the relative prices of long and short positions in trading securities, but are designed to be relatively unaffected by changes in the overall level of interest rates.

### Note 6 COMMON STOCK

On March 11, 2004, the Company declared dividends to its common stockholders of \$0.28 per share, payable on April 30, 2004 to stockholders of record on March 31, 2004. For U.S. Federal income tax purposes, the dividends are expected to be ordinary income to the Company's stockholders.

For the three months ended March 31, 2004, the Company issued 1,077,102 shares of Common Stock under its Dividend Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan"). Net proceeds to the Company were approximately \$12,606. For the three months ended March 31, 2003, the Company issued 333,328 shares of Common Stock under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately \$3,517. The Company suspended its Dividend Reinvestment Plan for all investments after March 26, 2004, and for all future investment dates. The Dividend Reinvestment Plan will remain in place and may be resumed by the Company at any time.

### Note 7 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"). During the second quarter of 2004 the Company will incur a one-time charge to income available to common stockholders of \$10,508, which represents the difference between the Series B Preferred Stock book value of \$19 per share and its \$25 redemption price. The Series B Preferred Stock was redeemed on May 6, 2004.

### Note 8 TRANSACTIONS WITH AFFILIATES

The Company has a Management Agreement with the Manager, a majority owned indirect subsidiary of PNC Bank 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. The Board of Directors of the Company was advised by Houlihan Lokey Howard & Zukin Financial Advisors, Inc., a national investment banking and financial advisory firm, in the 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 are similar to the prior agreement except for the incentive fee calculation which 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, is greater than what was paid to the Manager in the prior three quarters cumulatively. The Company will phase in the rolling four-quarter high watermark commencing with the second quarter of 2003.

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Calculation of the incentive fee will be based on GAAP 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 provides 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 (\$11.36 as of March 31, 2004) 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 and the greater of 8.5% or 400 basis points over the ten-year Treasury note.

During the year ended December 31, 2003 and 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 quarter of 2003 and the first quarter of 2004. This revision resulted in \$1,046 in savings to the Company during 2003 and \$532 for the three months ended March 31, 2004, respectively.

The Company incurred \$2,130 and \$2,577 in base management fees in accordance with the terms of the Management Agreement for the three months ended March 31, 2004 and 2003, respectively. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of \$34 and \$6 for certain expenses incurred on behalf of the Company for the three months ended March 31, 2004 and 2003, respectively, which are included in general and administration expense on the accompanying consolidated statements of operations.

Pursuant to the March 25, 2002 one-year Management Agreement extension, the incentive fee was based on 25% of earnings (calculated in accordance with GAAP) of the Company. For purposes of calculating the incentive fee during 2002, the cumulative transition adjustment of \$6,327 resulting from the Company's adoption of SFAS 142 was excluded from earnings in its entirety and included in the calculation of future incentive fees using an amortization period of three years. The Company did not incur incentive fees for the three months ended March 31, 2004 and 2003.

The Company has an administration agreement with the Manager. Under the terms of the administration agreement, the Manager provides financial reporting, audit coordination and accounting oversight services to the Company. The agreement can be cancelled upon 60-day written notice by either party. The Company pays the Manager a monthly administrative fee at an annual rate of 0.06% of the first \$125 million of average net assets, 0.04% of the next \$125 million of average net assets and 0.03% of average net assets in excess of \$250 million subject to a minimum annual fee of \$120. For the three months ended March 31, 2004 and 2003, the Company paid administration fees of \$44 and \$43, respectively, which are included in general and administration expense on the accompanying consolidated statements of operations.

The Company has entered into a \$50 million commitment to acquire shares in Carbon Capital, Inc. ("Carbon"), a private commercial real estate income opportunity fund managed by the Manager. The period during which the Company may

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be required to purchase shares under the commitment, expires in July 2004. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon. On March 31, 2004, the Company owned 19.8% of the outstanding shares in Carbon. The Company's remaining commitment at March 31, 2004 and December 31, 2003 was \$18,685 and \$23,034, respectively.

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 March 31, 2004, the Installment Payment would be \$8,000 payable over seven years. The Company does not accrue for this contingent liability.

### Note 9           BORROWINGS

Certain information with respect to the Company's collateralized borrowings at March 31, 2004 is summarized as follows:

	Lines of Credit and Term Loans	Reverse Repurchase Agreements	Collateralized Debt Obligations
Outstanding borrowings	\$25,083	\$765,339	\$1,057,522
Weighted average borrowing rate	2.93%	1.10%	6.05%
Weighted average remaining maturity	469 days	23 days	3,082 days
Estimated fair value of assets pledged	\$79,155	\$824,112	\$1,119,225

As of March 31, 2004, the Company's collateralized borrowings had the following remaining maturities:

	Lines of Credit and Term	Reverse Repurchase	Collateralized Debt
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	Loans	Agreements	Obligations
Within 30 days	\$ -	\$765,339	\$ -
31 to 59 days	-	-	-
Over 60 days	25,083	-	1,057,522
	=====	=====	=====
	\$25,083	\$765,339	\$1,057,522
	=====	=====	=====

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

Note 10 DERIVATIVE INSTRUMENTS

The Company accounts for its derivative investments under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. If the derivative is designated as a fair value hedge, the changes in the 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 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 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 as trading derivatives intended to offset changes in 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.

As of March 31, 2004, the Company had interest rate swaps with notional amounts aggregating \$1,040,295 that were designated as cash flow hedges of borrowings under reverse repurchase agreements. Cash flow hedges with a fair value of \$741 are included in other assets on the consolidated statement of financial condition and cash flow hedges with a fair value of \$(39,569) are included in other liabilities on the consolidated statement of financial condition. For the three months ended March 31, 2004, the net change in the fair value of the interest rate swaps was a decrease of \$26,184, of which \$973 was deemed ineffective and is included as an increase of interest expense and \$25,211 was recorded as a reduction of OCI. As of March 31, 2004, the \$1,040,295 notional of swaps that were designated as cash flow hedges had a weighted average remaining term of 8.2 years.

As of March 31, 2004, the Company had interest rate swaps with notional amounts aggregating \$479,445 designated as trading derivatives. Trading derivatives with a fair value of \$104 are included in other assets on the consolidated statement of financial condition and trading derivatives with a fair value of \$(1,148) are included in other liabilities on the consolidated statement of financial condition. For the three months ended March 31, 2004, the change in fair value for these trading derivatives was a decrease of \$4,092 and is included as an

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addition to loss on securities held-for-trading in the consolidated statements of operations. As of March 31, 2004, the \$479,445 notional of swaps that were designated as trading derivatives had a weighted average remaining term of 5.5 years.

Occasionally, counterparties will require the Company or the Company will require counterparties to provide collateral for the interest rate swap agreements in the form of margin deposits. Net deposits are recorded as a component of either accounts receivable or other liabilities. Should the counterparty fail to return deposits paid, the Company would be at risk for the fair market value of that asset. At March 31, 2004 and December 31, 2003, the balance of such net margin deposits owed to counterparties as collateral under these agreements totaled \$5,720 and \$10,445, respectively.

The contracts identified in the remaining portion of this note have been entered into to limit the Company's mark to market exposure to long-term interest rates.

Additionally, the Company had a forward London Interbank Offered Rate ("LIBOR") cap with a notional amount of \$85,000 and a fair value at March 31, 2004 of \$963 which is included in other assets, and the change in fair value related to this derivative is included as a component of loss on securities held-for-trading in the consolidated statements of operations.

### 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. (the "Company"), a Maryland corporation, is a real estate finance company that generates income based on the spread between the interest income on its mortgage loans and securities investments 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 \$321,000,000 of assets under management as of March 31, 2004. The Manager provides an operating platform that incorporates significant asset origination, risk management, and operational capabilities.

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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, \$0.01 par value per share ("Series B Preferred Stock"). During the second quarter of 2004 the Company will incur a one time charge to income available to common stockholders of \$10,508, which represents the difference between the Series B Preferred Stock book value of \$19 per share and its \$25 redemption price. The Series B Preferred Stock was redeemed on May 6, 2004.

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 following table illustrates the mix of the Company's asset types as of March 31, 2004 and December 31, 2003:

	Carrying Value as of			
	March 31, 2004 Amount	%	December 31, 2003 Amount	%
Commercial real estate securities	\$1,472,636	43.0%	\$1,366,508	64.
Commercial mortgage loan pools	1,222,103	35.7	-	
Commercial real estate loans(1)	122,263	3.6	97,984	4.
Residential mortgage backed securities(2)	606,871	17.7	653,668	30.
<b>Total</b>	<b>\$3,423,873</b>	<b>100.0%</b>	<b>\$2,118,160</b>	<b>10</b>

(1) Includes real estate joint ventures and equity investments.

(2) Net of RMBS securities sold, not yet settled

### Commercial Mortgage Loans Pools and Commercial Real Estate Securities Portfolio Activity

As of March 31, 2004, the Company owns eleven different trusts where the Company through its investment in subordinated CMBS of such trusts is in the first loss position ("Controlling Class"). In March 2004, the Company committed to acquire \$41,495 par value of the Controlling Class interests in a CMBS transaction. The securities that comprise the Controlling Class interests were acquired for a dollar price of 55.6% of par, or \$23,069. The total par amount of underlying loans in this transaction is \$1,234,613 which have a carrying value of \$1,222,103. A CMBS real estate mortgage investment conduit ("REMIC") trust will typically issue securities with a par amount equal to the par value of the underlying loans. As noted, the Company acquired \$41,495 of par value of these securities; other third party investors will acquire the remaining \$1,193,118 of securities. During the negotiations for the purchase of these Controlling Class interests, the Company was able to obtain a greater degree of control for the special servicer in the process of disposing of or working out defaulted loans. As a result of this added discretion, FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46R") requires the Company to consolidate the net assets and results of operations of the issuing REMIC trust.

Typically, the Company records securities purchased at their market price, and

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the securities appear as assets on the Company's consolidated statement of financial condition. For this CMBS transaction, the Company included on its consolidated statement of financial condition all of the underlying loans shown as commercial mortgage loan pools. The CMBS securities to be issued to third parties by the REMIC trust are shown as an offsetting liability ("obligation of REMIC trust"). The net effect on the Company's consolidated statement of financial condition at March 31, 2004 from the consolidation of the net assets of the REMIC trust is equivalent to the cost of the Controlling Class interests acquired of \$23,069.

The liability resulting from this transaction is non-recourse to Anthracite, and is secured only by the commercial mortgage loan pools. This accounting treatment increases the Company's debt to capital ratio from 4.6:1 to 7.6:1. The Company received authorization from its lenders to permit debt to capital ratios in excess of existing covenants. For income recognition purposes, the loans will carry their own yields and the Company will establish a loss reserve consistent with the credit assumptions made in establishing loss adjusted yields for Controlling Class securities.

The Company continues to increase its investments in commercial real estate securities. Commercial real estate securities include CMBS and investment grade REIT debt. During the three months ended March 31, 2004, the Company increased its commercial real estate securities portfolio by 7.8% from \$1,366,508 to \$1,472,636. This increase was primarily attributable to the purchase of CMBS and investment grade REIT debt which have market values as of March 31, 2004 of \$85,303 and December 31, 2003 of \$34,668.

On March 30, 2004 the Company issued its third collateralized debt obligation ("CDO III") offering through Anthracite CDO 2004-1. The total par value of bonds sold was \$372,456. The total cost of funds on a fully hedged basis was 5.0%. CDO III also includes a \$50,000 ramp facility that will be used to finance future commercial real estate assets, thus eliminating financing risk for up to \$50,000 of below investment grade CMBS investments to be acquired during the year.

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. The CDO debt is non-recourse to the Company; therefore, the Company's losses are limited to its equity investment in the CDO. The CDO debt is also fully hedged to protect the Company from an increase in short-term interest rates. The Company considers all of its CMBS rated BB+ down to B to be financeable in a CDO transaction; and as of March 31, 2004, over 95% of the market value of these assets are match funded in the Company's CDOs in this manner.

	Collateral as of March 31, 2004		Debt as of March 31, 2004	
	Adjusted Purchase Price	Loss Adjusted Yield	Adjusted Issue Price	Weighted Average Cost of Funds *
CDO I	\$442,740	8.89%	\$404,813	7.21%
CDO II	326,428	7.81%	280,256**	5.73%
CDO III	396,986	6.64%	372,453***	5.03%
Total **	\$1,166,154	7.82%	\$1,057,522	6.05%

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

\*\* The Company chose not to sell \$22,850 of par of CDO II debt rated

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BBB- and BB.

\*\*\*The Company chose not to sell \$13,069 of par of CDO III debt rated BB.

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

	Par	Fair Market Value	Dollar Price	Adjusted Purchase Price	Dolla
Investment grade CMBS	\$89,859	\$86,033	95.74	\$87,438	97
Investment grade REIT debt	11,000	11,202	101.84	11,223	102
CMBS rated BB+ to B	38,300	20,437	53.36	30,600	79
CMBS rated B- or lower	312,675	85,136	27.23	113,306	36
CMBS IOs	2,754,839	91,297	3.31	87,858	3
<b>Total</b>	<b>\$3,206,673</b>	<b>\$294,105</b>	<b>9.17</b>	<b>\$330,425</b>	<b>10</b>

The following table details the par, fair market value, adjusted purchase price and loss adjusted yield of the Company's commercial real estate securities outside of the CDOs as of December 31, 2003:

	Par	Fair Market Value	Dollar Price	Adjusted Purchase Price	Dolla
Investment grade CMBS	\$277,276	\$268,593	96.87	\$272,853	98
Investment grade REIT debt	29,000	29,567	101.95	30,210	104
CMBS rated BB+ to B	186,217	133,868	71.89	150,775	80
CMBS rated B- or lower	304,358	80,680	26.51	107,653	35
CMBS IOs	2,623,456	84,493	3.22	83,704	3
Other CMBS	20,266	20,142	99.39	20,264	99
<b>Total</b>	<b>\$3,440,573</b>	<b>\$617,343</b>	<b>17.94</b>	<b>\$665,459</b>	<b>19</b>

### Below Investment Grade CMBS and Underlying Loan Performance

The Company divides its below investment grade CMBS investment activity into two portfolios; Controlling Class CMBS and other below investment grade CMBS. The distinction between the two is in the controlling class rights the Company obtains with its investment in Controlling Class CMBS. Controlling Class rights allow the Company to control the workout and/or disposition of defaults that occur in the underlying loans. These securities absorb the first losses realized in the underlying loan pools. The 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

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first to absorb losses in the underlying pools. The coupon payment on the non-rated security can also be reduced for special servicer fees charged to the trust. The next highest rated security in the structure will then generally be downgraded to non-rated and becomes the first to absorb losses and expenses from that point on.

For the three months ended March 31, 2004, the Company acquired \$11,686 of par of other below investment grade CMBS and \$67,011 of par of new Controlling Class securities. The total par of the Company's other below investment grade CMBS at March 31, 2004 was \$315,859; the average credit protection, or subordination level, of this portfolio is 5.9%. The total par of the Company's Controlling Class CMBS securities at March 31, 2004 was \$833,209 and the total par of the loans underlying these securities was \$12,556,284.

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

	Par	Fair Market Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Subordination Level
BB+	\$86,139	\$78,134	90.71	\$73,806	85.68	7.15%
BB	93,330	83,316	89.27	79,796	85.50	5.92%
BB-	105,624	77,387	73.27	84,254	79.77	4.88%
B+	51,780	33,771	65.22	35,473	68.51	3.26%
B	185,106	108,936	58.85	135,177	73.03	2.87%
B-	86,284	34,722	40.24	53,159	61.61	1.98%
CCC+	11,924	5,780	48.47	7,166	60.09	1.56%
CCC	70,272	12,945	18.42	22,999	32.73	1.10%
C	8,940	2,797	31.28	2,692	30.11	0.63%
NR	132,210	24,614	18.62	23,316	17.64	n/a
<b>Total</b>	<b>\$831,609</b>	<b>\$462,402</b>	<b>55.60</b>	<b>\$517,838</b>	<b>62.27</b>	

The Company's investment in its Controlling Class CMBS securities by credit rating category at December 31, 2003 is as follows:

	Par	Fair Market Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Subordination Level
BB+	\$84,503	\$73,766	87.29	\$72,680	86.01	7.54%
BB	89,945	75,349	83.77	76,842	85.43	6.04%
BB-	101,393	71,285	70.31	81,036	79.92	5.12%
B+	44,314	28,904	65.22	31,179	70.36	3.43%
B	182,119	105,061	57.69	133,718	73.42	3.06%
B-	83,296	34,160	41.01	51,935	62.35	1.54%
CCC+	11,924	5,595	46.92	7,129	59.78	1.53%
CCC	70,273	13,375	19.03	22,844	32.51	1.23%
C	8,940	2,531	28.31	2,734	30.58	0.62%
NR	129,925	25,003	19.24	23,011	17.71	n/a
<b>Total</b>	<b>\$806,632</b>	<b>\$435,029</b>	<b>53.93</b>	<b>\$503,108</b>	<b>62.37</b>	

For the three months ended March 31, 2004, the par amount of the Company's Controlling Class CMBS securities was reduced by the servicers in the amount of

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\$15,526. Further delinquencies and losses may cause 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 consolidated statement of operations according to EITF 99-20. Also for the three months ended March 31, 2004, the underlying loan pools were paid down by \$68,009. 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 2.08% 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 5.2% over the life of the portfolio and an average assumed loss severity of 40.0% of the defaulted loan balance. All estimated workout expenses including special servicer fees are included in these assumptions. Actual results could differ materially from these estimated results. See Item 3 - "Quantitative and Qualitative Disclosures About Market Risk" for a discussion of how differences between estimated and actual losses could affect Company earnings.

The Company monitors credit performance on a monthly basis and debt service coverage ratios on a quarterly basis. Using these and other statistics, the Company maintains watch lists for loans that are delinquent thirty days or more and for loans that are not delinquent but have issues that the Company's management believes require close monitoring. As part of its ongoing credit monitoring the Company periodically performs a re-underwriting of a substantial number of the underlying loans supporting its Controlling Class CMBS. We are currently focusing on 1998 vintage transactions and expect to be completed with this vintage by the fourth quarter of 2004. As each transaction review is completed the Company may determine that its GAAP yields and book values need to be adjusted.

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, 2003 and 2004. Comparable delinquency statistics referenced by vintage year as a percentage of current par as of March 31, 2004 are shown in the table below:

Vintage Year	Underlying Collateral	Delinquencies Outstanding	Lehman Brothers Conduit Guide
1998	\$7,414,007	1.82%	2.45%
1999	711,544	0.17%	2.53%
2001	909,560	0.00%	1.13%
2003	2,193,990	0.00%	0.03%
2004	1,327,183	0.00%	0.00%
Total	\$12,556,284	1.08%*	1.68%*

\* 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 criterion will generally adjust for the

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lower delinquencies that occur in newly originated collateral. As of March 31, 2004, the Morgan Stanley index indicated that delinquencies on 253 securitizations were 2.36%, and as of December 31, 2003, this same index indicated that delinquencies on 243 securitizations were 2.47%. See Item 3 - "Quantitative and Qualitative Disclosures About Market Risks" for a detailed discussion of how delinquencies and loan losses affect the Company.

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

Of the 21 delinquent loans shown on the chart in Note 2 of the consolidated financial statements, 2 loans were real estate owned and being marketed for sale, 3 loans were in foreclosure, and the remaining 16 loans were in some form of workout negotiations. Aggregate losses of \$88 were realized during quarter ended March 31, 2004, bringing cumulative net losses realized to \$41,520 or 14.2% of total estimated losses. These losses include special servicer and other workout expenses. 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 ages.

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 March 31, 2004 and December 31, 2003 are as follows:

Property Type	3/31/04 Exposure		12/31/03 Exposure	
	Loan Balance	% of Total	Loan Balance	% of Total
Multifamily	\$4,119,354	32.8%	\$3,770,944	33.2%
Retail	3,820,594	30.4	3,446,371	30.4
Office	2,678,582	21.3	2,266,160	20.0
Lodging	786,895	6.3	786,920	7.0
Industrial	790,073	6.3	713,942	6.3
Healthcare	335,282	2.7	337,333	3.0
Parking	25,504	0.2	25,611	0.2
<b>Total</b>	<b>\$12,556,284</b>	<b>100%</b>	<b>\$11,347,281</b>	<b>100%</b>

As of March 31, 2004, the fair market value of the Company's holdings of Controlling Class CMBS securities is \$55,147 lower than the adjusted cost for these securities. The adjusted purchase price and market value of the Company's Controlling Class CMBS portfolio as of March 31, 2004 represents approximately 63% and 56%, respectively, of its par amount. As the portfolio matures, the Company expects to recoup the unrealized loss, provided that the credit losses experienced are not greater than the credit losses assumed in the purchase analysis. As of March 31, 2004, 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



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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 market value and therefore the Company's net asset value. Reduced market value will 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 market value of the securities. For the three months ended March 31, 2004, the Company experienced no ratings changes on its CMBS.

The Company's generally accepted accounting principles in the United States of America ("GAAP") income for its CMBS securities 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 will be credit losses, as a loss can only be deducted for tax purposes when it has occurred. As a result, for the period beginning with the year ended December 31, 1998 through the three months ended March 31, 2004, the Company's GAAP income accrued on its CMBS assets was approximately \$28,459 lower than the taxable income accrued on its 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 Company has never suffered a loss in this portfolio. Because the loan portfolio is relatively small and heterogeneous, the Company has determined it is not necessary to establish a loan loss reserve.

The following table summarizes the Company's commercial real estate loan portfolio by property type as of March 31, 2004 and December 31, 2003:

Property Type	Loan Outstanding				Weighted Average Coupon	
	March 31, 2004		December 31, 2003		March 31, 2004	December 31, 2003
	Amount	%	Amount	%		
Office	\$77,287	81.5%	\$57,381	76.4%	10.1%	
Residential	2,722	2.9	2,794	3.7	3.9%	
Retail	-	-	-	-	-%	
Hotel	14,842	15.6	14,951	19.9	6.6%	
Total	\$94,851	100.0%	\$75,126	100.0%	9.3%	

### Recent Events

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. During the second quarter of 2004 the Company will incur a one time charge to income available to common stockholders of \$10,508, which represents the difference between the Series B Preferred Stock book value of \$19 per share and its \$25 redemption price. The Series B Preferred Stock was redeemed on May 6, 2004.

## II. Results of Operations

Net income for the three months ended March 31, 2004 was \$9,843 or \$0.20

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per share (basic and diluted). Net income for the three months ended March 31, 2003 was \$8,502 or \$0.18 per share (basic and diluted). Net income increased to \$0.20 per share for the three months ended March 31, 2004 as compared to \$0.18 per share for the three months ended March 31, 2003.

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

	For the Three Months Ended March 31, 2004	For the Three Months Ended March 31, 2003
	Interest Income	Interest Income
Commercial real estate securities	\$29,185	\$19,953
Commercial real estate loans	1,479	1,430
RMBS	6,717	20,285
Cash and cash equivalents	88	176
<b>Total</b>	<b>\$37,469</b>	<b>\$41,844</b>

The following chart reconciles interest income and total income for the three months ended March 31, 2004 and 2003.

	For the Three Months Ended March 31, 2004	For the Three Months Ended March 31, 2003
Interest Income	\$37,469	\$41,844
Earnings from real estate joint ventures	223	236
Earnings from equity investment	1,372	743
<b>Total Income</b>	<b>\$39,064</b>	<b>\$42,823</b>

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

	For the Three Months Ended March 2004	For the Three Months Ended March 2003
	Interest Expense	Interest Expense

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Reverse repurchase agreements	\$3,147	\$5
Lines of credit and term loan	955	
CDO liabilities	11,167	6
	=====	=====
Total	\$15,269	\$12
	=====	=====

The foregoing interest expense amounts for the three months ended March 31, 2004 do not include a \$973 addition to interest expense related to hedge ineffectiveness, as well as a \$4,631 addition to interest expense related to swaps. The foregoing interest expense amounts for the three months ended March 31, 2003 do not include a \$262 addition to interest expense related to hedge ineffectiveness, as well as a \$7,050 addition to interest expense related to swaps. See Note 10 of the consolidated financial statements, Derivative Instruments, for a further description of the Company's hedge ineffectiveness.

Net Interest Margin and Net Interest Spread from the Portfolio: The Company considers its portfolio to consist of its securities available-for-sale, mortgage loan pools, 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 from the portfolio divided by the average market value of interest-earning assets in the portfolio. Net interest income from the portfolio is total interest income from the portfolio less interest expense relating to collateralized borrowings. Net interest spread from the portfolio 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 from the portfolio divided by average amortized cost of interest earning assets in the portfolio. The average cost of funds is interest expense from the portfolio divided by average outstanding collateralized borrowings.

The following chart describes the interest income, interest expense, net interest margin and net interest spread for the Company's portfolio. The following interest income and interest expense amounts exclude income and expense related to real estate joint ventures, equity investment and hedge ineffectiveness. The decrease in net interest margin is primarily a result of lower leverage and the net interest spread decreased due to investment in more higher credit quality CMBS.

	For the Three Months Ended March 31	
	2004	2003
	-----	
Interest income	\$37,470	\$41,898
Interest expense	\$19,898	\$19,898
Net interest margin	3.17%	3.17%
Net interest spread	2.48%	2.48%

Other Expenses: Expenses other than interest expense consist primarily of management fees and general and administrative expenses. Management fees paid to

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the Manager of \$2,130 and \$2,577 for the three months ended March 31, 2004 and 2003, respectively, were solely base management fees and were lower as the Manager agreed to reduce the management fees by 20% for the quarter ended March 31, 2004. General and administrative expense of \$602 and \$582 for the three months ended March 31, 2004, and 2003, respectively, were comprised of accounting agent fees, custodial agent fees, directors' fees, fees for professional services, and insurance premiums.

Other Gains (Losses): During the three months ended March 31, 2004, the Company sold a portion of its securities available-for-sale for total proceeds of \$111,790, resulting in a realized gain of \$2,813. No available-for-sale securities were sold during the three months ended March 31, 2003, although the Company did record a gain of \$142 due to prepayment fees received in connection with the early maturity of a security. The losses on securities held-for-trading were \$5,983 and \$10,389 for the three months ended March 31, 2004 and 2003, respectively.

Dividends Declared: On March 11, 2004, the Company declared distributions to its stockholders of \$0.28 per share, which was paid on April 30, 2004 to stockholders of record on March 31, 2004.

### 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 March 31, 2004 and December 31, 2003:

Security Description	March 31, 2004 Estimated Fair Value	Percentage	December 2003 Estim Fair Value
Commercial mortgage-backed securities:			
CMBS IOs	\$ 91,297	5.0%	\$8
Investment grade CMBS	342,024	18.5	33
Non-investment grade rated subordinated securities	723,033	39.3	67
Non-rated subordinated securities	28,840	1.6	2
Credit tenant lease	26,372	1.4	2
Investment grade REIT debt	261,070	14.2	21
Total CMBS	1,472,636	80.0	\$1,36
Single-family residential mortgage-backed securities:			
Agency adjustable rate securities	151,378	8.2	18
Agency fixed rate securities	185,460	10.1	22
Residential CMOs	2,910	0.2	
Hybrid arms	5,999	0.3	
Project Loans	21,282	1.2	2
Total RMBS	367,029	20.0	43
Total securities available-for-sale	\$1,839,665	100.0%	\$1,80

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The Company's CMBS and investment grade REIT debt increased slightly from December 31, 2003 as the Company is continuing to purchase these types of assets.

**Borrowings:** As of March 31, 2004 and December 31, 2003, the Company's debt consisted of collateralized debt obligations, line-of-credit borrowings, 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 March 31, 2004 and December 31, 2003, 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 market value. A reduction in the value of its pledged assets would require the Company to provide additional collateral or fund margin calls. From time to time, the Company expects that it will be required to provide such additional collateral or fund margin calls.

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

	For the Three Months Ended March 31, 2004	
	March 31, 2004 Balance	Maximum Balance
Collateralized debt obligations	\$1,057,522	\$1,057,522
Reverse repurchase agreements	765,399	1,148,306
Line of credit and term loan borrowings	25,083	391,511

**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 value of certain assets in the Company's portfolio. At March 31, 2004, the Company had no outstanding U.S. Treasury Note future contracts. At December 31, 2003, the Company had outstanding short positions of 30 five-year and 73 ten-year U.S. Treasury Note future contracts.

Interest rate swap agreements as of March 31, 2004 and December 31, 2003 consisted of the following:

March 31, 2004

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	Notional Value	Estimated Fair Value	Unamortized Cost	Weighted Average Remaining Term
Interest rate swaps	\$565,000	\$(6,095)	\$ -	4.
Interest rate swaps - CDO	954,740	(33,777)	-	9.
<b>Total</b>	<b>\$1,519,740</b>	<b>\$(39,872)</b>	<b>\$ -</b>	<b>7.</b>

December 31, 2003				
	Notional Value	Estimated Fair Value	Unamortized Cost	Weighted Average Remaining Term
Interest rate swaps	\$919,300	\$(2,929)	\$23	5.
Interest rate swaps - CDO	626,323	(23,423)	-	9.
<b>Total</b>	<b>\$1,545,623</b>	<b>\$(26,352)</b>	<b>\$23</b>	<b>6.</b>

As of March 31, 2004, the Company had designated \$1,040,295 notional of the interest rate swap agreements as cash flow hedges. As of December 31, 2003, the Company had designated \$1,066,078 notional of the interest rate swap agreements as cash flow hedges.

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.

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. During the second quarter of 2004 the Company will incur a one-time charge to income available to common stockholders of \$10,508, which represents the difference between the

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Series B Preferred Stock book value of \$19 per share and its \$25 redemption price. The Series B Preferred Stock was redeemed on May 6, 2004.

For the three months ended March 31, 2004, the Company issued 1,077,102 shares of Common Stock under its Dividend Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan"). Net proceeds to the Company were approximately \$12,606. The Company suspended its Dividend Reinvestment Plan for all investments after March 26, 2004, and for all future investment dates. The Dividend Reinvestment Plan will remain in place and may be resumed by the Company at any time.

As of March 31, 2004, \$167,347 of the Company's \$185,000 committed credit facility with Deutsche Bank, AG was available for future borrowings and \$67,570 of the Company's \$75,000 committed credit facility with Greenwich Capital, Inc. was available.

At March 31, 2004, the Company's collateralized borrowings had the following remaining maturities:

	Lines of Credit	Reverse Repurchase Agreements	Collateralized Debt Obligations	Colla Bor
	-----	-----	-----	-----
Within 30 days	\$ -	\$765,339	\$ -	
31 to 59 days	-	-	-	
60 days to less than 1 year	-	-	-	
1 year to 2 years	25,083	-	-	
Over 5 years	-	-	1,057,522*	
	-----	-----	-----	
	\$25,083	\$765,339	\$1,057,522	
	=====	=====	=====	=====

\* Comprised of \$404,813 of CDO debt with a weighted average remaining maturity of 8.04 years as of March 31, 2004, \$280,256 of CDO debt with a weighted average remaining maturity of 8.09 years as of March 31, 2004 and \$372,453 of CDO debt with a weighted average remaining maturity of 9.14 years as of March 31, 2004.

The Company has no off-balance sheet financing arrangements.

On March 30, 2004 the Company issued CDO III through Anthracite CDO 2004-1. The total par value of bonds sold was \$372,456. The total cost of funds on a fully hedged basis was 5.0%. CDO III also includes a \$50,000 ramp facility that will be used to finance future commercial real estate assets, thus eliminating financing risk for up to \$50,000 of below investment grade CMBS investments to be acquired during the year.

The Company's operating activities (used) provided cash flows of \$(11,773) and \$402,887 during the three months ended March 31, 2004 and 2003, respectively, primarily through purchase of trading securities offset by net income in 2004 and through the purchases of trading securities in 2003.

The Company's investing activities used cash flows of \$12,734 and \$383,540 during the three months ended March 31, 2004 and 2003, respectively, primarily to purchase securities available-for-sale and to fund commercial mortgage loans, offset by significant sales of securities.

The Company's financing activities provided (used) \$20,966 and \$(22,835) during the three months ended March 31, 2004 and 2003, respectively, primarily from

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increase in borrowings, issuance of common stock on dividends paid in 2004 and decrease in borrowings and dividends paid in 2003.

The Company is subject to various covenants in its lines of credit, including maintaining a minimum GAAP net worth of \$305,000, a debt-to-equity ratio not to exceed 5.5 to 1, a minimum cash requirement based upon certain debt to equity ratios, a minimum debt service coverage ratio of 1.5, and a minimum liquidity reserve of \$10,000. Due to the acquisition of the commercial mortgage loan pools (see Note 4 of the consolidated financial statements), the Company's debt to capital ratio increased from 4.4:1 at December 31, 2003 to 6.8:1 at March 31, 2004. The Company received authorization from its lenders to permit debt to capital ratios in excess of existing covenants. As of March 31, 2004, the Company was in compliance with all covenants.

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 March 31, 2004, the Installment Payment would be \$8,000 payable over seven 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. The Board of Directors of the Company was advised by Houlihan Lokey Howard & Zukin Financial Advisors, Inc., a national investment



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banking and financial advisory firm, in the 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 are similar to the prior agreement except for the incentive fee calculation which 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, is greater than what was paid to the Manager in the prior three quarters cumulatively. The Company will phase in the rolling four-quarter high watermark commencing with the second quarter of 2003. Calculation of the incentive fee will be based on GAAP 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 provides 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 (\$11.36 as of March 31, 2004) 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 and the greater of 8.5% or 400 basis points over the ten-year Treasury note.

During the years ended December 31, 2002 and 2003 and 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 quarter of 2003 and the first quarter of 2004. This revision resulted in \$1,046 in savings to the Company during 2003 and \$532 for the three months ended March 31, 2004, respectively.

The Company incurred \$2,130 and \$2,577 in base management fees in accordance with the terms of the Management Agreement for the three months ended March 31, 2004 and 2003, respectively. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of \$34 and \$6 for certain expenses incurred on behalf of the Company for the three months ended March 31, 2004 and 2003, respectively, which are included in general and administration expense on the accompanying consolidated statements of operations.

Pursuant to the March 25, 2002 one-year Management Agreement extension, the incentive fee was based on 25% of earnings (calculated in accordance with GAAP) of the Company. For purposes of calculating the incentive fee during 2002, the cumulative transition adjustment of \$6,327 resulting from the Company's adoption of SFAS 142 was excluded from earnings in its entirety and included in the calculation of future incentive fees using an amortization period of three years. The Company did not incur incentive compensation fees for the three months ended March 31, 2004 and 2003.

The Company has an administration agreement with the Manager. Under the terms of the administration agreement, the Manager provides financial reporting, audit

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coordination and accounting oversight services to the Company. The agreement can be cancelled upon 60-day written notice by either party. The Company pays the Manager a monthly administrative fee at an annual rate of 0.06% of the first \$125 million of average net assets, 0.04% of the next \$125 million of average net assets and 0.03% of average net assets in excess of \$250 million subject to a minimum annual fee of \$120. For the three months ended March 31, 2004 and 2003, the Company paid administration fees of \$44 and \$43, respectively, which are included in general and administration expense on the accompanying consolidated statements of operations.

The Company has entered into a \$50 million commitment to acquire shares in Carbon Capital, Inc. ("Carbon"), a private commercial real estate income opportunity fund managed by the Manager. The period during which the Company may be required to purchase shares under the commitment, expires in July 2004. The Company does not incur any additional management or incentive fees to the Manager as a result of its investment in Carbon. On March 31, 2004, the Company owned 19.8% of the outstanding shares in Carbon. The Company's remaining commitment at March 31, 2004 and December 31, 2003 was \$18,685 and \$23,034, respectively.

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 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 market 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 market 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 market value of the Company's portfolio may increase. Changes in the market 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 London Interbank Offered Rate ("LIBOR") money market rates can affect the

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Company's net interest income. As of March 31, 2004, all of the Company's liabilities outside of the CDOs are floating rate based on a market spread to LIBOR. As the level of LIBOR increases or decreases, the Company's interest expense will move in the same direction.

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

The Company monitors and manages interest rate risk based on a method that takes into consideration the interest rate sensitivity of the Company's assets and liabilities, including its preferred stock. The Company's objective is to acquire assets and match fund the purchase so that interest rate risk associated with financing these assets is reduced or eliminated. The primary risks associated with acquiring and financing these assets are mark to market risk and short-term rate risk. Examples of these financing types include 30-day repurchase agreements and committed borrowing facilities. Certain secured financing arrangements provide for an advance rate based upon a percentage of the market 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 0.79 years based on reported GAAP book value as of March 31, 2004.

The Company's reported book value incorporates the market value of the Company's interest bearing assets but it does not incorporate the market value of the Company's interest bearing liabilities. The fixed rate interest bearing liabilities of preferred stock will generally reduce the actual interest rate risk of the Company from a pure economic perspective even though changes in the value of these liabilities are not reflected in the Company's book value. The fixed rate liabilities issued in CDO I, CDO II and CDO III reduce the Company's economic duration by approximately 6.67 years. The Series C Preferred Stock reduces the Company's economic duration by approximately 0.87 year. The Company's reported book value is not reduced by these liabilities and therefore is approximately 7.63 years longer than the economic duration. The Company's duration management strategy focuses on the economic risk and maintains economic duration within a band of 3.0 to 5.0 years. At March 31, 2004, economic duration was 3.15 years. Earnings per share is analyzed using the assumptions that interest rates, as defined by the LIBOR curve, increase or decrease and that the yield curves of the LIBOR rate shocks will be parallel to each other. Market 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.

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Regarding the table below, all changes in income and value 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 March 31, 2004. Actual results could differ significantly from these estimates.

Projected Percentage Change In Earnings Per Share Given LIBOR Movements	
Change in LIBOR, +/- Basis Points	Projected Change in Earnings per Share
-100	\$(0.019)
-50	\$(0.010)
Base Case	
+50	\$0.010
+100	\$0.019
+200	\$0.038

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

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

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. 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

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originally assumed, there is less opportunity to receive interest coupon; which results in a lower or possibly negative return. Additional losses which occur due to greater severity will not have a significant effect as all principal is already assumed to be non-recoverable.

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

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

For purposes of illustration, a doubling of the losses in the Company's Controlling Class CMBS, without a significant acceleration of those losses, would reduce GAAP income going forward by approximately \$0.30 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 \$1.00 to \$1.30 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 increase in these estimates from December 31, 2003 is a result of the Company's purchase of the below investment grade portion of two additional Controlling Class CMBS trusts. 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 March 31, 2004, securities with a total market value of \$1,166,411 are collateralizing the CDO borrowings of \$1,057,522; therefore, the Company's residual interest in the three CDOs is \$108,889 (\$2.15 per share). In accordance with GAAP, The CDO borrowings are not marked to market even though their economic value will change in response to changes in interest rates and/or credit spreads.

Interest rate swap agreements contain an element of risk in the event that the counterparties to the agreements do not perform their obligations under the agreements. The Company minimizes its risk exposure by entering into agreements with parties rated at least A or better by Standard & Poor's Rating Services. Furthermore, the Company has interest rate swap agreements established with several different counterparties in order to reduce the risk of credit exposure to any one counterparty. Management does not expect any counterparty to default on their obligations.

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

Other methods for evaluating interest rate risk, such as interest rate sensitivity "gap" (defined as the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a given time period),

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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

(a) Evaluation of Disclosure Controls and Procedures. The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on such evaluation, Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in alerting them on a timely basis to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's reports filed or submitted under the Exchange Act.

(b) Changes in Internal Controls. There has been no change in the Company's internal control over financial reporting during the quarter ended March 31, 2004 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 March 31, 2004 there were no pending legal proceedings of which the Company was a defendant or of which any of its property was subject.

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

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Ma th Und
January 1, 2004 through January 31, 2004	-	-	-	
February 1, 2004 through February 29, 2004	-	-	-	
March 1, 2004 through March 31, 2004	1,757,257 (1)	25.00	1,757,257	

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Total	1,757,257	25.00	1,757,257
	=====		

(1) 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. During the second quarter, the Company will incur a one-time charge to income available to common stockholders of \$10,508, which represents the difference between the Series B Preferred Stock book value of \$19 per share and its \$25 redemption price. The Series B Preferred Stock was redeemed on May 6, 2004.

Item 3. Defaults Upon Senior Securities

Not applicable.

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

None.

Item 5. Other Information

On April 6, 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"), which redemption closed on May 6, 2004. The Company initially considered the decision to redeem as a recharacterization of the Series B Preferred Stock from conditionally redeemable to mandatorily redeemable, and recorded the cost to retire the Series B Preferred Stock in excess of its carrying value of \$10,508,000, in the Consolidated Statements of Operations for the three months ended March 31, 2004, as included in the Company's Form 8-K dated May 7, 2004.

At the time of the Company's May 7, 2004 8-K, the Company considered after consultation with its independent auditors Deloitte & Touche LLP ("D&T") the conversion option included in the Series B Preferred Stock to be nonsubstantive, as the redemption price of the Series B Preferred Stock of \$25 per share was substantially higher than the approximately \$16.24 per share shareholders would receive if the Series B Preferred Stock were converted into Common Stock of the Company on the date of redemption. Subsequent to May 7, 2004, the Company in consultation with D&T determined that the conversion option should be evaluated only at the original issuance of the Series B Preferred Stock, at which time the conversion feature was substantive. Therefore, the cost to retire the Series B Preferred Stock will be recorded in the second quarter of 2004 instead of the first quarter of 2004, as previously reported. As a result for the three months ended March 31, 2004 the Company's net income available to common stockholders per share is \$9,843 (\$0.20 per share) versus a net loss to common stockholders of \$665 (\$0.01 per share) as previously reported.

Item 6. Exhibits and Reports on Form 8-K

Exhibits

- 10.1 Amended and Restated Investment Advisory Agreement, dated as of March 11, 2004, between the Registrant and BlackRock Financial Management, Inc.
- 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

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Financial Officer

Reports on Form 8-K

On February 4, 2004, the Company filed a Current Report on Form 8-K to report under Item 5 the Company's earnings for the quarter and full year ended December 31, 2003.

On March 18, 2004, the Company filed a Current Report on Form 8-K to report under Item 5 the pricing of \$372,456,000 of non-recourse debt offered through Anthracite CDO III Ltd. and Anthracite CDO III Corp.

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: May 10, 2004

By: /s/ Christopher A. Milner

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

Dated: May 10, 2004

By: /s/ Richard M. Shea

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Name: Richard M. Shea  
Title: Chief Operating Officer and Chief  
Financial Officer