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ANTHRACITE CAPITAL INC

Form 10-K

March 16, 2007

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

(Mark one)

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2006

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 No. 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.)

40 East 52nd Street  
New York, New York  
(Address of principal executive office)

10022  
(Zip Code)

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

Securities registered pursuant to Section 12(b) of the Act:

COMMON STOCK, \$0.001 PAR VALUE	NEW YORK STOCK EXCHANGE
9.375% SERIES C CUMULATIVE REDEEMABLE PREFERRED STOCK, \$0.001 PAR VALUE	NEW YORK STOCK EXCHANGE
8.25% SERIES D CUMULATIVE REDEEMABLE PREFERRED STOCK, \$0.001 PAR VALUE	NEW YORK STOCK EXCHANGE
(Title of each class)	(Name of each exchange on which registered)

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Securities registered pursuant to Section 12(g) of the Act: Not Applicable

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes ☐ No ☒

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 if disclosure of delinquent filers pursuant to item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

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 on the Exchange Act Rule).  
Large accelerated filer [ ] Accelerated filer [X] Non-accelerated filer [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The aggregate market value of the registrant's Common Stock, \$.001 par value, held by non-affiliates of the registrant, computed by reference to the closing sale price of \$12.16 as reported on the New York Stock Exchange on June 30, 2006, was \$688,497,461 (for purposes of this calculation, affiliates include only directors and executive officers of the registrant).

The number of shares of the registrant's Common Stock, \$.001 par value, outstanding as of March 16, 2007 was 57,843,696 shares.

Documents Incorporated by Reference: Portions of the registrant's Definitive Proxy Statement for the 2007 Annual Meeting of Stockholders are incorporated by reference into Part III.

ANTHRACITE CAPITAL, INC. AND SUBSIDIARIES  
2006 FORM 10-K ANNUAL REPORT

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#### CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

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

In addition to factors previously disclosed in the Company's Securities and Exchange Commission (the "SEC") reports and those identified elsewhere in this

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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. (the "Manager");
- (4) the impact of increased competition;
- (5) the impact of capital improvement projects;
- (6) the impact of future acquisitions or divestitures;
- (7) the unfavorable resolution of legal proceedings;
- (8) the extent and timing of any share repurchases;
- (9) the impact, extent and timing of technological changes and the adequacy of intellectual property protection;
- (10) the impact of legislative and regulatory actions and reforms and regulatory, supervisory or enforcement actions of government agencies relating to the Company, the Manager, Merrill Lynch & Co., Inc. or The PNC Financial Services Group, Inc.;
- (11) terrorist activities and international hostilities, which may adversely affect the general economy, domestic and global financial and capital markets, specific industries, the Company and the Manager;
- (12) the ability of the Manager to attract and retain highly talented professionals;
- (13) fluctuations in foreign currency exchange rates;
- (14) the impact of changes to tax legislation and, generally, the tax position of the Company;
- (15) the Manager's ability to successfully integrate the Merrill Lynch Investment Managers ("MLIM") business with its existing business; and
- (16) the ability of the Manager to effectively manage the former MLIM assets along with its historical assets under management.

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

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### ITEM 1. BUSINESS

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

#### General

Anthracite Capital, Inc., a Maryland corporation, and subsidiaries (collectively, the "Company") is a specialty finance company that invests in commercial real estate assets on a global basis. The Company seeks to generate income from 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's primary activities are investing in high yielding commercial real estate debt and equity. The Company combines traditional real estate underwriting and capital markets expertise to maximize the opportunities arising from the continuing integration of these two disciplines. The Company focuses on acquiring pools of performing loans in the form of commercial mortgage-backed securities ("CMBS"), issuing secured debt backed by CMBS and providing strategic capital for the commercial real estate industry in the form of mezzanine loan financing. The Company also began investing in diversified portfolios of commercial real estate in the United States during December 2005. The Company commenced operations on March 24, 1998.

The Company's primary investment activities are conducted in three investment sectors:

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

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

The Company's common stock, par value \$0.001 per share ("Common Stock"), is traded on the New York Stock Exchange under the symbol "AHR". The Company's primary long-term objective is to distribute dividends supported by earnings. The Company establishes its dividend by analyzing the long-term sustainability of earnings given existing market conditions and the current composition of its portfolio. This includes an analysis of the Company's credit loss assumptions, general level of interest rates and projected hedging costs.

The Company is managed by BlackRock Financial Management, Inc. (the "Manager"), a subsidiary of BlackRock, Inc., a publicly traded (NYSE:BLK) asset management company with \$1.125 trillion of assets under management at December 31, 2006. The Manager provides an operating platform that incorporates significant asset origination, risk management, and operational capabilities.

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The following table indicates the amounts of each category of commercial real estate securities the Company owned at December 31, 2006. The dollar price ("Dollar Price") represents the estimated fair value or adjusted purchase price of a security, respectively, relative to its par value.

Commercial Real Estate Securities	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price*	Dollar Price	Loss Adjusted Yield
-----	-----	-----	-----	-----	-----	-----
Controlling Class CMBS	\$ 909,977	\$ 587,008	\$ 64.51	\$ 541,571	\$59.64	10.25%
Other Below Investment Grade CMBS	170,187	196,860	115.67	187,909	94.16	7.68%
Collateralized debt obligation ("CDO") investments	406,605	117,246	28.84	114,482	28.16	14.19%
Investment Grade Commercial Real Estate Related Securities	1,504,479	1,523,633	101.27	1,481,256	97.58	6.20%
CMBS interest only securities ("IOs")	2,980,467	69,352	2.33	69,183	2.32	7.36%
	5,971,715	2,494,099	41.77	2,394,401	40.10	7.65%
	-----	-----	-----	-----	-----	-----

\* Represents the amortized cost of the Company's investments.

Included in the table above are non-U.S. dollar denominated commercial real estate securities with a carrying value of \$181,597, \$37,320, and \$4,580 at December 31, 2006, 2005, and 2004, respectively.

The Company's principal activity is to underwrite and acquire high yield CMBS that are rated below investment grade (BB+ or lower). The Company's CMBS are securities backed by pools of loans secured by first mortgages on commercial real estate throughout the United States and Europe. The commercial real estate securing the first mortgages consists of income-producing properties including office buildings, shopping centers, apartment buildings, industrial properties, healthcare properties, and hotels, among others. The terms of a typical loan include a fixed rate of interest, thirty-year amortization, some form of prepayment protection, and a large interest rate increase if not paid off at the ten-year maturity. The loans are originated by various lenders and pooled together in trusts which issue securities in the form of various classes of fixed rate debt secured by the cash flows from the underlying loans. The securities issued by the trusts are rated by one or more nationally recognized credit rating organizations and are rated AAA down to CCC. The security that is affected first by loan losses is not rated. The principal amount of the pools of loans securing the CMBS securities varies.

The Company focuses on acquiring the securities rated below investment grade. The most subordinated CMBS classes are the first to absorb realized losses in the loan pools. To the extent there are losses in excess of the most subordinated class' stated entitlement to principal and interest, then the remaining CMBS classes will bear such losses in order of their relative subordination. If a loss of face value, or par, is experienced in the underlying loans, a corresponding reduction in the par of the lowest rated security occurs, reducing the cash flow entitlement. The majority owner of the first loss position has the right to influence the workout process and therefore designate

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the trust's special servicer. The Company will generally seek to influence the workout process in each of its CMBS transactions by purchasing the majority of the trust's non-rated securities and sequentially rated securities as high as BB+. Typically, the par amount of these below investment grade classes represents 2.0-3.5% of the par of the underlying loan pools. This is known as the subordination level because 2.0% - 3.5% of the collateral balance is subordinated to the senior, investment grade rated securities.

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Owning commercial real estate loans in these forms allows the Company to earn its loss-adjusted returns over a period of time while achieving significant diversification across geographic areas and property types.

### Controlling Class CMBS

At December 31, 2006, the Company owned 29 trusts ("Controlling Class") in which the Company through its investment in subordinated CMBS of such trusts is in the first loss position. As a result of this investment position, the Company influences the workout process on \$42,398,701 of underlying loans. The total par amount owned of these subordinated Controlling Class securities is \$909,977. The Company does not own the senior securities that represent the remaining par amount of the underlying mortgage loans.

Each trust has a designated special servicer. Special servicers are responsible for carrying out loan loss mitigation strategies. In addition, a special servicer will advance funds to a trust to maintain principal and interest cash flows on the trust's securities provided it believes there is a significant probability of recovering those advances from the underlying borrowers. The special servicer is paid interest on advanced funds and a fee for its efforts in carrying out loss mitigation strategies. The special servicer on 25 of the Company's 29 Controlling Class trusts is Midland Loan Services, Inc., the special servicer on two such trusts is GMAC Commercial Mortgage Management, Inc., and the special servicer on the remaining two such trusts is Lennar Partners, Inc. Midland Loan Services, Inc. is a related party of the Manager.

Prior to acquiring Controlling Class securities, the Company performs a significant amount of due diligence on the underlying loans to ensure their risk profiles meet the Company's criteria. Loans that do not meet the Company's criteria are either removed from the pool or price adjustments occur. The debt service coverage and loan to value ratios are evaluated to determine if they are appropriate for each asset class.

As part of its underwriting process, the Company assumes a certain amount of loans will incur losses over time. In performing continuing credit reviews on the 29 Controlling Class trusts, the Company estimates that specific losses totaling \$512,916 related to principal of the underlying loans will not be recoverable, of which \$215,816 is expected to occur over the next five years. The total loss estimate of \$512,916 represents 1.21% of the total underlying loan pools. Due to falling delinquency rates in the CMBS market, the Company no longer assumes an additional layer of unassigned losses. Previously, the Company assumed ten to forty basis points of additional defaults would occur with a 35% loss severity and a one-year recovery period. The effect of this change is to reduce total losses assumed by 15 to 62 basis points, depending on the deal.

The weighted average loss adjusted yield for all subordinated Controlling Class securities at December 31, 2006 was 10.25%. If the loss assumptions prove to be consistent with actual loss experience, the Company will maintain that level of income for the life of the security. As actual losses differ from the original loss assumptions, yields are adjusted to reflect the updated assumptions. In

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addition, a write-down of the adjusted purchase price or write-up of loss adjusted yields of the security may be required. (See Item 7A -"Quantitative and Qualitative Disclosures About Market Risk" for more information on the sensitivity of the Company's income and adjusted purchase price to changes in credit experience.)

Once acquired, the Company uses a performance monitoring system to track the credit experience of the mortgages in the pools securing both the Controlling Class and the other below investment grade CMBS. The Company receives remittance reports monthly from the trustees and monitors any

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delinquent loans or other issues that may affect the performance of the loans. The special servicer of a loan pool also assists in this process. The Company reviews its loss assumptions every quarter using updated payment and debt service coverage information on each loan in the context of economic trends on both a national and regional level.

The Company's anticipated yields on its investments are based upon a number of assumptions that are subject to certain business and economic uncertainties and contingencies. Examples of such contingencies include, among other things, the timing and severity of expected credit losses, the rate and timing of principal payments (including prepayments, repurchases, defaults, liquidations, special servicer fees, and other related expenses), the pass-through or coupon rate, and interest rate fluctuations. Additional factors that may affect the Company's anticipated yields on its Controlling Class CMBS include interest payment shortfalls due to delinquencies on the underlying mortgage loans, the timing and magnitude of credit losses on the mortgage loans underlying the Controlling Class CMBS that are a result of the general condition of the real estate market (including competition for tenants and their related credit quality), and changes in market rental rates. As these uncertainties and contingencies are difficult to predict and are subject to future events which may alter these assumptions, no assurance can be given that the Company's anticipated yields to maturity will be maintained.

### Other Below Investment Grade CMBS

The Company does not typically purchase a BB- or lower rated security unless the Company is involved in the new issue due diligence process and has a clear pari-passu alignment of interest with the special servicer, or can appoint the special servicer. The Company purchases BB+ and BB rated securities at their original issue or in the secondary market without necessarily having influence over the workout process. BB+ and BB rated CMBS do not absorb losses until the BB- and lower rated securities have experienced losses of their entire principal amounts. The Company believes the subordination levels of these securities provide additional credit protection and diversification with an attractive risk return profile.

### CDOs

The Company issues secured term debt through its CDO offerings. This entails creating a special purpose entity that holds assets used to secure the payments required of the debt issued. For those that qualify as a sale under Statement of Financial Accounting Standards ("SFAS") No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities ("SFAS No. 140"), the Company records the transaction as a sale and carries any retained bonds as a component of securities available-for-sale on its consolidated statement of financial condition. At December 31, 2006 and 2005, respectively,



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the Company had retained bonds with an estimated fair value of \$114,142 and \$121,159 on its consolidated statement of financial condition related to CDO HY1 and CDO HY2. The Company also owns preferred securities in LEAFs CMBS I Ltd ("Leaf"). Leaf issued non-recourse liabilities secured by investment grade commercial real estate securities. At December 31, 2006 and 2005, respectively, Leaf preferred securities were carried at an estimated fair value of \$3,104 and \$3,391 on the Company's consolidated statement of financial condition.

### Investment Grade Commercial Real Estate Related Securities

The Company also purchases investment grade commercial real estate related securities in the form of CMBS and unsecured debt of commercial real estate companies. The addition of these higher rated securities is intended to add greater stability to the long-term performance of the Company's portfolio as a whole and to provide greater diversification to optimize secured financing alternatives. The Company seeks to assemble a portfolio of high quality issues that will maintain consistent performance over the

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life of the security.

### CMBS IOs

The Company also acquires CMBS IOs. These securities represent a portion of the interest coupons paid by the underlying loans. The Company views this portfolio as possessing attractive relative value versus other alternatives. These securities do not have significant prepayment risk because the underlying loans generally have prepayment restrictions. Furthermore, the credit risk is also mitigated because the IO represents a portion of all underlying loans, not solely the first loss.

### COMMERCIAL REAL ESTATE LOANS

The following table summarizes the Company's commercial real estate loan portfolio by property type at December 31, 2006, 2005, and 2004:

Property Type	December 31, 2006		Loans Outstanding December 31, 2005		December 31, 2004		Weighted Average Yie	
	Amount	%	Amount	%	Amount	%	2006	2005
Office	\$130,016	27.0%	\$ 94,432	25.8%	\$ 88,311	33.5%	8.2%	8.9%
Residential	57,917	12.0	57,466	15.7	13,480	5.1	10.7	8.6
Retail	194,938	40.5	76,502	20.9	59,070	22.4	7.7	7.3
Hotel	38,899	8.1	79,840	21.8	102,645	39.0	10.0	8.6
Storage	34,009	7.1	32,913	9.0	--	--	9.0	9.1
Communication Tower	--	--	20,000	5.5	--	--	--	9.4
Industrial	19,317	4.0	2,423	0.7	--	--	9.1	8.1
Other Mixed Use	6,649	1.3	2,230	0.6	--	--	8.7	8.1
Total	\$481,745	100.0%	\$365,806	100.0%	\$263,506	100.0%	8.6%	8.5%

Included in the table above are non-U.S. dollar denominated commercial real

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estate loans with a carrying value of \$243,377, \$129,951, and \$21,119 at December 31, 2006, 2005, and 2004, respectively. The Company finances its non-U.S. dollar denominated loans by borrowing in the applicable local currency and hedging the un-financed portion.

The Company's loan activity is focused on providing mezzanine capital to the commercial real estate industry. The Company targets real estate operators with strong track records and compelling business plans designed to enhance the value of their real estate. These loans generally are subordinated to a senior lender or first mortgage and are priced to reflect a higher return. The Company has significant experience in closing large, complex loan transactions and believes it can deliver a timely and competitive financing package.

The types of investments in this class include subordinated participations in first mortgages, loans secured by partnership interests, preferred equity interests in real estate limited partnerships and loans secured by second mortgages. The weighted average life of these investments is generally two to three years and the investments have fixed or floating rate coupons.

The Company performs significant due diligence before making investments to evaluate risks and opportunities in this sector. The Company generally focuses on strong sponsorship, attractive real estate fundamentals, and pricing and structural characteristics that provide significant influence over the underlying asset.

The Company's activity in this sector generally has been conducted through Carbon Capital, Inc. ("Carbon I") and Carbon Capital II, Inc. ("Carbon II", and collectively with Carbon I, the "Carbon

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Capital Funds"), private commercial real estate income funds managed by the Company's Manager. The Company believes the use of the Carbon Capital Funds allows it to invest in larger institutional quality assets with greater diversification. The Company's consolidated financial statements include its share of the net assets and income of the Carbon Capital Funds. At December 31, 2006, the Company owned approximately 20% of Carbon I as well as approximately 26% of Carbon II. The Company's investments in the Carbon Capital Funds at December 31, 2006 were \$72,403, compared with \$59,646 at December 31, 2005.

The following table summarizes the loans held by the Carbon Capital Funds at December 31, 2006, 2005 and 2004.

Property Type	December 31, 2006		Loans Outstanding December 31, 2005		December 31, 2004		Weighted Average Yie	
	Amount	%	Amount	%	Amount	%	2006	2005
Office	\$162,759	23.1%	\$128,802	23.0%	\$135,487	26.1%	10.5%	10.1%
Residential	138,713	19.7	192,604	34.3	164,096	31.6	12.3	10.3
Retail	73,184	10.4	57,791	10.3	101,166	19.5	9.7	13.2
Hotel	241,086	34.2	146,710	26.1	73,249	14.1	12.1	12.8
Storage	--	--	10,171	1.8	10,171	2.0	--	16.4
Land	53,500	7.6	25,000	4.5	--	--	12.6	15.2
Other Mixed Use	35,384	5.0	--	--	34,739	6.7	8.8	--

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Total	\$704,626	100.0%	\$561,078	100.0%	\$518,908	100.0%	11.4%	11.5%
	=====	=====	=====	=====	=====	=====	=====	=====

### COMMERCIAL REAL ESTATE EQUITY

At December 31, 2006, the Company had invested an aggregate of \$92,603 in BlackRock Diamond Property Fund, Inc. ("BlackRock Diamond"). BlackRock Diamond is a private real estate investment trust ("REIT") managed by BlackRock Realty Advisors, Inc., a subsidiary of the Company's Manager. BlackRock Diamond's investment objective is to seek a high risk adjusted return through "value-added" capital appreciation and current income on properties through out the United States. This means the BlackRock Diamond's focuses on operating properties that will be repositioned, renovated, or expanded to achieve maximum returns. Part of the investment strategy includes a budgeted amount of capital expenditures that are used to improve the value of the investment and realize the full value potential of a given property. BlackRock Diamond relies on the Manager's extensive relationships in the real estate markets to source opportunities. BlackRock Diamond focuses on large urban locations where it believes the real estate equity markets will outperform.

BlackRock Diamond is an open-end fund. As such, it allows shares to be redeemed at a price equal to its quarter-end net asset value upon 60 days notice. The assets are subject to quarterly appraisals with one independent appraisal done annually. The Company does not pay a separate management fee to the Manager for management services associated with its investment in BlackRock Diamond.

The Company had a 21% ownership in BlackRock Diamond at December 31, 2006 and recorded \$15,763 of income during 2006 with respect to this investment under the equity method. At December 31, 2006, the Company had \$7,397 of remaining capital commitments to BlackRock Diamond, all of which was called in January 2007.

### FINANCING AND LEVERAGE

The Company has financed its assets with the net proceeds of common stock offerings, the issuance of common stock under the Company's Dividend Reinvestment and Stock Purchase Plan (the "Dividend Reinvestment Plan"), the issuance of preferred stock, long-term secured and unsecured borrowings,

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short-term borrowings under reverse repurchase agreements and the credit facilities discussed below. In the future, operations may be financed by offerings of equity securities, as well as unsecured and secured borrowings. The Company expects that, in general, it will employ leverage consistent with the type of assets acquired and the desired level of risk in various investment environments. The Company's governing documents do not explicitly limit the amount of leverage that the Company may employ. Instead, the Board of Directors has adopted an indebtedness policy for the Company that limits its recourse debt to equity ratio to a maximum of 3.0 to 1. The Company's recourse debt-to-equity ratio of 1.7 to 1 at December 31, 2006 was in compliance with the policy. The Company anticipates that it will maintain recourse debt-to-equity ratios between 1.0 to 1 and 3.0 to 1 in the foreseeable future, although this ratio may be higher or lower at any time. The Board of Directors may change the Company's indebtedness policy at any time.

### REVERSE REPURCHASE AGREEMENTS AND CREDIT FACILITIES

The Company has entered into reverse repurchase agreements to finance its

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securities that are not financed under its credit facilities or CDOs. The reverse repurchase agreements collateralized by most of these securities bear interest at rates that historically have moved in close relationship to the London Interbank Offered Rate for U.S. dollar deposits ("LIBOR").

The Company's credit facilities can be used to replace existing reverse repurchase agreement borrowings and to finance the acquisition of mortgage-backed securities and commercial real estate loans. Outstanding borrowings bear interest at a variable rate. The following table summarizes the Company's credit facilities at December 31, 2006 and 2005:

	Maturity Date	December 31, 2006			December 31, 2005	
		Facility Amount	Total Borrowings	Borrowing Capacity	Facility Amount	Unused Total Borrowing
Greenwich Capital, Inc. (1)	7/7/07	\$ 75,000*	\$12,064	\$ --*	\$ 75,000	\$ 75,000
Deutsche Bank, AG (2)	12/20/07	200,000	49,398	150,602	200,000	181,875
Bank of America, N.A. (3)	9/17/08	100,000	--	100,000	n/a	n/a
Morgan Stanley Bank (3) (4)	2/16/08	200,000	13,985	186,015	27,800	27,800
		-----	-----	-----	-----	-----
		\$575,000	\$75,447	\$436,617	\$302,800	\$284,675
		=====	=====	=====	=====	=====

\* Commitment expired December 23, 2006. No new borrowings permitted.

(1) USD only

(2) Multicurrency

(3) Non-USD only

(4) Can be increased up to \$15,000 based on the change in exchange rates of the non-US dollar loans. However, any amounts drawn under this provision must be repaid in ninety days.

The Company is subject to various covenants in its credit facilities, including maintaining a minimum net worth measured on a book value of \$305,000 in accordance with generally accepted accounting principles in the United States of America ("GAAP"), a maximum recourse debt-to-equity of 3.0 to 1, a minimum cash requirement based upon certain debt-to-equity ratios. During the first quarter of 2007, the Company amended the debt service coverage ratio covenant on its committed debt facilities. The terms of the calculation were revised and the debt service coverage ratio was reduced from 1.75 to 1.20. The revised calculation better reflects the Company's ability to service debt on a cash basis. At December 31, 2006 and 2005, the Company was in compliance with all other covenants.

Under the credit facilities and the reverse repurchase agreements, the respective lenders retain the right to mark the underlying collateral to estimated fair value. A reduction in the value of pledged assets could require the Company to provide additional collateral or fund cash margin calls. From

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time to time, the Company may be required to provide additional collateral or fund margin calls. The Company maintains adequate liquidity to meet such calls.

Further information with respect to the Company's reverse repurchase agreements, credit facilities, and commercial mortgage loan pools at December 31, 2006 is summarized as follows:

	Reverse Repurchase Agreements -----	Credit Facilities -----	Commercial Mortgage Loan Pools -----
Commercial Real Estate Securities			
Outstanding Borrowings	\$527,316	\$ 48,105	\$ --
Weighted average borrowing rate	5.38%	6.91%	--
Weighted average remaining maturity	79 days	243 days	--
Estimated fair value of assets pledged	\$570,864	\$ 69,462*	\$ --
Residential Mortgage-Backed Securities			
Outstanding Borrowings	\$266,731	\$ --	\$ --
Weighted average borrowing rate	5.34%	--	--
Weighted average remaining maturity	79 days	--	--
Estimated fair value of assets pledged	\$275,729	\$ --	\$ --
Commercial Mortgage Loan Pools			
Outstanding Borrowings	\$ 5,623	\$ 772	\$ 1,250,503
Weighted average borrowing rate	6.06%	6.60%	3.99%
Weighted average remaining maturity	8 days	29 days	5.84 years
Estimated fair value of assets pledged	\$ 7,481	\$ 1,209	\$ 1,271,014
Commercial Real Estate Loans			
Outstanding Borrowings	--	\$ 26,570	--
Weighted average borrowing rate	--	6.34%	--
Weighted average remaining maturity	--	245 days	--
Estimated fair value of assets pledged	--	\$ 41,748	--

\* \$21,742 of assets pledged are retained CDO bonds.

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Further information with respect to the Company's reverse repurchase agreements, credit facilities, and commercial mortgage loan pools at December 31, 2005 is summarized as follows:

	Reverse Repurchase Agreements -----	Credit Facilities -----	Commercial Mortgage Loan Pools -----
Commercial Real Estate Securities			
Outstanding Borrowings	\$562,315	\$ 54,347	\$ --
Weighted average borrowing rate	4.53%	5.18%	--
Weighted average remaining maturity	28 days	1.97 years	--
Estimated fair value of assets pledged	\$631,795	\$ 77,510*	\$ --

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### Residential Mortgage-Backed Securities

Outstanding Borrowings	\$249,122	\$	--	\$	--
Weighted average borrowing rate	4.34%		--		--
Weighted average remaining maturity	24 days		--		--
Estimated fair value of assets pledged	\$258,770	\$	--	\$	--

### Commercial Mortgage Loan Pools

Outstanding Borrowings	\$ 5,205	\$	772	\$	1,272,931
Weighted average borrowing rate	5.03%		5.80%		3.97%
Weighted average remaining maturity	17 days		1.53 years		6.89 years
Estimated fair value of assets pledged	\$ 7,321	\$	1,285	\$	1,292,407

### Commercial Real Estate Loans

Outstanding Borrowings	\$ --	\$	229,556	\$	--
Weighted average borrowing rate	--		5.29%		--
Weighted average remaining maturity	--		1.61 years		--
Estimated fair value of assets pledged	\$ --	\$	337,447	\$	--

\* \$23,233 of assets pledged are retained CDO bonds.

### CDOS

The Company finances the majority of its commercial real estate assets with match funded, secured term debt through CDO offerings. To accomplish this, the Company forms a special purpose entity ("SPE") and contributes a portfolio consisting of below investment grade CMBS, investment grade CMBS, unsecured debt of commercial real estate companies and commercial real estate loans in exchange for the preferred equity interest in the SPE. With the exceptions of the Company's fourth and fifth CDOs ("CDO HY1" and "CDO HY2", respectively), these transactions are considered financings and the SPEs are fully consolidated on the Company's consolidated financial statements. The SPE then will issue fixed and floating rate debt secured by the cash flows of the securities in its portfolio. The SPE will enter into an interest rate swap agreement to convert the floating rate debt issued to a fixed interest rate, thus matching the cash flow profile of the underlying portfolio. For those CDOs not denominated in

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U.S. dollars, the SPE will also enter into currency swap agreements to minimize any currency exposure. The structure of the CDO debt also eliminates the mark to market requirement commonly associated with other types of financing, thus eliminating the need to provide additional collateral if the value of the underlying portfolio declines. The debt issued by the SPE generally is rated AAA down to BB. Due to its preferred equity interest, the Company continues to manage the credit risk of the underlying portfolio as it did prior to the assets being contributed to the CDO. CDO debt is the Company's preferred capital structure to maximize returns on these types of portfolios on a non-recourse basis. Other forms of financing used for these types of assets include multi-year committed financing facilities and 90-day reverse repurchase agreements.

At December 31, 2006, outstanding borrowings under the Company's CDOs were \$1,812,574 with a weighted average borrowing rate of 6.02% and a weighted average maturity of 7.0 years. Estimated fair value of assets pledged was \$2,096,455, consisting of 80.3% of commercial real estate securities and 19.7% of commercial real estate loans.

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At December 31, 2005, outstanding borrowings under the Company's CDOs were \$1,066,930 with a weighted average borrowing rate of 5.86% and a weighted average maturity of 10.8 years. Estimated fair value of assets pledged was \$1,227,222 consisting of 100.0% of commercial real estate securities.

### UNSECURED BORROWINGS

During October 2006, the Company issued \$75,000 of unsecured senior notes due in 2016 with a weighted average cost of funds of 7.21%. The unsecured senior notes can be redeemed in whole by the Company subject to certain provisions, which could include the payment of fees.

On September 26, 2005, the Company issued \$75,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust I, a Delaware statutory trust ("Trust I"). The trust preferred securities have a thirty-year term ending October 30, 2035 with interest at a fixed rate of 7.497% for the first ten years and at a floating rate of three-month LIBOR plus 2.9% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in October 2010. Trust I issued \$2,380 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust I to the Company for a purchase price of \$2,380. The Company realized net proceeds from this offering of approximately \$72,618.

On February 2, 2006, the Company issued \$50,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust II, a Delaware statutory trust ("Trust II"). The trust preferred securities have a thirty-year term ending April 30, 2036 with interest at a fixed rate of 7.73% for the first ten years and at a floating rate of three-month LIBOR plus 2.7% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in April 2011. Trust II issued \$1,550 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust II to the Company for a purchase price of \$1,550. The Company realized net proceeds from this offering of approximately \$48,491.

On March 16, 2006, the Company issued \$50,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust III, a Delaware statutory trust ("Trust III"). The trust preferred securities have a thirty-year term ending March 15, 2036 with interest at a fixed rate of 7.77% for the first ten years and at a floating rate of three-month LIBOR plus 2.7% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in March 2011. Trust III issued \$1,547 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust III to the Company for a purchase price of \$1,547. The Company realized net proceeds from this offering of approximately \$48,435.

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### EQUITY ISSUANCES

For the years ended December 31, 2006 and 2005, respectively, the Company issued 608,747 and 1,318,568 shares of Common Stock under its Dividend Reinvestment Plan. Net proceeds under the Dividend Reinvestment Plan to the Company were approximately \$6,517 and \$14,327, respectively. Additionally, the Company issued 1,725,000 shares of Common Stock in a follow-on offering at \$11.59 per share in 2005.

For the year ended December 31, 2006, the Company issued 664,900 shares of Common Stock under a sales agency agreement with Brinson Patrick Securities Corporation. Net proceeds to the Company were approximately \$8,625.

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On February 12, 2007, the Company issued \$86,250 of Series D Cumulative Redeemable Preferred Stock ("Series D Preferred Stock"), including \$11,250 of Series D Preferred Stock sold to underwriters pursuant to an over-allotment option. The Series D Preferred Stock will pay an annual dividend of 8.25%.

### HEDGING ACTIVITIES

The Company enters into hedging transactions to protect its investment portfolio and related borrowings from interest rate fluctuations and other changes in market conditions. From time to time, the Company may modify its exposure to market interest rates by entering into various financial instruments that adjust portfolio duration and short-term rate exposure. These financial instruments are intended to mitigate the effect of changes in interest rates on the value of the Company's assets and the cost of borrowing. These transactions may include interest rate swaps, the purchase or sale of interest rate collars, caps or floors, options, and other hedging instruments. These instruments may be used to hedge as much of the interest rate risk as the Manager determines is in the best interest of the Company's stockholders, given the cost of such hedges. The Manager may elect to have the Company bear a level of interest rate risk that could otherwise be hedged when the Manager believes, based on all relevant facts, that bearing such risk is advisable. The Manager has extensive experience in hedging mortgages, mortgage-related assets and related borrowings with these types of instruments.

Hedging instruments often are not traded on regulated exchanges, guaranteed by an exchange or its clearinghouse, or regulated by any U.S. or foreign governmental authorities. The Company will enter into these transactions only with counterparties with long-term debt rated A or better by at least one nationally recognized credit rating organization. The business failure of a counterparty with which the Company has entered into a hedging transaction most likely will result in a default, which may result in the loss of unrealized profits. Although the Company generally will seek to reserve for itself the right to terminate its hedging positions, it may not always be possible to dispose of or close out a hedging position without the consent of the counterparty, and the Company may not be able to enter into an offsetting contract in order to cover its risk. There can be no assurance that a liquid secondary market will exist for hedging instruments purchased or sold, and the Company may be required to maintain a position until exercise or expiration, which could result in losses.

The Company's hedging activities are intended to address both income and capital preservation. Income preservation refers to maintaining a stable spread between yields from mortgage assets and the Company's borrowing costs across a reasonable range of adverse interest rate environments. Capital preservation refers to maintaining a relatively steady level in the estimated fair value of the Company's capital across a reasonable range of adverse interest rate scenarios. However, no strategy can insulate the Company completely from changes in interest rates.

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Interest rate hedging instruments at December 31, 2006 and 2005 consisted of the following:

At December 31, 2006

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	Notional Value	Estimated Fair Value	Unamortized Cost	Average Remaining Term (years)
	-----	-----	-----	-----
Cash flow hedges	\$644,200	\$5,048	\$ --	7.91
CDO cash flow hedges	895,499	8,230	--	7.19
Trading swaps	80,000	2,033	--	3.27
CDO timing swaps	223,445	212	--	6.08
CDO LIBOR cap	85,000	(38)	1,407	6.40

At December 31, 2005

	Notional Value	Estimated Fair Value	Unamortized Cost	Average Remaining Term (years)
	-----	-----	-----	-----
Cash flow hedges	\$500,350	\$ 6,234	\$ --	8.42
CDO cash flow hedges	701,603	10,616	--	7.51
Trading swaps	133,000	4,032	--	6.83
CDO timing swaps	223,445	(37)	--	7.08
CDO LIBOR cap	85,000	1,419	1,407	7.40

Foreign currency agreements at December 31, 2006 consisted of the following:

At December 31, 2006

	Estimated Fair Value	Unamortized Cost	Average Remaining Term
	-----	-----	-----
Currency swaps	\$ 1,179	\$ --	12.53 years
CDO currency swaps	(1,418)	--	12.53 years
Forwards	(2,659)	--	10 days

At December 31, 2005

	Estimated Fair Value	Unamortized Cost	Average Remaining Term
	-----	-----	-----
Forwards	\$ 1,108	--	10 days

The Company did not have any currency swaps at December 31, 2005.

## OPERATING POLICIES

The Company has adopted compliance guidelines, including restrictions on acquiring, holding, and selling assets, to ensure that the Company meets the

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requirements for qualification as a REIT under the United States Internal Revenue Code of 1986, as amended (the "Code"), and is excluded from regulation as an investment company under the Investment Company Act of 1940, as amended (the "Investment Company Act"). Before acquiring any asset, the Manager determines whether such asset would constitute a "Real Estate Asset" under the REIT provisions of the Code. The Company regularly monitors purchases of commercial real estate assets and the income generated from such assets, including income from its hedging activities, in an effort to ensure that at all times the Company's assets and income meet the requirements for qualification as a REIT and exclusion under the Investment Company Act.

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In order to maintain the Company's REIT status, the Company generally intends to distribute to its stockholders aggregate dividends equaling at least 90% of its taxable income each year. The Code permits the Company to fulfill this distribution requirement by the end of the year following the year in which the taxable income was earned.

### REGULATION

The Company intends to continue to conduct its business so as not to become regulated as an investment company under the Investment Company Act. Under the Investment Company Act, a non-exempt entity that is an investment company is required to register with the SEC and is subject to extensive, restrictive, and potentially adverse regulation relating to, among other things, operating methods, management, capital structure, dividends, and transactions with affiliates. The Investment Company Act exempts entities that are "primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate" ("Qualifying Interests"). Under current interpretation by the staff of the SEC, to qualify for this exemption, the Company, among other things, must maintain at least 55% of its assets in Qualifying Interests. Substantially all of the Company's interests in residential mortgage-backed securities ("RMBS") are Qualifying Interests.

A portion of the CMBS acquired by the Company are collateralized by pools of first mortgage loans where the Company can monitor the performance of the underlying mortgage loans through loan management, servicing rights and workout/foreclosure rights with respect to the underlying mortgage loans. When such arrangements exist, the Company believes that the related Controlling Class CMBS constitute Qualifying Interests for purposes of the Investment Company Act. Therefore, the Company believes that it should not be required to register as an "investment company" under the Investment Company Act as long as it continues to invest in a sufficient amount of such Controlling Class CMBS and/or in other Qualifying Interests.

If the SEC or its staff were to take a different position with respect to whether the Company's Controlling Class CMBS constitute Qualifying Interests, the Company could be required to modify its business plan so that either (i) it would not be required to register as an investment company or (ii) it would register as an investment company under the Investment Company Act. In such event, modification of the Company's business plan so that it would not be required to register as an investment company might entail a disposition of a significant portion of the Company's Controlling Class CMBS or the acquisition of significant additional assets, such as agency pass-through and other mortgage-backed securities, which are Qualifying Interests and modification of the Company's business plan to register as an investment company could result in increased operating expenses and could entail reducing the Company's indebtedness, which also could require it to sell a significant portion of its

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assets. No assurances can be given that any such dispositions or acquisitions of assets, or de-leveraging, could be accomplished on favorable terms. Consequently, any such modification of the Company's business plan could have a material adverse effect on the Company. Further, if it were established that the Company were operating as an unregistered investment company, there would be a risk that the Company would be subject to monetary penalties and injunctive relief in an action brought by the SEC, that the Company would be unable to enforce contracts with third parties, and that third parties could seek to obtain rescission of transactions undertaken during the period it was established that the Company was an unregistered investment company. Any such results would be likely to have a material adverse effect on the Company.

### COMPETITION

The Company's net income depends, in large part, on the Company's ability to acquire commercial real estate assets at favorable spreads over the Company's borrowing costs. In acquiring commercial real

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estate assets, the Company competes with other mortgage REITs, specialty finance companies, savings and loan associations, banks, mortgage bankers, insurance companies, mutual funds, institutional investors, investment banking firms, other lenders, governmental bodies, and other entities. In addition, there are numerous mortgage REITs with asset acquisition objectives similar to the Company's, and others may be organized in the future. The effect of the existence of additional REITs may be to increase competition for the available supply of commercial real estate assets suitable for purchase by the Company. Some of the Company's competitors are significantly larger than the Company, have access to greater capital and other resources, and may have other advantages over the Company. In addition to existing companies, other companies may be organized for purposes similar to that of the Company, including companies organized as REITs focused on purchasing commercial real estate assets. A proliferation of such companies may increase the competition for equity capital and thereby adversely affect the market price of the Company's Common Stock.

### EMPLOYEES

The Company does not have any employees. The Company's officers, each of whom is a full-time employee of the Manager, perform the duties required pursuant to the Management Agreement (as defined below) with the Manager and the Company's bylaws.

### MANAGEMENT AGREEMENTS

The Company has a Management Agreement, an administrative services agreement and an accounting services agreement with the Manager, the employer of certain directors and all of the officers of the Company, under which the Manager and the Company's officers manage the Company's day-to-day investment operations, subject to the direction and oversight of the Company's Board of Directors. Pursuant to the Management Agreement and these other agreements, the Manager and the Company's officers formulate investment strategies, arrange for the acquisition of assets, arrange for financing, monitor the performance of the Company's assets and provide certain other advisory, administrative and managerial services in connection with the operations of the Company. For performing certain of these services, the Company pays the Manager under the Management Agreement a base management fee equal to 2.0% of the quarterly average total stockholders' equity for the applicable quarter.

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To provide an incentive, the Manager is entitled to receive an incentive fee under the Management Agreement equal to 25% of the amount by which the rolling four-quarter GAAP net income before the incentive fee exceeds the greater of 8.5% or 400 basis points over the ten-year Treasury note multiplied by the adjusted per share issue price of the Company's Common Stock (\$11.37 per common share at December 31, 2006). Additionally, up to 30% of the incentive fees earned in 2005 or after may be paid in shares of the Company's Common Stock subject to certain provisions under a compensatory deferred stock plan approved by the stockholders of the Company in 2006. The Board of Directors also authorized a stock based incentive plan where one-half of one percent of common shares outstanding was paid to the Manager in 2006.

The Company's unaffiliated directors approved an extension of the Management Agreement to March 30, 2008 at the Board's March 2007 meeting.

The Manager primarily engages in four investment activities in its capacity as Manager on behalf of the Company: (i) acquiring and originating commercial real estate loans and other real estate related assets; (ii) asset/liability and risk management, hedging of floating rate liabilities, and financing, management and disposition of assets, including credit and prepayment risk management; (iii) surveillance and restructuring of real estate loans and (iv) capital management, structuring, analysis, capital raising, and

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investor relations activities. At all times, the Manager and the Company's officers are subject to the direction and oversight of the Company's Board of Directors.

The Company may terminate, or decline to renew the term of, the Management Agreement without cause at any time upon 60 days' written notice by a majority vote of the unaffiliated directors. Although no termination fee is payable in connection with a termination for cause, in connection with a termination without cause, the Company must pay the Manager a termination fee, which could be substantial. The amount of the termination fee will be determined by independent appraisal of the value of the Management Agreement. Such appraisal is to be conducted by a nationally-recognized appraisal firm mutually agreed upon by the Company and the Manager. The other agreements the Company has with the Manager also may be terminated by the Company; in the case of the administrative services agreement, at any time upon 60 days' written notice, and in the case of the accounting services agreement, following the 24 month anniversary thereof, on 60 days' written notice prior to the 12 month anniversary thereof, or upon 60 days' written notice following the termination of the Management Agreement.

In addition, the Company has the right at any time during the term of the Management Agreement to terminate the Management Agreement without the payment of any termination fee upon, among other things, a material breach by the Manager of any provision contained in the Management Agreement that remains uncured at the end of the applicable cure period.

### TAXATION OF THE COMPANY

The Company has elected to be taxed as a REIT under the Code, commencing with its taxable year ended December 31, 1998, and the Company intends to continue to operate in a manner consistent with the REIT provisions of the Code. The Company's qualification as a REIT depends on its ability to meet the various requirements imposed by the Code, through actual operating results, asset

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holdings, distribution levels, and diversity of stock ownership.

Provided the Company continues to qualify for taxation as a REIT, it generally will not be subject to Federal corporate income tax on its net income that is currently distributed to stockholders. This treatment substantially eliminates the "double taxation" (at the corporate and stockholder levels) that generally results from an investment in a corporation. If the Company fails to qualify as a REIT in any taxable year, its taxable income would be subject to Federal income tax at regular corporate rates (including any applicable alternative minimum tax). Even if the Company qualifies as a REIT, it will be subject to Federal income and excise taxes on its undistributed income.

If in any taxable year the Company fails to qualify as a REIT and, as a result, incurs additional tax liability, the Company may need to borrow funds or liquidate certain investments in order to pay the applicable tax, and the Company would not be compelled to make distributions under the Code. Unless entitled to relief under certain statutory provisions, the Company would also be disqualified from treatment as a REIT for the four taxable years following the year during which qualification is lost. Although the Company currently intends to operate in a manner designed to qualify as a REIT, it is possible that future economic, market, legal, tax, or other considerations may cause the Company to fail to qualify as a REIT or may cause the Board of Directors to revoke the Company's REIT election.

The Company and its stockholders may be subject to foreign, state, and local taxation in various foreign, state, and local jurisdictions, including those in which it or they transact business or reside. The state and local tax treatment of the Company and its stockholders may not conform to the Company's Federal income tax treatment.

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### WEBSITE

The Company's website address is [www.anthracitecapital.com](http://www.anthracitecapital.com). The Company makes available free of charge through its website its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, all amendments to those reports and other filings as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC, and also makes available on its website the charters for the Audit, Compensation and Nominating and Corporate Governance Committees of the Board of Directors and its Codes of Business Conduct and Ethics, as well as its corporate governance guidelines. Copies in print of these documents are available upon request to the Secretary of the Company at the address indicated on the cover of this report. To communicate with the Board of Directors electronically, the Company has established an e-mail address, [anthracitebod@blackrock.com](mailto:anthracitebod@blackrock.com), to which stockholders may send correspondence to the Board of Directors or any such individual directors or group or committee of directors.

In accordance with New York Stock Exchange ("NYSE") Rules, on June 6, 2006, the Company filed the annual certification by its Chief Executive Officer certifying that he was unaware of any violation by the Company of the NYSE's corporate governance listing standards at the time of the certification.

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### ITEM 1A. RISK FACTORS

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### RISKS

Risk is an inherent part of investing in high yielding commercial real estate debt and equity. Risk management is considered to be of paramount importance to the Company's day-to-day operations. Consequently, the Company devotes significant resources across all its operations to the identification, measurement, monitoring, management and analysis of risk.

#### RISKS RELATED TO THE MANAGER

Conflicts of interest of the Manager may result in decisions that do not fully reflect stockholders' best interests.

The Company and the Manager have common officers and directors, which may present conflicts of interest in the Company's dealings with the Manager and its affiliates, including the Company's purchase of assets originated by such affiliates.

The Manager and its employees may engage in other business activities that could reduce the time and effort spent on the management of the Company. The Manager also provides services to REITs not affiliated with the Company. As a result, there may be a conflict of interest between the operations of the Manager and its affiliates in the acquisition and disposition of commercial real estate assets. In addition, the Manager and its affiliates may from time to time purchase commercial real estate assets for their own account and may purchase or sell assets from or to the Company. For example, BlackRock Realty Advisors, Inc., a subsidiary of the Manager, provides real estate equity and other real estate related products and services in a variety of strategies to its institutional investor client base. In doing so, it purchases real estate on behalf of its clients that may underlie the real estate loans and securities the Company acquires, and consequently depending on the factual circumstances involved, there may be conflicts between the Company and those clients. Such conflicts may result in decisions and allocations of commercial real estate assets by the Manager, or decisions by the Manager's affiliates, that are not in the Company's best interests.

Although the Company has adopted investment guidelines, these guidelines give the Manager significant discretion in investing. The Company's investment and operating policies and the strategies that the Manager uses to implement those policies may be changed at any time without the consent of stockholders.

The Company is dependent on the Manager, and the termination by the Company of its Management Agreement with the Manager could result in a termination fee.

The Company's success is dependent on the Manager's ability to attract and retain quality personnel. The market for portfolio managers, investment analysts, financial advisers and other professionals is extremely competitive. There can be no assurance the Manager will be successful in its efforts to recruit and retain the required personnel.

The Management Agreement between the Company and the Manager provides for base management fees payable to the Manager without consideration of the performance of the Company's portfolio and also provides for incentive fees based on certain performance criteria, which could result in the Manager recommending riskier or more speculative investments. Termination of the Management Agreement between the Company and the Manager by the

Company would result in the payment of a substantial termination fee, which could adversely affect the Company's financial condition. Termination of the Management Agreement by the Company could also adversely affect the Company if the Company were unable to find a suitable replacement.

There is a limitation on the liability of the Manager.

Pursuant to the Management Agreement, the Manager will not assume any responsibility other than to render the services called for under the Management Agreement and will not be responsible for any action of the Company's Board of Directors in following or declining to follow its advice or recommendations. The Manager and its directors and officers will not be liable to the Company, any of its subsidiaries, its unaffiliated directors, its stockholders or any subsidiary's stockholders for acts performed in accordance with and pursuant to the Management Agreement, except by reason of acts constituting bad faith, willful misconduct, gross negligence or reckless disregard of their duties under the management agreement. The Company has agreed to indemnify the Manager and its directors and officers with respect to all expenses, losses, damages, liabilities, demands, charges and claims arising from acts of the Manager not constituting bad faith, willful misconduct, gross negligence or reckless disregard of duties, performed in good faith in accordance with and pursuant to the Management Agreement.

#### RISKS RELATED TO THE COMPANY'S BUSINESS

Interest rate fluctuations will affect the value of the Company's commercial real estate assets, net income and common stock.

Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors. Interest rate fluctuations can adversely affect the income and value of the Company's common stock in many ways and present a variety of risks, including the risk of a mismatch between asset yields and borrowing rates, variances in the yield curve, changing prepayment rates and margin calls.

The Company's operating results depend in large part on differences between the income from its assets (net of credit losses) and borrowing costs. The Company funds a substantial portion of its assets with borrowings that have interest rates that reset relatively rapidly, such as monthly or quarterly. The Company anticipates that, in most cases, the income from its floating-rate assets will respond more slowly to interest rate fluctuations than the cost of borrowings, creating a potential mismatch between asset yields and borrowing rates. Consequently, changes in interest rates, particularly short-term interest rates, may influence the Company's net income. Increases in these rates tend to decrease the Company's net income and estimated fair value of the Company's net assets. Interest rate fluctuations that result in the Company's interest expense exceeding interest income would result in the Company incurring operating losses.

The Company also invests in fixed-rate mortgage-backed securities. In a period of rising interest rates, the Company's interest payments could increase while the interest the Company earns on its fixed-rate mortgage-backed securities would not change. This would adversely affect the Company's profitability.

The relationship between short-term and long-term interest rates often is

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referred to as the "yield curve." Ordinarily, short-term interest rates are lower than long-term interest rates. If short-term

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interest rates rise disproportionately relative to long-term interest rates (a flattening of the yield curve), the Company's borrowing costs may increase more rapidly than the interest income earned on the Company's assets. Because the Company's borrowings primarily will bear interest at short-term rates and the Company's assets primarily will bear interest at medium-term to long-term rates, a flattening of the yield curve tends to decrease the Company's net income and estimated fair value of the Company's net assets. Additionally, to the extent cash flows from long-term assets that return scheduled and unscheduled principal are reinvested, the spread between the yields of the new assets and available borrowing rates may decline and also may tend to decrease the net income and estimated fair value of the Company's net assets. It is also possible that short-term interest rates may adjust relative to long-term interest rates such that the level of short-term rates exceeds the level of long-term rates (a yield curve inversion). In this case, the Company's borrowing costs may exceed the Company's interest income and operating losses could be incurred.

A portion of the Company's commercial real estate assets are financed under 90-day repurchase agreements and committed borrowing facilities which are subject to mark-to-market risk. Such secured financing arrangements provide for an advance rate based upon a percentage of the estimated fair value of the asset being financed. Market movements that cause asset values to decline would require a margin call or a cash payment to maintain the relationship between asset value and amount borrowed.

The Company's investments may be subject to impairment charges.

The Company periodically evaluates its investments for impairment indicators. The judgment regarding the existence of impairment indicators is based on a variety of factors depending on the nature of the investment and the manner in which the income related to such investment is calculated for purposes of the Company's financial statements. If the Company determines that a significant impairment has occurred, the Company would be required to make an adjustment to the net carrying value of the investment, which could adversely affect the Company's results of operations in the applicable period.

Interest rate caps on the Company's RMBS may adversely affect the Company's profitability.

The Company's adjustable-rate RMBS typically are subject to periodic and lifetime interest rate caps. Periodic interest rate caps limit the amount an interest rate can increase during any given period. Lifetime interest rate caps limit the amount an interest rate can increase through maturity of a mortgage-backed security. The Company's borrowings are not subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, the Company could experience a decrease in net income or a net loss because the interest rates on its borrowings could increase without limitation while the interest rates on its adjustable-rate mortgage-backed securities would be limited by caps.

The Company's assets include subordinated CMBS which are subordinate in right of payment to more senior securities.



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The Company's assets include a significant amount of subordinated CMBS, which are the most subordinate class of securities in a structure of securities secured by a pool of loans and accordingly are the first to bear the loss upon a restructuring or liquidation of the underlying collateral and the last to receive payment of interest and principal. The Company may not recover the full amount or, in extreme cases, any of its initial investment in such subordinated interests. Additionally, estimated fair values of these subordinated interests tend to be more

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sensitive to changes in economic conditions than more senior interests. As a result, such subordinated interests generally are not actively traded and may not provide holders thereof with liquidity of investment.

The Company's assets include mezzanine loans which have greater risks of loss than more senior loans.

The Company's assets include a significant amount of mezzanine loans that involve a higher degree of risk than long-term senior mortgage loans. In particular, a foreclosure by the holder of the senior loan could result in the mezzanine loan becoming unsecured. Accordingly, the Company may not recover some or all of its investment in such a mezzanine loan. Additionally, the Company may permit higher loan to value ratios on mezzanine loans than it would on conventional mortgage loans when the Company is entitled to share in the appreciation in value of the property securing the loan.

Prepayment rates can increase which would adversely affect yields on the Company's investments.

The yield on investments in mortgage loans and mortgage-backed securities and thus the value of the Company's common stock is sensitive to changes in prevailing interest rates and changes in prepayment rates, which results in a divergence between the Company's borrowing rates and asset yields, consequently reducing future income derived from the Company's investments.

The Company's ownership of non-investment grade commercial real estate assets subjects the Company to an increased risk of loss which could adversely affect yields on the Company's investments.

The Company acquires commercial real estate loans and non-investment grade mortgage-backed securities, which are subject to greater risk of credit loss on principal and non-payment of interest in contrast to investments in senior investment grade securities.

The Company's commercial real estate assets are subject to certain risks.

The Company acquires, accumulates and securitizes commercial real estate assets as part of its investment strategy. While exposed to such commercial real estate assets, either as collateral for a real estate security or directly, the Company is subject to risks of borrower defaults, bankruptcies, fraud and special hazard losses that are not covered by standard hazard insurance. Insurance on owned real estate, commercial mortgage loans and real estate securities collateral may not cover all losses.

The Company's commercial mortgage loans are subject to certain risks.

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The costs of financing and hedging the commercial mortgage loans can exceed the interest income on the commercial mortgage loans. In the event of any default under commercial mortgage loans held by the Company, the Company will bear the risk of loss of principal to the extent of any deficiency between the value of the commercial mortgage collateral and the principal amount of the commercial mortgage loan. In addition, delinquency and loss ratios on the Company's commercial mortgage loans are affected by the performance of third-party servicers and special servicers.

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The Company invests in multifamily and commercial loans which involve a greater risk of loss than single family loans.

The Company's investments include multifamily and commercial real estate loans which are considered to involve a higher degree of risk than single family residential lending because of a variety of factors, including generally larger loan balances, dependency for repayment on successful operation of the mortgaged property and tenant businesses operating therein, and loan terms that include amortization schedules longer than the stated maturity which provide for balloon payments at stated maturity rather than periodic principal payments. In addition, the value of multifamily and commercial real estate can be affected significantly by the supply and demand in the market for that type of property.

Limited recourse loans limit the Company's recovery to the value of the mortgaged property.

A substantial portion of the commercial mortgage loans the Company acquires may contain limitations on the mortgagee's recourse against the borrower. In other cases, the mortgagee's recourse against the borrower is limited by applicable provisions of the laws of the jurisdictions in which the mortgaged properties are located or by the mortgagee's selection of remedies and the impact of those laws on that selection. In those cases, in the event of a borrower default, recourse may be limited to only the specific mortgaged property and other assets, if any, pledged to secure the relevant commercial mortgage loan. As to those commercial mortgage loans that provide for recourse against the borrower and their assets generally, such recourse may not provide a recovery in respect of a defaulted commercial mortgage loan equal to the liquidation value of the mortgaged property securing that commercial mortgage loan.

The volatility of certain mortgaged property values may adversely affect the Company's commercial mortgage loans.

Commercial and multifamily property values and net operating income derived therefrom are subject to volatility and may be affected adversely by a number of factors, including, but not limited to, national, regional and local economic conditions (which may be adversely affected by plant closings, industry slowdowns and other factors); local real estate conditions (such as an oversupply of housing, retail, industrial, office or other commercial space); changes or continued weakness in specific industry segments; perceptions by prospective tenants, retailers and shoppers of the safety, convenience, services and attractiveness of the property; the willingness and ability of the property's owner to provide capable management and adequate maintenance; construction quality, age and design; demographic factors; retroactive changes to building or similar codes; and increases in operating expenses (such as energy costs).

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Leveraging the Company's investments may increase the Company's exposure to loss.

The Company leverages its investments and thereby increases the volatility of its income and net asset value that may result in operating or capital losses. If borrowing costs increase, or if the cash flow generated by the Company's assets decreases, the Company's use of leverage will increase the likelihood that the Company will experience reduced or negative cash flow and reduced liquidity.

The Company's investments may be illiquid and their value may decrease.

Many of the Company's assets are relatively illiquid. In addition, certain of the mortgage-backed securities that the Company has acquired or will acquire will include interests that have not been

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registered under the relevant securities laws, resulting in a prohibition against transfer, sale, pledge or other disposition of those mortgage-backed securities except in a transaction that is exempt from the registration requirements of, or otherwise in accordance with, those laws. The Company's ability to vary its portfolio in response to changes in economic and other conditions may be relatively limited. The estimated fair value of any of the Company's assets could decrease in the future.

The Company's hedging transactions can limit the Company's gains and increase the Company's exposure to losses.

The Company uses hedging strategies that involve risk and that may not be successful in insulating the Company from exposure to changing interest and prepayment rates. A liquid secondary market may not exist for hedging instruments purchased or sold, and the Company may be required to maintain a position until exercise or expiration, which could result in losses.

The Company's non-U.S. investments are subject to currency rate exposure and the uncertainty of foreign laws and markets which could adversely affect the Company's income.

Failure to maintain REIT status would have adverse tax consequences.

To continue to qualify as a REIT, the Company must comply with requirements regarding the nature of its assets and its sources of income. If the Company is compelled to liquidate its mortgage-backed securities, the Company may be unable to comply with these requirements, ultimately jeopardizing its status as a REIT.

If in any taxable year the Company fails to qualify as a REIT:

- the Company would be subject to Federal and state income tax on its taxable income at regular corporate rates;
- the Company would not be allowed to deduct distributions to stockholders in computing its taxable income; and
- unless the Company were entitled to relief under the Code, the Company also would be disqualified from treatment as a REIT for the four taxable years following the year during which the Company lost qualification.

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If the Company fails to qualify as a REIT, the Company might need to borrow funds or liquidate some investments in order to pay the additional tax liability. Accordingly, funds available for investment or distribution to the Company's stockholders would be reduced for each of the years involved.

Qualification as a REIT involves the application of highly technical and complex provisions of the Code to the Company's operations and the determination of various factual matters and circumstances not entirely within the Company's control. There are only limited judicial or administrative interpretations of these provisions. Although the Company operates in a manner consistent with the REIT qualification rules, the Company may not remain so qualified.

In addition, the rules dealing with Federal income taxation are constantly under review by persons involved in the legislative process and by the Internal Revenue Service and the United States Department of the Treasury. Changes to the tax law could adversely affect the Company's stockholders.

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Increased competition in the marketplace may adversely affect the Company's ability to acquire assets.

Because of increased competition in the marketplace, the Company may not be able to acquire mortgage-backed securities at favorable yields.

Failure to maintain an exemption from the Investment Company Act would restrict the Company's operating flexibility.

The Company conducts its business so as not to become regulated as an investment company under the Investment Company Act. Accordingly, the Company does not expect to be subject to the restrictive provisions of the Investment Company Act. Failure to maintain an exemption from the Investment Company Act would adversely affect the Company's ability to operate.

The Company may become subject to environmental liabilities.

The Company may become subject to environmental risks when it acquires interests in properties with material environmental problems. Such environmental risks include the risk that operating costs and values of these assets may be adversely affected by the obligation to pay for the cost of complying with existing environmental laws, ordinances and regulations, as well as the cost of complying with future legislation. Such laws often impose liability regardless of whether the owner or operator knows of, or was responsible for, the presence of such hazardous or toxic substances. The costs of investigation, remediation or removal of hazardous substances could exceed the value of the property. The Company's income and ability to make distributions to stockholders could be affected adversely by the existence of an environmental liability with respect to the Company's properties.

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None.

### ITEM 2. PROPERTIES

The Company does not maintain an office. It does not pay rent and utilizes the offices of the Manager, located at 40 East 52nd Street, New York, New York 10022.

### ITEM 3. LEGAL PROCEEDINGS

At December 31, 2006, there were no pending legal proceedings in which the Company was a defendant or of which any of its property was subject.

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of the Company's security holders during the fourth quarter of 2006 through the solicitation of proxies or otherwise.

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## PART II

### ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company's Common Stock has been listed and traded on the New York Stock Exchange under the symbol "AHR" since its initial public offering in March 1998. The following table sets forth, for the periods indicated, the high, low and last sale prices in dollars on the New York Stock Exchange for the Company's Common Stock and the dividends declared by the Company with respect to the periods indicated as were traded during these respective time periods.

	High	Low	Last Sale	Dividends Declared
	-----	-----	-----	-----
2006				
First Quarter.....	\$11.22	\$10.56	\$10.98	\$0.28
Second Quarter.....	12.28	10.27	12.16	0.29
Third Quarter.....	13.44	11.86	12.86	0.29
Fourth Quarter.....	14.42	11.50	12.73	0.29
2005				
First Quarter.....	12.21	10.85	11.14	0.28
Second Quarter.....	12.40	10.50	11.85	0.28
Third Quarter.....	12.19	11.33	11.58	0.28
Fourth Quarter.....	11.28	10.16	10.53	0.28

On March 2, 2007, the closing sale price for the Company's Common Stock, as reported on the New York Stock Exchange, was \$12.10. At March 2, 2007, there were approximately 1,089 record holders of the Common Stock. This figure does not reflect beneficial ownership of shares held in nominee name.

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Information relating to the Company's equity compensation plans in the Company's definitive proxy statement for its 2007 Annual Meeting of Stockholders (the "Proxy Statement"), to be filed with the SEC, is incorporated herein by reference.

The Company made no purchases of its equity securities in 2006.

### Recent Sales of Unregistered Securities

During the year ended December 31, 2006, the Company issued 194,077 shares of unregistered Common Stock with an aggregate value of \$2,164,979 as follows. Pursuant to resolutions of the Board of Directors which authorized that a portion of incentive fees earned by the Manager may be paid in shares of the Company's Common Stock, the Company issued 189,077 shares to the Manager as payment of a portion of the Manager's incentive fees. The Company issued 5,000 shares to its unaffiliated directors pursuant to its annual grant of restricted stock to unaffiliated directors as part of their annual compensation. The issuances of common stock were made in reliance upon the exemption from registration under Section 4(2) of the Securities Act.

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### ITEM 6. SELECTED FINANCIAL DATA

The selected financial data set forth below at and for the years ended December 31, 2006, 2005, 2004, 2003, and 2002 has been derived from the Company's audited financial statements. This information should be read in conjunction with "Item 1. Business" and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations", as well as the audited financial statements and notes thereto included in "Item 8. Financial Statements and Supplementary Data".

	For the Year Ended December 31,				
	2006	2005	2004	2003	
	(In thousands, except per share data)				
Operating Data:					
Interest income	\$ 275,986	\$ 231,768	\$ 194,967	\$ 159,456	\$
Other income	27,431	12,146	8,899	4,322	
Interest expense	212,388	163,458	128,166	83,249	
Other operating expenses	25,830	19,181	12,383	11,707	
Other gains (losses) (1)	13,906	9,322	(20,125)	(77,464)	
Cumulative transition adjustment (2)	--	--	--	--	
Income from discontinued operations (3)	1,366				
Net income (loss)	80,471	70,597	43,192	(8,642)	
Net income (loss) available to common stockholders	75,079	65,205	25,768	(16,386)	
Per Share Data:					
Net income (loss):					
Basic	1.31	1.20	0.50	(0.34)	

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Diluted	1.31	1.20	0.50	(0.34)	
Dividends declared per common share	1.15	1.12	1.12	1.26	
Balance Sheet Data:					
Total assets	5,218,263	4,234,825	3,729,134	2,398,846	2,
Total liabilities	4,562,154	3,636,807	3,215,396	1,981,416	2,
Total stockholders' equity	656,109	598,018	513,738	417,430	

- (1) Other gains (losses) for the year ended December 31, 2006 of \$13,906 consist primarily of a loss of \$(7,880) related to impairments on assets, a gain of \$3,254 related to securities held-for-trading, a gain of \$2,161 related to foreign currency, a loss of \$(12,661) related to a change in the Company's hedging policy and a gain of \$29,032 related to the sale of securities available-for-sale. Other gains (losses) for the year ended December 31, 2005 of \$9,322 consist primarily of a loss of \$(5,088) related to impairments on assets and a gain of \$16,543 related to securities available-for-sale. Other gains (losses) for the year ended December 31, 2004 of \$(20,125) consist primarily of a gain of \$17,544 related to securities available-for-sale, a loss of \$(26,018) related to impairments on assets and a loss of \$(11,464) related to securities held-for-trading. Other gains (losses) for the year ended December 31, 2003 of \$(77,464) consist primarily of a loss of \$(32,426) related to impairments on assets and a loss of \$(38,206) related to securities held-for-trading. Other gains (losses) for the year ended December 31, 2002 of \$(28,949) consist primarily of a loss of \$(10,273) related to impairments on assets, a loss of \$(29,255) related to securities held-for-trading, and a gain of \$11,391 related to the sale of securities available-for-sale.

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- (2) The cumulative transition adjustment represents the Company's adoption of SFAS No. 142, Goodwill and Other Intangible Assets ("SFAS No. 142") for the year ended December 31, 2002.
- (3) The Company purchased a defaulted loan from a Controlling Class CMBS trust during the first quarter of 2006. The Company sold the property during the second quarter of 2006 and recorded a gain from discontinued operations of \$1,366 on the consolidated statement of operations.

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### ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

All dollar figures expressed herein are expressed in thousands, except share and per share amounts.

#### General

Anthracite Capital, Inc., a Maryland corporation, and subsidiaries (collectively, the "Company") is a specialty finance company that invests in commercial real estate assets on a global basis. The Company seeks to generate income from 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's primary activities are investing in high yielding commercial real estate debt and equity. The Company

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combines traditional real estate underwriting and capital markets expertise to maximize the opportunities arising from the continuing integration of these two disciplines. The Company focuses on acquiring pools of performing loans in the form of commercial mortgage-backed securities ("CMBS"), issuing secured debt backed by CMBS and providing strategic capital for the commercial real estate industry in the form of mezzanine loan financing. The Company also began investing in diversified portfolios of commercial real estate in the United States during December 2005. The Company commenced operations on March 24, 1998.

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

The Company's principal focus is to invest in a diverse portfolio of primarily high yield commercial real estate loans and CMBS. The CMBS that the Company purchases are fixed income instruments similar to bonds that carry an interest coupon and stated principal. The cash flow used to pay the interest and principal on the CMBS comes from a designated pool of first mortgage loans on commercial real estate (the "Underlying Loans"). Underlying Loans usually are originated by commercial banks or investment banks and are secured by a first mortgage on office buildings, retail centers, apartment buildings, hotels and other types of commercial real estate. A typical loan pool may contain several hundred Underlying Loans with principal amounts of as little as \$1,000 to over \$100,000. The pooling concept permits significant geographic diversification. Converting loans into CMBS in this fashion allows investors to purchase these securities in global capital markets and to participate in the commercial real estate sector with significant diversification among property types, sizes and locations in one fixed income investment.

The type of CMBS issued from a typical loan pool is generally broken down by credit rating. The highest rated CMBS will receive payments of principal first and is therefore least exposed to the credit performance of the Underlying Loan. These securities will carry a credit rating of AAA and will be issued with a principal amount that represents some portion of the total principal amount of the Underlying Loan pool.

The CMBS that receive principal payments last are generally rated below investment grade (BB+ or lower.) As the last to receive principal, these CMBS are also the first to absorb any credit losses incurred in the Underlying Loan pool. Typically, the principal amount of these below investment grade classes represents 2.0-3.5% of the principal of the Underlying Loan pools. The investor that owns the lowest rated, or non-rated, CMBS class is designated as the controlling class representative for the underlying loan pool. This designation allows the holder to assert a significant degree of influence over

any workouts or foreclosures of defaulted Underlying Loans. These securities are generally issued with a high yield to compensate for the credit risk inherent in owning the CMBS class which is the first to absorb losses.

The Company's high yield commercial real estate loan strategy encompasses B notes (defined below) and mezzanine loans. B notes and mezzanine loans are based on a similar concept of investing in a portion of the principal and interest of a specific loan instead of a pool of loans as in CMBS. In the case of B notes



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the principal amount of a single loan is separated into a senior interest ("A note") and a junior interest ("B note"). Prior to a borrower default, the A note and the B note receive principal and interest pari passu; however after a borrower default, the A note would receive its principal and interest first and the B note would absorb the credit losses that occur, if any, up to the full amount of its principal. The B note holder generally has certain rights to influence workouts or foreclosures. The Company invests in B notes as they provide relatively high yields with a degree of influence over dispositions. Mezzanine loans generally are secured by ownership interests in an entity that owns real estate. These loans generally are subordinate to a first mortgage and would absorb a credit loss prior to the senior mortgage holder.

The Company is managed by BlackRock Financial Management, Inc. (the "Manager"), a subsidiary of BlackRock, Inc., a publicly traded (NYSE:BLK) asset management company with \$1.125 trillion of assets under management at December 31, 2006. The Company believes that the trend toward highly structured investment products requires significant expertise in traditional real estate underwriting as well as in the capital markets. Through its external management contract with the Manager, the Company can source and manage more opportunities by taking advantage of a unique platform that combines these two disciplines.

The table below is a summary of the Company's investments by asset class for the last five years:

	Carrying Value at December 31,							
	2006		2005		2004		2003	
	Amount	%	Amount	%	Amount	%	Amount	%
Commercial real estate securities	\$2,494,099	53.0%	\$2,005,383	49.7%	\$1,623,939	44.6%	\$1,393,010	62.0%
Commercial mortgage loan pools(1)	1,271,014	27.0	1,292,407	32.0	1,312,045	36.1	--	--
Commercial real estate loans(2)	554,148	11.8	425,453	10.6	329,930	9.1	97,984	4.3
Commercial real estate equity	109,744	2.3	51,003	1.3	--	--	--	--
Commercial real estate assets	4,429,005	94.1	3,774,246	93.6	3,265,914	89.8	1,490,994	67.0
Residential mortgage-backed securities ("RMBS")	276,344	5.9	259,026	6.4	372,071	10.2	726,717	32.0
Total	\$4,705,349	100.0%	\$4,033,272	100.0%	\$3,637,985	100.0%	\$2,217,711	100.0%

(1) Represents a Controlling Class CMBS that is consolidated for accounting purposes. See Note 5 of the consolidated financial statements.

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

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### SUMMARY OF COMMERCIAL REAL ESTATE ASSETS

A summary of the Company's commercial real estate assets with estimated fair values in local currencies at December 31, 2006 is as follows:

	Commercial Real Estate Securities	Commercial Real Estate Loans (1)	Commercial Real Estate Equity	Commercial Mortgage Loan Pools	Total Commercial Real Estate Assets	Total Commercial Real Estate Assets (U
	-----	-----	-----	-----	-----	-----
USD	\$2,312,503	\$310,771	\$ 105,894	\$1,271,014	\$ 4,000,182	\$4,000,1
GBP	L 27,532	L 28,977	--	--	L 56,509	110,6
Euro	E 80,923	E141,422	--	--	E 222,345	293,4
Canadian Dollars	\$ 24,339	--	--	--	\$ 24,339	20,8
Indian Rupees	--	--	Rs169,823	--	Rs 169,823	3,8
	-----	-----	-----	-----	-----	-----
Total USD Equivalent	\$2,494,100	\$554,148	\$ 109,744	\$1,271,014	\$ 4,429,006	\$4,429,0
	-----	-----	-----	-----	-----	-----

(1) Includes the Company's investments in the Carbon Capital Funds at December 31, 2006.

A summary of the Company's commercial real estate assets with estimated fair values in local currencies at December 31, 2005 is as follows:

	Commercial Real Estate Securities	Commercial Real Estate Loans (1)	Commercial Real Estate Equity	Commercial Mortgage Loan Pools	Total Commercial Real Estate Assets	Total Commercial Real Estate Assets (U
	-----	-----	-----	-----	-----	-----
USD	\$1,968,063	\$295,499	\$51,003	\$1,292,407	\$3,606,972	\$3,606,9
GBP	L 16,334	L 33,139	--	--	L 49,473	\$ 85,0
Euro	E 7,809	E 61,642	--	--	E 69,451	\$ 82,2
	-----	-----	-----	-----	-----	-----
Total USD Equivalent	\$2,005,383	\$425,453	\$51,003	\$1,292,407	\$3,774,246	\$3,774,2
	-----	-----	-----	-----	-----	-----

(1) Includes the Company's investments in the Carbon Capital Funds at December 31, 2005.

The Company has foreign currency rate exposure related to its non-U.S. dollar denominated assets. The Company's primary currency exposures are Euro and British pound. Changes in currency rates can adversely impact the estimated fair value and earnings of the Company's non-U.S. holdings. Outside its collateralized debt obligations ("CDOs"), the Company mitigates this impact by utilizing local currency-denominated financing on its foreign investments and foreign currency forward commitments to hedge the net exposure. In its Euro CDO, the Company mitigates the exposure to foreign exchange rates with currency swaps agreements. Net foreign currency gain (loss) was \$2,161 and \$(134) for the years ended December 31, 2006 and 2005, respectively.

## COMMERCIAL REAL ESTATE ASSETS PORTFOLIO ACTIVITY

The following table details the par, estimated fair value, adjusted purchase price, and loss adjusted yield of the Company's commercial real estate securities included in as well as outside of the Company's CDOs at December 31, 2006. The dollar price ("Dollar Price") represents the estimated fair value or adjusted purchase price of a security, respectively, relative to its par value.

	Par	Carrying Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Ex
	-----	-----	-----	-----	-----	-----
Commercial real estate securities outside CDOs						
Investment grade CMBS	\$ 23,060	\$ 21,426	92.92	\$ 21,753	102.58	
Investment grade REIT debt	23,121	21,566	93.28	22,973	99.36	
CMBS rated BB+ to B	108,176	86,677	80.13	87,486	81.59	
CMBS rated B- or lower	148,310	50,165	33.82	46,043	31.27	
CDO Investments	406,605	117,246	28.84	114,482	28.16	1
CMBS Interest Only securities ("IOs")	2,980,467	69,352	2.33	69,183	2.32	
Multifamily agency securities	447,191	449,827	100.59	452,781	101.25	
Commercial mortgage loan pools	1,207,212	1,271,014	105.29	1,271,014	105.29	
	-----	-----	-----	-----	-----	
Total commercial real estate assets outside CDOs	5,344,142	2,087,273	39.06	2,085,715	39.08	
	-----	-----	-----	-----	-----	
Commercial real estate loans and equity outside CDOs						
Commercial real estate loans	63,439	140,985		141,951		
Commercial real estate	96,453	109,744		96,453		
	-----	-----		-----		
Total commercial real estate loans and equity outside CDOs	159,892	250,729		238,404		
	-----	-----		-----		
Commercial real estate assets included in CDOs						
Investment grade CMBS	779,653	794,622	101.92	750,662	94.34	
Investment grade REIT debt	223,324	227,678	101.95	224,964	100.73	
CMBS rated BB+ to B	614,780	554,185	90.14	508,908	78.28	
CMBS rated B- or lower	193,236	77,038	39.87	70,727	36.60	1
Credit tenant lease	23,793	24,318	102.20	24,439	102.71	
Commercial real estate loans	357,111	413,163	115.70	400,559	96.95	
	-----	-----	-----	-----	-----	
Total commercial real estate assets included in CDOs	2,191,897	2,091,004	95.40	1,980,259	85.91	
	-----	-----	-----	-----	-----	
Total commercial real estate assets	\$7,695,931	\$4,429,006		\$4,304,378		
	=====	=====		=====		

During the year ended December 31, 2006, the Company increased its commercial real estate assets by 17% from \$3,774,246 to \$4,429,006. This increase was primarily attributable to the purchase of subordinated CMBS, multifamily agency securities, and investment grade CMBS that have an estimated fair value at

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December 31, 2006 of \$336,176, \$193,395, and \$75,841, respectively. The purchase of the aforementioned securities was offset by the sale of assets with an estimated fair value of \$182,211.

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The following table details the par, carrying value, adjusted purchase price and expected yield of the Company's commercial real estate assets included in as well as outside its CDOs at December 31, 2005:

	Par	Carrying Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Ex
	-----	-----	-----	-----	-----	-----
Commercial real estate securities outside CDOs						
Investment grade CMBS	\$ 150,128	\$ 151,889	96.22	\$ 161,314	102.17	
Investment grade REIT debt	23,000	21,828	94.90	22,828	99.25	
CMBS rated BB+ to B	104,784	90,289	78.38	92,931	80.69	
CMBS rated B- or lower	132,242	47,854	34.05	45,070	31.59	
CDO Investments	423,349	124,549	29.42	112,577	26.59	1
CMBS IOs	3,505,646	103,363	2.95	103,120	2.94	
Multifamily agency securities	256,398	263,362	102.72	268,319	104.65	
Commercial mortgage loan pools	1,221,302	1,292,407	105.82	1,292,407	105.82	
	-----	-----	-----	-----	-----	
Total commercial real estate securities outside CDOs	5,816,849	2,095,541	17.19	2,098,566	17.24	
	-----	-----	-----	-----	-----	
Commercial real estate loans and equity outside CDOs						
Commercial real estate loans	368,433	405,782		404,217		
Commercial real estate	50,704	51,004		50,704		
	-----	-----		-----		
Total commercial real estate loans and equity outside CDOs	419,137	456,786		454,921		
	-----	-----		-----		
Commercial real estate securities included in CDOs						
Investment grade CMBS	375,502	377,291	100.48	354,561	94.42	
Investment grade REIT debt	223,445	233,939	104.70	226,583	101.40	
CMBS rated BB+ to B	656,207	566,181	86.28	513,446	78.24	
Credit tenant lease	24,317	24,837	102.14	24,995	102.79	
Commercial real estate loans	20,175	19,671	97.49	20,160	99.93	
	-----	-----	-----	-----	-----	
Total commercial real estate assets included in CDOs	1,299,647	1,221,919	94.02	1,139,745	87.70	
	-----	-----	-----	-----	-----	
Total commercial real estate assets	\$7,535,633	\$3,774,246		\$3,693,232		
	=====	=====		=====		

The Company's CDO offerings allow the Company to match fund its commercial real estate portfolio by issuing long-term debt to finance long-term assets. The CDO debt is non-recourse to the Company; therefore, the Company's losses are limited to its equity investment in the CDO. The CDO debt is also hedged to protect the Company from an increase in short-term interest rates. At December 31, 2005, over 82% of the estimated fair value of the Company's subordinated CMBS was

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match funded in the Company's CDOs in this manner. The Company retained 100% of the equity of CDOs I, II, III, HY3 and Euro (each as defined below) and recorded the transactions on its consolidated financial statements as secured financing.

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The table below summarizes the Company's CDO collateral and debt at December 31, 2006.

	Collateral at December 31, 2006		Debt at December 31, 2006		
	Adjusted Purchase Price	Loss Adjusted Yield	Adjusted Issue Price	Weighted Average Cost of Funds *	Net Spread
CDO I	\$ 467,786	8.08%	\$ 405,490	7.33%	.75%
CDO II	335,293	7.56%	291,261**	6.02%	1.54%
CDO III	378,932	7.08%	366,019**	5.00%	2.08%
CDO HY3	444,615	9.69%	402,089	6.42%	3.27%
Euro CDO	359,084	7.29%	347,715	5.10%	2.19%
	-----	----	-----	----	----
Total **	\$1,985,710	8.02%	\$1,812,574	6.02%	2.00%
	=====	=====	=====	=====	=====

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

\*\* The Company chose not to sell \$10,000 of par of CDO II debt rated BB, \$13,069 of par of CDO III debt rated BB and \$12,500 of par of Euro CDO debt rated BB.

The Company's first CDO transaction ("CDO I") was issued as Anthracite CDO 2002 CIBC-1 and closed on May 15, 2002. The Company issued \$403,633 of debt secured by a portfolio of commercial real estate securities with a total par of \$515,880 and an adjusted purchase price of \$431,995.

On December 10, 2002, the Company issued \$280,607 of debt through Anthracite CDO 2002-2 ("CDO II") secured by a separate portfolio of commercial real estate securities with a par of \$313,444 and an average adjusted purchase price of \$289,197. Included in the Company's second CDO was a ramp facility that was utilized to fund the purchase of an additional \$50,000 of par of below investment grade CMBS. The Company utilized the ramp in February 2003 and July 2003, to contribute \$30,000 of par of CSFB 03-CPN1 and \$20,000 of par of GECCM 03-C2, respectively. In July 2004, the Company issued a bond with a par of \$12,850 from CDO II. Before issuing this security, the Company amended the indenture to reduce the coupon from 9.0% to 7.6%.

On March 30, 2004, the Company issued its third CDO ("CDO III") through Anthracite CDO 2004-1. The total par value of bonds sold was \$372,456. The total cost of funds on a fully hedged basis was 5.0%. Included in CDO III was a \$50,000 ramp facility that was fully utilized at December 31, 2004.

On May 23, 2006, the Company closed its sixth CDO issuance ("CDO HY3") resulting in the issuance of \$417,000 of non-recourse debt to investors. The debt is secured by a portfolio of CMBS and subordinated commercial real estate loans.

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This debt was rated AAA through BBB- and the Company retained additional debt rated BB and 100% of the preferred shares issued by the CDO HY3.

On December 14, 2006, the Company closed its seventh CDO ("Euro CDO"). The Euro CDO sold E263,500 of non-recourse debt at a weighted average spread to Euro Libor of 60 basis points. The E263,500 consists of E251,000 of investment grade debt at a weighted average spread to Euro Libor of 50 basis points and E12,500 of below investment grade debt. The Company retained an additional E12,500 of below investment grade debt and all of the CDO's preferred shares. This transaction represents the Company's first CDO that was not U.S. dollar denominated.

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### SECURITIZATIONS

On November 9, 2004, the Company closed its fourth CDO ("CDO HY1") secured by a portfolio of below investment grade CMBS with an average rating of CCC. The CMBS portfolio was carried at its estimated fair value of \$109,933 on the Company's consolidated statement of financial condition based on price quotes received from third parties. The transaction was accounted for as a sale under SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities ("SFAS No. 140.") The Company received cash proceeds of \$140,425 as well as all of the CDO HY1 preferred shares that had an estimated fair value of \$15,885 at December 31, 2004. The transaction raised investable proceeds of \$95,799.

On July 26, 2005, the Company closed its fifth CDO ("CDO HY2") and issued non-recourse debt with a face amount of \$365,010. Senior investment grade notes with a face amount of \$240,134 were issued. The Company retained the floating rate BBB- note, the below investment grade notes and the preferred shares. The Company recorded CDO HY2 as a secured financing for accounting purposes and consolidated the assets, liabilities, income and expenses of CDO HY2 until the sale of the floating rate BBB- note in December 2005, at which point CDO HY2 qualified as a sale under SFAS No. 140.

### REAL ESTATE CREDIT PROFILE OF BELOW INVESTMENT GRADE CMBS

The Company views its below investment grade CMBS investment activity as two portfolios: Controlling Class CMBS and other below investment grade CMBS. 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 distinction between the two is in the rights the Company obtains with its investment in Controlling Class CMBS. Controlling Class rights allow the Company to influence the workout and/or disposition of defaults that occur in the underlying loans. These securities absorb the first losses realized in the underlying loan pools. The coupon payment on the non-rated security also can be reduced for special servicer fees charged to the trust. The next highest rated security in the structure then generally will be downgraded to non-rated and become the first to absorb losses and expenses from that point on. At December 31, 2006, the Company owns 29 trusts where it is in the first loss position and is designated as the controlling class representative by owning the lowest rated or non-rated CMBS class. The total par of the loans underlying these securities was \$42,398,701. At December 31, 2006, subordinated Controlling Class CMBS with a par of \$909,977 were included on the Company's consolidated statement of financial condition and subordinated Controlling Class CMBS with a par of \$696,883 were held as collateral for CDO HY1 and CDO HY2.

The Company's other below investment grade CMBS have more limited rights associated with its ownership to influence the workout and/or disposition of

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underlying loan defaults. The total par of the Company's other below investment grade CMBS at December 31, 2006 was \$154,524; the average credit protection, or subordination level, of this portfolio is 1.9%.

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The Company's investment in its subordinated Controlling Class CMBS securities by credit rating category at December 31, 2006 is as follows:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Weighted Subordination
	-----	-----	-----	-----	-----	-----
BB+	\$158,220	\$142,415	90.01	\$130,966	82.77	3.51
BB	135,874	116,085	85.44	111,000	81.69	2.81
BB-	120,226	94,256	78.40	86,317	71.80	3.13
B+	71,277	51,030	71.59	47,861	67.15	2.05
B	88,217	60,237	68.28	52,988	60.07	1.88
B-	66,160	37,680	56.95	35,001	52.90	1.28
CCC	9,671	3,823	39.53	3,596	37.19	0.88
NR	260,332	81,480	31.30	73,842	28.36	n/a
	-----	-----	-----	-----	-----	
Total	\$909,977	\$587,006	64.51	\$541,571	59.54	
	=====	=====	=====	=====	=====	

The Company's investment in its subordinated Controlling Class CMBS securities by credit rating category at December 31, 2005 is as follows:

	Par	Estimated Fair Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Weighted Subordination
	-----	-----	-----	-----	-----	-----
BB+	\$139,541	\$131,676	94.36	\$120,541	86.38	5.64
BB	92,583	81,469	88.00	76,527	82.66	4.43
BB-	110,514	92,116	83.35	85,829	77.66	4.15
B+	79,564	56,651	71.20	52,828	66.40	2.60
B	132,247	84,201	63.37	77,784	58.82	2.81
B-	23,775	13,216	55.59	12,303	51.75	1.24
NR	96,626	27,777	28.75	25,727	26.63	n/a
	-----	-----	-----	-----	-----	
Total	\$674,850	\$487,106	72.18	\$451,539	66.91	
	=====	=====	=====	=====	=====	

During 2006, the par amount of the Company's Controlling Class CMBS was reduced by \$10,874; of this amount, \$9,174 of the par reductions were related to Controlling Class CMBS held in CDO HY1 and CDO HY2. Further delinquencies and losses may cause the par reductions to continue and cause the Company to conclude that a change in loss adjusted yield is required along with a write-down of the adjusted purchase price through the income statement according to Emerging Issues Task Force ("EITF") Issue 99-20, Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets ("EITF 99-20"). Also during 2006, the loan pools were paid down by \$682,017. Pay down proceeds are distributed to the highest

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rated CMBS class first and reduce the percent of total underlying collateral represented by each rating category.

As the portfolio matures and expected losses occur, subordination levels of the lower rated classes of a CMBS investment will be reduced. This may cause the lower rated classes to be downgraded, which would negatively affect their estimated fair value and therefore the Company's net asset value. Reduced estimated fair value would negatively affect the Company's ability to finance any such securities that are not financed through a CDO or similar matched funding vehicle. In some cases, securities held by the Company may be upgraded to reflect seasoning of the underlying collateral and thus would increase the

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estimated fair value of the securities. During the twelve months ended December 31, 2006, 21 securities in nine of the Company's Controlling Class CMBS were upgraded by at least one rating agency and none were downgraded. Additionally, at least one rating agency upgraded 69 of the Company's non-Controlling Class commercial real estate securities. Three of the Company's investment grade REIT debt securities were downgraded during the twelve months ended December 31, 2006.

The Company considers delinquency information from the Lehman Brothers Conduit Guide to be the most relevant benchmark to measure credit performance and market conditions applicable to its Controlling Class CMBS holdings. The year of issuance, or vintage year, is important, as older loan pools will tend to have more delinquencies than newly underwritten loans. The Company owns Controlling Class CMBS issued in 1998, 1999, 2001, 2002, 2003, 2004, 2005 and 2006. Comparable delinquency statistics referenced by vintage year as a percentage of par outstanding at December 31, 2006 are shown in the table below:

Vintage Year	Underlying Collateral	Delinquencies Outstanding	Lehman Brothers Conduit Guide
-----	-----	-----	-----
1998	\$ 5,284,446	1.29%	1.22%
1999	592,717	2.22%	1.13%
2001	829,692	--	1.11%
2002	1,147,467	0.37%	0.70%
2003	2,086,852	1.22%	0.45%
2004	6,616,657	0.22%	0.26%
2005	12,110,707	0.33%	0.20%
2006	13,730,163	--	0.07%
	-----	-----	-----
Total	\$42,398,701	0.39%*	0.35%*

\* Weighted average based on current principal balance.

Delinquencies on the Company's CMBS collateral as a percent of principal are in line with expectations and are consistent with comparable data provided in the Lehman Brothers Conduit Guide. These seasoning criteria generally will adjust for the lower delinquencies that occur in newly originated collateral. See Item 7A - "Quantitative and Qualitative Disclosures About Market Risks" for a detailed discussion of how delinquencies and loan losses affect the Company.



The following table sets forth certain information relating to the aggregate principal balance and payment status of delinquent commercial mortgage loans underlying the Controlling Class CMBS held by the Company at December 31, 2006 and 2005:

	December 31, 2006			December 31, 2005		
	Principal	Number of Loans	% of Collateral	Principal	Number of Loans	Co
Past due 30 days to 60 days	\$ 70,123	10	0.17%	\$ 50,751	7	
Past due 60 days to 90 days	19,767	5	0.05	37,155	5	
Past due 90 days or more	11,365	7	0.03	79,758	20	
Real Estate owned	56,486	10	0.13	19,666	4	
Foreclosure	7,164	2	0.02	3,625	1	
Total Delinquent	\$164,905	34	0.39%	\$ 190,954	37	
Total Collateral Balance	\$42,398,701	4,667		\$29,668,349	3,596	

Of the 34 delinquent loans at December 31, 2006, 10 loans were real estate owned and being marketed for sale, 2 loans were in foreclosure and the remaining 22 loans were in some form of workout negotiations. The Controlling Class CMBS owned by the Company have a delinquency rate of 0.39%, which is consistent with industry averages. During 2006, the underlying collateral experienced early payoffs of \$682,017 representing 1.6% of the year-end pool balance. These loans were paid off at par with no loss. Aggregate losses related to the underlying collateral of \$19,279 were realized during year ended December 31, 2006. This brings cumulative realized losses to \$109,449, which is 21.3% of total estimated losses. These losses include special servicer and other workout expenses. This experience to date is in line with the Company's loss expectations. Realized losses and special servicer expenses are expected to increase on the underlying loans as the portfolio matures. Special servicer expenses are also expected to increase as portfolios mature.

To the extent that realized losses differ from the Company's original loss estimates, it may be necessary to reduce or increase the projected 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 yields remain appropriate.

The Company manages its credit risk through disciplined underwriting, diversification, active monitoring of loan performance and exercise of its right to influence the workout process for delinquent loans as early as possible. The Company maintains diversification of credit exposures through its underwriting process and can shift its focus in future investments by adjusting the mix of loans in subsequent acquisitions. The comparative profiles of the loans underlying the Company's CMBS by property type at December 31, 2006 and 2005 are

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as follows:

Property Type	12/31/06 Exposure		12/31/05 Exposure	
	Collateral Balance	% of Total	Collateral Balance	% of Total
Office	\$13,415,671	31.6%	\$9,406,148	31.7%
Retail	13,217,676	31.2	9,195,747	31.0
Multifamily	8,978,823	21.2	6,874,450	23.2
Industrial	3,332,194	7.9	2,060,953	7.0
Lodging	2,726,441	6.4	1,670,436	5.6
Healthcare	305,612	0.7	299,692	1.0
Other	422,284	1.0	160,923	0.5
Total	\$42,398,701	100%	\$29,668,349	100%

At December 31, 2006 and 2005, the commercial mortgage loans underlying the Controlling Class CMBS held by the Company were secured by properties at the locations identified below:

Geographic Location	Percentage (1)	
	2006	2005
California	16.1%	16.7%
New York	12.5	14.5
Texas	8.8	8.7
Florida	7.2	8.1
Other (2)	55.4	52.0
Total	100%	100.0%

(1) Based on a percentage of the total unpaid principal balance of the underlying loans.

(2) No other individual category comprises more than 5% of the total.

As the portfolio matures and expected losses occur, subordination levels of the lower rated classes of a CMBS investment will be reduced. This may cause the lower rated classes to be downgraded, which would negatively affect their estimated fair value and therefore the Company's net asset value. Reduced estimated fair value will negatively affect the Company's ability to finance any such securities that are not financed through a CDO or similar matched funding vehicle. In some cases, securities held by the Company may be upgraded to reflect seasoning of the underlying collateral and thus would increase the estimated fair value of the securities.

The Company's interest income calculated in accordance with EITF 99-20 for its CMBS is computed based upon a yield, which assumes credit losses will occur. The yield to compute the Company's taxable income does not assume there would be credit losses, as a loss can only be deducted for tax purposes when it has occurred. This is the primary difference between the Company's income in

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accordance with accounting principles generally accepted in the United States of America ("GAAP") and taxable income. As a result, for the years 1998 through 2006, the Company's GAAP income was approximately \$44,856 lower than its taxable income.

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### COMMERCIAL REAL ESTATE LOAN ACTIVITY

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

The following table summarizes the Company's commercial real estate loan portfolio by property type at December 31, 2006, 2005, and 2004:

Property Type	December 31, 2006		Loans Outstanding December 31, 2005		December 31, 2004		Weighted Average Yield		
	Amount	%	Amount	%	Amount	%	2006	2005	2004
Office	\$130,016	27.0%	\$ 94,432	25.8%	\$ 88,311	33.5%	8.2%	8.9%	9.2%
Residential	57,917	12.0	57,466	15.7	13,480	5.1	10.7	8.6	12.2
Retail	194,938	40.5	76,502	20.9	59,070	22.4	7.7	7.3	6.6
Hotel	38,899	8.1	79,840	21.8	102,645	39.0	10.0	8.6	7.2
Storage	34,009	7.1	32,913	9.0	--	--	9.0	9.1	--
Communication Tower	--	--	20,000	5.5	--	--	--	9.4	--
Industrial	19,317	4.0	2,423	0.7	--	--	9.1	8.1	--
Other Mixed Use	6,649	1.3	2,230	0.6	--	--	8.7	8.1	--
Total	\$481,745	100.0%	\$365,806	100.0%	\$263,506	100.0%	8.6%	8.5%	8.0%

Included in the table above are non-U.S. dollar denominated commercial real estate loans with a carrying value of \$243,377, \$129,951, and \$21,119 at December 31, 2006, 2005, and 2004, respectively. The Company finances its non-U.S. dollar denominated loans by borrowing in the applicable local currency and hedging the un-financed portion.

For the year ended December 31, 2006, the Company purchased \$328,439 of commercial real estate loans. These acquisitions include commercial real estate loans denominated in British pounds of (pound)33,715 (\$61,008) and loans denominated in Euros of (euro)133,563 (\$171,464). For the year ended December 31, 2006, the Company experienced repayments of \$197,094 related to its commercial real estate loan portfolio.

Also included in commercial real estate loans are the Company's investments in Carbon Capital, Inc. ("Carbon I") and Carbon Capital II, Inc. ("Carbon II", and collectively with Carbon I, the "Carbon Capital Funds.") For the year ended December 31, 2006, the Company recorded \$11,668 of income for the Carbon Capital Funds. Carbon II increased its investment in U.S. commercial real estate loans by originating 17 loans for a total investment of \$452,541 during 2006. Paydowns in Carbon II during 2006 totaled \$217,911. As loans are repaid, Carbon II has redeployed capital into acquisitions of additional loans for the portfolio. The

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Carbon I investment period has expired and as repayments continue to occur, capital will be returned to investors.

The Company's investments in the Carbon Capital Funds are as follows:

	December 31, 2006	December 31, 2005
	-----	-----
Carbon I	\$ 3,144	\$18,458
Carbon II	69,259	41,185
	-----	-----
	\$72,403	\$59,643
	=====	=====

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At December 31, 2006, all commercial real estate loans owned directly by the Company were performing in line with expectations. As previously reported, investments held by Carbon II include a \$24,546 commercial real estate mezzanine loan which defaulted during July 2006. The default was subsequently cured. On March 9, 2007, the loan matured. The borrower did not repay the loan on the due date. In addition, the senior mortgage holder did not grant the borrower's request for extension of time to accommodate a sale of the property or refinancing of the loan. As a result, the loan is in default. The Company believes the underlying asset is sufficient collateral to repay the Company's loan in full. The underlying property is a hotel located in the South Beach area of Miami, Florida.

During February 2007, two other loans held by Carbon II defaulted. The aggregate carrying value of the two loans on Carbon II's consolidated financial statements is \$24,000 (\$12,000 per loan). The underlying properties for both loans are multi-family assets being converted to condominiums that are located in Florida. Carbon II is negotiating a workout arrangement with the borrower for one loan, whereby the borrower will cure its default and make additional capital contributions to sustain the property while the borrower continues its sales program. Based on credit analysis performed for this property, Carbon II believes a loan loss reserve is not necessary at this time.

For the second loan, the borrower was not able to achieve sufficient condominium sales to complete the condominium conversion. The borrower has indicated it will not contribute additional capital to sustain the rental property until such time as the condominium market recovers. As a result, Carbon II is expected to take title to the property and currently intends to operate it as a rental property while preparing the property for sale. Based on the credit analysis performed for this property, Carbon II has established a loan loss reserve of \$5,180 for the loan, of which the Company's share is \$1,361. All other commercial real estate loans in the Carbon Capital Funds are performing as expected.

### COMMERCIAL REAL ESTATE

At December 31, 2006, the Company had invested an aggregate of \$92,603 in BlackRock Diamond Property Fund, Inc. ("BlackRock Diamond"). BlackRock Diamond is a private real estate investment trust ("REIT") managed by BlackRock Realty Advisors, Inc., a subsidiary of the Company's Manager. BlackRock Diamond's investment objective is to seek a high risk adjusted return through "value-added" capital appreciation and current income on properties through out the United States. This means the BlackRock Diamond's focuses on operating

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properties that will be repositioned, renovated, or expanded to achieve maximum returns. Part of the investment strategy includes a budgeted amount of capital expenditures that are used to improve the value of the investment and realize the full value potential of a given property. BlackRock Diamond relies on the Manager's extensive relationships in the real estate markets to source opportunities. BlackRock Diamond focuses on large urban locations where it believes the real estate equity markets will outperform.

BlackRock Diamond is an open-end fund. As such, it allows shares to be redeemed at a price equal to its quarter-end net asset value upon 60 days notice. The assets are subject to quarterly appraisals with one independent appraisal done annually. The Company does not pay a separate management fee to the Manager for management services associated with its investment in BlackRock Diamond.

The Company had a 21% ownership in BlackRock Diamond at December 31, 2006 and recorded \$15,763 of income during 2006 with respect to this investment under the equity method. At December 31, 2006, the Company had \$7,397 of remaining capital commitments to BlackRock Diamond, all of which was called in January 2007.

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For the year ended December 31, 2006, the Company recorded \$15,763 of income, consisting of \$1,463 of current income and \$14,300 of unrealized gains on the underlying portfolio assets. At December 31, 2006, BlackRock Diamond's portfolio consisted of 26 assets with a total estimated market value of approximately \$680,134. All financial information was reported by BlackRock Diamond.

The Company purchased a defaulted loan from a Controlling Class CMBS trust during the first quarter of 2006. The loan was secured by a first mortgage on a multi-family property in Texas. Subsequent to the loan purchase, the Company foreclosed on the loan and acquired title to the property in the process. The Company sold the property during the second quarter of 2006 and recorded a gain from discontinued operations of \$1,366 on the consolidated statement of operations.

The Company has an indirect investment in a commercial real estate development fund located in India. At December 31, 2006, the Company's capital committed was \$11,000, of which \$3,850 had been drawn. The entity conducts its operations in the local currency, Indian Rupees.

### CRITICAL ACCOUNTING ESTIMATES

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

#### Securities Available-for-sale

The Company has designated certain investments in mortgage-backed securities, mortgage-related securities and certain other securities as available-for-sale. Securities available-for-sale are carried at estimated fair value with the net unrealized gains or losses reported as a component of accumulated other comprehensive income in stockholders' equity. Many of these investments are

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relatively illiquid, and management must estimate their values. In making these estimates, management generally utilizes market prices provided by dealers who make markets in these securities, but may, under certain circumstances, adjust these valuations based on management's judgment. Changes in the valuations do not affect the Company's reported net income or cash flows, but impact stockholders' equity and, accordingly, book value per share.

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

Income on these securities is recognized based upon a number of assumptions that are subject to uncertainties and contingencies. Examples include, among other things, the rate and timing of principal payments (including prepayments, repurchases, defaults and liquidations), the pass-through or coupon rate and interest rate fluctuations. Additional factors that may affect the Company's reported interest income on its commercial real estate securities include interest payment shortfalls due to delinquencies on the underlying commercial mortgage loans, the timing and magnitude of credit losses on the commercial mortgage loans underlying the securities that are a result of the general

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condition of the real estate market (including competition for tenants and their related credit quality) and changes in market rental rates. These uncertainties and contingencies are difficult to predict and are subject to future events that may alter the assumptions.

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

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

### Impairment - Securities

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

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

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

### 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 entities ("VIEs") in which the Company is the primary beneficiary under Financial Accounting Standards Board ("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 expected losses and/or the majority of the expected returns. The Company has evaluated its investments for potential variable interests by evaluating the sufficiency of the entity's equity investment at risk to absorb losses. All significant inter-company balances and transactions have been eliminated in consolidation.

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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. Additionally, the standard setters continue to review the FIN 46R provisions related to the computations used to determine the primary beneficiary of a VIE. Future guidance from the standard setters may require the Company to consolidate CMBS trusts in which the Company has invested.

### Commercial Mortgage Loans

The Company purchases and originates commercial mortgage loans to be held as long-term investments. The Company also has investments in private opportunity funds that invest in commercial mortgage loans that are managed by the Manager. Management periodically must evaluate each loan for possible impairment. Impairment is indicated when it is deemed probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan. If a loan were determined to be impaired, the Company would establish a reserve for probable losses and a corresponding charge to earnings. Given the nature of the Company's loan portfolio and the underlying commercial real estate collateral, significant judgment of management is required in determining impairment and the resulting loan loss allowance, which includes but is not limited to making assumptions regarding the value of the real estate that

secures the commercial mortgage loan.

#### Equity Investments

For those investments in real estate entities where the Company does not control the investee, or is not the primary beneficiary of a VIE, but can exert significant influence over the financial and operating policies of the investee, the Company uses the equity method of accounting. The Company recognizes its share of each investee's income or loss, and reduces its investment balance by distributions received. The Company owns an equity method investment in BlackRock Diamond, a privately held REIT that maintains its financial records on a fair value basis. The Company has retained such accounting relative to its investment in this REIT pursuant to EITF Issue 85-12, Retention of Specialized Accounting for Investments in Consolidation.

#### Derivative Instruments

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

#### Securitizations

When the Company sells assets in securitizations, it can retain certain tranches which are considered retained interests in the securitization. Gain or loss on the sale of assets depends in part on the previous carrying amount of the financial assets securitized, allocated between the assets sold and the retained

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interests based on their relative fair value at the date of securitization. To obtain fair values, quoted market prices are used. Gain or loss on securitizations of financial assets is reported as a component of sale of securities available-for-sale on the consolidated statement of operations. Retained interests are carried at estimated fair value on the consolidated statement of financial condition. Adjustments to estimated fair value for retained interests classified as securities available-for-sale are included in accumulated other comprehensive income on the consolidated statement of financial condition.

#### RECENT ACCOUNTING PRONOUNCEMENTS

##### Reverse Repurchase Agreements

Accounting standard setters are currently reviewing the treatment of transactions where mortgage-backed securities purchased from a particular counterparty are financed via a repurchase agreement with the same counterparty. Currently, the Company records such assets and the related financing gross on the 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, because the security is



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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 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's net equity would not be materially affected. At December 31, 2006, the Company has identified available-for-sale securities with a fair value of approximately \$36,649 which had been purchased from and financed with reverse repurchase agreements totaling approximately \$31,375 with the same counterparty since their purchase. If the Company were to change the current accounting treatment for these transactions at December 31, 2006, total assets and total liabilities would be reduced by approximately \$31,375.

### 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 VIEs in which the Company is the primary beneficiary under 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 significant inter-company balances and transactions have been eliminated in consolidation.

The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the QSPE criteria.

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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 consolidate CMBS trusts in which the Company has invested.

### Impairment of Investments

In November 2005, the FASB issued FASB Staff Position ("FSP") FAS 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, which provides guidance for determining when impairment charges should be taken on certain debt and equity securities. FSP FAS 115-1/124-1

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requires that debt and equity securities subject to the provisions of SFAS No. 115, and equity securities subject to the provisions of APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock ("APB Opinion No. 18"), but which are not accounted for under the equity method (i.e., securities accounted for under the cost method) shall be reviewed for impairment when circumstances warrant. For securities subject to SFAS No. 115, a review for other-than-temporary impairments shall occur in each accounting period where the fair value of the security is less than its cost. For securities subject to APB Opinion No. 18, a review for other-than-temporary impairments shall occur in each accounting period where a) circumstances indicate that impairment may exist and b) the fair value of the security is less than its carrying value. The provisions of the FSP were required to be applied to reporting periods beginning after December 15, 2005. The adoption of FSP FAS 115-1/124-1 on January 1, 2006 had no material impact on the Company's consolidated financial statements.

### Certain Hybrid Financial Instruments

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments ("SFAS No. 155"), which amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS No. 133"), 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 which 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 Company is currently evaluating the impact of adopting SFAS No. 155.

### Determining the Variability in a Potential VIE

The FASB issued FASB Staff Position FIN 46(R)-6, Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R) ("FSP FIN 46(R)-6") in April 2006. FSP FIN 46(R)-6 addresses the application of FIN 46(R), Consolidation of Variable Interest Entities ("FIN 46(R)"), in

determining whether certain contracts or arrangements with a VIE are variable interests by requiring companies to base such evaluations on an analysis of the VIE's purpose and design, rather than its legal form or accounting classification.

FSP FIN 46(R)-6 is required to be applied for all reporting periods beginning

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after June 15, 2006. The adoption of this FSP did not result in material differences from the Company's existing accounting policies regarding the consolidation of VIEs.

### 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 No. 48"). FIN No. 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 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 Company is currently evaluating the impact of implementing this new standard but does not expect its implementation to have a material impact on the consolidated financial statements.

### Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements ("SFAS No. 157"). 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 its 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 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 is currently evaluating the impact of adopting SFAS No. 157.

### Effects of Prior Year Misstatements

In September 2006, the SEC issued Staff Accounting Bulletin ("SAB") No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements ("SAB No. 108"). SAB No. 108 provides guidance on the consideration of effects of the prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. The SEC staff believes registrants must quantify errors using both a balance sheet and income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB No. 108 is effective for the first annual period ending after November 15, 2006 with early application encouraged. The adoption of SAB No. 108 on December 31, 2006 had no effect on the Company's consolidated financial statements.

### Valuation of Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities ("SFAS No. 159"). 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

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option has been elected should be reported in earnings. The decision to elect the fair value options 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 separately in the balance sheet 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 is currently analyzing the potential impact of adoption of SFAS No. 159.

**INTEREST INCOME:** The following tables set forth information regarding interest income from certain of the Company's interest-earning assets.

	Year Ended December 31,			Variance		
				2006 vs. 2005		2005 vs.
	2006	2005	2004	Variance	%	Variance
Commercial real estate securities	\$168,271	\$142,634	\$123,860	\$25,637	18.0%	\$18,774
Commercial mortgage loan pools	52,917	54,025	39,672	(1,108)	(2.1)%	14,353
Commercial real estate loans	40,537	23,181	11,896	17,356	74.9%	11,285
RMBS	11,858	9,851	18,901	2,007	20.4%	(9,050)
Cash and cash equivalents	2,403	2,077	638	326	15.7%	1,439
Total	\$275,986	\$231,768	\$194,967	\$44,218	19.1%	\$36,801

The following table reconciles interest income and total income for the years ended December 31, 2006, 2005 and 2004.

	Year Ended December 31,			Variance		
				2006 vs.2005		2005
	2006	2005	2004	Variance	%	Variance
Interest income	\$275,986	\$231,768	\$194,967	\$44,218	19.1%	\$36,801
Earnings from BlackRock Diamond	15,763	299	--	15,464	5,171.9%	299
Earnings from Carbon I	924	4,983	6,763	(4,059)	(81.5)%	(1,780)
Earnings from Carbon II	10,744	6,805	297	3,939	57.9%	6,508
Earnings from real estate joint ventures	--	59	1,097	(59)	n/a	(1,038)
Other income	--	--	742	--	n/a	(742)
Total Income	\$303,417	\$243,914	\$203,866	\$59,503	24.4%	\$40,048

For the year ended December 31, 2006 versus 2005, interest income increased \$44,218, or 19.1%. For the year ended December 31, 2005 versus 2004, interest income increased \$36,801, or 18.9%. The Company continued to increase its investments in commercial real estate securities and loans, resulting

in an increase of \$42,993, or 25.9%, during 2006 and \$30,059, or 22.1%, during 2005. Income from BlackRock Diamond was \$15,763 and \$299 for the year ended December 31, 2006 and 2005, respectively. The Company began investing in BlackRock Diamond in the fourth quarter of 2005. BlackRock Diamond maintains its financial records on a fair value basis. The Company has retained such accounting in its consolidated financial statements pursuant to EITF Issue 85-12, Retention of Specialized Accounting for Investments in Consolidation. For the year ended December 31, 2006 and 2005, respectively, income from Carbon I decreased \$(4,059), or (81.5)%, and \$(1,780), or (26.3)%. The decrease in Carbon I income is attributable to Carbon I's investment period expiring on July 12, 2004 and the subsequent pay down of its assets. For the year ended December 31, 2006 and 2005, respectively, income from Carbon II increased \$3,939, or 57.9%, and \$6,508, or 2,191.3%. The increase in Carbon II income during 2006 is attributable to the investment of additional capital in 2006 and prepayment penalties received on its underlying commercial real estate loans primarily during the second quarter of 2006. The increase in Carbon II income during 2005 is attributable to the investment of additional capital subsequent to the Company's initial investment in Carbon II in the fourth quarter of 2004. The consolidation of a VIE (see Note 5 of the consolidated financial statements) that included commercial mortgage loan pools decreased interest income by \$(1,108) during 2006 and increased interest income by \$14,353 during 2005. The VIE was consolidated for year ended December 31, 2006 and 2005 and for nine months of 2004, as the entity was acquired in April 2004.

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

	Year Ended December 31,			Variance		
				2006 vs. 2005		2005 v
	2006	2005	2004	Variance	%	Variance
Collateralized debt obligations	\$ 81,337	\$ 69,794	\$ 58,986	\$11,543	16.5%	\$10,808
Commercial mortgage loan pools	50,213	50,864	37,408	(651)	(1.3%)	13,456
Commercial real estate securities*	39,322	17,231	7,517	22,091	128.2%	9,714
Commercial real estate loans	10,626	5,907	1,790	4,719	79.9%	4,117
RMBS	14,916	9,821	7,016	5,095	51.9%	2,805
Senior unsecured notes	1,299	--	--	1,299	n/a	--
Junior subordinated notes - net	12,447	1,543	--	10,904	706.7%	1,543
Cash flow hedges	1,966	7,110	14,434	(5,144)	(72.3)%	(7,324)
Hedge ineffectiveness**	262	1,188	1,015	(926)	(77.9)%	173
Total Interest Expense	\$212,388	\$163,458	\$128,166	\$48,930	29.9%	\$35,292

\* Includes \$227, \$124, and \$119 of interest expense for the years ended December 31, 2006, 2005, and 2004, respectively, from short-term financings of securities related to the consolidation of commercial mortgage loan pools.

\*\* See Note 16 of the consolidated financial statements, Derivative

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Instruments and Hedging Activities, for a further description of the Company's hedge ineffectiveness.

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For the year ended December 31, 2006 and 2005, respectively, interest expense increased \$48,930, or 29.9%, and \$35,292, or 27.5%. The increase in interest expense related to CDOs of \$11,543, or 16.5%, during 2006 is primarily attributable to the issuance of CDO HY3 and the Euro CDO in 2006. The increase in interest expense related to CDOs of \$10,808, or 18.3%, during 2005 is primarily attributable to the issuance of CDO III and CDO HY2 which was accounted for as a secured financing from July 2005 through December 2006. The financing of additional commercial real estate securities and commercial real estate loans along with higher short-term borrowing rates increased interest expense \$26,810, or 115.9%, and \$13,826, or 148.6%, respectively, for year ended December 31, 2006 and 2005, respectively. Interest expense related to the senior unsecured notes was \$1,299 for the year ended December 31, 2006. The Company issued \$75,000 of senior unsecured notes during the fourth quarter of 2006. For year ended December 31, 2006 and 2005, respectively, the issuance of \$175,000 of junior subordinated notes since the third quarter of 2005 increased interest expense \$10,904 and \$1,543. Cash flow hedge expense decreased \$5,144, or 72.5%, and \$7,324, or 50.7%, for the year ended December 31, 2006 and 2005, respectively. This decrease is due to the cash flow hedges offsetting higher short-term interest rates on floating rate liabilities. The consolidation of a VIE (see Note 5 of the consolidated financial statements) that included commercial mortgage loan pools decreased interest expense by \$(548), or (1.1)%, during 2006 and increased interest expense by 13,461, or 35.9%, in 2005. The VIE was consolidated for years ended December 31, 2006 and 2005 and for nine months of 2004 as the entity was acquired in April 2004.

**NET INTEREST MARGIN AND NET INTEREST SPREAD FROM THE PORTFOLIO:** The Company considers its interest generating portfolio to consist of its securities available-for-sale, securities held-for-trading, commercial mortgage loans, and cash and cash equivalents because these assets relate to its core strategy of acquiring and originating high yield loans and securities backed by commercial real estate, while at the same time maintaining a portfolio of investment grade securities to enhance the Company's liquidity. The Company's equity investments, which include the Carbon Capital Funds and BlackRock Diamond, also generate a significant portion of the Company's income.

The Company believes interest income and expense related to these assets excluding the effects of hedge ineffectiveness and the consolidation of a VIE better reflect the Company's net interest margin and net interest spread from its portfolio. Adjusted interest income and adjusted interest expense are better indicators for both management and investors of the Company's financial performance over time.

The following charts reconcile interest income and expense to adjusted interest income and adjusted interest expense.

	For the Year Ended December 31		
	2006	2005	2004
	-----	-----	-----
Interest income	\$ 275,986	\$ 231,768	\$ 19

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Interest expense related to the consolidation of commercial mortgage loan pools\*

	(50,213)	(50,864)	(3
	-----	-----	-----
Adjusted interest income	\$ 225,773	\$ 180,904	\$ 15
	-----	-----	-----

\* Includes short-term interest expense of \$227, \$124, and \$119 for the year ended December 31, 2006, 2005, and 2004, respectively.

	For the Year Ended 2006	2005	December
	-----	-----	-----
Interest expense	\$ 212,388	\$ 163,458	\$
Interest expense related to the consolidation of commercial mortgage loan pools	(50,213)	(50,864)	
Hedge ineffectiveness	(262)	(1,188)	
	-----	-----	-----
Adjusted interest expense	\$ 161,913	\$ 111,406	\$
	-----	-----	-----

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

The ratios below are also presented including the income from equity investments. The Company believes the ratios including income from equity investments are indicative of the performance of the Company's entire portfolio.

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

	For the Year Ended 2006	2005	December
	-----	-----	-----
Adjusted interest income	\$ 225,773	\$ 180,904	
Adjusted interest expense	\$ 161,913	\$ 111,406	
Adjusted net interest income ratios			
Net interest margin	2.1%	3.0%	
Average yield	7.4%	7.8%	
Cost of funds	6.1%	5.5%	
Net interest spread	1.3%	2.3%	

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Ratios including income from equity investments

Net interest margin	2.9%	3.4%
Average yield	7.9%	8.1%
Cost of funds	6.1%	5.5%
Net interest spread	1.8%	2.6%

Net interest margin and net interest spread have declined due to CMBS spread tightening and the yield curve having been flat to inverted in recent periods.

OTHER EXPENSES: Expenses other than interest expense consist primarily of management fees, incentive fees and general and administrative expenses. The table below summarizes those expenses for the years ended December 31, 2006, 2005, and 2004, respectively.

	For the Year Ended December 31,			Variance			
				2006 vs. 2005		2005 vs. 2004	
	2006	2005	2004	Variance	%	Variance	%
Management fee	\$12,617	\$10,974	\$ 8,956	\$1,643	15.0%	\$2,018	22.5%
Incentive fee	5,919	4,290	--	1,629	38.0%	4,290	n/a
Incentive fee- stock based	2,761	--	--	2,761	--	n/a	n/a
General and administrative expense	4,533	3,917	3,427	616	15.8%	490	14.3%
Total other expenses	\$25,830	\$19,181	\$12,383	\$6,649	34.7%	\$6,798	54.9%

Commencing in March 2004, management fees are based on 2% of average quarterly stockholders' equity. The increase of \$1,643, or 15.0%, from 2005 and \$6,308, or 70.4%, from 2004 is primarily due to the increase in the Company's stockholders' equity. The Manager earned an incentive fee of \$5,919 and \$4,290 in 2006 and 2005, respectively, as the Company achieved the necessary performance goals specified in the Management Agreement. The expense of \$2,761 for 2006 is the related to the stock based incentive fee that was approved by the Company's Board of Directors in February 2006. See Note 14 of the consolidated financial statements, Transactions with Affiliates, for further discussion of the Company's Management Agreement.

General and administrative expense is comprised of accounting agent fees, custodial agent fees, directors' fees, fees for professional services, insurance premiums, broken deal expenses, and due diligence costs. The increase in general and administrative expense for the year ended December 31, 2006 and 2005 is primarily attributable to costs associated with the Company's global expansion.

OTHER GAINS (LOSSES): During the year ended December 31, 2006, the Company sold seven CMBS held as collateral for three of its CDOs, resulting in a realized gain of \$28,520. The gain from these seasoned CMBS was a result of increased value of the securities due to multiple credit upgrades and spread tightening of approximately 475 basis points. Investment grade CMBS owned by the Company outside of its CDOs were used to replace this collateral.



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During the year ended December 31, 2006, the Company changed its financing strategy and de-designated a portion of its cash flows hedges and incurred a loss of \$12,661. The Company changed its financing strategy to emphasize the use of 90-day reverse repurchase agreements and concurrently reduced the use of 30-day reverse repurchase agreements. The Company expects 90-day repurchase agreements to be its primary source for short-term financings in future periods. As a result of the reduction in the balance of 30-day reverse repurchase agreements, certain interest swaps that were hedging the 30-day reverse repurchase agreements were de-designated as hedges.

During the years ended December 31, 2006, 2005, and 2004, respectively, the Company sold a portion of its securities available-for-sale resulting in realized gains of \$512, \$16,543, and \$17,544. The gain on sales of securities available-for-sale during 2004 and 2005, respectively, primarily are attributable to CDO HY1 and CDO HY2. The gain (loss) on securities held-for-trading of \$3,254, \$(1,999), and \$11,464 for the years ended December 31, 2006, 2005, and 2004, respectively, consisted primarily of realized and unrealized gains and losses on U.S. Treasury and Agency securities, forward commitments to purchase or sell agency RMBS and hedges. The net foreign currency gain of \$2,161 and \$134 for the years ended December 31, 2006 and 2005, respectively, relates to the Company's hedging of its net investment in commercial mortgage loans denominated in pounds sterling and euros. The losses on impairment of assets of \$7,880, \$5,088, and \$26,018 for the years ended December 31, 2006, 2005, and 2004, respectively, were related to the impairment charges of Controlling Class CMBS and franchise loan backed securities under EITF 99-20. (See Note 3 of the consolidated financial statements.)

**INCOME FROM DISCONTINUED OPERATIONS:** The Company purchased a defaulted loan from a Controlling Class CMBS trust during the first quarter of 2006. The Company sold the property during the second quarter of 2006 and recorded a gain from discontinued operations of \$1,366 on the consolidated statement of operations.

**DIVIDENDS DECLARED:** During the year ended December 31, 2006, the Company declared dividends to common stockholders totaling \$66,017, or \$1.15 per share, of which \$49,246 was paid during the year and \$16,771 was paid on February 1, 2007. During the year ended December 31, 2005, the Company declared dividends to common stockholders totaling \$61,168, or \$1.12 per share, of which \$45,394 was paid during the 2005 calendar year and \$15,774 was paid on February 1, 2006. During the year ended December 31, 2004, the Company declared dividends to common stockholders totaling \$58,208, or \$1.12 per share, of which \$43,287 was paid during the year and \$14,920 was paid on February 1, 2005. For U.S. Federal income tax purposes, the dividends are ordinary income to the Company's stockholders.

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### CHANGES IN FINANCIAL CONDITION

**Securities available-for-sale:** The Company's securities available-for-sale, which are carried at estimated fair value, included the following at December 31, 2006 and December 31, 2005:

Security Description	December 31, 2006		December 31, 2005	
	Estimated Fair Value	Percentage	Estimated Fair Value	Percentage

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Commercial mortgage-backed securities:				
CMBS IOs	\$ 69,352	2.7%	\$ 103,363	5
Investment grade CMBS	795,543	30.4	509,835	24
Non-investment grade rated subordinated securities	686,019	26.2	675,995	32
Non-rated subordinated securities	80,167	3.1	26,411	1
Credit tenant lease	24,318	0.9	24,837	1
Investment grade REIT debt	249,244	9.5	255,767	12
Multifamily agency securities	449,827	17.2	263,362	12
CDO investments	117,246	4.5	124,549	6
	-----	-----	-----	-----
Total CMBS	2,471,716	94.5	1,984,119	95
	-----	-----	-----	-----
Residential mortgage-backed securities:				
Agency adjustable rate securities	1,774	0.1	76,491	3
Residential CMOs	130,850	5.0	725	0
Hybrid adjustable rate mortgages ("ARMs")	11,516	0.4	15,601	0
	-----	-----	-----	-----
Total RMBS	144,140	5.5	92,817	4
	-----	-----	-----	-----
Total securities available-for-sale	\$2,615,856	100.0%	\$2,076,936	100
	=====	=====	=====	=====

Borrowings: At December 31, 2006 and 2005, the Company's debt consisted of credit facilities, CDOs, senior unsecured notes, trust preferred securities, reverse repurchase agreements, and commercial mortgage loans pools collateralized by a pledge of most of the Company's securities available-for-sale, securities held-for-trading, and its commercial mortgage loans. The Company's financial flexibility is affected by its ability to renew or replace on a continuous basis its maturing short-term borrowings. At December 31, 2006 and 2005, the Company obtained financing in amounts and at interest rates consistent with the Company's short-term financing objectives.

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

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

	For the Year Ended December 31, 2006		
	December 31, 2006 Balance	Maximum Balance	Range of Maturities
	-----	-----	-----
CDO debt*	\$1,812,574	\$1,812,574	5.3 to 9.7 years
Commercial mortgage loan pools	1,250,503	1,278,908	2.0 to 12.0 years
Reverse repurchase agreements	799,669	1,079,980	8 to 81 days
Credit facilities	75,447	403,188	8 days to 1.1 years

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Senior unsecured notes	75,000	75,000	10.0 years
Junior subordinated notes	180.477	180,407	29.1 years**

	For the Year Ended December 31, 2005		
	December 31, 2005 Balance	Maximum Balance	Range of Maturities
CDO debt*	\$1,066,930	\$1,306,963	5.9 to 8.1 years
Commercial mortgage loan pools	1,278,908	1,294,058	3.0 to 13.0 years
Reverse repurchase agreements	816,641	888,712	16 days to 20.0 years
Credit facilities	284,675	350,554	130 days to 2.0 years
Junior subordinated notes	77,380	77,380	29.7 years**

\* Disclosed as adjusted issue price. Total par of the Company's CDO debt at December 31, 2006 and 2005 was \$1,824,063 and \$1,079,463, respectively.

\*\* The junior subordinated notes can be redeemed at par by the Company beginning in October 2010.

The table above does not include interest payments on the Company's borrowings. Such disclosure of interest payments has been omitted because certain borrowings require variable rate interest payments. The Company's total interest payments for the year ended December 31, 2006 were \$208,879.

At December 31, 2006, the Company's borrowings had the following weighted average yields and range of interest rates and yields:

	Reverse Repurchase Agreements	Lines of Credit	Commercial Mortgage Loan Pools	Collateralized Debt Obligations	Senior Unsecured Notes	Jun Subord No
Weighted average yield	5.37%	6.69%	3.99%	6.02%	7.21%	7.
Interest Rate						
Fixed	--%	--%	3.99%	6.68%	7.21%	7.
Floating	5.37%	6.69%	--%	5.58%	--%	
Effective Yield						
Fixed	--%	--%	3.99%	7.27%	7.21%	7.
Floating	5.37%	6.69%	--%	5.58%	--%	

**HEDGING INSTRUMENTS:** The Company may modify its exposure to market interest rates by entering into various financial instruments that adjust portfolio duration. These financial instruments are intended to mitigate the effect of changes in interest rates on the value of the Company's assets and the cost of borrowing.

Interest rate hedging instruments at December 31, 2006 and 2005 consisted of the

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following:

	At December 31, 2006			
	Notional Value	Estimated Fair Value	Unamortized Cost	Average Remaining Term (years)
Cash flow hedges	\$644,200	\$5,048	--	7.91
CDO cash flow hedges	895,499	8,230	--	7.19
Trading swaps	80,000	2,033	--	3.27
CDO timing swaps	223,445	212	--	6.08
CDO LIBOR cap	85,000	(38)	1,407	6.40

	At December 31, 2005			
	Notional Value	Estimated Fair Value	Unamortized Cost	Average Remaining Term (years)
Cash flow hedges	\$500,350	\$ 6,234	--	8.42
CDO cash flow hedges	701,603	10,616	--	7.51
Trading swaps	133,000	4,032	--	6.83
CDO timing swaps	223,445	(37)	--	7.08
CDO LIBOR cap	85,000	1,419	1,407	7.40

Foreign currency agreements at December 31, 2006 consisted of the following:

	At December 31, 2006		
	Estimated Fair Value	Unamortized Cost	Average Remaining Term
Currency swaps	\$ 1,179	\$ --	12.53 years
CDO currency swaps	(1,418)	--	12.53 years
Forwards	(2,659)	--	10 days

	At December 31, 2005		
	Estimated Fair Value	Unamortized Cost	Average Remaining Term
Forwards	\$ 1,108	--	10 days

The Company did not have any currency swaps at December 31, 2005.

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### CAPITAL RESOURCES AND LIQUIDITY

The Company requires capital to fund its investment activities and operating expenses. The Company believes it currently has sufficient access to capital resources to fund its existing business plan. The Company's capital sources include cash flow from operations, borrowings under reverse repurchase agreements, credit facilities, CDOs, and the issuance of preferred and common equity securities.

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The distribution requirements under the REIT provisions of the Code limit the Company's ability to retain earnings and thereby replenish or increase capital committed to its operations. However, the Company believes that its access to significant capital resources and financing will enable the Company to meet current and anticipated capital requirements.

The Company believes that its existing sources of funds will be adequate for purposes of meeting its short- and long-term liquidity needs. The Company's ability to meet its long-term (i.e., beyond one year) liquidity requirements is subject to obtaining additional debt and equity financing. Any decision by the Company's lenders and investors to provide the Company with financing will depend upon a number of factors, such as the Company's compliance with the terms of its existing credit arrangements, the Company's financial performance, industry or market trends, the general availability of and rates applicable to financing transactions, such lenders' and investors' resources and policies concerning the terms under which they make capital commitments and the relative attractiveness of alternative investment or lending opportunities.

Certain information with respect to the Company's borrowings at December 31, 2006 is summarized as follows:

	CDOs	Reverse Repurchase Agreements	Credit Facilities	Commercial Mortgage Loan Pools	Senior Unsecured Notes	Tru Prefe Secur
	-----	-----	-----	-----	-----	-----
Outstanding borrowings	\$1,812,574	\$799,669	\$ 75,447	\$1,250,503	\$ 75,000	\$ 18
Weighted average						
borrowing rate	6.02%	5.37%	6.69%	3.99%	7.20%	
Weighted average						
remaining maturity	7.0 years	78 days	193 days	5.8 years	10.0 years	29.1
Estimated fair value						
of assets pledged	\$2,096,455	\$854,074	\$ 88,876	\$1,271,014	--	

At December 31, 2006, the Company's borrowings had the following remaining maturities:

	CDOs*	Reverse Repurchase Agreements	Credit Facilities	Commercial Mortgage Loan Pools	Senior Unsecured Notes	Tru Prefe Secur
	-----	-----	-----	-----	-----	-----
Within 30 days	\$ --	\$ 18,700	\$27,569	\$ --	\$ --	\$

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31 to 59 days	--	--	--	--	--	--
60 days to less than 1 year	--	780,969	33,893	--	--	--
1 year to 3 years	--	--	13,985	--	--	--
3 years to 5 years	--	--	--	--	--	--
Over 5 years	1,812,574	--	--	1,250,503	75,000	180
	-----	-----	-----	-----	-----	-----
	\$1,812,574	\$799,669	\$75,447	\$1,250,503	\$75,000	\$180
	=====	=====	=====	=====	=====	=====

- \* At December 31, 2006, CDOs are comprised of \$405,490 of CDO debt with a weighted average remaining maturity of 5.29 years, \$291,261 of CDO debt with a weighted average remaining maturity of 5.63 years, \$366,019 of CDO debt with a weighted average remaining maturity of 6.39 years, \$402,089 of CDO debt with a weighted average remaining maturity of 9.68 years and \$347,715 of CDO debt with a weighted average remaining maturity of 7.75 years.

### Reverse Repurchase Agreements and Credit Facilities

Reverse repurchase agreements are secured loans generally with a term of 90 days. The interest rate is based on 90-day LIBOR plus a spread that is determined based on the asset pledged as security. The terms include a daily mark to market provision that requires the posting of additional collateral if the value of the pledged asset declines. After the 90-day period expires, there is no obligation for the lender

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to extend credit for an additional period. This type of financing generally is available only for more liquid securities. The interest rate charged on reverse repurchase agreements is usually the lowest relative to the alternatives due to the lower risk inherent in these transactions.

Committed financing facilities represent multi-year agreements to provide secured financing for a specific asset class. These facilities include a mark to market provision requiring the Company to repay borrowings if the value of the pledged asset declines in excess of a threshold amount. A significant difference between committed financing facilities and reverse repurchase agreements is the term of the financing. A committed facility provider generally is required to provide financing for the full term of the agreement, usually two to three years, rather than ninety days as generally used in the reverse repurchase market. This longer term makes the financing of less liquid assets viable.

### CDOs

Issuance of secured term debt is generally done through a CDO offering in a private placement. This entails creating a special purpose entity that holds assets used to secure the payments required of the debt issued. Asset cash flows generally are matched with the debt service requirements over their respective lives and an interest rate swap is used to match the fixed or floating rate nature of the coupon payments where necessary. This type of transaction is usually referred to as "match funding" or "term financing" the assets. There is no mark to market requirement in this structure and the debt cannot be called or terminated by the bondholders. Furthermore, the debt issued is non-recourse to the issuer; and therefore permanent reductions in asset value do not affect the liquidity of the Company. However, since the Company expects to earn a positive spread between the income generated by the assets and the expense of the debt

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issued, a permanent impairment of any of the assets would negatively affect the spread over time.

### Senior Unsecured Notes

During October 2006, the Company issued \$75,000 of unsecured senior notes due in 2016 with a weighted average cost of funds of 7.21%. The unsecured senior notes can be redeemed in whole by the Company subject to certain provisions, which could include the payment of fees.

### Trust Preferred

On September 26, 2005, the Company issued \$75,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust I, a Delaware statutory trust ("Trust I"). The trust preferred securities have a thirty-year term ending October 30, 2035 with interest at a fixed rate of 7.497% for the first ten years and at a floating rate of three-month LIBOR plus 2.9% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in October 2010. Trust I issued \$2,380 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust I to the Company for a purchase price of \$2,380. The Company realized net proceeds from this offering of approximately \$72,618.

On January 31, 2006, the Company issued \$50,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust II, a Delaware statutory trust ("Trust II"). The trust preferred securities have a thirty-year term ending April 30, 2036 with interest at a fixed rate of 7.73% for the first ten years and at a floating rate of three-month LIBOR plus 2.7% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in April 2011. Trust II issued \$1,550 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust II to the Company for a purchase price of \$1,550. The Company realized net proceeds from this offering of approximately \$48,491.

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On March 16, 2006, the Company issued \$50,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust III, a Delaware statutory trust ("Trust III"). The trust preferred securities have a thirty-year term ending March 15, 2036 with interest at a fixed rate of 7.77% for the first ten years and at a floating rate of three-month LIBOR plus 2.7% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in March 2011. Trust III issued \$1,547 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust III to the Company for a purchase price of \$1,547. The Company realized net proceeds from this offering of approximately \$48,435.

### Preferred Equity Issuances

The Company may issue preferred stock from time to time as a source of long-term or permanent capital. Preferred stock generally has a fixed coupon and may have a fixed term in the form of a maturity date or other redemption or conversion features. The preferred stockholder typically has the right to a preferential distribution for dividends and any liquidity proceeds.

On February 12, 2007, the Company issued \$86,250 of Series D Cumulative Redeemable Preferred Stock ("Series D Preferred Stock"), including \$11,250 of Series D Preferred Stock sold to underwriters pursuant to an over-allotment option. The Series D Preferred Stock will pay an annual dividend of 8.25%.

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### Common Equity Issuances

Another source of permanent capital is the issuance of common stock through a follow-on offering. This allows investors to purchase a large block of common stock in one transaction. A common stock issuance can be accretive to the Company's book value per share if the issue price per share exceeds the Company's book value per share. It also can be accretive to earnings per share if the Company deploys the new capital into assets that generate a risk adjusted return that exceeds the return of the Company's existing assets. Furthermore, earnings accretion also can be achieved at reinvestment rates that are lower than the return on existing assets if common stock is issued at a premium to book value.

The Company continuously evaluates the market for follow-on Common Stock offerings as well as the available opportunities to deploy new capital on an accretive basis. In 2005, the Company issued 1,725,000 shares of Common Stock in a follow-on offering at \$11.59 per share. Additionally, for the years ended December 31, 2006 and 2005, respectively, the Company issued 608,747 and 1,318,568 shares of Common Stock under its Dividend Reinvestment Plan. Net proceeds to the Company under the Dividend Reinvestment Plan were approximately \$6,517 and \$14,327, respectively.

For the year ended December 31, 2006, the Company issued 664,900 shares of Common Stock under a sales agency agreement with Brinson Patrick Securities Corporation. Net proceeds to the Company were approximately \$8,625.

### Off Balance Sheet Arrangements

The Company's ownership of the subordinated classes of CMBS from a single issuer gives it the right to influence the foreclosure/workout process on the underlying loans ("Controlling Class CMBS"). FASB Staff Position FIN 46(R)-5, Implicit Variable Interests under FASB Interpretation No. 46 ("FIN 46(R)-5") has certain scope exceptions, one of which provides that an enterprise that holds a variable interest in a QSPE does not consolidate that entity unless that enterprise has the unilateral ability to cause the entity to liquidate. SFAS No. 140 provides the requirements for an entity to be considered a QSPE. To

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maintain the QSPE exception, the trust must continue to meet the QSPE criteria both initially and in subsequent periods. A trust's QSPE status can be impacted in future periods by activities by its transferors or other involved parties, including the manner in which certain servicing activities are performed. To the extent its CMBS investments were issued by a trust that meets the requirements to be considered a QSPE, the Company records the investments at the purchase price paid. To the extent the underlying trusts are not QSPEs the Company follows the guidance set forth in FIN 46(R)-5 as the trusts would be considered VIEs.

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



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consolidate CMBS trusts in which the Company has invested.

At December 31, 2006, the Company owned securities of 29 Controlling Class CMBS trusts with a par of \$1,171,054. The total par amount of CMBS issued by the 29 trusts was \$42,398,701. One of the Company's 29 Controlling Class trusts does not qualify as a QSPE and has been consolidated by the Company (see Note 5 of the consolidated financial statements).

The Company's maximum exposure to loss as a result of its investment in these VIEs totaled \$762,567 and \$565,231 at December 31, 2006 and 2005, respectively.

In addition, the Company has completed two securitizations that qualify as QSPE's under SFAS No. 140. Through CDO HY1 and CDO HY2 the Company issued non-recourse liabilities secured by commercial related assets including portions of 17 Controlling Class CMBS. Should future guidance from the standard setters determine that Controlling Class CMBS are not QSPE's, the Company would be required to consolidate the assets, liabilities, income and expense of CDO HY1 and CDO HY2.

The Company's total maximum exposure to loss as a result of its investment in CDO HY1 and CDO HY2 at December 31, 2006 and 2005, respectively, was \$111,076 and \$109,003.

The Company also owns non-investment debt and preferred securities in LEAFs CMBS I Ltd ("Leaf"), a QSPE under SFAS No. 140. Leaf issued non-recourse liabilities secured by investment grade commercial real estate securities. At December 31, 2006 and 2005, the Company's total maximum exposure to loss as a result of its investment in Leaf was \$6,796 and \$6,936, respectively.

### Cash Flows

Cash provided by operating activities is net income adjusted for certain non-cash items and changes in assets and liabilities including the Company's trading securities. Operating activities provided cash flows of \$117,655, 107,373, and 125,756 for the year ended December 31, 2006, 2005, and 2004, respectively. Operating cash flow is affected by the purchase and sale of fixed income securities classified as trading securities. Proceeds received from repayment of trading securities also increases operating cash flows. The Company received \$36,140, \$43,477, and \$69,345 from trading securities for the year ended December 31, 2006, 2005, and 2004, respectively. In addition, in 2006 the Company closed interest rate swaps classified as a cash flow hedges and received cash of \$11,634.

The Company's investing cash flow consists primarily of the purchase, sale, and repayments on securities activities available for sale, commercial loan pools, commercial mortgage loans and equity investments. The Company's investing activities used cash flows of \$703,451, \$419,992, and \$95,022 during the year ended December 31, 2006, 2005, and 2006, respectively. The variance in investing cash flows is primarily attributable to significant purchases of securities and commercial mortgage loans.

Net cash flow provided by (used in) financing activities was \$611,628, \$329,420, and \$(27,784) for the years ended December 31, 2006, 2005, and 2004, respectively, primarily due to borrowings and repayments under reverse repurchase agreements and credit facilities and dividends payments, offset by common stock issuances, and CDO issuances. In addition, at the end of the first

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quarter of 2004, the Board of Directors approved the Company's decision to redeem its Series B Preferred Stock, \$0.001 par value per share ("Series B Preferred Stock") for \$43,930. The Series B Preferred Stock was redeemed on May 6, 2004.

### TRANSACTIONS WITH AFFILIATES

The Company has a Management Agreement, an administrative services agreement and an accounting services agreement with the Manager, the employer of certain directors and all of the officers of the Company, under which the Manager and the Company's officers manage the Company's day-to-day investment operations, subject to the direction and oversight of the Company's Board of Directors. Pursuant to the Management Agreement and these other agreements, the Manager and the Company's officers formulate investment strategies, arrange for the acquisition of assets, arrange for financing, monitor the performance of the Company's assets and provide certain other advisory, administrative and managerial services in connection with the operations of the Company. For performing certain of these services, the Company pays the Manager under the Management Agreement a base management fee equal to 2.0% of the quarterly average total stockholders' equity for the applicable quarter.

To provide an incentive, the Manager is entitled to receive an incentive fee under the Management Agreement equal to 25% of the amount by which the rolling four-quarter GAAP net income before the incentive fee exceeds the greater of 8.5% or 400 basis points over the ten-year Treasury note multiplied by the adjusted per share issue price of the Company's Common Stock (\$11.37 per common share at December 31, 2006). Additionally, up to 30% of the incentive fees earned in 2005 or after may be paid in shares of the Company's Common Stock subject to certain provisions under a compensatory deferred stock plan approved by the stockholders of the Company in 2006. The Board of Directors also authorized a stock based incentive plan where one-half of one percent of common shares outstanding was paid to the Manager in 2006.

The Company's unaffiliated directors approved an extension of the Management Agreement to March 30, 2008 at the Board's March 2007 meeting.

The following is a summary of management and incentive fees incurred for the year ended December 31, 2006, 2005 and 2004:

	For the Year Ended December 31,		
	2006	2005	2004
Management fee	\$12,617	\$10,974	\$8,956
Incentive fee	5,919	4,290	--
Incentive fee- stock based	2,761	--	--
Total management and incentive fees	\$21,297	\$15,264	\$8,956

At December 31, 2006, 2005, and 2004, respectively, management and incentive fees of \$8,989, \$5,734, and \$2,309 remain payable to the Manager and are

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included on the accompanying consolidated statement of financial condition as a component of other liabilities.

In accordance with the provisions of the Management Agreement, the Company recorded reimbursements to the Manager of \$400, \$350, and \$120 for certain expenses incurred on behalf of the Company during 2006, 2005, and 2004, respectively.

The Company also has administration and accounting services agreements with the Manager. Under the terms of the administration agreement, the Manager provides financial reporting, audit coordination and accounting oversight services to the Company. Under the terms of the accounting services agreement, the Manager provides investment accounting services to the Company. For the years ended December 31, 2006, 2005, and 2004, the Company paid administration fees of \$234, \$209, and \$174, respectively, which are included in general and administrative expense on the accompanying statement of operations. No payments were made in each of the three years in the period ended December 31, 2006 under the accounting services agreement.

The special servicer on 25 of the Company's 29 Controlling Class trusts is Midland Loan Services, Inc. ("Midland"), a wholly owned indirect subsidiary of PNC Bank, and therefore a related party of the Manager. The Company's fees for Midland's services are at market rates.

On December 13, 2005, the Company entered into a \$75,000 commitment to acquire shares of BlackRock Diamond. BlackRock Diamond is a private REIT managed by BlackRock Realty Advisors, Inc., a subsidiary of the Manager. On February 21, 2006, the Company increased its capital commitment by an additional \$25,000, resulting in a total capital commitment of \$100,000. At December 31, 2006, 93% of the commitment had been called and the Company owned approximately 21% of BlackRock Diamond. The Company does not incur any additional management or incentive fees to the Manager related to its investment in BlackRock Diamond. The Company's investment in BlackRock Diamond at December 31, 2006 was \$105,894. At December 31, 2006, the Company had \$7,397 of remaining capital commitments to BlackRock Diamond, all of which was called in January 2007.

During 2001, the Company entered into a \$50,000 commitment to acquire shares in Carbon I, a private commercial real estate income opportunity fund managed by the Manager. The Carbon I investment period ended on July 12, 2004 and the Company's investment in Carbon I at December 31, 2006 was \$3,144. The Company does not incur any additional management or incentive fees to the Manager related to its investment in Carbon I. On December 31, 2006, the Company owned approximately 20% of the outstanding shares in Carbon I.

The Company entered into an aggregate commitment of \$100,000 to acquire shares in Carbon II, a private commercial real estate income opportunity fund managed by the Manager. At December 31, 2006, the Company's investment in Carbon II was \$69,259 and the Company's remaining commitment to Carbon II is \$28,958. The Company does not incur any additional management or incentive fees to the Manager related to its investment in Carbon II. On December 31, 2006, the Company owned approximately 26% of the outstanding shares in Carbon II.

The Company's unaffiliated directors approved the investments in BlackRock Diamond and the Carbon Capital Funds prior to the investments being made.

REIT STATUS: The Company has elected to be taxed as a REIT and therefore must comply with the provisions of the Code with respect thereto. Accordingly, the

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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.

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### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

The majority of the Company's assets are fixed rate securities valued based on a market credit spread to U.S. Treasuries. As U.S. Treasury securities are priced to a higher yield and/or the spread to U.S. Treasuries used to price the Company's assets is increased, the estimated fair value of the Company's portfolio may decline. Conversely, as U.S. Treasury securities are priced to a lower yield and/or the spread to U.S. Treasuries used to price the Company's assets is decreased, the estimated fair value of the Company's portfolio may increase. Changes in the estimated fair value of the Company's portfolio may affect the Company's net income or cash flow directly through their impact on unrealized gains or losses on securities held-for-trading or indirectly through their impact on the Company's ability to borrow. Changes in the level of the U.S. Treasury yield curve can also affect, among other things, the prepayment assumptions used to value certain of the Company's securities and the Company's ability to realize gains from the sale of such assets. In addition, changes in the general level of the LIBOR money market rates can affect the Company's net interest income. At December 31, 2006, all of the Company's collateralized liabilities outside of the CDOs are floating rate based on a market spread to LIBOR. As the level of LIBOR increases or decreases, the Company's interest expense will move in the same direction.

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

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anticipates that the income from any such hedging transaction will not be qualifying income for REIT income purposes, the Company may conduct part or all of its hedging activities through a to-be-formed corporate subsidiary that is fully subject to Federal corporate income taxation. The profitability of the Company may be adversely affected during any period as a result of changing interest rates.

The Company monitors and manages interest rate risk based on a method that takes into consideration the interest rate sensitivity of the Company's assets and liabilities, including preferred stock. The Company's objective is to acquire assets and match fund the purchase so that interest rate risk associated with financing these assets is reduced or eliminated. The primary risks

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associated with acquiring and financing these assets under 90-day repurchase agreements and committed borrowing facilities are mark-to-market risk and short-term rate risk. Certain secured financing arrangements provide for an advance rate based upon a percentage of the estimated fair value of the asset being financed. Market movements that cause asset values to decline would require a margin call or a cash payment to maintain the relationship between asset value and amount borrowed. A cash flow based CDO is an example of a secured financing vehicle that does not require a mark-to-market to establish or maintain a level of financing. When financed assets are subject to a mark-to-market margin call, the Company carefully monitors the interest rate sensitivity of those assets. The duration of the assets financed which are subject to a mark-to-market margin call was 2.0 years based on net asset value at December 31, 2006. This means that a 100 basis point increase in interest rates would cause a margin call of approximately \$13,000.

Net interest income sensitivity to changes in interest rates is analyzed using the assumptions that interest rates, as defined by the LIBOR curve, increase or decrease and that the yield curves of the LIBOR rate shocks will be parallel to each other.

Regarding the table below, all changes in net interest income are measured as percentage changes from the respective values calculated in the scenario labeled as "Base Case." The base interest rate scenario assumes interest rates at December 31, 2006. Actual results could differ significantly from these estimates.

### PROJECTED PERCENTAGE CHANGE IN EARNINGS PER SHARE GIVEN LIBOR MOVEMENTS

Change in LIBOR, +/- Basis Points	Projected Change in Earnings per Share
-200	\$ 0.03
-100	\$ 0.01
-50	\$ 0.01
Base Case	
+50	\$(0.01)
+100	\$(0.01)
+200	\$(0.03)

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The Company's GAAP book value incorporates the estimated fair value of the Company's interest bearing assets but it does not incorporate the estimated fair value of the Company's interest bearing fixed rate liabilities and preferred stock. The fixed rate liabilities and preferred stock generally will reduce the actual interest rate risk of the Company from an economic perspective even though changes in the estimated fair value of these liabilities are not reflected in the Company's reported book value. The Company focuses on economic risk in managing its sensitivity to interest rates and maintains an economic duration within a band of 2.0 to 5.0 years. At December 31, 2006, economic duration for the Company's entire portfolio was 2.3 years. This implies that for each 100 basis points of change in interest rates the Company's economic value will change by approximately 2.3%. At December 31, 2006 the Company estimates its economic value, or net asset value of its common stock to be \$572,947.

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

Duration - GAAP book value at December 31, 2006	8.3
Less:	
Duration contribution of CDO I liabilities	(1.2)
Duration contribution of CDO II liabilities	(1.0)
Duration contribution of CDO III liabilities	(1.0)
Duration contribution of CDO HY3 liabilities	(0.8)
Duration contribution of Euro CDO liabilities	(0.1)
Duration contribution of Series C Preferred Stock	(0.1)
Duration contribution of junior subordinated notes	(1.1)
Duration contribution of senior unsecured notes	(0.7)
	----
Economic duration at December 31, 2006	2.3
	=====

The GAAP book value of the Company's common stock is \$10.35 per share. As indicated in the table above a 100 basis point change in interest rates will change reported book value by approximately 8.3%, or \$54,000. As indicated above, approximately \$13,000 of that change would be required to meet margin calls in the event rates rise by 100 basis points.

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

All loans are subject to a certain probability of default. Before acquiring a Controlling Class security, the Company will perform an analysis of the quality of all of the loans proposed. As a result of this analysis, loans with unacceptable risk profiles are either removed from the proposed pool or the Company receives a price adjustment. The Company underwrites its Controlling Class CMBS investments assuming the underlying loans will suffer a certain dollar amount of defaults and these defaults will lead to some level of realized losses. Loss adjusted yields are computed based on these assumptions and applied to each class of security supported by the cash flow on the underlying loans. The most significant variables affecting loss adjusted yields include, but are

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not limited to, the number of defaults, the severity of loss that occurs subsequent to a default and the timing of the actual loss. The different rating levels of CMBS will react differently to changes in these assumptions. The lowest rated securities (B- or lower) are generally more sensitive to changes in timing of actual losses. The higher rated securities (B or higher) are more sensitive to the severity of losses and timing of cash flows.

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

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

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

For purposes of illustration, a doubling of the losses in the Company's Controlling Class CMBS, without a significant acceleration of those losses, would reduce GAAP income by approximately \$0.87 per share of Common Stock per year and cause a significant write-down at the time the loss assumption is changed. The amount of the write-down depends on several factors, including which securities are most affected at the time of the write-down, but is estimated to be in the range of \$0.01 to \$0.19 per share based on a doubling of expected losses. A significant acceleration of the timing of these losses would cause the Company's net income to decrease. The Company's exposure to a write-down is mitigated by the fact that most of these assets are financed on a non-recourse basis in the Company's CDOs, where a significant portion of the risk of loss is transferred to the CDO bondholders. At December 31, 2006, securities with a total estimated fair value of \$2,103,441 are collateralizing the CDO borrowings of \$1,828,078; therefore, the Company's preferred equity interest in the five CDOs is \$275,363 (\$4.76 per share).

**ASSET AND LIABILITY MANAGEMENT:** Asset and liability management is concerned with the timing and magnitude of the re-pricing and/or maturing of assets and liabilities. It is the Company's objective to attempt to control risks associated with interest rate movements. In general, management's strategy is to match the term of the Company's liabilities as closely as possible with the expected holding period of the Company's assets. This is less important for

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those assets in the Company's portfolio considered liquid, as there is a very stable market for the financing of these securities.

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

**CURRENCY RISK:** The Company has foreign currency rate exposures related to certain CMBS and commercial real estate loans. The Company's principal currency exposures are to the Euro and British pound. Changes in currency rates can adversely impact the fair values and earnings of the Company's non-U.S. holdings. The Company mitigates this impact by utilizing local currency-denominated financings on its foreign investments and foreign currency forward commitments and swaps to hedge the net exposure.

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### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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All schedules have been omitted because either the required information is not applicable or the information is shown in the financial statements or notes thereto.

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### MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING



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Management of Anthracite Capital, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended, as a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting can provide only reasonable assurance with respect to financial statement preparation and presentation. Projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company's internal control over financial reporting at December 31, 2006. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on its assessment, management concluded that, at December 31, 2006, the Company's internal control over financial reporting is effective.

The Company's independent registered public accounting firm has issued a report on management's assessment of the Company's internal control over financial reporting. This report begins on the following page.

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### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of  
Anthracite Capital, Inc.  
New York, New York

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Anthracite Capital, Inc. and subsidiaries (the "Company") maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control--Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over

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financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the criteria established in Internal Control--Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on

the criteria established in Internal Control--Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of financial condition as of December 31, 2006, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for

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each of the three years in the period ended December 31, 2006 of the Company and our report dated March 14, 2007 expressed an unqualified opinion on those financial statements.

/s/ Deloitte & Touche LLP

New York, New York  
March 14, 2007

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### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of  
Anthracite Capital, Inc.  
New York, New York

We have audited the accompanying consolidated statements of financial condition of Anthracite Capital, Inc. and subsidiaries (the "Company") as of December 31, 2006 and 2005, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Anthracite Capital, Inc. and subsidiaries as of December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, based on the criteria established in Internal Control--Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 14, 2007 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ Deloitte & Touche LLP

New York, New York  
March 14, 2007

ANTHRACITE CAPITAL, INC.  
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION  
(IN THOUSANDS, EXCEPT SHARE DATA)

	December 31, 2006	
	-----	-----
ASSETS		
Cash and cash equivalents	\$ 66,388	
Restricted cash equivalents	59,801	
Securities available-for-sale, at fair value		
CMBS	\$ 883,432	\$
Investment grade CMBS	1,588,284	1
RMBS	144,140	
	-----	-----
Total securities available-for-sale	2,615,856	
Commercial mortgage loan pools, at amortized cost	1,271,014	
Securities held-for-trading, at estimated fair value		
CMBS	22,383	
RMBS	132,204	
	-----	-----
Total securities held-for-trading	154,587	
Commercial mortgage loans, net	481,745	
Equity investments	182,147	
Derivative instruments, at fair value	317,574	
Other assets	69,151	
	-----	-----
Total Assets	\$5,218,263	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Borrowings:		
CDOs	\$1,812,574	\$1
Secured by pledge of subordinated CMBS	48,628	
Secured by pledge of other securities available-for-sale	666,275	
Secured by pledge of commercial mortgage loan pools	1,256,897	1
Secured by pledge of securities held-for-trading	127,249	
Secured by pledge of commercial mortgage loans	26,570	
Senior unsecured notes	75,000	
Junior subordinated notes to subsidiary trust issuing preferred securities	180,477	
	-----	-----
Total borrowings	4,193,670	
Payable for investments purchased	23,796	
Distributions payable	17,669	
Derivative instruments, at fair value	304,987	
Other liabilities	22,032	
	-----	-----
Total Liabilities	\$4,562,154	-----
Commitments and Contingencies		
Stockholders' Equity:		

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Common Stock, par value \$0.001 per share; 400,000,000 shares  
authorized;  
57,830,964 shares issued and outstanding in 2006;  
56,338,540 shares issued and outstanding in 2005

9.375% Series C Preferred stock, liquidation preference \$57,500	58
Additional paid-in capital	55,435
Distributions in excess of earnings	629,785
Accumulated other comprehensive income	(120,976)
	91,807
	-----
Total Stockholders' Equity	656,109
	-----
Total Liabilities and Stockholders' Equity	\$5,218,263
	=====

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONSOLIDATED FINANCIAL STATEMENTS.

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ANTHRACITE CAPITAL, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS (IN THOUSANDS, EXCEPT PER SHARE DATA)

	Year ended December 31,		
	2006	2005	2004
	-----	-----	-----
Income:			
Interest from securities available-for-sale	\$ 171,686	\$ 141,113	\$ 131,113
Interest from commercial mortgage loans	41,773	23,183	11,113
Interest from commercial mortgage loan pools	52,917	54,025	39,113
Interest from securities held-for-trading	7,207	11,370	11,113
Earnings from equity investments	27,431	12,087	7,113
Earnings from real estate joint ventures	--	59	1,113
Interest from cash and cash equivalents	2,403	2,077	
Other income	--	--	
	-----	-----	-----
Total Income	303,417	243,914	203,113
	-----	-----	-----
Expenses:			
Interest	205,023	156,865	124,113
Interest - securities held-for-trading	7,365	6,593	3,113
Management and incentive fees	21,297	15,264	8,113
General and administrative expense	4,533	3,917	3,113
	-----	-----	-----
Total Expenses	238,218	182,639	140,113
	-----	-----	-----
Other gain (loss):			
Sale of securities available-for-sale	29,032	16,543	17,113
Dedesignation of derivative instruments	(12,661)	--	
Securities held-for-trading	3,254	(1,999)	(11,113)
Foreign currency gain (loss)	2,161	(134)	
Loss on impairment of assets	(7,880)	(5,088)	(26,113)
	-----	-----	-----

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Total Other gain (loss)	13,906	9,322	(20,
Income from continuing operations	79,105	70,597	43,
Income from discontinued operations	1,366	--	
Net income	80,471	70,597	43,
Dividends on Preferred Stock	5,392	5,392	6,
Cost to retire preferred stock in excess of carrying value	--	--	10,
Net income available to Common Stockholders	\$ 75,079	\$ 65,205	\$ 25,
Net income per common share, basic	\$ 1.31	\$ 1.20	\$ 0
Net income per common share, diluted	\$ 1.31	\$ 1.20	\$ 0
Weighted average number of shares outstanding:			
Basic	57,182,434	54,144,243	51,766,
Diluted	57,401,664	54,152,820	51,775,
Dividend declared per share of Common Stock	\$ 1.15	\$ 1.12	\$ 1

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## ANTHRACITE CAPITAL, INC. CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY FOR THE YEAR ENDED DECEMBER 31, 2006, 2005 AND 2004 (IN THOUSANDS)

	Common Stock, Par Value	Series B Preferred Stock	Series C Preferred Stock	Additional Paid-In Capital	Distributions In Excess Of Earnings	Accumula Other Comprehen Income (L
Balance at December 31, 2003	\$49	\$ 33,431	\$55,435	\$536,333	\$ (101,635)	\$ (106,1
Net Income					43,192	
Unrealized gain on cash flow hedges						1,0
Reclassification adjustments from cash flow hedges included in net income						6,1
Change in net unrealized gain on securities available-for-sale, net of reclassification adjustment						112,3
Other comprehensive income						
Comprehensive income						
Dividends declared-common						

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stock					(58,208)	
Dividends on preferred stock					(6,916)	
Issuance of common stock	4			42,577		
Conversion of Series B preferred stock to common stock		(9)		9		
Redemption of Series B preferred stock		(33,422)			(10,508)	
Balance at December 31, 2004	\$53	\$ --	\$55,435	\$578,919	\$ (134,075)	\$ 13,4
Net Income					70,597	
Unrealized gain on cash flow hedges						26,6
Reclassification adjustments from cash flow hedges included in net income						6,1
Change in net unrealized gain on securities available-for-sale, net of reclassification adjustment						14,0
Other comprehensive income						
Comprehensive income						
Dividends declared-common stock					(61,168)	
Dividends on preferred stock					(5,392)	
Issuance of common stock	3			33,449		
Balance at December 31, 2005	\$56	\$ --	\$55,435	\$612,368	\$ (130,038)	\$ 60,1
Net Income					80,471	
Unrealized gain on cash flow hedges						2,9
Reclassification adjustments from cash flow hedges included in net loss						5,0
Foreign currency translation						2
Dedesignation of cash flow hedges						12,6
Change in net unrealized gain on securities available-for-sale, net of reclassification adjustment						10,7
Other comprehensive income						
Comprehensive income						
Dividends declared-common stock					(66,017)	
Dividends on preferred stock					(5,392)	
Issuance of common stock	2			17,417		
Balance at December 31, 2006	\$58	\$ --	\$55,435	\$629,785	\$ (120,976)	\$ 91,8

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## DISCLOSURE OF RECLASSIFICATION ADJUSTMENT:

	Year ended December 31,		
	2006	2005	2004
Unrealized holding gain (loss) on securities available-for-sale	\$ 7,249	\$ (2,507)	\$ 94,834
Reclassification for realized gains previously recorded as unrealized	16,371	16,543	17,544
	\$23,620	\$14,036	\$112,378
	=====	=====	=====

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONSOLIDATED FINANCIAL STATEMENTS.

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## ANTHRACITE CAPITAL, INC. CONSOLIDATED STATEMENTS OF CASH FLOW (IN THOUSANDS)

	Year Ended Dece	
	2006	2005
Cash flows from operating activities:		
Net income	\$ 80,471	\$ 70,59
Adjustments to reconcile net income to net cash provided by operating activities:		
Decrease in trading securities	36,140	43,44
Net gain on sale of securities	(19,625)	(14,54
Gain on sale of real estate held for sale	(1,366)	
Earnings from subsidiary trust	(388)	(4
Distributions from subsidiary trust	363	4
Earnings from equity investments and real estate joint ventures	(27,431)	(12,14
Distributions of earnings from equity investments and real estate joint ventures	19,725	8,48
Amortization of collateralized debt obligation issuance costs	2,677	2,21
Amortization of junior subordinated note issuance costs	197	3
Amortization of senior unsecured notes issuance costs	32	-
(Discount accretion) premium amortization, net	(469)	5,42
Loss on impairment of assets	7,880	5,08
Unrealized net foreign currency (gain) loss	(19,200)	63
Non-cash management and incentive fees	4,537	1,28
Non-cash directors compensation	64	6
Proceeds (disbursements) from sale of interest rate swap agreements	11,634	(2,10
Decrease (increase) in other assets	33,832	(25
(Decrease) increase in other liabilities	(11,418)	(84



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Net cash provided by operating activities	117,655	107,37
Cash flows from investing activities:		
Purchase of securities available-for-sale	(806,452)	(517,02
Proceeds from sale of securities available-for-sale	236,945	172,73
Principal payments received on securities available-for-sale	51,193	53,77
Purchase of securities related to consolidated variable interest entity	--	--
Sale of securities related to consolidated variable interest entity	--	--
Repayments received from commercial mortgage loan pools	9,004	7,87
Purchase of real estate held-for-sale	(5,435)	--
Proceeds from sale of real estate held-for-sale	6,801	--
Funding of commercial mortgage loans	(270,362)	(243,55
Repayments received from commercial mortgage loans	197,094	112,83
Sale of commercial mortgage loans	--	20,07
(Increase) decrease in restricted cash equivalents	(58,448)	18,43
Return of capital from equity investments and joint ventures	14,742	26,86
Investment in equity investments	(78,533)	(72,00
Net cash used in investing activities	(703,451)	(419,99
Cash flows from financing activities:		
Net (decrease) increase in borrowings under reverse repurchase agreements and credit facilities	(228,633)	293,68
Repayments of borrowings secured by commercial mortgage loan pools	(8,587)	(2,67
Issuance of collateralized debt obligations	765,388	--
Repayments of collateralized debt obligations	(20,115)	(1,95
Issuance costs for collateralized debt obligations	(11,662)	--
Issuance of junior subordinated notes to subsidiary trust	100,000	75,00
Issuance costs of junior subordinated notes	(3,208)	(2,38
Issuance of senior unsecured notes	75,000	--
Issuance costs of senior unsecured notes	(1,396)	--
Redemption of Series B preferred stock	--	--
Dividends paid on preferred stock	(5,392)	(5,39
Proceeds from issuance of common stock, net of offering costs	15,256	33,45
Dividends paid on common stock	(65,023)	(60,31
Net cash provided by (used in) financing activities	611,628	329,42
Net increase in cash and cash equivalents	25,832	16,80
Cash and cash equivalents, beginning of year	40,556	23,75
Cash and cash equivalents, end of year	\$ 66,388	\$ 40,55

Year Ended December

2006 2005

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### Supplemental disclosure of cash flow information:

Interest paid	\$208,879	\$156,480	\$
	=====	=====	=
Commercial mortgage loans purchased not settled	\$ 23,796	\$ --	\$
	=====	=====	=

### Supplemental disclosure of non-cash investing and financing activities:

Securitizations:			
Available-for-sale securities retained	\$ --	\$ 75,844	\$
	=====	=====	=
Residual interests	\$ --	\$ 20,317	\$
	=====	=====	=
Investment in subsidiary trust	\$ 3,097	\$ 2,380	\$
	=====	=====	=
Consolidated variable interest entity:			
Carrying value of assets acquired	\$ -	\$ --	\$
	=====	=====	=
Liabilities assumed	\$ -	\$ --	\$
	=====	=====	=

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONSOLIDATED FINANCIAL STATEMENTS.

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ANTHRACITE CAPITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

#### NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

The Company was incorporated in Maryland in November 1997 and commenced operations on March 24, 1998. The Company's principal business activity is to invest in a diversified portfolio of CMBS, multifamily and commercial mortgage loans, and other real estate related assets in the U.S. and non-U.S. markets. The Company is organized and managed as a single business segment.

A summary of the Company's significant accounting policies follows:

#### USE OF ESTIMATES

In preparing the consolidated financial statements in accordance with GAAP, 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 consolidated statements of financial condition and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates and assumptions. Significant estimates in the consolidated financial statements include the valuation of the Company's securities and estimates pertaining to credit performance related to CMBS and commercial real estate loans.

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the financial statements of Anthracite Capital, Inc. and its majority owned subsidiaries, and those VIEs in which the Company is the primary beneficiary under FIN 46R. All inter-company balances and transactions have been eliminated in consolidation.

#### VARIABLE INTEREST ENTITIES

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

The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the QSPE criteria. However, there is uncertainty with respect to QSPE treatment due to ongoing review by accounting standard setters, potential actions by various parties involved with the QSPE, as discussed above, as well as varying and evolving interpretations of the QSPE criteria under SFAS No. 140. Additionally, the standard setters continue to review the FIN 46R provisions related to the computations used to

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determine the primary beneficiary of a VIE. Future guidance from the standard setters may require the Company to consolidate CMBS trusts in which the Company has invested.

At December 31, 2006, the Company owned securities of 29 Controlling Class CMBS trusts with a par of \$1,171,054. However, portions of the non-rated securities of 17 of the 29 Controlling Class CMBS transactions are included in CDO HY1 and CDO HY2. The total par amount of CMBS issued by the 29 trusts was \$42,398,701. One of the Company's 29 Controlling Class trusts does not qualify as a QSPE and has been consolidated by the Company (see Note 5 of the consolidated financial statements). The Company's maximum exposure to loss as a result of its investment in these VIEs totaled \$762,567 and \$565,231 at December 31, 2006 and 2005, respectively.

In addition, the Company has completed two securitizations that qualify as QSPE's under SFAS No. 140. Through CDO HY1 and CDO HY2 the Company issued non-recourse liabilities primarily secured by non-investment grade commercial real estate assets including portions of 17 Controlling Class CMBS. Should future guidance from the standard setters determine that Controlling Class CMBS are not QSPE's, the Company would be required to consolidate the assets, liabilities, income and expenses of CDO HY1 and CDO HY2. The Company's total maximum exposure to loss as a result of its investment in CDO HY1 and CDO HY2 at December 31, 2006 and 2005, respectively, is \$111,076 and \$109,003.

#### FOREIGN CURRENCY TRANSLATION

Assets and liabilities denominated in foreign currencies are translated into U.S. dollars using foreign exchange rates at the end of the reporting period. Income and expenses are translated at the approximate weighted average exchange rates for each reporting period. The effects of translating income with a

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functional currency other than the U.S. dollar are included in stockholders' equity along with the related hedge effects. The effects of translating operations with the U.S. dollar as the functional currency are included in foreign currency gain (loss) along with the related hedge effects.

### CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash and short-term, highly liquid investments with original maturities of three months or less. Cash and cash equivalents are held at major financial institutions, to which the Company is exposed to credit risk.

### RESTRICTED CASH

On December 31, 2006, the Company had restricted cash of \$59,801, consisting of \$56,266 on deposit with the trustees for the Company's collateralized debt obligations ("CDOs") and \$3,535 pledged as collateral for interest rate swap agreements. The balance \$1,246 at December 31, 2005 primarily represents cash held as collateral for the Company's interest rate swap agreements.

### DEFERRED FINANCING COSTS

Deferred financing costs, which are included in other assets on the Company's consolidated statements of financial condition, includes issuance costs related to the Company's debt. These costs are amortized by applying the effective interest rate method and the amortization is reflected in interest expense.

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### SECURITIES AVAILABLE-FOR-SALE

The Company has designated certain investments in mortgage-backed securities, mortgage-related securities and certain other securities as assets available-for-sale because the Company may dispose of them prior to maturity and does not hold them principally for the purpose of selling them in the near term. Securities available-for-sale are carried at estimated fair value with the net unrealized gains or losses reported as a component of accumulated other comprehensive income (loss) in stockholders' equity. Unrealized losses on securities that reflect a decline in value that is judged by management to be other than temporary, if any, are charged to earnings. At disposition, the realized net gain or loss is included in income on a specific identification basis.

In accordance with SFAS No. 115, when the estimated fair value of the security classified as available-for-sale has been below amortized cost for a significant period of time and the Company concludes that it no longer has the ability or intent to hold the security for the period of time over which the Company expects the values to recover to amortized cost, the investment is written down to its fair value. The resulting charge is included in income, and a new cost basis established. Additionally, under EITF 99-20, when changes in estimated cash flows from the cash flows previously estimated occur due to actual prepayment and credit loss experience, and the present value of the revised cash flows using the current expected yield is less than the present value of the previously estimated remaining cash flows (adjusted for cash receipts during the intervening period), an other-than-temporary impairment is deemed to have occurred. Accordingly, the security is written down to fair value with the resulting change being included in income, and a new cost basis established. In both instances, the original discount or premium is written off when the new cost basis is established.

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### REVENUE RECOGNITION

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

For other mortgage-backed and related mortgage securities, the Company accounts for interest income under SFAS No. 91, by applying the effective yield method which includes the amortization of discount or premium arising at the time of purchase and the stated or coupon interest payments. Actual prepayment and credit loss experience is reviewed quarterly and effective yields are recalculated when differences arise between prepayments and credit losses originally anticipated and amounts actually received plus anticipated future prepayments and credit losses.

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

### SECURITIES HELD-FOR-TRADING

Securities held-for-trading are carried at estimated fair value with net realized and unrealized gains or losses included in the consolidated statements of operations.

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### SECURITIZATIONS

When the Company sells assets in securitizations, it can retain certain tranches which are considered retained interests in the securitization. Gain or loss on the sale of assets depends in part on the previous carrying amount of the financial assets securitized, allocated between the assets sold and the retained interests based on their relative fair value at the date of securitization. To obtain fair values, quoted market prices are used. Gain or loss on securitizations of financial assets is reported as a component of sale of securities available-for-sale on the consolidated statement of operations. Retained interests are carried at estimated fair value on the consolidated statement of financial condition. Adjustments to estimated fair value for retained interests classified as securities available-for-sale are included in accumulated other comprehensive income on the consolidated statement of financial condition.

### COMMERCIAL MORTGAGE LOANS AND LOAN POOLS

The Company purchases and originates certain commercial mortgage loans to be held as long-term investments. In accordance with SFAS No. 65, Accounting for Certain Mortgage Banking Activities, commercial mortgage loans and loan pools are classified as long term investments because the Company has the ability and

the intent to hold these loans to maturity. Loans are recorded at cost at the date of purchase. Premiums and discounts related to these loans are amortized over their estimated lives using the effective interest method. Any origination fee income and application fee income, net of direct costs, associated with originating or purchasing commercial mortgage loans are deferred and included in the basis of the loans on the consolidated statements of financial condition. The net fees are amortized over the life of the loans using the effective interest method. The Company recognizes impairment on the loans when it is probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Company measures impairment (both interest and principal) based on the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent.

#### EQUITY INVESTMENTS

For those investments in real estate entities where the Company does not control the investee, or is not the primary beneficiary of a VIE, but can exert significant influence over the financial and operating policies of the investee, the Company uses the equity method of accounting. The Company recognizes its share of each investee's income or loss, and reduces its investment balance by distributions received. The Company owns an equity method investment in a privately held REIT that maintains its financial records on a fair value basis. The Company has retained such accounting relative to its investment in this REIT pursuant to EITF Issue 85-12, Retention of Specialized Accounting for Investments in Consolidation.

#### DERIVATIVE INSTRUMENTS

As part of its asset/liability risk management activities, the Company may enter into interest rate swap agreements, forward currency exchange contracts and other financial instruments in order to hedge interest rate and foreign currency exposures or to modify the interest rate or foreign currency characteristics of related items in its consolidated statement of financial condition.

Income and expense from interest rate swap agreements that are, for accounting purposes, designated as cash flow hedges are recognized as a net adjustment to the interest expense of the hedged item and changes in fair value are recognized as a component of accumulated other comprehensive income in stockholders' equity. Changes in fair value are included as a component of accumulated other

comprehensive income in stockholders' equity, to the extent effective. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings. If the underlying hedged securities are sold, the amount of unrealized gain or loss in accumulated other comprehensive income relating to the corresponding interest rate swap agreement is included in the determination of gain or loss on the sale of the securities. If interest rate swap agreements are terminated, the associated gain or loss is deferred and amortized over the shorter of the remaining term of the original swap agreement, or the underlying hedged item, provided that the underlying hedged item has not been sold.

Income and expense from interest rate swap agreements that are, for accounting purposes, designated as trading derivatives are recognized as a net adjustment to securities held-for-trading in the accompanying consolidated statement of operations. During the term of the interest rate swap agreement, changes in fair value are recognized in the consolidated statements of operations. A corresponding amount is included as loss on securities held-for-trading in the

consolidated statement of operations.

Gains and losses from forward currency exchange contracts are recognized as a net adjustment to foreign currency gain or loss in the consolidated statement of operations. During the term of the forward currency exchange contracts, changes in fair value are recognized in the consolidated statement of financial condition and included in other assets (if there is an unrealized gain) or in other liabilities (if there is an unrealized loss). A corresponding amount is included as a component of net foreign currency gain or loss in the consolidated statement of operations.

The Company monitors its hedging instruments throughout their terms to ensure that they remain effective for their intended purpose. The Company is exposed to interest rate and/or currency risk on these hedging instruments, as well as to credit loss in the event of nonperformance by any other party to the Company's hedging instruments. The Company's policy is to enter into hedging agreements with counterparties rated A or better.

#### SHARE-BASED COMPENSATION

In December 2004, the FASB issued SFAS No. 123R, Share-Based Payment. This statement is a revision to SFAS No. 123, Accounting for Stock-Based Compensation, and superseded APB Opinion No. 25, Accounting for Stock Issued to Employees. This statement establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, primarily focusing on the accounting for transactions in which an entity obtains employee services in share-based payment transactions. Entities will be required to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). That cost will be recognized over the period during which an employee is required to provide service (usually the vesting period) in exchange for the award. The grant-date fair value of employee share options and similar instruments will be estimated using option-pricing models. If an equity award is modified after the grant date, incremental compensation cost will be recognized in an amount equal to the excess of the fair value of the modified award over the fair value of the original award immediately before the modification. As amended by Rule 4-01(a) of Regulation S-X promulgated by the SEC, this statement is effective as of the beginning of the first interim or annual reporting period of the Company's first fiscal year beginning on or after December 15, 2005. The Company adopted SFAS No. 123R, as amended, effective January 1, 2006 with no impact on the consolidated financial statements as there are no unvested options as of December 31, 2005 and the Company applied the fair value method to all options issued after January 1, 2003.

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#### INCOME TAXES

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. At December 31, 2006, the Company had a Federal capital loss carryover of approximately \$34,637 available to offset future capital gains.

#### RECENT ACCOUNTING PRONOUNCEMENTS

##### Reverse Repurchase Agreements

Accounting standard setters are currently reviewing treatment of transactions

where mortgage-backed securities purchased from a particular counterparty are financed via a repurchase agreement with the same counterparty. Currently, the Company records such assets and the related financing gross on the 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 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's net equity would not be materially affected. At December 31, 2006, the Company has identified available-for-sale securities with a fair value of approximately \$36,649 which had been purchased from and financed with reverse repurchase agreements totaling approximately \$31,375 with the same counterparty since their purchase. If the Company were to change the current accounting treatment for these transactions at December 31, 2006, total assets and total liabilities would be reduced by approximately \$31,375.

#### 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 VIEs in which the Company is the primary beneficiary under 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 significant inter-company balances and transactions have been eliminated in consolidation.

The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the 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 consolidate CMBS trusts in which the Company has invested.

#### Impairment of Investments



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In November 2005, the FASB issued FASB Staff Position ("FSP") FAS 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, which provides guidance for determining when impairment charges should be taken on certain debt and equity securities. FSP FAS 115-1/124-1 requires that debt and equity securities subject to the provisions of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, and equity securities subject to the provisions of APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock, but which are not accounted for under the equity method (i.e., securities accounted for under the cost method) shall be reviewed for impairment when circumstances warrant. For securities subject to SFAS No. 115, a review for other-than-temporary impairments shall occur in each accounting period where the fair value of the security is less than its cost. For securities subject to APB Opinion No. 18, a review for other-than-temporary impairments shall occur in each accounting period where a) circumstances indicate that impairment may exist and b) the fair value of the security is less than its carrying value. The provisions of the FSP were required to be applied to reporting periods beginning after December 15, 2005. The adoption of FSP FAS 115-1/124-1 on January 1, 2006 had no material impact on the Company's consolidated financial statements.

### 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. The Statement 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 Company is currently evaluating the impact of adopting SFAS No. 155.

### Determining the Variability in a Potential VIE

The FASB issued FASB Staff Position FIN 46(R)-6, Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R) ("FSP FIN 46(R)-6") in April 2006. FSP FIN 46(R)-6 addresses the application of FIN 46(R), Consolidation of Variable Interest Entities, in determining whether certain contracts or arrangements with a VIE are variable interests by requiring

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companies to base such evaluations on an analysis of the VIE's purpose and design, rather than its legal form or accounting classification.

FSP FIN 46(R)-6 is required to be applied for all reporting periods beginning after June 15, 2006. The adoption of this FSP did not result in material differences from the Company's existing accounting policies regarding the consolidation of VIEs.

### Accounting for Uncertainty in Income Taxes

In July 2006, the FASB issued FIN 48. FIN No. 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 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 Company is currently evaluating the effect of implementing this new standard but does not expect its implementation to have a material impact on the consolidated financial statements.

### Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157. 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 its 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 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 is currently evaluating the impact of adopting SFAS No. 157.

### Effects of Prior Year Misstatements

In September 2006, the SEC issued SAB No. 108. SAB No. 108 provides guidance on the consideration of effects of the prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. The SEC staff believes registrants must quantify errors using both a balance sheet and income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB No. 108 is effective for the first annual period ending after November 15, 2006 with early application encouraged. The adoption of SAB No. 108 on December 31, 2006 has no effect on the Company's consolidated financial statements.

### Valuation of Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159. 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 options

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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 separately in the balance sheet 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 is currently analyzing the potential impact of adoption of SFAS No. 159 to its consolidated financial statements.

### RECLASSIFICATIONS

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

### NOTE 2 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 December 31, 2006 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Esti Fa Va
-----	-----	-----	-----	-----
CMBS:				
CMBS IOs	\$ 69,183	\$ 1,450	\$ (1,280)	\$ 6
Investment grade CMBS	751,945	51,386	(7,788)	79
Non-investment grade rated subordinated securities	638,709	52,304	(4,994)	68
Non-rated subordinated securities	72,751	7,483	(67)	8
Credit tenant leases	24,439	391	(512)	2
Investment grade REIT debt	247,937	4,627	(3,320)	24
Multifamily agency securities	452,781	3,048	(6,003)	44
CDO investments	114,482	5,806	(3,042)	11
	-----	-----	-----	-----
Total CMBS	2,372,227	126,495	(27,006)	2,47
	-----	-----	-----	-----
RMBS:				
Agency adjustable rate securities	1,768	5	--	
Residential CMOs	131,563	265	(978)	13
Hybrid ARMs	11,798	--	(283)	1
	-----	-----	-----	-----
Total RMBS	145,129	270	(1,261)	14
	-----	-----	-----	-----
Total securities available-for-sale	\$2,517,356	\$126,765	\$ (28,267)	\$2,61
	=====	=====	=====	=====

At December 31, 2006, the Company's securities available-for-sale included non-U.S. dollar denominated assets with an estimated fair value of \$181,597.

At December 31, 2006, an aggregate of \$2,415,765 in estimated fair value of the Company's securities available-for-sale was pledged to secure its collateralized borrowings.

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The amortized cost and estimated fair value of securities available-for-sale at December 31, 2005 are summarized as follows:

Security Description	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
-----	-----	-----	-----	-----
CMBS:				
CMBS IOs	\$ 103,120	\$ 1,784	\$ (1,541)	\$ 103,363
Investment grade CMBS	495,555	24,757	(10,477)	509,835
Non-investment grade rated subordinated securities	625,132	55,693	(4,830)	675,995
Non-rated subordinated securities	24,436	2,303	(328)	26,411
Credit tenant leases	24,995	526	(684)	24,837
Investment grade REIT debt	249,412	8,887	(2,532)	255,767
Multifamily agency securities	268,319	490	(5,447)	273,362
CDO investments	112,571	12,155	(183)	124,543
	-----	-----	-----	-----
Total CMBS	1,903,546	106,595	(26,022)	1,984,119
	-----	-----	-----	-----
RMBS:				
Agency adjustable rate securities	77,629	--	(1,138)	76,491
Residential CMOs	667	58	--	725
Hybrid ARMs	16,012	--	(411)	15,601
	-----	-----	-----	-----
Total RMBS	94,308	58	(1,549)	92,817
	-----	-----	-----	-----
Total securities available-for-sale	\$1,997,854	\$106,653	\$ (27,571)	\$2,076,936
	=====	=====	=====	=====

At December 31, 2005, the Company's securities available-for-sale included non-U.S. dollar denominated assets with an estimated fair value of \$37,320.

At December 31, 2005, an aggregate of \$1,940,734 in estimated fair value of the Company's securities available-for-sale was pledged to secure its collateralized borrowings.

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At December 31, 2006 and 2005, the aggregate estimated fair values by underlying credit rating of the Company's securities available-for-sale are as follows:

Security Rating	December 31, 2006		December 31, 2005	
	Estimated Fair Value	Percentage	Estimated Fair Value	Percentage
-----	-----	-----	-----	-----
Agency and agency insured securities	\$ 593,170	23%	\$ 359,044	17%
AAA	207,482	8	192,482	9

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AA+	10,719	--	--	--
AA	5,810	--	--	--
AA-	14,859	1	2,580	--
A+	41,090	2	11,612	1
A	141,544	5	26,725	1
A-	112,906	4	57,733	3
BBB+	226,512	9	145,066	7
BBB	207,382	8	209,763	10
BBB-	154,776	6	228,406	11
-----				
Total investment grade securities available-for -sale	1,716,250	66	1,233,411	59
-----				
BB+	178,378	7	287,308	14
BB	276,044	10	173,110	8
BB-	99,892	4	97,883	5
B+	51,271	2	56,934	3
B	113,509	4	126,711	6
B-	41,334	2	16,884	1
CCC	3,823	--	--	--
Not rated	135,355	5	84,695	4
-----				
Total below investment grade securities available-for -sale	899,606	34	843,525	41
-----				
Total securities available-for-sale	\$2,615,856	100%	\$2,076,936	100%
=====				

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 December 31, 2006.

	Less than 12 Months		12 Months or More		To
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value
-----					
CMBS IOs	\$ 5,524	\$ (378)	\$ 22,181	\$ (902)	\$ 27,705
Investment grade CMBS	32,051	(151)	139,776	(7,637)	171,827
Non-investment grade rated subordinated securities	125,396	(2,457)	74,852	(2,537)	200,248
Non-rated subordinated securities	1,548	(6)	2,468	(61)	4,016
Credit tenant leases	--	--	15,803	(512)	15,803
Investment grade REIT debt	10,450	(152)	72,524	(3,168)	82,974
Multifamily agency securities	153,266	(600)	181,102	(5,403)	334,368
CDO investments	35,417	(3,042)	--	--	35,417
Residential CMOs	111,859	(978)	--	--	111,859
Hybrid ARMs	--	--	11,516	(283)	11,516
-----					
Total temporarily impaired securities	\$475,511	\$ (7,764)	\$520,222	\$ (20,503)	\$955,733
=====					

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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 December 31, 2005.

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Unrealized Losses
CMBS IOs	\$ 35,719	\$ (1,012)	\$ 11,506	\$ (529)	\$ 47,225	\$ (1,541)
Investment grade CMBS	107,478	(2,950)	118,941	(7,527)	226,419	(10,477)
Investment grade REIT debt	19,757	(244)	58,830	(2,288)	78,587	(2,532)
Non-investment grade rated subordinated securities	99,207	(2,941)	22,269	(1,889)	121,476	(4,830)
Non-rated subordinated securities	9,233	(328)	--	--	9,233	(328)
Credit tenant leases	--	--	15,923	(684)	15,923	(684)
Multifamily agency securities	181,072	(5,084)	22,320	(363)	203,392	(5,447)
CDO investments	3,391	(183)	--	--	3,391	(183)
Agency adjustable rate securities	76,491	(1,138)	--	--	76,491	(1,138)
Hybrid ARMS	--	--	15,601	(411)	15,601	(411)
Total temporarily impaired securities	\$532,348	\$ (13,880)	\$265,390	\$ (13,691)	\$797,738	\$ (27,571)

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. Management possesses both the intent and the ability to hold the securities until the Company has recovered the amortized cost. As such, management does not believe any of the securities are other than temporarily impaired.

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 flow 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 December 31, 2006 and 2005, the anticipated weighted average unleverged yield based upon the adjusted cost of the Company's entire subordinated CMBS portfolio was 10.3% and 10.2% per annum, respectively, and of the Company's other securities available-for-sale was 6.1% and 5.8% per annum, respectively. 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 December 31, 2006 and 2005, adjustable rate RMBS with an estimated fair value of \$144,140 and \$92,817, respectively, is included in securities available-for-sale on the consolidated statements of financial condition.

During 2006, the Company sold securities available-for-sale for total proceeds of \$236,945, resulting in a gross realized gain of \$30,884 and a gross realized loss of \$1,852. The Company sold the securities with unrealized losses prior to maturity due to changes in the underlying collateral which were expected to significantly impact the market value of the securities. During 2005, the Company sold securities available-for-sale for total proceeds of \$172,737, resulting in a realized gain of \$16,543. During 2004, the Company sold securities available-for-sale for total proceeds of \$486,942, resulting in a realized gain of \$17,544.

#### NOTE 3 IMPAIRMENTS - CMBS

In 2001, the Company adopted EITF 99-20. The Company updates its estimated cash flows for securities subject to EITF 99-20 on a quarterly basis. The Company compares the yields resulting from the updated cash flows to the current accrual yields. An impairment charge is required under EITF 99-20 if the updated yield is lower than the current accrual yield and the security has an estimated fair value less than its adjusted purchase price. The Company carries all these securities at their estimated fair value on its consolidated statement of financial condition.

#### 2006

During 2006, the Company had sixteen CMBS that required an impairment charge of \$7,880, of which \$6,133 was attributed to higher prepayment rates on a pool of Small Business Administration commercial mortgages. The decline in the updated yields that caused the remaining impairment charge of \$1,747 is not related to

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increases in losses but rather accelerated prepayments and changes in the timing of credit losses.

2005

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During 2005, the Company had six CMBS that required impairment charges of \$5,088. For one below investment grade CMBS, the Company increased its underlying loan loss expectations on a 1998 vintage CMBS transaction resulting in a charge of \$3,072. This CMBS transaction has two underlying mortgage loans secured by assisted living facilities located in Texas that were performing below management's original expectations. The two underlying mortgage loans were resolved in the fourth quarter of 2005 with lower than expected loss severities. The effect of the improved loss severity will be recognized over the remaining life of the security in the form of an increased yield. For the remaining five securities, changes in the timing of credit losses and prepayments caused yields to decline.

2004

During 2004, six 1998 vintage CMBS securities in four separate CMBS transactions required impairment charges of \$26,018. A variety of factors influenced updated yields for these securities including magnitude of credit loss, timing of credit loss, prepayments and servicer advances. The Company completed a re-evaluation of credit assumptions of its 1998 vintage CMBS portfolio in the fourth quarter of 2004. The magnitude of credit losses did not significantly change as a result of this process, as total loss expectations on the underlying loans moved from 2.06% to 2.04%. Changes in the timing of credit losses and prepayments caused updated yields on these securities to decline by a weighted average of 66 basis points. Market dislocations in 1998 caused disproportionate unrealized losses in the estimated fair value of these securities based on price quotes received from third parties. The Company had recorded these unrealized losses as other comprehensive loss on its consolidated statement of financial condition since that time. In addition, the Company increased underlying loan loss expectations on one non-rated security resulting in an impairment charge of \$663.

### NOTE 4 SECURITIZATION TRANSACTIONS

During 2005, the Company closed CDO HY2 and issued non-recourse liabilities with a face amount of \$365,010. Senior investment grade notes with a face amount of \$240,134 were issued and sold in a private placement. The Company retained the floating rate BBB- note, the below investment grade notes and the preferred shares. The Company recorded CDO HY2 as a secured financing for accounting purposes and consolidated the assets, liabilities, income and expenses of CDO HY2 until the sale of the floating rate BBB- note in the fourth quarter of 2005, at which point CDO HY2 qualified as a sale under SFAS No. 140. In exchange for a portfolio of CMBS and investment grade REIT debt with an estimated fair value of \$323,103, the Company received cash proceeds of \$244,212 as well as all of the retained interests that had an estimated fair value of \$105,025 at December 31, 2005. The total gain from CDO HY2 of \$16,523 is included in sale of securities available-for-sale on the consolidated statement of operations.

During 2004, the Company sold non-investment grade CMBS with an estimated fair value of \$109,933 to a qualifying special purpose entity ("CDO HY1"). These CMBS were securitized into various classes of non-recourse bonds and preferred equity. CDO HY1 sold the investment grade rated bonds to unrelated third parties for net proceeds of \$121,547. In accordance with SFAS No. 140, a gain of \$14,769 was recognized on the sale of the CMBS collateral to CDO HY1. At closing, the



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Company retained the A- rated bond and the preferred equity in CDO HY1. Subsequently, the A- rated bond was sold at a gain of \$1,825 during the fourth quarter of 2004.

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The table below summarizes the cash flows received from securitizations during the year ended December 31, 2006, 2005 and 2004, respectively.

	2006 -----	2005 -----	2004 -----
Proceeds from securitizations	\$ --	\$235,197	\$121,547
Sale of retained interest	\$ --	\$ 9,015	\$ 18,879
Cash flow on retained interests	\$17,951	\$ 11,347	\$ 0(1)

(1) For 2004, the retained interest's first scheduled quarterly payment was in January 2005.

Key economic assumptions used in measuring the fair value of the retained interests at the date of the securitization was as follows:

### Subordinated Debt

	2005 -----	2004 ----
Weighted average life	9.9 years	n/a
Subordinated discount rate	12.1%	n/a

### Preferred Equity

	2005 -----	2004 -----
Expected life	18.2 years	11.5 years
Preferred equity discount rate	4.93%	67.4%

When subsequently measuring the fair value of the retained interests, the Company applies certain loss assumptions to after-loss cash flows. The Company estimated credit losses and the timing of losses for each loan underlying the CMBS collateral, and accordingly does not apply a constant default rate to the portfolio. At December 31, 2006, 2005, and 2004, respectively, the amortized costs of the retained interests were \$111,076, \$119,003, and \$15,851, with an estimated fair value of \$114,142, \$121,159, and \$15,885, based on key economic assumptions. The sensitivity of the retained interest to immediate adverse changes in those assumptions follows:

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	2006	2005	2004
	-----	-----	-----
Reduction of income per share:			
50% adverse change in credit losses	\$0.12	\$0.09	\$0.02
100% adverse change in credit losses	\$0.24	\$0.18	\$0.04
EITF 99-20 impairment per share:			
50% adverse change in credit losses	\$0.05	\$0.03	\$0.04
100% adverse change in credit losses	\$0.05	\$0.03	\$0.07

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a variation in key assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. This non-linear relationship exists because the Company applies its key assumptions on a loan-by-loan basis to the assets underlying the CMBS collateral. Also, in this table, the effect of a variation in a particular assumption on the fair value of the retained interest was calculated without changing any other assumption; in reality, changes in one factor may result in changes to another, which might magnify or counteract the sensitivities. The Company reviews all major assumptions periodically using the most recent empirical and market data available, and makes adjustments where warranted.

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## 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.

## NOTE 6 SECURITIES HELD-FOR-TRADING

The Company's securities held-for-trading are carried at estimated fair value. At December 31, 2006, the Company's securities held-for-trading consisted of FNMA Mortgage Pools with an estimated fair value of \$132,204 and CMBS with an estimated fair value of \$22,383. At December 31, 2005, the Company's securities

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held-for-trading consisted of FNMA Mortgage Pools with an estimated fair value of \$166,209 and CMBS with an estimated fair value of \$21,264. 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.

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### NOTE 7 COMMERCIAL MORTGAGE LOANS

The following table summarizes the Company's commercial real estate loan portfolio by property type at December 31, 2006 and 2005:

Property Type	Loan Outstanding				Weighted Average Yield	
	December 31, 2006		December 31, 2005		Yield	
	Amount	%	Amount	%	2006	2005
Office	\$130,016	27.0%	\$ 94,432	25.8%	8.2%	8.9%
Residential	57,917	12.0	57,466	15.7	10.7	8.6
Retail	194,938	40.5	76,502	20.9	7.7	7.3
Hotel	38,899	8.1	79,840	21.8	10.0	8.6
Storage	34,009	7.1	32,913	9.0	9.0	9.1
Communication Tower	--	--	20,000	5.5	--	9.4
Industrial	19,317	4.0	2,423	0.7	9.1	8.1
Other Mixed Use	6,649	1.3	2,230	0.6	8.7	8.1
Total	\$481,745	100.0%	\$365,806	100.0%	8.6%	8.5%

Included in the table above are non-U.S. dollar denominated commercial real estate loans with a carrying value of \$243,377 and \$129,951 at December 31, 2006 and 2005, respectively. The Company finances its non-U.S. dollar denominated loans by borrowing in the applicable local currency and hedging the un-financed portion.

Reconciliation of commercial mortgage loans:

	Par	Book Value
Balance at December 31, 2004	\$ 272,686	\$ 263,506
Adjustment for discount accretion and foreign currency	--	(4,456)
Proceeds from repayment of mortgage loans	(112,830)	(112,830)
Principal receivable	(3,899)	(3,899)
Reduction in notional par value	(2,479)	--
Sale of commercial mortgage loans	(22,425)	(20,072)
Investments in commercial mortgage loans	242,572	243,557
Balance at December 31, 2005	\$ 373,625	\$ 365,806
Adjustment for discount accretion and		

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foreign currency	--	18,875
Proceeds from repayment of mortgage loans	(189,720)	(197,094)
Investments in commercial mortgage loans	236,545	294,158
	-----	-----
Balance at December 31, 2006	\$ 420,450	\$ 481,745

There were no loans subject to delinquent principal or interest at December 31, 2006 or 2005.

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### NOTE 8 EQUITY INVESTMENTS

The following table is a summary of the Company's equity investments for the year ended December 31, 2006:

	BlackRock Diamond	Carbon I	Carbon II	Dynamic India Fund IV	Total
	-----	-----	-----	-----	-----
Balance at					
December 31, 2005	\$ 51,004	\$ 18,458	\$ 41,188	\$ --	\$110,650
Contributions to					
Investments	41,901	--	32,782	3,850	78,533
Distributions from					
Investments	(2,774)	(16,238)	(15,455)	--	(34,467)
Equity earnings	15,763	924	10,744	--	27,431
	-----	-----	-----	-----	-----
Balance at					
December 31, 2006	\$105,894	\$ 3,144	\$ 69,259	\$3,850	\$182,147
	=====	=====	=====	=====	=====

At December 31, 2006, the Company owned approximately 20% of Carbon I. The Company also owned approximately 26% of Carbon II at December 31, 2006. Collectively, the Carbon Capital Funds are private commercial real estate income opportunity funds managed by the Manager (see Note 14 of the consolidated financial statements).

The Company entered into a \$50,000 commitment on July 20, 2001 to acquire shares in Carbon I. On July 12, 2004, the investment period expired and as repayments occur, capital will be returned to investors. The Company's investment in Carbon I at December 31, 2006 and 2005 was \$3,144 and \$18,458, respectively.

The Company entered into an aggregate commitment of \$100,000 to acquire shares in Carbon II. The Company's investment in Carbon II at December 31, 2006 and 2005 was \$69,259 and \$41,188, respectively. The Company's remaining commitment to Carbon II at December 31, 2006 was \$28,958.

The following table summarizes the loan investments held by the Carbon Capital Funds at December 31, 2006 and 2005.

Loan Outstanding

Weighted

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Property Type	December 31, 2006		December 31, 2005		Average Yield	
	Amount	%	Amount	%	2006	2005
Office	\$162,759	23.1%	\$128,802	23.0%	10.5%	10.1%
Residential	138,713	19.7	192,604	34.3	12.3	10.3
Retail	73,184	10.4	57,791	10.3	9.7	13.2
Hotel	241,086	34.2	146,710	26.1	12.1	12.8
Storage	--	--	10,171	1.8	--	16.4
Land	53,500	7.6	25,000	4.5	12.6	15.2
Other Mixed Use	35,384	5.0	--	--	8.8	--
Total	\$704,626	100.0%	\$561,078	100.0%	11.4%	11.5%

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At December 31, 2006, all commercial real estate loans owned directly by the Company were performing in line with expectations. As previously reported, investments held by Carbon II include a \$24,546 commercial real estate mezzanine loan which defaulted during July 2006. The default was subsequently cured. On March 9, 2007, the loan matured. The borrower did not repay the loan on the due date. In addition, the senior mortgage holder did not grant the borrower's request for extension of time to accommodate a sale of the property or refinancing of the loan. As a result, the loan is in default. The Company believes the underlying asset is sufficient collateral to repay the Company's loan in full. The underlying property is a hotel located in the South Beach area of Miami, Florida.

During February 2007, two other loans held by Carbon II defaulted. The aggregate carrying value of the two loans on Carbon II's consolidated financial statements is \$24,000 (\$12,000 per loan). The underlying properties for both loans are multi-family assets being converted to condominiums that are located in Florida. Carbon II is negotiating a workout arrangement with the borrower for one loan, whereby the borrower will cure its default and make additional capital contributions to sustain the property while the borrower continues its sales program. Based on credit analysis performed for this property, Carbon II believes a loan loss reserve is not necessary at this time.

For the second loan, the borrower was not able to achieve sufficient condominium sales to complete the condominium conversion. The borrower has indicated it will not contribute additional capital to sustain the rental property until such time as the condominium market recovers. As a result, Carbon II is expected to take title to the property and currently intends to operate it as a rental property while preparing the property for sale. Based on the credit analysis performed for this property, Carbon II has established a loan loss reserve of \$5,180 for the loan, of which the Company's share is \$1,361. All other commercial real estate loans in the Carbon Capital Funds are performing as expected.

On December 13, 2005, the Company entered into a \$75,000 commitment to acquire shares of BlackRock Diamond. On February 21, 2006, the Company increased its capital commitment by an additional \$25,000, resulting in a total capital commitment of \$100,000. At December 31, 2006, 93% of the commitment has been called and the Company owned approximately 21% of BlackRock Diamond. The Company's investment in BlackRock Diamond at December 31, 2006 was \$105,894. At December 31, 2006, the Company had \$7,397 of remaining capital commitments to

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BlackRock Diamond, all of which was called in January 2007.

On December 22, 2005, the Company entered into an \$11,000 commitment to acquire shares of Dynamic India Fund IV. On February 13, 2006, the Company received a notice calling 35% of its commitment.

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Combined summarized financial information of the unconsolidated equity investments of the Company is as follows:

	December 31,	
	2006	2005
Combined Balance Sheets:		
Real estate property, at fair value	\$ 680,134	\$273,432
Commercial mortgage loans, net	699,444	561,078
Other assets	138,060	101,947
Total Assets	\$1,517,638	\$936,457
Secured borrowings	\$ 654,385	\$402,876
Other liabilities	90,581	105,507
Partners', members' and stockholders' equity	772,672	428,074
Total liabilities, partners', members', and stockholders' equity	\$1,157,638	\$936,457
The Company's share of equity	\$ 182,147	\$110,650

	For the year ended December 31,		
	2006	2005	2004
Combined Statements of Operations:			
Income	\$95,470	\$82,973	\$49,107
Expenses			
Interest expense	42,483	21,834	7,731
Depreciation and amortization	--	--	1,274
Operating expenses	22,506	16,250	6,752
Total expenses	64,989	38,084	15,757
Realized/Unrealized gain	57,677	17,124	--
Net Income	\$88,158	\$62,013	\$33,350
The Company's share of net income	\$27,431	\$12,146	\$ 8,157

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## NOTE 9 REAL ESTATE, HELD-FOR-SALE

SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets specifies that long-lived assets to be disposed by sale, which meet certain criteria, should be classified as real estate held-for-sale and measured at the lower of its carrying amount or fair value less costs of sale. In addition, depreciation is not recorded for real estate held-for-sale.

On March 6, 2006, the Company purchased a defaulted loan from a Controlling Class CMBS trust. The loan was secured by a first mortgage on a multi-family property in Texas. Subsequent to the loan purchase, the property was acquired by the Company at foreclosure. The Company sold the property

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during the second quarter of 2006 and recorded a gain from discontinued operations of \$1,366 on the consolidated statement of operations.

## NOTE 10 BORROWINGS

The Company's borrowings consist of credit facilities, CDOs, senior unsecured notes, trust preferred securities, reverse repurchase agreements, and commercial mortgage loan pools.

Certain information with respect to the Company's borrowings at December 31, 2006 is summarized as follows:

	Reverse Repurchase Agreements	Credit Facilities	Commercial Mortgage Loan Pools	CDOs	Unsecured Notes
	-----	-----	-----	-----	-----
Outstanding borrowings	\$799,669	\$75,447	\$1,250,503	\$1,812,574	\$
Weighted average borrowing rate	5.37%	6.69%	3.99%	6.02%	
Weighted average remaining maturity	78 days	193 days	5.8 years	7.0 years	10.
Estimated fair value of assets pledged	\$854,074	\$88,876	\$1,271,014	\$2,096,455	

At December 31, 2006, the Company's borrowings had the following remaining maturities:

	Reverse Repurchase Agreements	Credit Facilities	Commercial Mortgage Loan Pools	CDOs*	Senior Unsecured Notes	Trust Preferred Securities
	-----	-----	-----	-----	-----	-----
Within 30 days	\$ 18,700	\$27,569	\$ --	\$ --	\$ --	\$ --
31 to 59 days	--	--	--	--	--	--
60 days to less than 1 year	780,969	33,893	--	--	--	--
1 year to 3 years	--	13,985	--	--	--	--
3 years to 5 years	--	--	--	--	--	--

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Over 5 years	--	--	1,250,503	1,812,574	75,000	180,47
	-----	-----	-----	-----	-----	-----
	\$799,669	\$75,447	\$1,250,503	\$1,812,574	\$75,000	\$180,47
	=====	=====	=====	=====	=====	=====

- \* At December 31, 2006, CDOs are comprised of \$405,490 of CDO debt with a weighted average remaining maturity of 5.29 years, \$291,261 of CDO debt with a weighted average remaining maturity of 5.63 years, \$366,019 of CDO debt with a weighted average remaining maturity of 6.39 years, \$402,089 of CDO debt with a weighted average remaining maturity of 9.68 years and \$347,715 of CDO debt with a weighted average remaining maturity of 7.75 years.

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Information with respect to the Company's borrowings at December 31, 2005 is summarized as follows:

	Reverse Repurchase Agreements	Credit Facilities	Commercial Mortgage Loan Pools	CDOs	Trust Preferred Securities
	-----	-----	-----	-----	-----
Outstanding borrowings	\$816,641	\$ 284,675	\$ 1,272,931	\$ 1,066,930	\$ 77,380
Weighted average borrowing rate	4.47%	5.27%	3.97%	5.96%	7.64%
Weighted average remaining maturity	27 days	1.37 years	6.80 years	6.78 years	30.1 years
Estimated fair value of assets pledged	\$897,886	\$ 415,501	\$ 1,292,407	\$ 1,227,222	--

At December 31, 2005, the Company's borrowings had the following remaining maturities:

	Reverse Repurchase Agreements	Credit Facilities	Commercial Mortgage Loan Pools	CDOs*	Trust Preferred Securities	Total Borrowings
	-----	-----	-----	-----	-----	-----
Within 30 days	\$796,365	\$ --	\$ --	\$ --	\$ --	\$ 796,365
31 to 59 days	20,276	--	--	--	--	20,276
60 days to less than 1 year	--	113,009	--	--	--	113,009
1 year to 3 years	--	171,666	--	--	--	171,666
3 years to 5 years	--	--	--	--	--	--
Over 5 years	--	--	1,272,931	1,066,930	77,380	2,417,241
	-----	-----	-----	-----	-----	-----
	\$816,641	\$284,675	\$1,272,931	\$1,066,930	\$77,380	\$3,518,181
	=====	=====	=====	=====	=====	=====

- \* Comprised of \$406,208 of CDO debt with a weighted average remaining maturity of 6.29 years at December 31, 2005 and \$292,807 of CDO debt with a



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weighted average remaining maturity of 6.68 years at December 31, 2005, and \$367,915 of CDO debt with a weighted average remaining maturity of 7.39 years at December 31, 2005.

### Reverse Repurchase Agreements and Credit Facilities

The Company has entered into reverse repurchase agreements to finance most of its securities available-for-sale that are not financed under its credit facilities or CDOs. The reverse repurchase agreements bear interest at a LIBOR-based variable rate.

Under the credit facilities and the reverse repurchase agreements, the respective lender retains the right to mark the underlying collateral to estimated fair value. A reduction in the value of pledged assets would require the Company to provide additional collateral or fund margin calls. From time to time, the Company may be required to provide additional collateral or fund margin calls. At December 31, 2006, more than ten percent of the Company's net assets were held as collateral for reverse repurchase agreements with Citigroup Global Markets, Inc. and Lehman Brothers, Inc.

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The Company's credit facilities can be used to replace existing reverse repurchase agreement borrowings and to finance the acquisition of mortgage-backed securities and commercial real estate loans. Outstanding borrowings bear interest at a variable rate. The following table summarizes the Company's credit facilities at December 31, 2006 and 2005.

	Maturity Date	December 31, 2006			December 31, 2005	
		Facility Amount	Total Borrowings	Unused Borrowing Capacity	Facility Amount	Total Borrowings
Greenwich Capital, Inc. (1)	7/7/07	\$ 75,000*	\$12,064	\$ --	\$ 75,000	\$ 75,000
Deutsche Bank, AG (2)	12/20/07	200,000	\$49,398	\$150,602	200,000	\$181,875
Bank of America, N.A. (3)	9/17/08	\$100,000	\$ --	\$100,000	n/a	n/a
Morgan Stanley Bank (3) (4)	2/16/08	\$200,000	\$13,985	\$186,015	\$ 27,800	\$ 27,800
		-----	-----	-----	-----	-----
		\$575,000	\$75,447	\$436,617	\$302,800	\$284,675
		=====	=====	=====	=====	=====

\* Commitment expired December 23, 2006. No new borrowings permitted.

(1) USD only

(2) Multicurrency

(3) Non-USD only

(4) Can be increased up to \$15,000 based on the change in exchange rates of the non-U.S. dollar loans. However, any amounts drawn under this provision must be repaid in ninety days.

The Company is subject to various covenants in its credit facilities, including

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maintaining a minimum net worth measured on a book value of \$305,000 in accordance with generally accepted accounting principles in the United States of America ("GAAP"), a maximum recourse debt-to-equity of 3.0 to 1, a minimum cash requirement based upon certain debt-to-equity ratios. During the first quarter of 2007, the Company amended the debt service coverage ratio covenant on its committed debt facilities. The terms of the calculation were revised and the debt service coverage ratio was reduced from 1.75 to 1.20. The revised calculation better reflects the Company's ability to service debt on a cash basis. At December 31, 2006 and 2005, the Company was in compliance with all other covenants.

### CDOs

On May 29, 2002, the Company issued ten tranches of secured debt through CDO I. In this transaction, a wholly owned subsidiary of the Company issued debt in the par amount of \$419,185 secured by the subsidiary's assets. The adjusted issue price of the CDO I debt, at December 31, 2006, is \$405,490. Five tranches were issued at a fixed rate coupon and five tranches were issued at a floating rate coupon with a combined weighted average remaining maturity of 5.3 years at December 31, 2006. All floating rate coupons were swapped to fixed rate coupons resulting in a total fixed rate cost of funds for CDO I of approximately 7.3%. The Company incurred \$9,890 of issuance costs that will be amortized over the weighted average life of CDO I. CDO I was structured to match fund the cash flows from a significant portion of the Company's CMBS and investment grade REIT debt. The par amount at December 31, 2006 of the collateral securing CDO I consisted of 78.2% CMBS rated B or higher and 21.8% REIT debt rated BBB or higher. At December 31, 2006, the collateral securing CDO I had a fair value of \$516,347.

On December 10, 2002, the Company issued seven tranches of secured debt through CDO II. In this transaction, a wholly owned subsidiary of the Company issued debt in the par amount of \$280,783 secured by the subsidiary's assets. In July 2004, the Company sold a CDO II bond with a par of

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\$12,850 that it had previously retained. Before the sale of this security, the Company amended the indenture to reduce the coupon from 9.0% to 7.6%. The adjusted issue price of the CDO II debt at December 31, 2006 is \$291,261. Five tranches were issued at a fixed rate coupon and three tranches were issued at a floating rate coupon with a combined weighted average remaining maturity of 5.6 years at December 31, 2006. All floating rate coupons were swapped to fixed rate coupons resulting in a total fixed rate cost of funds for CDO II of approximately 6.0%. The Company incurred \$6,004 of issuance costs that will be amortized over the weighted average life of CDO II. CDO II was structured to match fund the cash flows from a significant portion of the Company's CMBS and investment grade REIT debt. The par amount at December 31, 2006 of the collateral securing CDO II consisted of 81.4% CMBS rated B or higher and 18.6% REIT debt rated BBB or higher. At December 31, 2006, the collateral securing CDO II had a fair value of \$358,447.

On March 30, 2004, the Company issued eleven tranches of secured debt through CDO III. In this transaction, a wholly owned subsidiary of the Company issued secured debt in the par amount of \$372,456 secured by the subsidiary's assets. The adjusted issue price of the CDO III debt, at December 31, 2006, is \$366,019. Five tranches were issued at a fixed rate coupon and six tranches were issued at a floating rate coupon with a combined weighted average remaining maturity of 6.4 years at December 31, 2006. All floating rate coupons were swapped to fixed rate coupons resulting in a total fixed rate cost of funds for CDO III of

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approximately 5.0%. The Company incurred \$2,006 of issuance costs that will be amortized over the weighted average life of CDO III. CDO III was structured to match fund the cash flows from a significant portion of the Company's CMBS and investment grade REIT. The par amount at December 31, 2006 of the collateral securing CDO III consisted of 84.3% CMBS rated B or higher and 15.7% REIT debt rated BBB or higher. At December 31, 2006, the collateral securing CDO III had a fair value of \$391,061.

On May 23, 2006, the Company issued nine tranches of secured debt through CDO HY3. In this transaction, a wholly owned subsidiary of the Company issued secured debt in the par amount of \$417,000 secured by the subsidiary's assets. The adjusted issue price of the CDO HY3 debt at December 31, 2006 is \$402,089. Three tranches were issued at a fixed rate coupon and six tranches were issued at a floating rate coupon with a combined weighted average remaining maturity of 9.7 years at December 31, 2006. All floating rate coupons were swapped to fixed rate coupons resulting in a total fixed rate cost of funds for CDO HY3 of approximately 6.4%. The Company incurred \$7,057 of issuance costs that will be amortized over the weighted average life of CDO HY3. CDO HY3 was structured to match fund the cash flows from a significant portion of the Company's CMBS and commercial real estate loans. The par amount at December 31, 2006 of the collateral securing CDO HY3 consisted of 75.6% CMBS rated B or higher and 24.4% commercial real estate loans. At December 31, 2006, the collateral securing CDO HY3 had a fair value of \$449,649.

On December 14, 2006, the Company closed its seventh CDO ("Euro CDO"). The Euro CDO sold E263,500 of non-recourse debt at a weighted average spread to Euro Libor of 60 basis points. The E263,500 consists of E251,000 of investment grade debt at a weighted average spread to Euro Libor of 50 basis points and E12,500 of below investment grade debt. The Company retained an additional E12,500 of below investment grade debt and all of Euro CDO's preferred shares. The Company incurred E3,489 of issuance costs that will be amortized over the weighted average life of Euro CDO. This transaction represents the Company's seventh CDO. The previous six were U.S. dollar denominated.

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### Senior Unsecured Notes

During October 2006, the Company issued \$75,000 of unsecured senior notes due in 2016 with a weighted average cost of funds of 7.21%. The unsecured senior notes can be redeemed in whole by the Company subject to certain provisions, which could include the payment of fees.

### Trust Preferred Securities

On September 26, 2005, the Company issued \$75,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust I, a Delaware statutory trust ("Trust I"). The trust preferred securities have a thirty-year term ending October 30, 2035 with interest at a fixed rate of 7.497% for the first ten years and at a floating rate of three-month LIBOR plus 2.9% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in October 2010. Trust I issued \$2,380 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust I to the Company for a purchase price of \$2,380. The Company realized net proceeds from this offering of approximately \$72,618.

On January 31, 2006, the Company issued \$50,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust II, a Delaware

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statutory trust ("Trust II"). The trust preferred securities have a thirty-year term ending April 30, 2036 with interest at a fixed rate of 7.73% for the first ten years and at a floating rate of three-month LIBOR plus 2.7% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in April 2011. Trust II issued \$1,550 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust II to the Company for a purchase price of \$1,550. The Company realized net proceeds from this offering of approximately \$48,491.

On March 16, 2006, the Company issued \$50,000 of trust preferred securities through its wholly owned subsidiary, Anthracite Capital Trust III, a Delaware statutory trust ("Trust III" and collectively with Trust I and Trust II, the "Trusts"). The trust preferred securities have a thirty-year term ending March 15, 2036 with interest at a fixed rate of 7.77% for the first ten years and at a floating rate of three-month LIBOR plus 2.7% thereafter. The trust preferred securities can be redeemed at par by the Company beginning in March 2011. Trust III issued \$1,547 aggregate liquidation amount of common securities, representing 100% of the voting common stock of Trust III to the Company for a purchase price of \$1,547. The Company realized net proceeds from this offering of approximately \$48,435.

The Trusts used the proceeds from the sale of the trust preferred securities and the common securities to purchase the Company's junior subordinated notes. The terms of the junior subordinated notes match the terms of the trust preferred securities. The notes are subordinate and junior in right of payment to all present and future senior indebtedness and certain other of our financial obligations.

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

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### NOTE 11 FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the notional amount, carrying value and estimated fair value of financial instruments at December 31, 2006 and 2005:

	December 31, 2006			December 31, 2005	
	Notional Amount	Carrying Value	Estimated Fair Value	Notional Amount	Carrying Value
Securities available-for-sale	\$ --	\$2,615,856	\$2,615,856	\$ --	\$ 2,076,936
Securities held-for-trading	--	154,587	154,587	--	187,473
Commercial mortgage loans	--	481,745	481,745	--	365,806
Secured borrowings	--	875,116	875,116	--	1,101,316
CDO borrowings	--	1,812,574	1,834,787	--	1,066,930
Commercial mortgage loan pool borrowings	--	1,250,503	1,250,503	--	1,272,931
Senior unsecured notes	--	75,000	75,000	--	--
Junior subordinated notes	--	180,477	180,477	--	77,380

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Currency forward contracts	--	(2,659)	(2,659)	--	1,108
Currency swap agreements	--	(240)	(240)	--	--
Interest rate swap agreements	1,843,144	15,274	15,274	1,558,398	20,845

Notional amounts are a unit of measure specified in a derivative instrument. The estimated fair values of the Company's securities available-for-sale, securities held-for-trading, currency forward contracts and interest rate swap agreements are based on market prices provided by certain dealers who make markets in these financial instruments. The estimated fair values reported reflect estimates and may not necessarily be indicative of the amounts the Company could realize in a current market exchange. Commercial mortgage loans and secured borrowings are floating rate instruments, and based on these terms, their carrying value approximates fair value.

### NOTE 12 PREFERRED STOCK

The Series B Preferred Stock was redeemed on May 6, 2004. The consolidated statement of operations for 2004 includes a charge of \$10,508 for the redemption of the Company's Series B Preferred Stock.

On February 12, 2007, the Company issued \$86,250 of Series D Cumulative Redeemable Preferred Stock ("Series D Preferred Stock"), including \$11,250 of Series D Preferred Stock sold to underwriters pursuant to an over-allotment option. The Series D Preferred Stock will pay an annual dividend of 8.25%.

At December 31, 2006, the Company had 94,394,003 authorized and un-issued shares of preferred stock. Following the issuance of the Series D Preferred Stock on February 12, 2007, the Company had 90,944,003 authorized and un-issued shares of preferred stock.

### NOTE 13 COMMON STOCK

On August 18, 2005, the Company completed a follow-on offering of 1,725,000 shares of its Common Stock, at a price of \$11.59 per share, which included a 15% over-allotment option exercised by the underwriter. Net proceeds (after deducting underwriting fees and expenses) were \$19,125.

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The following table summarizes Common Stock issued by the Company for the years ended December 31, 2006 and 2005:

	2006		2005	
	Shares	Net Proceeds	Shares	Net Proceeds
Dividend Reinvestment Plan	608,747	\$ 6,517	1,318,568	\$14,327
Follow-on offerings	--	--	1,725,000	19,125
Sales agency agreement	664,900	8,625	--	--
Director compensation	5,000	64	6,000	70
Incentive fees	189,077	2,100	--	--
Stock options	24,700	209	--	--
Total	1,492,424	\$17,515	3,049,568	\$33,522

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The following table summarizes dividends declared and paid by the Company for the years ended December 31, 2006, 2005, and 2004:

Year	Dividend Declared	Dividend Declared per Share	Paid in Current Year	Paid in Subsequent Year (1)
----	-----	-----	-----	-----
2006	\$66,017	\$1.15	\$49,246	\$16,771
2005	\$61,168	\$1.12	\$45,394	\$15,774
2004	\$58,208	\$1.12	\$43,287	\$14,920

(1) Paid on February 1

Dividends related to 2006, 2005 and 2004 were 100% ordinary income.

### NOTE 14 TRANSACTIONS WITH AFFILIATES

The Company has a Management Agreement, an administrative services agreement and an accounting services agreement with the Manager, the employer of certain directors and all of the officers of the Company, under which the Manager and the Company's officers manage the Company's day-to-day investment operations, subject to the direction and oversight of the Company's Board of Directors. Pursuant to the Management Agreement and these other agreements, the Manager and the Company's officers formulate investment strategies, arrange for the acquisition of assets, arrange for financing, monitor the performance of the Company's assets and provide certain other advisory, administrative and managerial services in connection with the operations of the Company. For performing certain of these services, the Company pays the Manager under the Management Agreement a base management fee equal to 2.0% of the quarterly average total stockholders' equity for the applicable quarter.

To provide an incentive, the Manager is entitled to receive an incentive fee under the Management Agreement equal to 25% of the amount by which the rolling four-quarter GAAP net income before the incentive fee exceeds the greater of 8.5% or 400 basis points over the ten-year Treasury note multiplied by the adjusted per share issue price of the Company's Common Stock (\$11.37 per common share at December 31, 2006). Additionally, up to 30% of the incentive fees earned in 2005 or after may be paid in shares of the Company's Common Stock subject to certain provisions under a compensatory deferred stock plan approved by the stockholders of the Company in 2006. The Board of Directors also authorized a stock based incentive plan where one-half of one percent of common shares outstanding was paid to the Manager in 2006.

The Company's unaffiliated directors approved an extension of the Management Agreement to March 30, 2008 at the Board's March 2007 meeting.

The following is a summary of management and incentive fees incurred for the years ended December 31, 2006, 2005, and 2004:

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	For the Year Ended December 31,		
	2006	2005	2004
Management fee	\$12,617	\$10,974	\$8,956
Incentive fee	5,919	4,290	--
Incentive fee- stock based	2,761	--	--
Total management and incentive fees	\$21,297	\$15,264	\$8,956

The Company has administration and accounting services agreements with the Manager. Under the terms of the administration agreement, the Manager provides financial reporting, audit coordination and accounting oversight services to the Company. Under the terms of the accounting services agreement, the Manager provides investment accounting services to the Company. For the years ended December 31, 2006, 2005, and 2004, the Company paid administration fees of \$234, \$209, and \$174, respectively, which are included in general and administrative expense on the accompanying statement of operations. No payments were made in each of the three years in the period ended December 31, 2006 under the accounting services agreement.

The special servicer on 25 of the Company's 29 Controlling Class trusts is Midland, a wholly owned indirect subsidiary of PNC Bank, and therefore a related party to the Manager. The Company's fees for Midland's services are at market rates.

On December 13, 2005, the Company entered into a \$75,000 commitment to acquire shares of BlackRock Diamond. BlackRock Diamond is a private REIT managed by BlackRock Realty Advisors, Inc., a subsidiary of the Manager. During February 2006, the Company increased its capital commitments by an additional \$25,000. At December 31, 2006, 93% of the commitment has been called and the Company owned approximately 21% of BlackRock Diamond. The Company does not incur any additional management or incentive fees to the Manager related to its investment in BlackRock Diamond. The Company's investment in BlackRock Diamond at December 31, 2006 was \$105,894. At December 31, 2006, the Company had \$7,397 of remaining capital commitments to BlackRock Diamond, all of which was called in January 2007.

During 2001, the Company entered into a \$50,000 commitment to acquire shares in Carbon I, a private commercial real estate income opportunity fund managed by the Manager. The Carbon I investment period ended on July 12, 2004 and the Company's investment in Carbon I at December 31, 2006 was \$3,144. The Company does not incur any additional management or incentive fees to the Manager related to its investment in Carbon I. On December 31, 2006, the Company owned approximately 20% of the outstanding shares in Carbon I. The Company's unaffiliated directors approved this transaction in July 2001.

The Company entered into an aggregate commitment of \$100,000 to acquire shares in Carbon II, a private commercial real estate income opportunity fund managed by the Manager. At December 31, 2006, the Company's investment in Carbon II was \$69,259 and the Company's remaining commitment to Carbon II is \$28,958. The Company does not incur any additional management or incentive fees to the Manager related to its investment in Carbon II. On December 31, 2006, the

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Company owned approximately 26% of the outstanding shares in Carbon II. The Company's unaffiliated directors approved this transaction in September 2004.

During 2000, the Company completed the acquisition of CORE Cap, Inc. At the time of the CORE Cap, Inc. acquisition, the Manager agreed to pay GMAC (CORE Cap, Inc.'s external advisor) \$12,500 over a ten-year period ("Installment Payment") to purchase the right to manage the Core Cap, Inc. assets under the existing management contract ("GMAC Contract"). The GMAC Contract had to be terminated in order to allow the Company to complete the merger, as the Company's management agreement with the Manager did not provide for multiple managers. As a result the Manager offered to buy-out the GMAC Contract as the Manager estimated it would receive incremental fees above and beyond the Installment Payment, and thus was willing to pay for, and separately negotiate, the termination of the GMAC Contract. Accordingly, the value of the Installment Payment was not considered in the Company's allocation of its purchase price to the net assets acquired in the acquisition of CORE Cap, Inc. The Company agreed that should the Management Agreement with its Manager be terminated, not renewed or not extended for any reason other than for cause, the Company would pay to the Manager an amount equal to the Installment Payment less the sum of all payments made by the Manager to GMAC. At December 31, 2006, the Installment Payment would be \$4,000 payable over four years. The Company does not accrue for this contingent liability.

### NOTE 15 STOCK OPTIONS

The Company has adopted a stock option plan (the "1998 Stock Option Plan") that provides for the grant of both qualified incentive stock options that meet the requirements of Section 422 of the Code and non-qualified stock options, stock appreciation rights and dividend equivalent rights. Stock options may be granted to the Manager, directors and officers of the Company and directors, officers and key employees of the Manager and to any other individual or entity performing services for the Company.

The exercise price for any stock option granted under the 1998 Stock Option Plan may not be less than 100% of the fair market value of the shares of Common Stock at the time the option is granted. Each option must terminate no more than ten years from the date it is granted and have vested over either a two or three-year period. Subject to anti-dilution provisions for stock splits, stock dividends and similar events, the 1998 Stock Option Plan authorizes the grant of options to purchase up to an aggregate of 2,470,453 shares of Common Stock.

The following table summarizes information about options outstanding under the 1998 Stock Option Plan:

	2006		2005	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at January 1	1,417,851	\$14.87	1,417,851	\$14.87
Granted	--	--	--	--
Exercised	(24,700)	8.45	--	--
Cancelled	(1,000)	11.81	--	--
Outstanding at December 31	1,392,151	\$14.98	1,417,851	\$14.87
	=====	=====	=====	=====
Options exercisable at December 31	1,392,151	\$14.98	1,417,851	\$14.87
	=====	=====	=====	=====



The following table summarizes information about options outstanding under the 1998 Stock Option Plan at December 31, 2006:

Exercise Price	Options Outstanding	Remaining Contractual Life (Years)	Options Exercisable
-----	-----	-----	-----
\$ 8.44	8,000	2.2	8,000
11.81	4,000	7.4	4,000
15.00	1,310,851	1.2	1,310,851
15.58	57,750	0.7	57,750
15.83	11,550	1.2	11,550
-----	-----	---	-----
\$7.82-\$15.83	1,392,151	1.2	1,392,151
=====	=====	===	=====

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

	2004
	-----
Estimated volatility	22.6%
Expected term	7 years
Risk-free interest rate	1.2%
Expected dividend yield	9.5%

There were no options granted in 2006 or 2005. Shares of Common Stock available for future grant under the 1998 Stock Option Plan at December 31, 2006 were 775,502.

#### NOTE 16 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company accounts for its derivative investments under SFAS No. 133, as amended, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the consolidated statement of financial condition at estimated fair value. If the derivative is designated as a cash flow hedge, the effective portions of change in the estimated fair value of the derivative are recorded in other comprehensive income ("OCI") and are recognized in the consolidated statement of operations when the hedged item affects earnings. Ineffective portions of changes in the estimated fair value of cash flow hedges are recognized in earnings. If the derivative is designated as a fair value hedge, the changes in the estimated fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings.

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

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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.

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

Where the Company elects to apply hedge accounting, it 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.

Occasionally, counterparties will require the Company or the Company will require counterparties to provide collateral for the interest rate swap agreements in the form of margin deposits. Such deposits are recorded as a component of other assets, other liabilities or restricted cash. Should the counterparty fail to return deposits paid, the Company would be at risk for the value of that asset. At December 31, 2006, the balance of such net deposits pledged to counterparties as collateral under these agreements totaled \$520. At December 31, 2005, the balance of such net deposits held by the Company as collateral under these agreements totaled \$1,246.

2006

During the fourth quarter, the Company changed its financing strategy to emphasize the use of 90-day reverse repurchase agreements and concurrently reduced the use of 30-day reverse repurchase agreements. The Company expects 90-day repurchase agreements to be its primary source for short-term financings in future periods. As a result of the reduction in the balance of 30-day reverse repurchase agreements, certain interest swaps that were hedging the 30-day reverse repurchase agreements were de-designated as hedges. As a result of the de-designation, the Company incurred a loss of \$12,661. Of this amount, \$9,433 were previously recorded in OCI and was being reclassified to interest expense over the weighted average remaining term of the swaps at the time the swaps were closed. The balance of \$3,228 relates to costs associated with interest rate swaps that were closed or redesignated in the fourth quarter of 2006. At December 31, 2006, a loss of \$8,210 remained in OCI and \$1,637 will be reclassified as an increase to interest expense over the next twelve months.

At December 31, 2006, the Company had interest rate swaps with notional amounts aggregating \$1,539,699 designated as cash flow hedges of borrowings under reverse repurchase agreements and the floating rate debt of its CDOs. Cash flow hedges with an estimated fair value of \$24,290 are included in other assets on the consolidated statement of financial condition and cash flow hedges with an estimated fair value of \$11,012 are included in other liabilities on the consolidated statement of financial condition. This liability was collateralized with the restricted cash equivalents recorded on the

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Company's consolidated statement of financial condition. For the year ended December 31, 2006, the net change in the estimated fair value of the interest rate swaps was an increase of \$2,699, of which \$262 was deemed ineffective and is included as an increase of interest expense and \$2,961 was recorded as an increase of OCI. At December 31, 2006, the \$1,539,699 notional of swaps that were designated as cash flow hedges had a weighted average remaining term of 7.5 years.

At December 31, 2006, the Company had interest rate swaps with notional amounts aggregating \$446,599 designated as trading derivatives. Trading derivatives with an estimated fair value of \$3,294 are included in other assets on the consolidated statement of financial condition and trading derivatives with a fair value of \$1,537 are included in other liabilities on the consolidated statement of financial condition. For the year ended December 31, 2006, the change in fair value for these trading derivatives was an increase of \$717 and is included as an addition to gain on securities held-for-trading in the consolidated statement of operations. At December 31, 2006, the \$446,599 notional of swaps, which were designated as trading derivatives, had a weighted average remaining term of 7.6 years.

At December 31, 2006, the Company had a forward LIBOR cap with a notional amount of \$85,000 and a fair value of \$211 that is included in interest rate swap agreement on the consolidated statement of financial condition. The change in estimated fair value related to this derivative is included as a component of gain (loss) on securities held-for-trading in the consolidated statements of operations.

2005

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

At December 31, 2005, the Company had interest rate swaps with notional amounts aggregating \$1,201,953 designated as cash flow hedges of borrowings under reverse repurchase agreements and the floating rate debt of its CDOs. Cash flow hedges with an estimated fair value of \$25,632 are included in other assets on the consolidated statement of financial condition and cash flow hedges with an estimated fair value of \$8,782 are included in other liabilities on the consolidated statement of financial condition. For the year ended December 31, 2005, the net change in the estimated fair value of the interest rate swaps was an increase of \$25,436, of which \$1,190 was deemed ineffective and is included as an increase of interest expense and \$26,626 was recorded as an addition to OCI. At December 31, 2005, the \$1,201,953 notional of swaps designated as cash flow hedges had a weighted average remaining term of 7.89 years.

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During the year ended December 31, 2005, the Company terminated nine of its interest rate swaps with a notional amount of \$204,300 that were designated as cash flow hedges of borrowings under reverse repurchase agreements. The Company will reclassify the \$2,034 loss in value incurred from OCI to interest expense over 8.86 years, which was the weighted average remaining term of the swaps at the time they were closed out. For the year ended December 31, 2005, \$103 was reclassified as an increase to interest expense and \$252 will be reclassified as an increase to interest expense for the next 12 months. As of December 31, 2005 the Company has, in aggregate, \$35,530 of losses related to terminated swaps in OCI. For the year ended December 31, 2005, \$6,129 was reclassified as an increase to interest expense and \$6,029 will be reclassified as an increase to interest expense for the next twelve months.

At December 31, 2005, the Company had interest rate swaps with notional amounts aggregating \$356,445 designated as trading derivatives. Trading derivatives with an estimated fair value of \$4,119 are included in

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other assets on the consolidated statement of financial condition and trading derivatives with an estimated fair value of \$125 are included in other liabilities on the consolidated statement of financial condition. For the year ended December 31, 2005, the change in estimated fair value for these trading derivatives was an increase of \$3,030 and is included as a reduction of loss on securities held-for-trading in the consolidated statements of operations. At December 31, 2005, the \$356,445 notional of swaps designated as trading derivatives had a weighted average remaining term of 6.99 years.

At December 31, 2005, the Company had a forward LIBOR cap with a notional amount of \$85,000 and a fair value of \$1,491 that is included in interest rate swap agreement on the consolidated statement of financial condition. The change in estimated fair value related to this derivative is included as a component of gain (loss) on securities held-for-trading in the consolidated statements of operations.

### FOREIGN CURRENCY

The U.S. dollar is considered the functional currency for certain of the Company's international subsidiaries. Foreign currency transaction gains or losses are recognized in the period incurred and are included in foreign currency gain (loss) in the consolidated statement of operations. Gains and losses on foreign currency forward commitments are included in foreign currency gain (loss) in the consolidated statement of operations. The Company recorded foreign currency gain (loss) of \$2,161, \$(134), and \$(187) for the years ended December 31, 2006, 2005 and 2004, respectively. At December 31, 2006, the Company had foreign currency forward commitments with an estimated fair value of \$289,779 included in other assets and \$(292,438) included in other liabilities on the consolidated statement of financial condition. At December 31, 2005, the Company had foreign currency forward commitments with an estimated fair value of \$71,673 included in other assets and \$(70,565) included in other liabilities on the consolidated statement of financial condition.

### NOTE 17 NET INTEREST INCOME

The following is a presentation of the Company net interest income for the year ended December 31, 2006, 2005 and 2004:

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	Year ended December 31,		
	2006	2005	2004
Interest Income:			
Interest from securities available-for-sale	\$171,686	\$141,113	\$131,342
Interest from commercial mortgage loans	41,773	23,183	11,896
Interest from commercial mortgage loan pools	52,917	54,025	39,672
Interest from securities held-for-trading	7,207	11,370	11,419
Interest from cash and cash equivalents	2,403	2,077	638
Total interest income	275,986	231,768	194,967
Interest Expense:			
Interest	205,023	156,865	124,289
Interest - securities held-for-trading	7,365	6,593	3,877
Total interest expense	212,388	163,458	128,166
Net interest income	\$ 63,598	\$ 68,310	\$ 66,801

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NOTE 18 NET INCOME PER SHARE

Net income per share is computed in accordance with SFAS No. 128, Earnings Per Share ("SFAS No. 128"). 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, and the dilutive effect of preferred stock is calculated using the "if converted" method.

	For the year ended December 31,		
	2006	2005	2004
Numerator:			
Net income available to common stockholders	\$ 75,079	\$ 65,205	\$ 25,768
Numerator for basic and diluted earnings per share	\$ 75,079	\$ 65,205	\$ 25,768
Denominator:			
Denominator for basic earnings per share--weighted average common shares outstanding	57,182,434	54,144,243	51,766,877
Dilutive effect of stock options	2,364	8,577	8,903
Dilutive effect of stock based incentive fee	216,866	--	--
Denominator for diluted earnings per share--weighted average common shares			

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outstanding and common stock equivalents			
outstanding	57,401,664	54,152,820	51,775,780
	=====	=====	=====
Basic net income per weighted average common share:	\$ 1.31	\$ 1.20	\$ 0.50
	-----	-----	-----
Diluted net income per weighted average common stock			
and common stock equivalents:	\$ 1.31	\$ 1.20	\$ 0.50
	-----	-----	-----

Total anti-dilutive stock options and warrants excluded from the calculation of net income per share were \$1,380,151, 1,375,151, and 1,385,151 for the years ended December 31, 2006, 2005, and 2004, respectively.

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## NOTE 19 SUMMARIZED QUARTERLY RESULTS (UNAUDITED)

The following is a presentation of quarterly results of operations:

	Quarters Ending					
	March 31		June 30		September 30	
	2006	2005	2006	2005	2006	2005
Total Income	\$71,743	\$57,308	\$77,441	\$58,125	\$74,553	\$61,938
Expenses:						
Interest	46,524	36,504	51,358	38,970	56,060	42,804
Management fee and Other	5,323	3,399	6,638	3,599	5,320	3,732
Total Expenses	51,847	39,903	57,996	42,569	61,380	46,536
Gain (loss) on sale of securities available-for-sale	32	10	(93)	47	446	31
Dedesignation of derivative instruments	--	--	--	--	--	--
Gain (loss) on securities held-for-trading	950	(1,372)	1,365	(1,306)	(18)	897
Foreign currency gain (loss)	43	(168)	271	(176)	682	87
Loss on impairment of assets	(781)	(159)	(4,653)	(3,072)	(361)	--
Income from continuing operations	20,140	15,716	16,335	11,049	13,922	16,417
Income from discontinued operations	--	--	1,366	--	--	--
Net income	\$20,140	\$15,716	\$17,701	\$11,049	\$13,922	\$16,417
Dividends on convertible preferred stock	1,348	1,348	1,348	1,348	1,348	1,348
Net income available to common stockholders	\$18,792	\$14,368	\$16,353	\$ 9,701	\$12,574	\$15,069
Net income per share, basic:	\$ 0.33	\$ 0.27	\$ 0.29	\$ 0.18	\$ 0.22	\$ 0.28

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	=====	=====	=====	=====	=====	=====
Net income per share, diluted:	\$ 0.33	\$ 0.27	\$ 0.29	\$ 0.18	\$ 0.22	\$ 0.28
	=====	=====	=====	=====	=====	=====

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### ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

#### ITEM 9A. CONTROLS AND PROCEDURES

The Company, under the direction and with the participation of its management, including the Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective at December 31, 2006.

No change in internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) occurred during the quarter ended December 31, 2006 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm thereon are set forth in Part II, Item 8 of this Annual Report on Form 10-K.

#### ITEM 9B. OTHER INFORMATION

None.

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## PART III

### ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE OF THE REGISTRANT

Information regarding directors of the Company, including its audit committee and audit committee financial experts, and its executive officers and compliance with Section 16(a) of the Exchange Act will be in the Company's Proxy Statement and is incorporated herein by reference.

The Company has adopted Codes of Business Conduct and Ethics that govern both the Company's senior officers, including the Company's chief executive officer and chief financial officer, and employees. Copies of the Company's Codes of Business Conduct and Ethics are available on the Company's website at [www.anthracitecapital.com](http://www.anthracitecapital.com) and may also be obtained upon request without charge by writing to the Secretary of the Company, Anthracite Capital, Inc., 40 East 52nd Street, New York, NY 10022. The Company will post to its website any

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amendments to the Codes of Business Conduct and Ethics, and any waivers that are required to be disclosed by the rules of either the SEC or the NYSE.

Copies of the Company's Corporate Governance Guidelines and the charters of the Company's Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee are available on the Company's website and may also be obtained upon request without charge as described in the preceding paragraph.

### ITEM 11. EXECUTIVE COMPENSATION

The information set forth under the captions "Executive Officers" and "Compensation of Directors" in the Proxy Statement is incorporated herein by reference.

### ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information set forth under the captions "Security Ownership of Certain Beneficial Owners and Management" and "Executive Officers" and other information relating to security ownership of certain beneficial owners of the Company's Common Stock and of the Company's management in the Proxy Statement are incorporated herein by reference.

### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information set forth under the caption "Certain Relationships and Related Transactions" and the information regarding director independence under the caption "Corporate Governance" in the Proxy Statement are incorporated herein by reference.

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### ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information set forth under the caption "Independent Registered Public Accounting Firm" and other information regarding principal accountant fees and services in the Proxy Statement are incorporated herein by reference.

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## PART IV

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) List of documents filed as part of this report:

- (1) Consolidated Financial Statements and Report of Independent Registered Public Accounting Firm

See the Index to Financial Statements at Item 8 of this report.

- (2) Financial Statement Schedules



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All financial statement schedules have been omitted because either the required information is not applicable or the information is shown in the financial statements or notes thereto.

### (3) List of Exhibits

EXHIBIT NO. -----	DESCRIPTION -----
3.1	Articles of Amendment and Restatement of the Company (incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 1999, filed on March 29, 2000)
3.2	Bylaws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form S-11 (File No. 333-40813) filed on March 18, 1998)
3.3	Articles Supplementary of the Company establishing 9.375% Series C Cumulative Redeemable Preferred Stock (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K, filed on May 30, 2003)
3.4	Articles Supplementary of the Company establishing 8.25% Series D Cumulative Redeemable Preferred Stock (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form 8-A, filed on February 12, 2007)
4.1	Junior Subordinated Indenture, dated as of September 26, 2005, between the Company and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005, filed on March 16, 2006)
4.2	Junior Subordinated Indenture, dated as of January 31, 2006, between the Company and JPMorgan Chase Bank, National Association, as trustee (incorporated by reference to Exhibit 4.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005, filed on March 16, 2006)
4.3	Junior Subordinated Indenture, dated as of March 16, 2006, between the Company and Wilmington Trust Company, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006, filed on May 10, 2006)
4.4	Amended and Restated Trust Agreement, dated as of September 26, 2005, among the Company, as depositor, Wells Fargo Bank, National Association, as property trustee, Wells Fargo Delaware Trust Company, as Delaware trustee, and three administrative trustees, each of whom is an officer of the Company (incorporated by reference to Exhibit 4.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005, filed on March 16, 2006)

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- 4.5 Amended and Restated Trust Agreement, dated as of January 31, 2006, among the Company, as depositor, JPMorgan Chase Bank, National Association, as property trustee, Chase Bank USA, National Association, as Delaware trustee, and three administrative trustees, each of whom is an officer of the Company (incorporated by reference to Exhibit 4.5 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005, filed on March 16, 2006)
- 4.6 Amended and Restated Trust Agreement, dated as of March 16, 2006, among the Company, as depositor, Wilmington Trust Company, as property trustee, Wilmington Trust Company, as Delaware trustee, and the three administrative trustees, each of whom is an officer of the Company (incorporated by reference to Exhibit 4.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006, filed on May 10, 2006)
- 10.1\* Amended and Restated Investment Advisory Agreement, dated as of March 15, 2007, between the Company and BlackRock Financial Management, Inc.
- 10.2\* Amended and Restated Accounting Services Agreement, dated as of March 15, 2007, between the Company and BlackRock Financial Management, Inc.
- 10.3\* Amended and Restated Administration Agreement, dated as of March 15, 2007, between the Company and BlackRock Financial Management, Inc.
- 10.4 Form of 1998 Stock Option Incentive Plan (incorporated by reference to Exhibit 10.6 to the Company's Registration Statement on Form S-11 (File No. 333-40813) filed on March 18, 1998)
- 10.5\* Form of 2006 Stock Award and Incentive Plan
- 10.6 Multicurrency Revolving Facility Agreement, dated as of February 14, 2006, among AHR Capital MS Limited, as borrower, Morgan Stanley Mortgage Servicing Inc., as security trustee and Morgan Stanley Bank, as initial lender and agent (incorporated by reference to Exhibit 10.9 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005, filed on March 16, 2006)
- 10.7 Multicurrency Revolving Facility Agreement, dated as of March 17, 2006, among AHR Capital BofA Limited, as borrower, the Company, as borrower agent, and Bank of America, N.A., as lender (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006, filed on May 10, 2006)
- 10.8a Parent Guaranty, dated as of March 17, 2006, executed by the Company, as guarantor, in favor of Bank of America, N.A., as lender (incorporated by reference to Exhibit 10.1a to the Company's Current Report on Form 8-K, filed on March 1, 2007)
- 10.8b Amendment No. 1, dated as of February 23, 2007, to Parent Guaranty, dated as of March 17, 2006 (incorporated by reference to Exhibit 10.1b to the Company's Current Report on Form 8-K, filed

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on March 1, 2007)

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- 10.9 Master Repurchase Agreement, dated as of December 23, 2004, between Anthracite Funding, LLC, as seller, and Deutsche Bank AG, Cayman Islands Branch, as buyer
- 10.10a Guaranty, dated as of December 23, 2004, executed by the Company, as guarantor
- 10.10b Amendment, dated as of February 27, 2007, to Guaranty, dated as of December 23, 2004 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, filed on March 1, 2007)
- 10.11 Annex I to Master Repurchase Agreement, dated as of July 8, 2002, between Anthracite Funding LLC and Deutsche Bank AG, Cayman Islands
- 10.12 Letter agreement, dated as of July 1, 2006 to Master Repurchase Agreement, dated as of July 8, 2002 between the Company, as seller, and Greenwich Capital Financial Products, Inc., as buyer (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006, filed on August 9, 2006)
- 12.1\* Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends
- 21.1\* List of subsidiaries of the Company as of December 31, 2006
- 23.1\* Consent of Deloitte & Touche LLP, Independent Registered Public Accounting Firm
- 24.1\* Powers of Attorney (included on signature page hereto)
- 31.1\* Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
- 31.2\* Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
- 32.1\* Certification of Chief Executive Officer and Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

\* Filed herewith.

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### SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on

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its behalf by the undersigned, thereunto duly authorized.

ANTHRACITE CAPITAL, INC.

Date: March 16, 2007

By: /s/ Christopher A. Milner

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

KNOW ALL MEN BY THESE PRESENTS, that each individual whose signature appears below constitutes and appoints Richard M. Shea his true and lawful attorney-in-fact and agent with full power of substitution and re-substitution, for his name, place and stead, in any and all capacities, to sign any and all amendments (including post-effective amendments) to this Form 10-K and to file the same with all exhibits thereto, and all documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof. This power of attorney may be executed in counterparts.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date: March 16, 2007

By: /s/ Christopher A. Milner

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Christopher A. Milner  
Chief Executive Officer  
(Principal Executive Officer)

Date: March 16, 2007

By: /s/ James J. Lillis

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James J. Lillis  
Chief Financial Officer  
(Principal Financial Officer and  
Principal Accounting Officer)

Date: March 16, 2007

By: /s/ Ralph L. Schlosstein

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Ralph L. Schlosstein  
Chairman of the Board of Directors

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Date: March 16, 2007

By: /s/ Scott M. Amero

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Scott M. Amero  
Director

Date: March 16, 2007

By: /s/ Hugh R. Frater

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Hugh R. Frater  
Director

Date: March 16, 2007

By: /s/ Donald G. Drapkin

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Donald G. Drapkin  
Director

Date: March 16, 2007

By: /s/ Carl F. Geuther

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Carl F. Geuther  
Director

Date: March 16, 2007

By: /s/ Jeffrey C. Keil

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Jeffrey C. Keil  
Director

Date: March 16, 2007

By: /s/ Leon T. Kendall

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Leon T. Kendall  
Director

Date: March 16, 2007

By: /s/ Deborah J. Lucas

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Deborah J. Lucas  
Director