

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

ANTHRACITE CAPITAL INC
Form 10-Q
August 14, 2001

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

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

For the quarterly period ended June 30, 2001

Commission File Number 001-13937

ANTHRACITE CAPITAL, INC.
(Exact name of registrant as specified in its charter)

Maryland ----- (State or other jurisdiction of incorporation or organization)	13-3978906 ----- (I.R.S. Employer Identification No.)
345 Park Avenue, New York, New York ----- (Address of principal executive offices)	10154 ----- (Zip Code)
(Registrant's telephone number including area code): (212) 409-3333 -----	

NOT APPLICABLE
(Former name, former address, and former 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 ___

As of August 13, 2001, 35,364,012 shares of voting common stock (\$.001 par value) were outstanding.

ANTHRACITE CAPITAL, INC.,
FORM 10-Q
INDEX

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

PART I - FINANCIAL INFORMATION	Page ----
Item 1. Interim Financial Statements.....	3
Consolidated Statements of Financial Condition At June 30, 2001 (Unaudited) and December 31, 2000.....	3
Consolidated Statements of Operations For the Three and Six Months Ended June 30, 2001 and 2000 (Unaudited).....	4
Consolidated Statement of Changes in Stockholders' Equity For the Six Months Ended June 30, 2001 (Unaudited).....	5
Consolidated Statements of Cash Flows For the Six Months Ended June 30, 2001 and 2000 (Unaudited).....	6
Notes to Consolidated Financial Statements (Unaudited).....	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.....	16
Item 3. Quantitative and Qualitative Disclosures about Market Risk.....	29
Part II - OTHER INFORMATION	
Item 1. Legal Proceedings.....	33
Item 2. Changes in Securities and Use of Proceeds.....	33
Item 3. Defaults Upon Senior Securities.....	33
Item 4. Submission of Matters to a Vote of Security Holders.....	33
Item 5. Other Information.....	33
Item 6. Exhibits and Reports on Form 8-K.....	33
SIGNATURES.....	34

Part I - FINANCIAL INFORMATION
Item 1. Consolidated Financial Statements

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

	June 30, 2001

	(Unaudited)
ASSETS	
Cash and cash equivalents	\$ 21,6
Restricted cash equivalents	30,0

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Securities available for sale, at fair value		
Subordinated commercial mortgage-backed securities (CMBS)		\$290,397
Investment grade securities		787,340

Total securities available for sale		1,077,737
Securities held for trading, at fair value		500,600
Mortgage loan pools available for sale, at fair value		
Commercial mortgage loans		98,800
Investments in real estate joint ventures		10,200
Receivable for investments sold		69,500
Other assets		20,200

Total Assets		\$ 1,828,937
		=====
 LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Borrowings:		
Secured by pledge of subordinated CMBS		\$165,319
Secured by pledge of other securities available for sale and cash equivalents		651,381
Secured by mortgage loans pools		-
Secured by pledge of securities held for trading		489,346
Secured by pledge of investments in real estate joint ventures		2,633
Secured by pledge of commercial mortgage loans		43,658

Total borrowings		\$ 1,352,337
Payable for investments purchased		94,000
Distributions payable		13,300
Other liabilities		18,400

Total Liabilities		1,478,037

10.5% Series A preferred stock, redeemable convertible, liquidation preference \$34,200		30,600

 Commitments and Contingencies		
 Stockholders' Equity:		
Common stock, par value \$0.001 per share; 400,000 shares authorized; 35,124 shares issued and outstanding in 2001; and 25,136 shares issued and outstanding in 2000		
10% Series B preferred stock, liquidation preference \$55,317 in 2001, \$56,525 in 2000		42,000
Additional paid-in capital		405,200
Distributions in excess of earnings		(13,200)
Accumulated other comprehensive loss		(113,900)

Total Stockholders' Equity		320,100

Total Liabilities and Stockholders' Equity		\$1,828,937
		=====

The accompanying notes are an integral part of these financial statements

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

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

	For the Three Months Ended June 30,	
	2001	2000
Income:		
Securities available for sale	\$ 19,204	\$ 19,186
Commercial mortgage loans	4,209	2,989
Mortgage loan pools	137	3,465
Trading securities	3,663	-
Earnings from real estate joint ventures	317	-
Cash and cash equivalents	875	363
Total income	28,405	26,003
Expenses:		
Interest	9,258	15,096
Interest - trading securities	2,407	-
Management and incentive fee	2,668	1,700
Other expenses - net	283	548
Total expenses	14,616	17,344
Other gain (losses):		
Gain on sale of securities available for sale	5,134	682
Gain/loss on securities held for trading	(124)	-
Foreign currency gain (loss)	5	(7)
Loss on impairment of asset	(5,702)	-
Total other gain (loss)	(687)	675
Income before cumulative transition adjustment	13,102	9,334
Cumulative transition adjustment - SFAS 133	-	-
Net Income	13,102	9,334
Dividends and accretion on preferred stock	2,287	1,575
Net Income available to Common Shareholders	10,815	7,759
Net income per common share, basic:		
Income before cumulative transition adjustment	\$0.33	\$0.34
Cumulative transition adjustment - SFAS 133	-	-
Net income	\$0.33	\$0.34

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Net income per common share, diluted:		
Income before cumulative transition adjustment	\$0.32	\$0.32
Cumulative transition adjustment - SFAS 133	-	-
	-----	-----
Net income	\$0.32	\$0.32
	=====	=====
Weighted average number of shares outstanding:		
Basic	32,470	23,115
Diluted	36,631	27,196

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

Anthracite Capital, Inc. and Subsidiaries
Consolidated Statement of Changes in Stockholders' Equity (Unaudited)
For the Six Months Ended June 30, 2001
(in thousands)

	Common Stock, Par Value	Series B Preferred Stock	Additional Paid-In Capital	Distributions In Excess Of Earnings	Accumul Othe Comprehe Loss
	-----	-----	-----	-----	-----
Balance at January 1, 2001	\$25	\$43,004	\$315,533	(\$13,437)	(\$102,
Issuance of common stock	9		88,624		
Net income				24,875	
Net charge associated with current period hedging transactions					(5,
Net amount reclassified into earnings due to amortization of de-designated hedges					
Cumulative transition adjustment - SFAS 133					1,
Change in net unrealized loss on securities available for sale, net of reclassification adjustment					(7,
Other Comprehensive loss					
Comprehensive Income					
Dividends declared-common stock				(20,160)	
Dividends and accretion on Preferred stock				(4,576)	
Conversion of Series B preferred stock to common stock	1	(918)	917		

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Compensation cost - stock options 132

 Balance at June 30, 2001 \$35 \$42,086 \$405,206 (\$13,298) (\$113,298)
 =====

Disclosure of reclassification adjustment:

Unrealized holding loss

Less: reclassification for realized gains
 previously recorded as unrealized

Net charge associated with current period
 hedging transactions

Net amount reclassified into earnings due
 to amortization of de-designated hedges

Cumulative transition adjustment - SFAS 133

Net unrealized loss on securities

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

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

 F
 June 3

Cash flows from operating activities:

Net income \$ 2

Adjustments to reconcile net income to net cash provided by operating activities:

Net (purchase) sale of trading securities (38)

Amortization on negative goodwill

Cumulative transition adjustment - SFAS 133

Premium amortization, net

Compensation cost - stock options

Loss on impairment of asset

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Non-cash portion of net foreign currency (gain) loss	
Net (gain) loss on sale of securities	(
Distributions from real estate joint ventures in excess of earnings	
Decrease (increase) in other assets	
(Decrease) increase in other liabilities	(
Net cash (used in) provided by operating activities	(36
Cash flows from investing activities:	
Purchase of securities available for sale	(1,26
Funding of commercial mortgage loans	(1
Repayments received from commercial mortgage loans	6
Increase in restricted cash equivalents	(2
Principal payments received on securities available for sale	2
Principal payments received on mortgage loan pools	1
Proceeds from sales of securities available for sale and mortgage loan pools	84
Net payments under hedging securities	(5
Net cash (used in) provided by investing activities	(352
Cash flows from financing activities:	
Net increase (decrease) in borrowings	63
Proceeds from issuance of common stock, net of offering costs	8
Distributions on common stock	(1
Distributions on preferred stock	(
Net proceeds from merger	
Acquisition costs against goodwill	
Purchase of common shares	
Net cash provided by (used in) financing activities	70
Net decrease in cash and cash equivalents	(1
Cash and cash equivalents, beginning of period	3
Cash and cash equivalents, end of period	\$ 2

Supplemental disclosure of cash flow information:

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Interest paid	\$ 2
Investments purchased not settled	\$ 9
Investments sold not settled	\$ 6

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

Anthracite Capital, Inc. and Subsidiaries
 Notes to Consolidated Financial Statements (Unaudited)
 (In thousands, except per 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, therefore, its income is largely exempt from corporate taxation. The Company commenced operations on March 24, 1998.

The Company's business focuses on (i) originating high yield commercial real estate loans, (ii) investing in below investment grade commercial mortgage backed securities ("CMBS") where the Company has the right to control the foreclosure/workout process on the underlying loans, and (iii) acquiring investment grade real estate related securities as a liquidity diversification.

The accompanying unaudited 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 for complete financial statements. These financial statements should be read in conjunction with the annual financial statements and notes thereto included in the Company's annual report on Form 10-K for 2000 filed with the Securities and Exchange Commission.

In the opinion of management, the accompanying financial statements contain all adjustments, consisting of normal and recurring accruals (except for the cumulative transition adjustment for SFAS 133 in the first quarter 2001 - see note 2), necessary for a fair presentation of the results for the interim periods. Operating results for interim periods are not necessarily indicative of the results that may be expected for the entire year.

In preparing the 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 the Company's mortgage-backed securities and certain other investments.

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Note 2

ACCOUNTING CHANGE - DERIVATIVE FINANCIAL INSTRUMENTS

Effective January 1, 2001, the Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended and interpreted, 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.

On January 1, 2001 the Company reclassified certain of its agency debt securities, with an amortized cost of \$64,432 from available-for-sale to trading. An interest rate swap agreement with a \$25,000 notional amount that had been designated as hedging these debt securities was similarly reclassified. The unrealized gain of \$895 related to the agency debt securities and the unrealized loss of \$2,830 related to the interest rate swap as of January 1, 2001 were removed from OCI and recorded as the cumulative transition adjustment to earnings upon adoption of SFAS 133. The net cumulative effect of adopting SFAS 133 was (\$1,903) and is reflected as "Cumulative Transition Adjustment - SFAS 133" on the consolidated statement of operations.

In addition, on January 1, 2001, the Company re-designated interest rate swap agreements with notional amounts aggregating \$98,000 that had been hedging available-for-sale debt securities as cash flow hedges of its variable rate borrowings under reverse repurchase agreements. The fair value of these swap agreements on January 1, 2001, an unrealized loss of (\$9,853), remained in OCI at the date of adoption of FAS 133, and therefore, did not result in a transition adjustment.

Because of the de-designation and re-designation of the \$98,000 interest rate swaps, the Company is required to amortize the related \$9,853 recorded in OCI. Amortization is on a straight-line basis over the shorter of the life of the swap or the previously hedged assets and is recognized as a reduction of interest income. For the three and six months ended June 30, 2001, \$248 and \$497 was amortized as a reduction of interest income respectively, and \$248 will be amortized as a reduction of interest income each quarter for the next 12 months.

In addition, on January 1, 2001 the Company re-designated interest rate swap agreements with notional amounts aggregating \$57,744 that had been hedging available-for-sale debt securities as trading securities. These interest rate swap agreements were sold in January 2001; the loss of \$795 is included in gain on securities held for trading. As of December 31, 2000 the accumulated loss for these interest rate swaps was \$3,226. This accumulated loss is being amortized as a reduction of income from securities available for sale over the weighted average life of the securities these interest rate swaps were hedging on December 31, 2000. For the six months ended June 30, 2001 \$129 was amortized as a reduction of interest income.

The Company uses interest rate swaps to manage exposure to variable cash flows on 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

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

entered, the Company designates the derivative as either a cash flow hedge or a trading derivative.

The Company has entered into reverse repurchase agreements to finance securities available for sale that are not financed under its lines of credit. The reverse repurchase agreements bear interest at a LIBOR based variable rate. Increases in the LIBOR rate could negatively impact earnings. The interest rate swap agreements allow the Company to receive a variable rate cash flow based on LIBOR and pay a fixed rate cash flow, mitigating the impact of this exposure.

As of June 30, 2001, the Company had interest rate swaps with notional amounts aggregating \$251,000 that were designated as cash flow hedges of borrowings under reverse repurchase agreements. Their aggregate fair value was a \$5,488 liability included in other liabilities on the statement of financial condition. For the three months ended June 30, 2001, the net change in the fair value of the interest rate swaps was \$7,611 of which \$1,615 of this change in value was deemed ineffective and is included as a reduction of interest expense and \$5,996 was recorded in OCI.

As of June 30, 2001, the Company had interest rate swaps with notional amounts aggregating \$25,000 designated as trading derivatives. Their aggregate fair value at June 30, 2001 was \$(2,192), included in trading securities. For the three months ended June 30, 2001, the change in fair value for these trading derivatives was \$774 and is included in gain on securities held for trading in the consolidated statement of operations.

The implementation of SFAS 133 did not change the manner in which the Company accounts for its forward currency exchange contracts; these contracts are carried at fair value, with changes in fair value included as a component of net foreign currency gain or loss in the consolidated statement of operations.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objectives and strategies for undertaking various hedge transactions. The Company assesses, both at the inception of the hedge and on an on-going basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. When it is determined that a derivative is not highly effective as a hedge, the Company discontinues hedge accounting prospectively.

Note 3 RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board issued Statement No. 141, "Business Combinations" (SFAS 141) and Statement No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). These statements establish new standards for accounting and reporting for business combinations and for goodwill and intangible assets resulting from business combinations. SFAS 141 applies to all business combinations initiated after June 30, 2001; the Company is required to implement SFAS 142 on January 1, 2002. For the Company, this will result in the unamortized balance of negative goodwill being recognized in income during the first quarter of 2002 as the cumulative effect of implementing the new accounting standard. The Company estimates that the gain recognized upon implementation will be approximately \$6,596.

In July of 2000, the FASB's Emerging Issues Task Force reached a consensus on Issue 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Interests." This issue provides guidance on the appropriate methodology to be used in recognizing changes in the estimated yield on asset-backed securities, and

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

in determining whether impairment exists. This consensus was applied by the Company beginning in the second quarter of 2001, and did not have an impact on the Company's financial statements, but it may require earlier recognition of impairment of CMBS investments than under previous guidance, should the Company experience credit losses on the loans underlying a CMBS investment in amounts greater than anticipated at acquisition.

Note 4 NET INCOME PER SHARE

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

	For the Three Months Ended		
	June 30,		
	2001	2000	
	----	----	
Numerator:			
Net Income available to common shareholders			
before cumulative transition adjustment	\$ 10,815	\$ 7,759	\$
Cumulative transition adjustment - SFAS 133	-	-	
	-----	-----	
Numerator for basic earnings per share	10,815	7,759	
Effect of 10.5% series A senior cumulative redeemable preferred stock	904	868	
	-----	-----	
Numerator for diluted earnings per share	\$11,719	\$8,627	
	=====	=====	
Denominator:			
Denominator for basic earnings per share--weighted average common shares outstanding	32,470	23,115	
Effect of 10.5% series A senior cumulative redeemable preferred stock	4,106	4,081	
Dilutive effect of stock options	56	-	
	-----	-----	
Denominator for diluted earnings per share--weighted average common shares outstanding and common share equivalents outstanding	36,632	27,196	
	=====	=====	
Basic net income per weighted average common share:			
Income before cumulative transition adjustment	\$0.33	\$0.34	
Cumulative transition adjustment - SFAS 133	-	-	
	-----	-----	

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Net income	\$0.33	\$0.34
	=====	=====
Diluted net income per weighted average common share and common share equivalents:		
Income before cumulative transition adjustment	\$0.32	\$0.32
Cumulative transition adjustment - SFAS 133	-	-
	-----	-----
Net income	\$0.32	\$0.32
	=====	=====

Note 5 SECURITIES AVAILABLE FOR SALE

The Company's securities available for sale are carried at estimated fair value. The amortized cost and estimated fair value of securities available for sale as of June 30, 2001 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain

Commercial mortgage-backed securities ("CMBS"):		
CMBS IO's	\$ 78,125	\$ 1,591
Investment grade CMBS	31,591	3
Non-investment grade rated subordinated securities	349,245	441
Non-rated subordinated securities	34,213	713
	-----	-----
Total CMBS	493,174	2,748
Single-family residential mortgage-backed securities ("RMBS"):		
Fixed Rate Securities	44,483	133
Home Equity Loans	32,915	729
Hybrid Adjustable Rate Mortgages	68,645	32
Agency adjustable rate securities	120,570	884
Agency fixed rate securities	414,043	2
	-----	-----
Total RMBS	680,656	1,780
	-----	-----
	1,173,830	4,528
	=====	=====

As of June 30, 2001, an aggregate of \$778,181 in estimated fair value of the Company's securities available for sale was pledged to secure its collateralized borrowings.

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 June 30, 2001:

June 30, 2001

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

	Principal	Number of Loans	% of Collateral
Past due 30 to 60 days	\$17,002	7	0.19%
Past due 60 to 90 days	\$16,891	2	0.18%
Past due 90 or more	\$34,072	6	0.37%
Real Estate owned	\$8,851	1	0.10%
Total Delinquent	\$76,816	16	0.84%
Total Principal Balance	\$9,092,199	1,756	

The Company's delinquency experience of 0.84% is compared to the 0.95% for directly comparable collateral experience shown in the Lehman Brothers CMBS 1998 vintage collateral delinquency index.

To the extent that realized losses, if any, or such resolutions differ significantly from the Company's original loss estimates, it may be necessary to reduce the projected GAAP yield on the applicable CMBS investment to better reflect such investment's expected earnings net of expected losses, from the date of purchase. While realized losses on individual assets may be higher or lower than original estimates, the Company currently believes its aggregate loss estimates and GAAP yields are appropriate.

As of June 30, 2001, the anticipated weighted average unleveraged yield to maturity based upon adjusted cost of the Company's subordinated CMBS was 9.88% per annum, and of the Company's other securities available for sale was 6.15% per annum. The Company's anticipated yields to maturity on its subordinated CMBS and other securities available for sale are based upon a number of assumptions that are subject to certain business and economic uncertainties and contingencies. Examples of these include, among other things, the rate and timing of principal payments (including prepayments, repurchases, defaults and liquidations), 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.

As part of the acquisition of CORE Cap, Inc. in May 2000 the Company inherited three securities backed by franchise loans originated by Franchise Mortgage Acceptance Corporation ("FMAC"). The securities were the class B, C and D securities issued by the FMACT 1998 - BA trust. The total principal amount of all three securities was \$47,609. The respective credit ratings at the date of acquisition were AA, A and BBB. The Company immediately sold the class D security at a gain of approximately \$150. In October 2000 the Company sold \$10,000 of principal amount of the class C security at a loss of approximately \$990. The Company currently owns \$16,366 of class B principal and \$10,829 of class C principal. The trust is collateralized by loans on 365 properties to 75 borrowers. The properties

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

are largely franchise restaurants and gas station convenience stores. Collateral performance has been poor. In March of 2001 the class B securities were downgraded to BBB and the class C securities were downgraded to BB. In July 2001 the class B was downgraded to BBB and class C was downgraded to B.

Although the class C bond is current on all payments, the Company concluded that due to poor collateral performance, future cash flows on the class C bond were not likely to be received as originally provided and, accordingly, the bond was deemed to be impaired. The Company performed an analysis assuming 40% of the underlying collateral balance was nonrecoverable. Given the current level of credit enhancement to the class C securities the loss would amount to 51% of the current principal amount over time. Under this scenario a yield of approximately 14% results in a dollar price of 40. As a point of comparison the yield on the 10 year Treasury on June 30, 2001 was 5.41%. During the second quarter of 2001, the Company took a charge to income of \$5,702 on the class C bond, to write this bond down to its estimated fair value. At June 30, 2001, the fair value of class B was marked at a dollar price of 70 and the class C was marked at a dollar price of 40. As of August 10, 2001, both bonds were current on all payments. The Company anticipates the class B bond will remain current.

Note 6 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. 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. Any taxable gains from such strategies will be applied as an offset against the tax basis capital loss carry forward that the Company incurred during 1998 as a result of the sale of a substantial portion of its securities available for sale.

The Company's securities held for trading are carried at estimated fair value. At June 30, 2001, the Company's securities held for trading consisted of FNMA and Federal Home Loan Mortgage Pools with an estimated fair value of \$502,838 and a interest rate swap agreement which represented a notional amount of \$25,000 and a fair value of \$(2,192). 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. The Federal Home Loan Mortgage Pools and the underlying mortgages generally bear interest at fixed rates through maturities of fifteen to thirty years.

The Company's trading strategies are subject to the risk of unanticipated 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 7 COMMERCIAL MORTGAGE LOANS

A summary of activity for commercial mortgage loans at June 30, 2001 is as follows:

Balance at January 1, 2001	\$153,187
Principal payments received during the period	(1,867)
Proceeds from repayment of mortgage loans	(65,600)
Funding of mortgage loan	13,170

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Balance at June 30, 2001

\$98,890

=====

On June 25, 2001, the Company funded a \$13,170 mezzanine loan secured by a first mortgage on a commercial office condominium located in New York City. The loan is subordinate to a \$38,500 A rated note and a \$6,080 BBB- rated note, which BBB- note is also owned by the Company. The entire principal balance of the Company's investment is pledged to secure borrowings. Current payments are interest only based upon LIBOR plus a spread. The loan matures in January 2004, and may be extended by the borrower for two additional twelve-month periods. As of June 30, 2001, the interest rate was 7.98% and the borrower has made all payments when due.

Note 8 COMMON STOCK

On February 14, 2001 the Company completed a secondary offering of 4,000,000 shares of its common stock in an underwritten public offering. The aggregate net proceeds to the Company (after deducting underwriting fees and expenses) were approximately \$33,200. The Company had granted the underwriters an option, exercisable for 30 days, to purchase up to 600,000 additional shares of common stock to cover over-allotments. This option was exercised on March 13, 2001 and resulted in net proceeds to the Company of approximately \$5,000.

On May 11, 2001, the Company completed another secondary offering of 4,000,000 shares of its common stock in an underwritten public offering. The aggregate net proceeds to the Company (after deducting underwriting fees and expenses) were approximately \$37,800. The Company had granted the underwriters an option, exercisable for 30 days, to purchase up to 600,000 additional shares of common stock to cover over-allotments. This option was exercised on June 6, 2001 and resulted in net proceeds to the Company of approximately \$5,675.

On June 22, 2001, the Company declared distributions to its common shareholders of \$0.32 per share, payable on July 31, 2001 to stockholders of record on June 29, 2001. For U.S. Federal income tax purposes, the dividends are expected to be ordinary income to the Company's shareholders.

During the second quarter of 2001, the Company issued 718,000 shares of common stock under its Dividend Reinvestment Plan. Net proceeds to the Company were approximately \$7,065. No shares were issued in the second quarter of 2000 under the Dividend Reinvestment Plan.

Note 9 TRANSACTIONS WITH AFFILIATES

The Company has a management agreement (the "Management Agreement") with BlackRock Financial Management, Inc. (the "Manager"), a majority owned indirect subsidiary of PNC Financial Services Group, Inc. ("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. The Management Agreement expires on March 20, 2002. The Company pays 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 is 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 0.35% of average invested assets rated above BB+.

The Company incurred \$2,109 and \$3,980 in base management fees in accordance with the terms of the Management Agreement for the three and six months ended June 30, 2001 and \$1,614 and \$2,904 in base management fees for the three and six months ended June 30, 2000. In accordance with the

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

provisions of the Management Agreement, the Company recorded reimbursements to the Manager of \$68 and \$156 for certain expenses incurred on behalf of the Company during the three and six months ended June 30, 2001. No reimbursement of expenses were incurred during the six months ended June 30, 2000.

The Company will also pay the Manager, as incentive compensation, an amount equal to 25% of the funds from operations of the Company (as defined) plus gains (minus losses) from debt restructuring and sales of property, before incentive compensation, in excess of the amount that would produce an annualized return on equity equal to 3.5% over the ten-year U.S. Treasury Rate as defined in the Management Agreement. For purposes of the incentive compensation calculation, equity is generally defined as proceeds from issuance of Common Stock before underwriting discounts and commissions and other costs of issuance. The Company incurred \$559 and \$1,137 in incentive compensation for the three and six months ended June 30, 2001 and \$86 for the three and six months ended June 30, 2000.

Under the terms of an administration agreement, the Manager provides financial reporting, audit coordination and accounting oversight services. The Company pays the Manager a monthly administrative fee at an annual rate of 0.06% of the first \$125 million of average net assets, 0.04% of the next \$125 million of average net assets and 0.03% of average net assets in excess of \$250 million subject to a minimum annual fee of \$120. For the three and six months ended June 30, 2001, the administration fee was \$35 and \$66. For the three and six months ended June 30, 2000 the administration fee was \$30 and \$60.

On March 30, 2001, the Company purchased two certificates representing a 1% interest in PNC Loan Trust - III for an aggregate investment of \$1,732. These certificates were purchased from PNC Bank, an affiliate of the Company. The assets of the Trusts consist of commercial mortgage loans originated or acquired by PNC. The Company has a committed line of credit for \$4,500 from PNC Funding Corp., a wholly owned indirect subsidiary of PNC Bank, to borrow up to 90% of the fair market value of the Company's interest in such Trusts. Outstanding borrowings against this line of credit bear interest at a LIBOR based variable rate. As of June 30, 2001, there were no outstanding borrowings against this line of credit.

During the three months ended March 30, 2001, the Company purchased twelve certificates each representing a 1% interest in different classes of Owner Trust NS I Trust ("Owner Trusts") for an aggregate investment of \$37,868. These certificates were purchased from PNC Bank. The assets of the Owner Trusts consist of commercial mortgage loans originated or acquired by an affiliate of PNC. The Company entered into a \$50,000 committed line of credit from PNC Funding Corp. to borrow up to 95% of the fair market value of the Company's interest in the Owner Trusts. Outstanding borrowings against this line of credit bear interest at a LIBOR based variable rate. As of June 30, 2001, there was \$27,310 borrowed under this line of credit. The Company earned \$592 and \$717 from the Owner Trusts and paid interest of approximately \$432 and \$531 to PNC Funding Corp. as interest on borrowings under a related line of credit for the three and six months ended June 30, 2001. During the three months ended June 30, 2001, the Company sold four Owner Trusts. The gain on the sale of those Owner Trusts was \$45.

Note 10 BORROWINGS

Certain information with respect to the Company's collateralized borrowings at June 30, 2001 is summarized as follows:

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

	Lines of Credit and Term Loans	Reverse Repurchase Agreements
Outstanding borrowings	\$ 119,729	\$1,232,608
Weighted average borrowing rate	5.01%	3.97%
Weighted average remaining maturity	274 days	19 days
Estimated fair value of assets pledged	\$156,958	\$1,325,239

As of June 30, 2001, \$24,803 of borrowings outstanding under the lines of credit were denominated in pounds sterling and interest payable is based on sterling LIBOR.

As of June 30, 2001, the Company's collateralized borrowings had the following remaining maturities:

	Lines of Credit and Term Loan	Reverse Repurchase Agreements
Within 30 days	-	\$1,232,608
31 to 59 days	-	-
Over 60 days	119,729	-
	\$119,729	\$1,232,608

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.

During the second quarter the Company extended its \$185,000 committed credit facility with Deutsche Bank, AG until July 18, 2002.

The Company has a facility with ABN Amro, in the amount of \$200,000, which matured on June 18, 2001. Borrowings under this facility were repaid in April 2001 when the sale of the mortgage loan pool assets was completed.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

General:

During the second quarter of 2001 the Company increased its quarterly dividend rate to \$0.32 per share. This contributed to the second quarter's total return of 23% with performance during the first two quarters exceeding 50%. The Company is focused on increasing scale with the long-term goals of increasing earnings, increasing dividends and providing greater financial flexibility. So far this year the Company has raised over

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

\$85 million through accretive common stock offerings. The Company is currently deploying its new capital in the investment grade real estate related securities sector employing greater leverage and less credit risk to create a higher level of operating earnings. This strategy will be followed by a continued focus on strategic redeployment of this capital into the high yield commercial real estate loan portfolio, and the below investment grade CMBS creating a sustainable level of higher earnings on a risk adjusted basis. The Company believes that this approach will allow shareholders to benefit from rising dividends, improved stock market valuation and more flexible financing opportunities.

The Company's business focuses on (i) originating high yield commercial real estate loans, which includes senior interests in partnerships that own real property and are reported as real estate or joint venture investments, (ii) investing in below investment grade commercial mortgage backed securities ("CMBS") where the Company has the right to control the foreclosure/workout process on the underlying loans, and (iii) acquiring investment grade real estate related securities.

The Company's management believes that this represents an integrated strategy where each line of business supports the others and creates additional value for shareholders over and above operating each line in isolation. The commercial real estate loans provide high risk adjusted returns for shorter periods of time, the CMBS portfolio provides diversification and high loss adjusted returns over a weighted average life of approximately 10 years, and the investment grade securities investments are an actively managed portfolio that supports the liquidity needs of the Company while earning attractive returns.

These strategies are pursued within an aggregate risk management framework that seeks to limit the exposure of the Company's equity and earnings to changes in interest rates and other factors beyond the Company's control.

The principal risks that the Company faces are (i) credit risk on the high yield real estate loans and securities it underwrites, (ii) interest rate risk on the spread between the rates (typically one month LIBOR) at which the Company borrows and the generally longer term rates (as represented by the U.S. Ten Year Treasury) at which the Company lends, and (iii) funding risk in the amount and cost of debt financing employed by the Company over time versus the level of such funding that is sustainable by the financing markets. These risks are discussed in more detail below, under the heading, "Quantitative and Qualitative Disclosures About Market Risk" and under "Capital Resources and Liquidity".

The following discussion should be read in conjunction with the financial statements and related notes. Dollar amounts are expressed in thousands, other than per share amounts.

Market Conditions and their Effect on Company Performance:

Two of the most significant factors that affect the Company's earnings are credit experience and the relationship of long term interest rates to short term interest rates. The Company's interest income from credit sensitive securities is based on a loss adjusted yield. The Company establishes loss assumptions on the pools of loans underlying its CMBS portfolios. It then computes a loss adjusted yield based on the assumed cash flows that are projected after applying the loss assumptions. To the extent that actual losses are substantially similar to the loss assumptions the loss adjusted yield would stay constant. If actual losses are greater or lower than expectations the loss adjusted yields would be decreased or increased respectively.

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

The relationship of long term rates to short term rates is important because the Company invests over the long term and finances for a short term. When long term rates exceed short term rates (i.e. the yield curve is steep) the Company will generally report higher earnings. When short term rates are higher than long term rates (an inverted yield curve) the Company will generally report lower earnings.

Credit Experience: The Company considers delinquency information from the Lehman Brothers Conduit Guide for 1998 transactions to be the most relevant measure of market conditions applicable to its below investment grade CMBS holdings. Pursuant to these statistics as of June 30, 2001, 40 securitizations were included and 0.95% of principal balances were delinquent, compared to 0.99% as of March 31, 2001. The broader measure of all transactions issued since 1994 and tracked in the Conduit Guide also provides relevant comparable information. As of June 30, 2001, 190 securitizations were being monitored among the larger universe and 0.93% of the outstanding balances were delinquent, compared to an overall delinquency rate of 0.94% across 180 transactions as of March 31, 2001.

Morgan Stanley Dean Witter (MSDW) also tracks CMBS loan delinquencies using a slightly smaller universe. Their index tracks all CMBS transactions with more than \$200,000 of collateral that have been seasoned for at least one year. This will generally adjust for the lower delinquencies that occur in newly originated collateral. As of June 30, 2001, MSDW delinquencies on 158 securitizations were 1.21% of current balances. As of March 31, 2001, this same index tracked 150 securitizations with delinquencies of 1.27%. Over the life of these types of transactions, and as the economy slows, delinquencies and losses will naturally increase.

The Company's below investment grade CMBS represent approximately \$613,845 of face value collateralized by underlying pools of first lien commercial mortgages. The CMBS owned by the Company include 1,756 loans with an aggregate principal balance of over \$9.0 billion as of June 30, 2001. The Company is in a first loss position with respect to these loans. The Company manages its credit risk through conservative underwriting, diversification, active monitoring of loan performance and exercise of its right to control the workout process as early as possible. All of these processes are based on the extensive intranet-based analytic systems developed by BlackRock.

The following table shows the comparison of delinquencies:

----- March 31, 2001 -----				
	Principal	Number of Loans	% of Collateral	Principal

Past due 30 to 60 days	\$3,234	1	0.04%	\$17,002
Past due 60 to 90 days	21,586	4	0.24%	\$16,891
Past due 90 or more	27,879	6	0.31%	\$34,072
Real Estate owned	10,107	2	0.11%	\$8,851

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Total Delinquent	\$62,806	13	0.69%	\$76,816

Total Principal Balance	\$9,101,437	1,760		\$9,092,199

Of the 16 delinquent loans as of June 30, 2001, six were delinquent due to technical reasons, one was REO and being marketed for sale, three were in foreclosure, and the remaining six loans were in workout negotiations. Realizing the estimated losses on all the properties currently in delinquency would not cause the Company to change its loss adjusted yields. The 16 delinquent loans do not indicate any weakness in any geographic area or property type.

The Company's delinquency experience of 0.84% remains slightly better than the 0.95% for directly comparable collateral experience shown in the Lehman Brothers Conduit Guide for 1998 Transactions.

During the second quarter of 2001 the Company also experienced early payoffs of \$5,008, representing 0.55% of the existing pool balance. These loans were paid at par with no loss. The anticipated losses attributable to these loans will be reallocated to the loans remaining in the pools.

During the second quarter one REO property was sold. The realized loss to the trust is expected to be approximately \$1,000. This is well within expectations and will not cause a change in loss-adjusted yields on the portfolio. Total realized losses in the underlying pools for the year 2001 is \$3,455. This is in line with expectations.

Yield Curve: During the second quarter of 2001 the yield on the ten-year U.S. Treasury Note increased by 49 basis points from 4.92% to 5.41%. The Federal Reserve Board continued its policy of reducing short-term interest rates. The most recent reduction in short rates came on June 27, 2001 with a 25 basis point reduction. This marked the sixth easing move of the year - the prior five each were reductions of 50 basis points. The Fed Funds target has dropped to 3.75% from 6.50% at the beginning of the year. The next meeting of the Federal Reserve Board is scheduled for August 21, 2001.

The chart below compares the rate for the ten-year U.S. Treasury securities to the one-month LIBOR rate.

	Ten Year U.S Treasury Securities	One month LIBOR	Difference
	-----	-----	-----
June 30, 2001	5.40%	3.86%	1.53%
March 31, 2001	4.92%	5.09%	0.17%
June 30, 2000	6.02%	6.66%	(0.64%)

The decrease in LIBOR from March 31, 2001 to June 30, 2001 had a positive impact on the Company's financing costs and net income.

Approximately \$83,000 of the Company's assets earn interest at rates that are determined with reference to LIBOR. The Company also had \$276,000 notional amount of interest rate swap agreements where the Company pays a fixed rate of interest and receives a floating rate based on LIBOR. All of the Company's borrowings bear interest at rates that are determined with reference to LIBOR. The Company has a net inverse exposure to LIBOR, such that decreases in LIBOR will cause earnings to increase and increases in LIBOR will cause earnings to decrease.

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Real Estate Capital Markets: The valuation of the Company's CMBS assets depends on credit spreads, interest rates and liquidity of the real estate capital markets. The Company also finances itself based on the value of these assets.

Credit Spreads: CMBS exhibited slight spread widening at the double-B rating level and very modest spread tightening at the single-B level as shown in the chart below. Despite increased CBO activity, older, seasoned BB-rated classes traded approximately 20 basis points wider than new issue bonds due to lack of two ratings, frequently lacking one from Moody's. Single-B bonds are not typically part of arbitrage CBO's but have been included in CBO issues done by first-loss buyers as part of long-term funding strategies. Low interest rates and steady credit spreads for borrowers has sparked increased CMBS issuance. First half domestic issuance of \$32.6 billion represents a 56% increase over 2000's first half issuance of \$20.9 billion. During the first half of the year REIT equities had a total return of 10.4% that exceeded the returns of both the Russell 2000 index (+6.3%) and the S&P 500 (-6.5%).

Corporate bonds continued to rebound from their underperformance in the fourth quarter of 2000 increasing the relative attractiveness of CMBS.

	BB CMBS	BB Corporate	Difference
June 30, 2001	564	419	145
March 31, 2001	556	448	108
Dec. 31, 2000	558	523	35

	B CMBS	B Corporate	Difference
June 30, 2001	983	785	198
March 31, 2001	990	818	172
Dec. 31, 2000	987	978	9

Source: Lehman Brothers CMBS High Yield Index & Lehman Brothers High Yield Index

The unrealized loss on the Company's holdings of CMBS at June 30, 2001 was \$93,012. This decline in the value of the investment portfolio represents market valuation changes and is not due to credit experience or credit expectations. The adjusted purchase price of the Company's CMBS portfolio as of June 30, 2001 represents approximately 62% 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. The Company performs a detailed review of its loss assumptions on a quarterly basis and will adjust them when it believes that credit experience or expectations justify such an adjustment. As of June 30, 2001 the Company concluded that real estate credit fundamentals remain solid, and there has been no material change in the credit quality of its portfolio.

As the portfolio matures and expected losses occur subordination levels of the lower rated classes of a CMBS investment will be reduced. This will cause the lower rated classes to be downgraded. This is the natural course for this type of security and is built into the loss expectations of the portfolio. This would negatively affect the market value and liquidity of the portfolio, but will not affect its credit performance.

Real Estate: The slowdown in real GDP growth continues to affect property markets across the country. Reduction in tenant demand for office space has increased vacancy rates, particularly in markets that had experienced the greatest absorption in 2000. Retail properties have seen sales remain relatively stable as consumers have continued to spend. It is generally

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

believed that continued strength in residential housing has provided consumers with increased asset values and a source of borrowing power. Owners of retail properties continue to "re-cycle" space retrieved from tenants who have closed stores to increase profitability or ceased operations. Multifamily markets continue to benefit from increased demand as larger numbers of 20-29 and 65+ year olds enter their prime renting years. Supply of multifamily space is expected to lag demand nationally in 2001, although in selected markets higher supply will suppress rent growth. Lodging markets have slowed in tandem with the slower economy. Growth in revenue-per-available-room "revpar" has turned in a negative 3.8% in the second quarter. Since hotels have the shortest lease terms (nightly turnover) they exhibit the greatest sensitivity to changes in GDP growth.

Commercial Lending: The Company also owns five mezzanine whole loans and two preferred equity interests in partnerships that own office buildings. The Company's commercial loan portfolio generally emphasizes larger transactions located in metropolitan markets as compared to the loans in the CMBS portfolio. The credit performance of the Company's commercial mortgage backed securities remains consistent with expectations. There are no delinquencies on the Company's direct holdings of commercial mezzanine loans.

During fiscal year 2001 two loans have paid down their principal in full representing over \$65,000 in proceeds. In March the Santa Monica Loan paid off in full its \$35,000 loan balance and in June The New York Loan Paid off in full its \$30,600 loan balance. These loans generated a realized return to the Company of over 22.5%. The contribution of these two loans to net income prior to their repayment was approximately \$6,000 on an annualized basis.

On June 25, 2001, the Company funded a \$13,170 mezzanine loan secured by a first mortgage on a commercial office condominium located in New York City. The loan is subordinate to a \$38,500 A rated note and a \$6,080 BBB- rated note, of which the BBB- note is also owned by the Company. The entire principal balance of the Company's investment is pledged to secure borrowings. Current payments are interest only based upon LIBOR plus a spread. The loan matures in January 2004, and may be extended by the borrower for two additional twelve-month periods. As of June 30, 2001, the interest rate was 7.98% and the borrower has made all payments when due.

Investment Grade Real Estate Related Securities: The yields on residential mortgage backed securities (RMBS) rose along with longer dated fixed income securities as investors grew fearful of the inflationary potential of an economic recovery. Declining prepayments and a steeper yield curve improved the fundamentals for residential mortgages evidenced by tightening spreads to both treasuries and swaps.

Investment Grade CMBS yields followed RMBS as spreads tightened on fundamentals but absolute yields increased. The low delinquency rates of commercial mortgages in general continued to help the performance of this assets class.

The proceeds from the Company's two equity raises and commercial mortgage paydowns have been redeployed into RMBS to the maximum amount permitted by the Company's debt to capital covenants. The Company's RMBS portfolio currently consists of approximately \$1.2 billion worth of residential mortgage backed Securities financed with over \$1.1 billion of reverse repurchase agreements.

As part of the acquisition of CORE Cap, Inc. in May 2000 the Company inherited three securities backed by franchise loans originated by Franchise Mortgage Acceptance Corporation ("FMAC"). The securities were the

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

class B, C and D securities issued by the FMACT 1998 - BA trust. The total principal amount of all three securities was \$47,609. The respective credit ratings at the date of acquisition were AA, A and BBB. The Company immediately sold the class D security at a gain of approximately \$150. In October 2000 the Company sold \$10,000 of principal amount of the class C security at a loss of approximately \$990. The Company currently owns \$16,366 of class B principal and \$10,829 of class C principal. The trust is collateralized by loans on 365 properties to 75 borrowers. The properties are largely franchise restaurants and gas station convenience stores. Collateral performance has been poor. In March of 2001 the class B securities were downgraded to BBB and the class C securities were downgraded to BB. In July 2001 the class B was downgraded to BBB and class C was downgraded to B.

Although the class C bond is current on all payments, the Company concluded that due to poor collateral performance, future cash flows on the class C bond were not likely to be received as originally provided and, accordingly, the bond was deemed to be impaired. The Company performed an analysis assuming 40% of the underlying collateral balance was nonrecoverable. Given the current level of credit enhancement to the class C securities the loss would amount to 51% of the current principal amount over time. Under this scenario a yield of approximately 14% results in a dollar price of 40. As a point of comparison the yield on the 10 year Treasury on June 30, 2001 was 5.41%. During the second quarter of 2001, the Company took a charge to income of \$5,702 on the class C bond, to write this bond down to its estimated fair value. At June 30, 2001, the fair value of class B was marked at a dollar price of 70 and the class C was marked at a dollar price of 40. As of August 10, 2001, both bonds were current on all payments. The Company anticipates the class B bond will remain current.

Recent Events:

The Company recently obtained the consent of the holders of the Series A preferred stock to increase the Company's debt to capital ratio for a period of one year. Under the terms of the preferred stock, the Company was not permitted to have a debt to capital ratio of more than 4.5:1. Beginning on August 1, 2001 the Company may maintain a debt to capital ratio of 5.0:1 until July 31, 2002. This 5.0:1 ratio is the same limit in other borrowing facilities; so no other waivers were required. The Company will use this increased borrowing ability to acquire additional RMBS to take advantage of investment opportunities available in the current steep yield curve environment. The Company will not increase its aggregate leverage ratios on its high yielding CMBS or mezzanine loan portfolios.

At the beginning of the third quarter of 2001, the Company entered into a \$50 million commitment to acquire shares in Carbon Capital, Inc., a private commercial real estate income opportunity fund managed by BlackRock Financial Management, Inc., who is also the manager of the Company. This commitment deploys a portion of the Company's excess liquidity into mezzanine lending with better diversification and on a more cost effective basis. By participating in Carbon, the Company seeks to reduce its maximum exposure to any given mezzanine holding while improving the return on invested capital. Anthracite does not pay BlackRock management or incentive fees through Carbon and has received a reduced fee for this investment on its own management contract with BlackRock. This transaction was reviewed by outside council and approved by the Company's unaffiliated Directors in June of 2001.

It is anticipated that funds will be drawn over time as opportunities are identified. Carbon will be managed by the same management team that has been managing the Company's commercial loan portfolio. The risk profile of

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

Carbon is substantially similar to the Company's commercial loan program and the structure of Carbon is a Real Estate Investment Trust so the tax and regulatory issues are identical.

Funds From Operations (FFO): Most industry analysts, including the Company, consider FFO an appropriate supplementary measure of operating performance of a REIT. In general, FFO adjusts net income for non-cash charges such as depreciation, certain amortization expenses and gains or losses from debt restructuring and sales of property. However, FFO does not represent cash provided by operating activities in accordance with GAAP and should not be considered an alternative to net income as an indication of the results of the Company's performance or to cash flows as a measure of liquidity.

The Company computes FFO in accordance with the definition recommended by the National Association of Real Estate Investment Trusts. The Company believes that the exclusion from FFO of gains or losses from sales of property was not intended to address gains or losses from sales of securities as it applies to the Company. Accordingly, the Company includes gains or losses from sales of securities in its calculation of FFO.

The Company's FFO for the three months ended June 30, 2001 and 2000 was \$13,102, and \$9,334, respectively, and \$24,875 and \$16,659 for the six months ended June 30, 2001 and 2000, respectively. FFO was the same as its reported GAAP net income for the periods. The Company reported cash flows (used in) provided by operating activities of \$(364,872) and \$15,676, cash flows (used in) provided by investing activities of \$(352,100) and of \$672,479 and cash flows provided by (used in) financing activities of \$700,767 and \$(699,842) in its statement of cash flows for the six months ended June 30, 2001 and 2000, respectively.

Results of Operations: Net income for the three and six months ended June 30, 2001 was \$13,102, or \$0.33 per share (\$0.32 diluted), and \$24,875, or \$0.69 (\$0.65 diluted), respectively. Net income for the three and six months ended June 30, 2000 was \$9,334, or \$0.34 per share (\$0.32 diluted), and \$16,659, or \$0.65 (\$0.61 diluted), respectively.

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 June 30, 2001	2000
	Interest Income	Inter- Income
	-----	-----
CMBS	\$14,207	\$9,334
Other securities available for sale	4,997	9,334
Commercial mortgage loans	4,209	2,000
Mortgage loan pools	137	3,334
Trading securities	3,663	
Cash and cash equivalents	875	
	-----	-----
Total	\$28,088	\$26,000
	=====	=====
	For the Six Months Ended June 30, 2001	2000
	Interest Income	Inter- Income

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

CMBS	\$24,514	\$18
Other securities available for sale	11,937	15
Commercial mortgage loans	10,196	4
Mortgage loan pools	1,575	3
Trading securities	4,767	
Cash and cash equivalents	1,072	
Total	\$54,061	\$42

In addition to the foregoing, the Company earned \$317 and \$684 from real estate joint ventures during the three and the six months ended June 30, 2001, respectively.

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 June 30, 2001	2000
	Interest Expense	Interest Expense
Reverse repurchase agreements	\$9,392	\$4,392
Lines of credit and term loan	2,273	10,273
Total	\$ 11,665	\$15,665

	For the Six Months Ended June 30, 2001	2000
	Interest Expense	Interest Expense
Reverse repurchase agreements	\$ 18,148	\$10,148
Lines of credit and term loan	5,789	11,789
Total	\$ 23,937	\$22,937

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 liquid investment grade securities to enhance the Company's liquidity.

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

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. Interest income for the three months ended June 30, 2001 does not include earnings from real estate joint ventures of \$317 and interest expense of \$41. There were no earnings from real estate joint ventures for the three months ended June 30, 2000.

	For the Three Months Ended	
	June 30, 2001	June 30, 2000
Interest income	\$28,088	\$26,003
Interest expense	\$11,624	\$15,906
Net interest margin	4.95%	4.19%
Net interest spread	3.54%	2.82%

Other Expenses: Expenses other than interest expense consist primarily of management fees and general and administrative expenses. The Company incurred \$2,109 and \$3,980 in base management fees in accordance with the terms of the Management Agreement for the three and six months ended June 30, 2001 and \$1,614 and \$2,904 in base management fees for the six months ended June 30, 2000. The Company incurred \$559 and \$1,137 in incentive compensation for the three and six months ended June 30, 2001 and \$86 for the three and six months ended June 30, 2000. In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of \$68 and \$156 for certain expenses incurred on behalf of the Company during the three and six months ended June 30, 2001. No reimbursement of expenses were incurred during the six months ended June 30, 2000. Other expenses - net of \$283 and \$969 for the three and six months ended June 30, 2001, and \$548 and \$1,435 for the three and six months ended June 30, 2000, were comprised of accounting agent fees, custodial agent fees, directors' fees, fees for professional services, insurance premiums, broken deal expenses, due diligence costs and amortization of negative goodwill.

Other Gains (Losses): During the six months ended June 30, 2001 and 2000 the Company sold a portion of its securities available-for-sale for total proceeds of \$842,238 and \$1,310,456, which resulted in a realized gain of \$5,134 and \$682 for the three months ended June 30, 2001 and 2000, respectively and \$7,081 and \$705 for the six months ended June 30, 2001 and 2000, respectively. The (loss) gain on securities held for trading were \$(124) for the three months ended June 30, 2001 and \$568 and \$324 for the six months ended June 30, 2001 and 2000, respectively. There were no purchases or sales of trading securities for the three months ended June 30, 2000. The foreign currency gains (losses) of \$5 and \$(7) for the three

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

months ended June 30, 2001 and 2000, and \$109 and \$(11) for the six months ended June 30, 2001 and 2000 respectively, relate to the Company's net investment in a commercial mortgage loan denominated in pounds sterling and associated hedging.

Dividends Declared: On June 22, 2001, the Company declared distributions to its shareholders of \$.32 per share, payable on July 31, 2001 to shareholders of record on June 29, 2001.

Tax Basis Net Income and GAAP Net Income: Net income as calculated for tax purposes (tax basis net income) was estimated at \$19,844, or \$0.54 (\$0.50 diluted) per share, and \$35,054, or \$1.02 (\$0.95 diluted) per share, for the three and six months ended June 30, 2001, compared to a net income as calculated in accordance with GAAP of \$13,102, or \$0.33 (\$0.32 diluted) per share, and \$24,875, or \$0.69 (\$0.65 diluted) per share, respectively.

Differences between tax basis net income and GAAP net income arise for various reasons. For example, in computing income from its subordinated CMBS for GAAP purposes, the Company takes into account estimated credit losses on the underlying loans whereas for tax basis income purposes, only actual credit losses are taken into account. As there were no actual credit losses incurred in 2001, tax basis income for subordinate CMBS is higher the GAAP income. Certain general and administrative expenses may differ due to differing treatment of the deductibility of such expenses for tax basis income. Also, differences could arise in the treatment of premium and discount amortization on the Company's securities available for sale.

A reconciliation of GAAP net income to tax basis net income is as follows:

	For the Three Months Ended June 30, 2001
GAAP net income	\$13,102
FAS 133 adjustment	-
Loss (Gain) on trading securities	(54)
Loss on Impairment of asset	5,702
Subordinate CMBS income differences	1,094
	\$19,844
Tax basis net income	\$19,844
	For the Three Months Ended June 30, 2000
GAAP net income	\$ 9,334
Subordinate CMBS income differences	658
CORE Cap merger expenses	(2,300)
	\$ 7,692
Tax basis net income	\$ 7,692

Changes in Financial Condition

Securities Available for Sale: The Company's securities available for sale,

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

which are carried at estimated fair value, included the following at June 30, 2001 and December 31, 2000:

Security Description	June 30, 2001 Estimated Fair Value	Percentage

Commercial mortgage-backed securities:		
CMBS IO's	\$ 79,449	7.4%
Investment grade CMBS	30,003	2.8
Non-investment grade rated subordinated securities	264,219	24.5
Non-rated subordinated securities	26,178	2.4
	399,849	37.1

Single-family residential mortgage-backed securities:		
Fixed Rate Securities	44,592	4.1
Home Equity Loans	33,644	3.1
Hybrid Adjustable Rate Mortgages	68,677	6.4
Agency adjustable rate securities	121,437	11.3
Agency fixed rate securities	409,538	38.0
	677,888	62.9
	\$1,077,737	100.0%

Borrowings: As of June 30, 2001, the Company's debt consisted of line-of-credit borrowings, term loans and reverse repurchase agreements, collateralized by a pledge of most of the Company's securities available for sale, securities held for trading, mortgage loans held for sale and its commercial mortgage loans. The Company's financial flexibility is affected by its ability to renew or replace on a continuous basis its maturing short-term borrowings. As of June 30, 2001, 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, term loans, 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 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.

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

For the Six Months Ended
June 30, 2001

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

	June 30, 2001 Balance	Maximum Balance	Ran Matur
Reverse repurchase agreements	\$1,232,608	\$1,266,970	2 to 3
Line of credit and term loan borrowings	119,729	\$205,889	230 to

Hedging Instruments: Effective January 1, 2001, the Company adopted 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.

As a result, on January 1, 2001 the Company reclassified certain of its agency debt securities, with an amortized cost of \$64,432 from available-for-sale to trading. An interest rate swap agreement with a \$25,000 notional amount that had been designated as hedging these debt securities was similarly reclassified. The unrealized gain of \$895 related to the debt securities and the unrealized loss of \$2,830 related to the interest rate swap were removed from other comprehensive income and recorded as the cumulative transition adjustment to earnings upon adoption of SFAS 133. The net cumulative effect of adopting SFAS 133 was (\$1,903) or (\$0.06) per share, and is reflected as cumulative transition adjustment on the statement of operations.

In addition, on January 1, 2001, the Company re-designated interest rate swap agreements with notional amounts aggregating \$98,000 that had been hedging available-for-sale debt securities as cash flow hedges of its variable rate borrowings under reverse repurchase agreements. The fair value of these swap agreements on January 1, 2001, an unrealized loss of (\$9,853), remained in other comprehensive income at the date of adoption of FAS 133, and therefore, did not result in a transition adjustment.

In addition, on January 1, 2001 the Company re-designated interest rate swap agreements with notional amounts aggregating \$57,744 that had been hedging available-for-sale debt securities as trading securities. These interest rate swap agreements were sold in January 2001; the loss of \$795 is included in gain on securities held for trading.

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 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 earnings would decline. The Company's principal strategies for mitigating this risk are to maintain portfolio leverage at levels it believes are sustainable, to diversify the sources and types of available borrowing and capital and to maintain at least 25% of equity in liquid assets that can be converted into cash if required. The current liquid assets ratio is 54%. The Company has utilized committed bank facilities, preferred stock, and will consider resecuritization or other achievable term funding of existing

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

assets.

On February 14, 2001 the Company completed a secondary offering of 4,000,000 shares of its common stock in an underwritten public offering. The aggregate net proceeds to the Company (after deducting underwriting fees and expenses) were approximately \$33,200. The Company had granted the underwriters an option, exercisable for 30 days, to purchase up to 600,000 additional shares of common stock to cover over-allotments. This option was exercised on March 13, 2001 and resulted in net proceeds to the Company of approximately \$5,000.

On May 11, 2001 the Company completed another secondary offering of 4,000,000 shares of its common stock in an underwritten public offering. The aggregate net proceeds to the Company (after deducting underwriting fees and expenses) were approximately \$37,800. The Company had granted the underwriters an option, exercisable for 30 days, to purchase up to 600,000 additional shares of common stock to cover over-allotments. This option was exercised on June 6, 2001 and resulted in net proceeds to the Company of approximately \$5,675.

As of June 30, 2001, \$154,140 of the Company's \$185,000 committed credit facility with Deutsche Bank, AG was available for future borrowings, and \$134,873 was available under the Company's \$200,000 term facility with Merrill Lynch.

The Company's operating activities (used) provided cash of \$(364,872) and \$15,676 during the six months ended June 30, 2001, and 2000, respectively, primarily through net income and, in 2001, net purchases of trading securities.

The Company's investing activities (used) provided cash totaling \$(352,100) and \$672,479 during the six months ended June 30, 2001, and 2000, respectively, primarily to purchase securities available-for-sale and to fund commercial mortgage loans, offset by principal payments received on securities available-for-sale, mortgage loans, and proceeds from sales of securities available-for-sale.

The Company's financing activities provided (used) cash of \$700,767 and \$(699,842) during the six months ended June 30, 2001 and 2000, respectively, primarily from repayment of short-term borrowings and payment of distributions, offset in 2001, by proceeds from the issuance of common stock and short term borrowings.

Although the Company's portfolio of securities available-for-sale was acquired at a net discount to the face amount of such securities, the Company has received to date and expects to continue to receive sufficient cash flows from these securities to fund distributions to the Company's stockholders.

The Company is subject to various covenants in its lines of credit, including maintaining a minimum GAAP net worth of \$140,000, a debt-to-equity ratio not to exceed 4.5 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. Additionally, the Company's GAAP net worth cannot decline by more than 37% during the course of any two consecutive fiscal quarters. As of June 30, 2001, the Company was in compliance with all such 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

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

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. 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.

REIT Status: The Company has elected to be taxed as a REIT and to comply with the provisions of the 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 is 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 risk is highly sensitive to dynamics of the markets for commercial mortgage securities and other loans and securities held by the Company. Credit risk is valued based on a spread over comparable maturity Treasury obligations. This spread represents the additional compensation required by investors to assume the credit risk of a debt obligation. 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 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, indeed, 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 counter parties 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 test 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 following tables quantify the potential changes in the Company's Portfolio Net Market Value and net interest income under various interest

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

rate and credit-spread scenarios. Portfolio Net Market Value is defined as the value of interest-earning assets net of the value of interest-bearing liabilities. It is evaluated using an assumption that interest rates, as defined by the U.S. Treasury yield curve, or credit spreads, as defined by the U.S. Interest rate swap curve, increase or decrease up to 200 basis points and the assumption that the yield curves of the rate shocks will be parallel to each other. Portfolio Net Market Value in the Credit Spread Movements scenario is calculated using the assumption that the U.S. Treasury yield curve remains constant. The Company feels that 200 basis point variations encompasses periods of significant volatility in these markets.

Net interest income is defined as interest income earned from interest-earning assets net of the interest expense incurred by the interest bearing liabilities. It is evaluated using the assumptions that interest rates, as defined by the U.S. LIBOR curve, increase or decrease by 200 basis points and the assumption that the yield curves of the LIBOR rate shocks will be parallel to each other. 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 June 30, 2001. Actual results could differ significantly from these estimates.

Projected Percentage Change In Portfolio Net Market Value Given U.S. Treasury Yield Curve Movements

Change in Treasury Yield Curve, +/- Basis Points	Projected Change in Portfolio Net Market Value
-200	8.3%
-100	4.9%
-50	2.7%
Base Case	0
+50	(3.0)%
+100	(6.5)%
+200	(14.5)%

Projected Percentage Change In Portfolio Net Market Value Given Credit Spread Movements

Change in Credit Spreads, +/- Basis Points	Projected Change in Portfolio Net Market Value
-200	44.6%
-100	21.8%
-50	10.8%
Base Case	0
+50	(10.5)%
+100	(20.8)%
+200	(40.6)%

Projected Percentage Change In Portfolio Net Interest Income and Change in Net Income per Share Given LIBOR Movements

Change in LIBOR,	Projected Change in Portfolio	Projected Change in Net Income per Share
------------------	----------------------------------	---

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

+/- Basis Points	Net Interest Income	
-100	14.0%	\$0.29
-50	7.0%	\$0.15
Base Case	0	0
+50	(7.0)%	\$(0.15)
+100	(14.0)%	\$(0.29)

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 American economy, and other factors beyond the control of the Company.

All loans are subject to a certain probability of default. The nature of the CMBS assets owned are such that all losses experienced by a pool of mortgages will be borne by the Company. Changes in the expected default rates of the underlying mortgages will significantly affect the value of the Company, the income it accrues and the cash flow it receives. An increase in default rates will reduce the book value of the Company's assets and the Company earnings and cash flow available to fund operations and pay dividends. This change in value can be independent of changes in spreads, as actual credit experience and pricing of credit are not necessarily correlated.

The Company manages credit risk through the underwriting process, establishing loss assumptions, and careful monitoring of loan performance. Before acquiring a security that represents a pool of loans, the Company will perform a rigorous analysis of the quality of substantially all of the loans proposed for that security. As a result of this analysis, loans with unacceptable risk profiles will be removed from the proposed security. Information from this review is then used to establish loss assumptions. The Company will assume that a certain portion of the loans will default and calculate an expected, or loss adjusted yield based on that assumption. 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 timing experience is likely to cause a reduction in the expected yield and therefore reduce the earnings of the Company, and may require a significant write down of assets.

For purposes of illustration, a doubling of the losses in the Company's credit sensitive portfolio, without a significant acceleration of those losses would reduce the expected yield on adjusted purchase price from 9.78% to 8.35%. This would reduce GAAP income going forward by approximately \$0.15 per common share and cause a significant write down in assets at the time the loss assumption is changed. The amount of the write-down depends on several factors but it could be in excess of \$100 per share.

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 objective of the Company 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

Edgar Filing: ANTHRACITE CAPITAL INC - Form 10-Q

securities.

The Company uses interest rate duration as its primary measure of interest rate risk. This metric, expressed when considering any existing leverage, allows the Company's management to approximate changes in the net market value of the Company's portfolio given potential changes in the U.S. Treasury yield curve. Interest