ANTHRACITE CAPITAL INC
Form 10-Q
August 09, 2007
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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2007

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from: to

Commission File Number 001-13937

ANTHRACITE CAPITAL, INC.

(Exact name of registrant as specified in its charter)

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

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

NOT APPLICABLE
(Former name, former address, and for new fiscal year; if changed since last report)

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

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of ‘‘accelerated filer and large accelerated filer’’ in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

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

Yes No

At August 9, 2007, 64,291,460 shares of common stock ($.001 par value per share) were outstanding.

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Cautionary Statement Regarding Forward-Looking Statements

Certain statements contained herein constitute ''forward-looking statements'' within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to future financial or business performance, strategies or expectations. Forward-looking statements are typically identified by words or phrases such as ''trend,'' ''opportunity,'' ''pipeline,'' ''believ ''comfortable,'' ''expect,'' ''anticipate,'' ''current,'' ''intention,'' ''estimate,'' ''position,'' ''assume,'' ''potential,'' ''outlook ''maintain,'' ''sustain,'' ''seek,'' ''achieve'' and similar expressions, or future or conditional verbs such as ''will,'' ''would,'' ''could,'' ''may'' or similar expressions. Anthracite Capital, Inc. (the ''Company'') cautions that forward-looking statements are subject to numerous assumptions, risks and uncertainties, which change over time. Forward-looking statements speak only as of the date they are made, and the Company assumes no duty to and does not undertake to update forward-looking statements. Actual results could differ materially from those anticipated in forward-looking statements and future results could differ materially from historical performance.

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

(1) the introduction, withdrawal, success and timing of business initiatives and strategies;
(2) changes in political, economic or industry conditions, the interest rate environment or financial and capital markets, which could result in changes in the value of the Company's assets;
(3) the relative and absolute investment performance and operations of BlackRock Financial Management, Inc. (''BlackRock''), the Company's Manager;
(4) the impact of increased competition;
(5) the impact of future acquisitions or divestitures;
(6) the unfavorable resolution of legal proceedings;
(7) the impact of legislative and regulatory actions and reforms and regulatory, supervisory or enforcement actions of government agencies relating to the Company or BlackRock;
(8) terrorist activities and international hostilities, which may adversely affect the general economy, domestic and global financial and capital markets, specific industries, and the Company;
(9) the ability of BlackRock to attract and retain highly talented professionals;
(10) fluctuations in foreign currency exchange rates; and
(11) the impact of changes to tax legislation and, generally, the tax position of the Company.

The Company's Annual Report on Form 10-K for the year ended December 31, 2006 and the Company's subsequent reports filed with the SEC, accessible on the SEC's website at www.sec.gov, identify additional factors that can affect forward-looking statements.

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Part I — FINANCIAL INFORMATION

Item 1. Financial Statements
Anthracite Capital, Inc. and Subsidiaries
Consolidated Statements of Financial Condition
(in thousands, except share data)

	June 30, 2007 (unaudited)		December 31, 2006	
ASSETS				
Cash and cash equivalents		$ 107,716		$ 66,388
Restricted cash equivalents		19,253		59,801
Securities available-for-sale, at fair value				
Subordinated commercial mortgage-backed securities (‘‘CMBS’’)	$1,006,794		$ 883,432	
Investment grade CMBS	1,633,459		1,588,284	
Residential mortgage-backed securities (‘‘RMBS’’)	128,776		144,140	
Total securities available-for-sale		2,769,029		2,615,856
Commercial mortgage loan pools, at amortized cost		1,252,111		1,271,014
Securities held-for-trading, at estimated fair value				
CMBS	21,169		22,383	
RMBS	919		132,204	
Total securities held-for-trading		22,088		154,587
Commercial mortgage loans, net		883,787		481,745
Equity investments		195,846		182,147
Derivative instruments, at fair value		429,809		317,574
Receivable for investment sold		25,000		—
Other assets		81,855		69,151
Total Assets		$5,786,494		$5,218,263
LIABILITIES AND STOCKHOLDERS’ EQUITY				
Liabilities:				
Borrowings:				
Collateralized debt obligations (‘‘CDOs’’)	$1,815,679		$1,812,574	
Secured by pledge of subordinated CMBS	147,305		48,628	
Secured by pledge of other securities available-for-sale and cash equivalents	626,522		666,275	
Secured by pledge of commercial mortgage loan pools	1,236,996		1,256,897	
Secured by pledge of securities held-for-trading	—		127,249	
Secured by pledge of commercial mortgage loans	247,479		26,570	
Senior unsecured notes	162,500		75,000	
Junior unsecured notes	67,528		—	
Junior subordinated notes to subsidiary trust issuing preferred securities	180,477		180,477	
Total borrowings		4,484,486		4,193,670
Payable for investments purchased		66,211		23,796
Distributions payable		21,343		17,669
Derivative instruments, at fair value		394,972		304,987
Other liabilities		24,740		22,032
Total Liabilities		4,991,752		4,562,154
Commitments and Contingencies				
Stockholders’ Equity:				
Common Stock, par value $0.001 per share; 400,000,000 shares authorized; 64,194,747 shares issued and outstanding in 2007; 57,830,964 shares issued and outstanding in 2006		64		58
		55,435		55,435

9.375% Series C Preferred stock, liquidation preference $57,500		
8.25% Series D Preferred stock, liquidation preference $86,250	83,267	—
Additional paid-in capital	701,326	629,785
Distributions in excess of earnings	(112,496)	(120,976)
Accumulated other comprehensive income	67,146	91,807
Total Stockholders' Equity	794,742	656,109
Total Liabilities and Stockholders' Equity	$5,786,494	$5,218,263

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

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

	For the Three Months Ended June 30		For the Six Months Ended June 30	
	2007	2006	2007	2006
Income:				
Interest from securities available-for-sale	$ 49,075	$ 43,080	$ 95,748	$ 81,977
Interest from commercial mortgage loans	18,282	8,973	29,449	16,989
Interest from commercial mortgage loan pools	13,002	13,287	26,133	26,513
Interest from securities held-for-trading	382	1,847	1,888	3,771
Earnings from equity investments	12,413	9,674	22,369	19,016
Interest from cash and cash equivalents	939	580	1,863	918
Total income	94,093	77,441	177,450	149,184
Expenses:				
Interest	60,085	49,529	114,450	94,160
Interest – securities held-for-trading	—	1,829	1,474	3,722
Management and incentive fees	7,729	5,503	14,682	9,724
General and administrative expense	1,519	1,135	2,824	2,238
Total expenses	69,333	57,996	133,430	109,844
Other gains (losses):				
Gain (loss) on sale of securities available-for-sale, net	158	(93)	6,908	(60)
Gain on securities held-for-trading, net	388	1,365	371	2,315
Foreign currency gain	1,371	271	2,855	315
Loss on impairment of assets	(2,900)	(4,653)	(4,098)	(5,434)
Total other gains (losses)	(983)	(3,110)	6,036	(2,864)
Income from Continuing Operations	23,777	16,335	50,056	36,476
Income from Discontinued Operations	—	1,366	—	1,366
Net income	23,777	17,701	50,056	37,842
Dividends on preferred stock	3,127	1,348	5,403	2,696

Net income available to common stockholders	$ 20,650	$ 16,353	$ 44,653	$ 35,146
Net income per common share, basic:	$ 0.35	$ 0.29	$ 0.76	$ 0.62
Net income per common share, diluted:	$ 0.34	$ 0.29	$ 0.76	$ 0.62
Income from continuing operations per share of common stock, after preferred dividends				
Basic	$ 0.35	$ 0.26	$ 0.76	$ 0.60
Diluted	$ 0.34	$ 0.26	$ 0.76	$ 0.60
Income from discontinued operations per share of common stock				
Basic	$ —	$ 0.03	$ —	$ 0.02
Diluted	$ —	$ 0.03	$ —	$ 0.02
Weighted average number of shares outstanding:				
Basic	59,568,536	57,065,593	58,715,762	56,869,865
Diluted	59,891,468	57,354,817	58,878,837	57,016,222
Dividend declared per share of common stock	$ 0.30	$ 0.29	$ 0.59	$ 0.57

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

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Anthracite Capital, Inc. and Subsidiaries
Consolidated Statement of Changes in Stockholders' Equity (Unaudited)
For the Six Months Ended June 30, 2007
(in thousands)

	Common Stock, Par Value	Series C Preferred Stock	Series D Preferred Stock	Additional Paid-In Capital	Distributions In Excess Of Earnings	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income	Total Stockholders' Equity
Balance at January 1, 2007	$58	$55,435		$629,785	$(120,976)	$ 91,807		$656,109
Net income					50,056		$ 50,056	50,056
Unrealized gain on cash flow hedges						32,665	32,665	32,665
Reclassification adjustments from cash flow hedges included in net income						763	763	763
Foreign currency translation						(58)	(58)	(58)
Change in net unrealized gain on securities available-for-sale, net						(58,031)	(58,031)	(58,031)

of reclassification adjustment								
Other comprehensive income							(24,661)	
Comprehensive income							$ 25,395	
Dividends declared-common stock					(36,173)			(36,173)
Dividends on preferred stock					(5,403)			(5,403)
Issuance of common stock	6			71,541				71,547
Issuance of preferred stock			83,267					83,267
Balance at June 30, 2007	$64	$55,435	$83,267	$701,326	$(112,496)	$ 67,146		$794,742

Disclosure of reclassification adjustment:

	For the six months ended June 30, 2007
Unrealized holding loss on securities available-for-sale	$ (64,939)
Reclassification for realized gains previously recorded as unrealized	6,908
	(58,031)

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

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

	For the Six Months Ended June 30, 2007	For the Six Months Ended June 30, 2006
Cash flows from operating activities:		
Net income	$ 50,056	$ 37,842

Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Net decrease in trading securities	132,870	22,509
Net gain on sale of securities	(7,279)	(2,255)
Gain on sale of real estate held for sale	—	(1,366)
Earnings from subsidiary trust	(209)	(201)
Distributions from subsidiary trust	209	171
Earnings from equity investments	(22,369)	(19,016)
Distributions of earnings from equity investments	8,878	8,659
Amortization of collateralized debt obligation issuance costs	1,794	1,171
Amortization of junior subordinated note issuance costs	92	76
Amortization of senior unsecured notes issuance costs	94	—
Discount accretion (net)	(5,525)	(2,613)
Loss on impairment of assets	4,098	5,434
Unrealized net foreign currency gain	(7,152)	(7,772)
Non-cash management and incentive fees	2,893	1,668
Proceeds from sale of interest rate swap agreements	8,175	15,102
Decrease increase in other assets	(8,911)	22,333
Increase (decrease) in other liabilities	5,065	(5,599)
Net cash provided by operating activities	162,779	76,143
Cash flows from investing activities:		
Purchase of securities available-for-sale	(215,210)	(506,068)
Proceeds from sale of securities available-for-sale	50,335	73,563
Principal payments received on securities available-for-sale	42,659	24,643
Funding of commercial mortgage loans	(574,980)	(123,779)
Repayments received from commercial mortgage loans	155,173	65,981
Repayments received from commercial mortgage loan pools	12,436	4,344
Purchase of real estate held-for-sale	—	(5,435)
Proceeds from sale of real estate held-for-sale	—	6,801
Increase (decrease) in restricted cash equivalents	40,548	(52,401)
Return of capital from equity investments and joint ventures	—	14,742
Investment in equity investments	(25,209)	(55,990)
Net cash used in investing activities	(514,248)	(553,599)

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

	For the Six Months Ended June 30, 2007	For the Six Months Ended June 30, 2006
Cash flows from financing activities:		

Net increase (decrease) increase in borrowings under reverse repurchase agreements and credit facilities	150,615	(5,659)
Repayments of borrowings secured by commercial mortgage loan pools	(12,849)	(3,994)
Issuance of collateralized debt obligations	23,875	417,000
Issuance costs for collateralized debt obligations	(1,518)	(7,057)
Repayments of collateralized debt obligations	(29,447)	(1,353)
Issuance of junior subordinated notes to subsidiary trust	—	100,000
Issuance costs of junior subordinated notes	—	(3,146)
Issuance of senior unsecured notes	87,500	—
Issuance costs of senior unsecured notes	(2,456)	
Issuance of junior unsecured notes	67,528	—
Issuance costs of junior unsecured notes	(2,113)	—
Dividends paid on preferred stock	(4,217)	(2,695)
Proceeds from issuance of preferred stock, net of offering costs	83,267	6,764
Proceeds from issuance of common stock, net of offering costs	66,297	—
Dividends paid on common stock	(33,685)	(31,749)
Net cash provided by financing activities	392,797	468,111
Net increase (decrease) in cash and cash equivalents	41,328	(9,345)
Cash and cash equivalents, beginning of period	66,388	40,556
Cash and cash equivalents, end of period	$ 107,716	$ 31,211
	2007	2006
Supplemental disclosure of cash flow information:		
Interest paid	$ 109,355	$ 93,843
Investments purchased not settled	$ 66,211	$ 11,996
Investments sold not settled	$ 25,000	$ 21,372
Supplemental disclosure of non-cash investing and financing activities:		
Investments in subsidiary trusts	$ —	$ 3,097
Incentive fees paid by the issuance of common stock	$ 5,250	$ 1,287

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)
(Dollar amounts in thousands, except share and per share data)

Note 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Anthracite Capital, Inc., a Maryland corporation, and its subsidiaries (the ‘‘Company’’) is a specialty finance company that invests in commercial real estate assets on a global basis. The Company primarily generates income based on the spread between the interest income, gains and net operating income on its commercial real estate assets and the interest expense from borrowings 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 United States Internal Revenue Code of 1986, as amended (the ‘‘Code’’) and, therefore, its income is largely exempt from corporate taxation. The Company commenced operations on March 24, 1998.

The Company's ongoing investment activities primarily encompass three core investment activities:

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

The accompanying June 30, 2007 unaudited consolidated financial statements have been prepared in conformity with the instructions to Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (''GAAP'') for complete financial statements. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and changes in cash flows have been made. These consolidated financial statements should be read in conjunction with the annual audited financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2006 filed with the Securities and Exchange Commission (the ''SEC'').

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

Recent Accounting Developments

Reverse Repurchase Agreements

In July 2007, the FASB issued proposed FSP FAS 140-d, Accounting for Transfers of Financial Assets and Repurchase Financing Transactions. The FASB currently seeks written comments on the proposed FSP, which addresses the accounting for the transfer of financial assets and a subsequent repurchase financing. The proposed FSP focuses on the circumstances that would permit a transferor and a transferee to separately evaluate the accounting for a transfer of a financial asset and a repurchase financing under SFAS No. 140, Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.

The proposed FSP states that a transfer of a financial asset and a repurchase agreement involving the transferred financial asset should be considered part of the same arrangement when the counterparties to the two transactions are the same unless certain criteria are met. The criteria in the proposed FSP are intended to identify whether (1) there is a valid and distinct business or economic

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purpose for entering separately into the two transactions and (2) the repurchase financing does not result in the initial transferor regaining control over the previously transferred financial assets. The FASB has stated that the proposed FSP's purpose is to limit diversity of practice in accounting for these situations, resulting in more consistent financial reporting. Consequently, the FASB has stated that it is the FASB's desire to have the proposed FSP effective as soon as practicable.

Currently, the Company records such assets and the related financing gross on its consolidated statement of financial condition, and the corresponding interest income and interest expense gross on the consolidated statement of operations. Any change in fair value of the security is reported through other comprehensive income pursuant to SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, because the security is classified as available-for-sale. However, in a transaction where the mortgage-backed securities are acquired from and financed under a repurchase agreement with the same counterparty, the acquisition may not qualify as a sale from the seller's perspective under the provisions of SFAS No. 140. In such cases, the seller may be required to continue to consolidate the assets sold to the Company, based on their continuing involvement with such investments. Depending on the ultimate outcome of the accounting standard setters' deliberations, the Company may be precluded from presenting the assets gross on the Company's consolidated statement of financial condition and should instead be treating the Company's net investment in such assets as a derivative. If it is determined that these transactions should be treated as investments in derivatives, the derivative instruments entered into by the Company to hedge the Company's interest rate exposure with respect to the borrowings under the associated repurchase agreements may no longer qualify for hedge accounting, and would then, as with the underlying asset transactions, also be marked to market through the consolidated statement of operations. This potential change in accounting treatment does not affect the economics of the transactions but does affect how the transactions would be reported on the Company's consolidated financial statements. The Company's cash flows, liquidity and ability to pay a dividend would be unchanged, and the Company does not believe its REIT taxable income or REIT status would be affected. The Company believes net equity would not be materially affected. At June 30, 2007, the Company has identified available-for-sale securities with a fair value of approximately $30,956 which had been purchased from and financed with reverse repurchase agreements totaling approximately $26,002 with the same counterparty since their purchase. If the Company were to change the current accounting treatment for these transactions at June 30, 2007 to that required by the proposed FSP, total assets and total liabilities would be reduced by approximately $26,002.

Investment Companies

In June, 2007, the American Institute of Certified Public Accountants (''AICPA'') issued Statement of Position (''SOP'') 07-1, Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting for Parent Companies and Equity Method Investors for Investments in Investment Companies. This SOP provides guidance for determining whether an entity is within the scope of the AICPA Audit and Accounting Guide Investment Companies the ''Guide''. Entities that are within the scope of the Guide are required, among other things, to carry their investments at fair value, with changes in fair value included in earnings. The provisions of this SOP are effective for the Company on January 1, 2008. The Company is currently evaluating this new guidance and has not determined whether it will be required to apply the provisions of the Guide in presenting its financial statements.

Fair Value Accounting

In February 2007, the Financial Accounting Standards Board (''FASB'') issued Statement of Financial Accounting Standards (''SFAS No. 159''), The Fair Value Option for Financial Assets and Financial Liabilities. SFAS No. 159 permits entities to choose to measure eligible financial instruments at fair value. The unrealized gains and losses on items for which the fair value option has been elected should be reported in earnings. The decision to elect the fair value option is determined on an instrument by instrument basis, it should be applied to an entire instrument, and it is irrevocable. Assets and liabilities measured at fair value pursuant to the fair value option should be reported

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separately in the consolidated statement of financial condition from those instruments measured using another measurement attribute. SFAS No. 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. The Company currently is analyzing the potential impact of adoption of SFAS No. 159 to its consolidated financial statements.

Variable Interest Entities

The consolidated financial statements include the financial statements of Anthracite Capital, Inc. and its subsidiaries, which are wholly owned or controlled by the Company or entities which are variable interest entitites (‘‘VIEs’’) in which the Company is the primary beneficiary under FASB Interpretation No. 46, Consolidation of Variable Interest Entities (revised December 2003) (‘‘FIN 46R’’). FIN 46R requires a VIE to be consolidated by its primary beneficiary. The primary beneficiary is the party that absorbs the majority of the VIE’s anticipated losses and/or the majority of the expected returns. All inter-company balances and transactions have been eliminated in consolidation.

The Company considers the CMBS securities where it maintains the right to influence the foreclosure/workout process on the underlying loans its controlling class CMBS (‘‘Controlling Class’’). The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the qualifying special-purpose entity (‘‘QSPE’’) criteria. However, there is uncertainty with respect to QSPE treatment due to ongoing review by accounting standard setters, potential actions by various parties involved with the QSPE, as well as varying and evolving interpretations of the QSPE criteria under SFAS No. 140. Future guidance from the accounting standard setters may require the Company to evaluate these trusts for possible consolidation under FIN 46R.

Certain Hybrid Financial Instruments

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, which amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, and SFAS No. 140. SFAS No. 155 provides, among other things, that:

- For embedded derivatives which would otherwise be required to be bifurcated from their host contracts and accounted for at fair value in accordance with SFAS No. 133, an irrevocable election may be made on an instrument-by-instrument basis, to be measured as hybrid financial instrument at fair value in its entirety, with changes in fair value recognized in earnings.
- Concentrations of credit risk in the form of subordination are not considered embedded derivatives.
- Clarification regarding interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133.

SFAS No. 155 is effective for all financial instruments acquired, issued or subject to remeasurement after the beginning of an entity’s first fiscal year that begins after September 15, 2006. Upon adoption, differences between the total carrying amount of the individual components of an existing bifurcated hybrid financial instrument and the fair value of the combined hybrid financial instrument should be recognized as a cumulative effect adjustment to beginning retained earnings. Prior periods should not be restated. The adoption of SFAS No. 155 on January 1, 2007 did not have an impact on the Company’s consolidated financial statements.

Accounting for Uncertainty in Income Taxes

In July 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes and Related Implementation Issues (‘‘FIN 48’’). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a Company’s financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 prescribes a threshold and measurement attribute for

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recognition in the financial statements of an asset or liability resulting from a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective as of the beginning of fiscal years that begin after December 15, 2006. The adoption of FIN 48 on January 1, 2007 did not have a material impact on the Company's consolidated financial statements.

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of their financial instruments according to a fair value hierarchy (i.e., levels 1, 2, and 3, as defined). Additionally, companies are required to provide enhanced disclosure regarding instruments in the level 3 category (which have inputs to the valuation techniques that are unobservable and require significant management judgment), including a reconciliation of the beginning and ending balances separately for each major category of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and all interim periods within those fiscal years. The Company currently is evaluating the impact adoption will have on its consolidated financial statements.

Note 2 NET INCOME PER SHARE

Net income per share is computed in accordance with SFAS No. 128, Earnings Per Share. Basic income per share is calculated by dividing net income available to common stockholders by the weighted average number of shares of common stock outstanding during the period. Diluted income per share is calculated using the weighted average number of shares of common stock 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.

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2007	2006	2007	2006
Numerator:				
Net income available to common stockholders	$ 20,650	$ 16,353	$ 44,653	$ 35,146
Numerator for basic and diluted earnings per share	$ 20,650	$ 16,353	$ 44,653	$ 35,146
Denominator:				
Denominator for basic earnings per share – weighted average common shares outstanding	59,568,356	57,065,593	58,715,762	56,869,865
Dilutive effect of stock options	2,480	3,741	2,760	3,616
Dilutive effect of stock based incentive fee	320,632	285,483	160,315	142,741
Denominator for diluted earnings per share – weighted average common shares outstanding and common stock equivalents outstanding	59,891,468	57,354,817	58,878,837	57,016,222
Basic net income per weighted average common share:	$ 0.35	$ 0.29	$ 0.76	$ 0.62

Diluted net income per weighted average common share and common share equivalents:	$ 0.34	$ 0.29	$ 0.76	$ 0.62

Total anti-dilutive stock options excluded from the calculation of net income per share were 1,380,151 for the three and six months ended June 30, 2007. Total anti-dilutive stock options excluded from the calculation of net income per share were 1,384,151 for the three and six months ended June 30, 2006.

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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 at June 30, 2007 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
CMBS:				
CMBS interest only securities (''IOs'')	$ 61,713	$ 1,194	$ (2,781)	$ 60,126
Investment grade CMBS	846,716	39,906	(12,841)	873,781
Non-investment grade rated subordinated securities	805,938	50,793	(22,554)	834,177
Non-rated subordinated securities	97,263	11,294	(152)	108,405
Credit tenant leases	24,147	244	(989)	23,402
Investment grade REIT debt	247,802	3,180	(3,980)	247,002
Multifamily agency securities	438,676	484	(10,011)	429,149
CDO investments	66,135	9,770	(11,694)	64,211
Total CMBS	2,588,390	116,865	(65,002)	2,640,253
RMBS:				
Agency adjustable rate securities	1,256	9	—	1,265
Residential CMOs	119,843	75	(2,306)	117,612
Hybrid adjustable rate mortgages (''ARMs'')	10,129	—	(230)	9,899
Total RMBS	131,228	84	(2,536)	128,776
Total securities available-for-sale	$ 2,719,618	$ 116,949	$ (67,538)	$ 2,769,029

At June 30, 2007, the Company's securities available-for-sale included non-U.S. dollar denominated assets with an estimated fair value of $343,862.

At June 30, 2007, an aggregate of $2,480,060 in estimated fair value of the Company's securities available-for-sale was pledged to secure its collateralized borrowings.

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 June 30, 2007.

	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
CMBS IOs	$ 26,218	$ (1,081)	$ 23,015	$ (1,700)	$ 49,233	$ (2,781)
Investment grade CMBS	163,986	(3,293)	137,529	(9,548)	301,515	(12,841)
Non-investment grade rated subordinated securities	271,832	(13,093)	123,178	(9,461)	395,010	(22,554)
Non-rated subordinated securities	11,242	—	2,406	(152)	13,648	(152)
Credit tenant leases	—	—	15,174	(989)	15,174	(989)
Investment grade REIT debt	25,420	(296)	71,962	(3,684)	97,382	(3,980)
Multifamily agency securities	101,994	(1,279)	265,315	(8,732)	367,309	(10,011)
CDO investments	10,116	(9,511)	33,522	(2,183)	43,638	(11,694)
Residential CMOs	36,518	(108)	80,833	(2,198)	117,351	(2,306)
Hybrid ARMs	—	—	9,898	(230)	9,898	(230)
Total temporarily impaired securities	$ 647,326	$ (28,661)	$ 762,832	$ (38,877)	$ 1,410,158	$ (67,538)

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The temporary impairment of the available-for-sale securities results from the fair value of the securities falling below the amortized cost basis. These unrealized losses are primarily the result of market factors other than credit impairment and the Company believes the carrying value of the securities are fully recoverable over their expected holding period. At June 30, 2007, management had both the intent and the ability to hold the securities until the amortized cost was recovered and concluded that none of the securities are other than temporarily impaired.

Due to unanticipated changes in market conditions subsequent to June 30, 2007, the Company sold a portion of its high credit quality liquid securities to further increase its liquidity. The sale of these securities, which consisted of CMBS IOs and multifamily agency securities, generated a loss which will be reported in the statement of operations for the third quarter of 2007.

The CMBS held by the Company consist of subordinated securities collateralized by adjustable and fixed rate commercial and multifamily mortgage loans. The CMBS provide credit support to the more senior classes of the related commercial securitization. The Company generally does not own the senior classes of its below investment grade CMBS. Cash flows from the mortgages underlying the CMBS generally is allocated first to the senior classes, with the most senior class having a priority entitlement to cash flow. Then, any remaining cash flow is allocated generally among the other CMBS classes in order of their relative seniority. To the extent there are defaults and unrecoverable losses on the underlying mortgages, resulting in reduced cash flows, the most subordinated CMBS class will bear this loss first. To the extent there are losses in excess of the most subordinated class' stated entitlement to principal and interest, the remaining CMBS classes will bear such losses in order of their relative subordination.

At June 30, 2007, the anticipated weighted average unlevered yield based upon the adjusted cost of the Company's entire subordinated CMBS portfolio was 10.1% per annum. The anticipated reported yield of the Company's investment grade securities available-for-sale was 6.1%. 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, liquidations, and related expenses), the pass-through or coupon rate, and interest rate fluctuations. Additional factors that may affect the Company's anticipated yields to maturity on its Controlling Class CMBS include interest payment shortfalls due to delinquencies on the underlying mortgage loans, and the timing and magnitude of credit losses on the mortgage loans underlying the Controlling Class CMBS that are a result of the general condition of the real estate market (including competition for tenants and their related credit quality), and changes in market rental rates. As these uncertainties and contingencies are difficult to predict and are subject to future events that may alter these assumptions, no assurance can be given that the anticipated yields to maturity, discussed above and elsewhere, will be achieved.

The RMBS held by the Company consist of adjustable rate and fixed rate residential pass-through or mortgage-backed securities collateralized by adjustable and fixed rate single-family residential mortgage loans. All of the Company's RMBS were issued by FHLMC, FNMA or GNMA. The Company does not have any subprime exposure. The Company's securities available-for-sale are subject to credit, interest rate, and/or prepayment risks. The agency adjustable rate RMBS held by the Company are subject to periodic and lifetime caps that limit the amount the interest rates of such securities can change during any given period and over the life of the loan. At June 30, 2007, adjustable rate RMBS with an estimated fair value of $128,775 was included in securities available-for-sale on the consolidated statements of financial condition.

Note 4 IMPAIRMENTS — CMBS

The Company updates its estimated cash flows for securities subject to Emerging Issues Task Force Issue 99-20, Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets (''EITF 99-20'') on a quarterly basis. The Company compares the yields resulting from the updated cash flows to the current accrual yields. An impairment charge is required under EITF 99-20 if the updated yield is lower than the current accrual

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yield and the security has a market value less than its adjusted purchase price. The Company carries all these securities at their market value on its consolidated statement of financial condition.

For the six months ended June 30, 2007, changes in timing of assumed credit loss and prepayments on three CMBS required an impairment charge totaling $2,777. The Company also increased its underlying loss expectations for one below investment grade European CMBS during the six months ended June 30, 2007, resulting in an additional impairment charge of $1,321. During the quarter ended June 30, 2007, 45 of the Company's Controlling Class CMBS with an aggregate adjusted purchase price of $159,637 experienced a weighted average yield increase of 68 basis points and 22 Controlling Class CMBS with an aggregate adjusted purchase price of $176,960 experienced a weighted average yield decrease of nine basis points.

For the six months ended June 30, 2006, the Company had eight CMBS that required an impairment charge of $5,434, of which $4,226 was attributed to higher prepayment rates on a pool of Small Business Administration commercial mortgages. The decline in the updated yields that caused the impairments was not related to increases in losses but rather changes in the timing of credit losses and prepayments. Based on current economic conditions, the Company believes the impairments will be recovered over the remaining life of the bonds.

Note 5 COMMERCIAL MORTGAGE LOAN POOLS

During the second quarter of 2004, the Company acquired subordinated CMBS in a trust establishing a Controlling Class interest. The Company obtained a greater degree of influence over the disposition of the commercial mortgage loans than is typically granted to the special servicer. As a result of this expanded influence, the trust was not a QSPE and FIN 46R required the Company to consolidate the net assets and results of operations of the trust.

Approximately 45% of the par amount of the commercial mortgage loan pool is comprised of investment grade loans and the remaining 55% are unrated. For income recognition purposes, the Company considers the investment grade and unrated commercial mortgage loans in the pool as single assets reflecting the credit assumptions made in establishing loss adjusted yields for Controlling Class securities. The Company has taken into account the credit quality of the underlying loans in formulating its loss assumptions. Credit losses assumed on the entire pool are 1.40% of the principal balance, or 2.53% of the unrated principal balance.

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

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Note 6 COMMERCIAL MORTGAGE LOANS

The following table summarizes the Company’s commercial real estate loan portfolio by property type at June 30, 2007 and December 31, 2006:

	Loan Outstanding				Weighted Average Yield	
	June 30, 2007		December 31, 2006			
Property Type	Amount	%	Amount	%	2007	2006
Retail	$ 374,319	42.4%	$ 194,938	40.5%	7.7%	