ANTHRACITE CAPITAL INC
Form 10-Q
November 10, 2008

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

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

For the quarterly period ended September 30, 2008

OR

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

For the transition period from: ________ to ________

Commission File Number 001-13937

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

Maryland (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 offices)	10022 (Zip Code)

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer”, “accelerated filer”, and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ Accelerated filer ¨ Non-accelerated filer ¨

Smaller reporting company ¨

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

Yes ¨ No x

At November 10, 2008, 76,898,810 shares of common stock ($0.001 par value per share) were outstanding.

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Cautionary Statement Regarding Forward-Looking Statements

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

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

(1) the introduction, withdrawal, success and timing of business initiatives and strategies;
(2) changes in political, economic or industry conditions, the interest rate environment or financial and capital markets, which could result in changes in the value of the Company’s assets and liabilities;
(3) the amount and timing of any future margin calls and their impact on the Company's financial condition and liquidity;
(4) the Company's ability to meet its liquidity requirements to continue to fund its business operations, including its ability to renew the existing facilities or obtain replacement financing, to meet margin calls and amortization payments under the facilities;
(5) the relative and absolute investment performance and operations of BlackRock Financial Management, Inc. (“BlackRock”), the Company’s Manager;
(6) the impact of increased competition;
(7) the impact of future acquisitions or divestitures;
(8) the unfavorable resolution of legal proceedings;
(9) the impact of legislative and regulatory actions and reforms and regulatory, supervisory or enforcement actions of government agencies relating to the Company or BlackRock;
(10) terrorist activities and international hostilities, which may adversely affect the general economy, domestic and global financial and capital markets, specific industries, and the Company;
(11) the ability of BlackRock to attract and retain highly talented professionals;
(12) fluctuations in foreign currency exchange rates; and
(13) the impact of changes to tax legislation and, generally, the tax position of the Company.

The Company’s Annual Report on Form 10-K for the year ended December 31, 2007 and the Company’s subsequent reports filed with the SEC, accessible on the SEC's website at www.sec.gov, identify additional factors that can affect forward-looking statements.

Part I – FINANCIAL INFORMATION
Item 1. Financial Statements

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

	September 30, 2008		December 31, 2007	
ASSETS				
Cash and cash equivalents		$ 45,810		$ 91,547
Restricted cash equivalents		16,019		32,105
Securities held-for-trading, at estimated fair value:				
Subordinated commercial mortgage-backed securities (“CMBS”)	$ 607,864		$ 1,380	
Investment grade CMBS	1,005,630		15,923	
Residential mortgage-backed securities (“RMBS”)	840		901	
Total securities held-for-trading		1,614,334		18,204
Securities available-for-sale, at estimated fair value:				
Subordinated CMBS	-		1,026,773	
Investment grade CMBS	-		1,230,075	
RMBS	-		9,282	
Total securities available-for-sale		-		2,266,130
Commercial mortgage loans (net of loan loss reserve of $43,752 in 2008)		897,955		983,387
Commercial mortgage loan pools, at amortized cost		1,223,630		1,240,793
Equity investments		136,545		108,748
Derivative instruments, at estimated fair value		495,032		404,910
Other assets (includes $1,389 at estimated fair value in 2008)		64,948		101,886
Total Assets		$ 4,494,273		$ 5,247,710
LIABILITIES AND STOCKHOLDERS' EQUITY				
Liabilities:				
Borrowings:				
Secured by pledge of subordinated CMBS	$ 189,299		$ 293,287	
Secured by pledge of investment grade CMBS	121,448		207,829	
Secured by pledge of commercial mortgage loans	201,348		244,476	
Secured by pledge of equity investments	30,000		-	
Collateralized debt obligations ("CDOs") (at estimated fair value in 2008)	1,040,435		1,823,328	
Senior unsecured notes (at estimated fair value in 2008)	47,305		162,500	
Senior unsecured convertible notes (at estimated fair value in 2008)	58,744		80,000	
	16,641		73,103	

Junior unsecured notes (at estimated fair value in 2008)				
Junior subordinated notes to subsidiary trusts issuing preferred securities (at estimated fair value in 2008)	37,056		180,477	
Secured by pledge of commercial mortgage loan pools	1,205,628		1,225,223	
Total borrowings		2,947,904		4,290,223
Payable for investments purchased		-		4,693
Distributions payable		26,784		21,064
Derivative instruments, at estimated fair value		523,898		442,114
Other liabilities		34,015		38,245
Total Liabilities		3,532,601		4,796,339
Commitments and Contingencies				
12% Series E-1 Cumulative Convertible Redeemable Preferred Stock, liquidation preference $23,375		23,275		-
12% Series E-2 Cumulative Convertible Redeemable Preferred Stock, liquidation preference $23,375		23,275		-
Stockholders' Equity:				
Preferred stock, 100,000,000 shares authorized; 9.375% Series C Preferred Stock, liquidation preference $57,500		55,435		55,435
8.25% Series D Preferred Stock, liquidation preference $86,250		83,259		83,259
Common Stock, par value $0.001 per share; 400,000,000 shares authorized; 76,660,206 shares issued and outstanding in 2008; 63,263,998 shares issued and outstanding in 2007		77		63
Additional paid-in capital		782,930		691,071
Retained earnings (distributions in excess of earnings)		24,073		(122,738)
Accumulated other comprehensive loss ("OCI")		(30,652)		(255,719)
Total Stockholders' Equity		915,122		451,371
Total Liabilities, Mezzanine and Stockholders' Equity		$ 4,494,273		$ 5,247,710

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

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

	For the Three Months Ended September 30, 2008	For the Three Months Ended September 30, 2007	For the Nine Months Ended September 30, 2008	For the Nine Months Ended September 30, 2007
Income:				
Interest from securities	$ 53,387	$ 49,560	$ 156,261	$ 147,195
Interest from commercial mortgage loans	22,674	20,494	69,506	49,942
Interest from commercial mortgage loan pools	12,779	12,985	38,445	39,119
Earnings from equity investments	3,067	6,611	2,510	28,982
Interest from cash and cash equivalents	558	1,784	2,540	3,648
Total income	92,465	91,434	269,262	268,886
Expenses:				
Interest	56,652	62,525	164,189	178,450
Management and incentive fees	3,432	3,970	22,591	18,652
General and administrative expense	2,025	1,624	5,706	4,448
Total expenses	62,109	68,119	192,486	201,550
Other gains (losses):				
Realized loss on securities and swaps held-for-trading, net	(5,005)	(4,435)	(14,840)	(4,063)
Unrealized loss on securities held-for-trading	(247,348)	-	(572,675)	-
Unrealized loss on swaps classified as held-for-trading	(5,859)	-	(811)	-
Unrealized gain on liabilities	261,723	-	667,980	-
Gain (loss) on sale of securities available-for-sale, net	-	(1,331)	-	5,576
Dedesignation of derivative instruments	(7,084)	-	(7,084)	-
Provision for loan losses	(18,752)	-	(43,942)	-
Foreign currency gain (loss)	7,273	775	(2,913)	3,631
Loss on impairment of assets	-	(2,938)	-	(7,036)
Total other gains (losses)	(15,052)	(7,929)	25,715	(1,892)
Net income	15,304	15,386	102,491	65,444
Dividends on preferred stock	4,529	3,127	12,738	8,530
Net income available to common stockholders	$ 10,775	$ 12,259	$ 89,753	$ 56,914
Net income per common share, basic:	$ 0.14	$ 0.19	$ 1.30	$ 0.94

Net income per common share, diluted:	$	0.14	$	0.19	$	1.23	$	0.94
Weighted average number of shares outstanding:								
Basic		74,365,259		63,861,985		69,099,689		60,450,020
Diluted		74,748,560		64,178,519		81,724,651		60,662,477
Dividend declared per share of common stock	$	0.31	$	0.30	$	0.92	$	0.89

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

Anthracite Capital, Inc. and Subsidiaries
Consolidated Statement of Changes in Stockholders' Equity (Unaudited)
For the Nine Months Ended September 30, 2008
(in thousands)

	Common Stock, Par Value	Series C Preferred Stock	Series D Preferred Stock	Additional Paid-In Capital	Retained Earnings (Distributions in Excess of Earnings)	Accumulated Other Comprehensive Loss	Comprehensive Income	Total Stockholders' Equity
Balance at January 1, 2008	$ 63	$ 55,435	$ 83,259	$ 691,071	$ (122,738)	$ (255,719)		$ 451,371
Cumulative effect of adjustment from adoption of SFAS No. 159					122,988	227,635		350,623
Net income					102,491		$ 102,491	102,491
Unrealized loss on cash flow hedges						(6,219)	(6,219)	(6,219)
Reclassification adjustments from cash flow hedges included in net income						4,577	4,577	4,577
Dedesigation of cash flow hedges						7,084	7,084	7,084
Foreign currency translation						(8,010)	(8,010)	(8,010)
Other comprehensive income							(2,568)	
Comprehensive income							99,923	
Dividends declared-common stock					(65,930)			(65,930)
Dividends on preferred stock					(12,738)			(12,738)
Issuance of common stock	14			91,859				91,873
Balance at September 30, 2008	$ 77	$ 55,435	$ 83,259	$ 782,930	$ 24,073	$ (30,652)		$ 915,122

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

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

	For the Nine Months Ended September 30, 2008	For the Nine Months Ended September 30, 2007
Cash flows from operating activities:		
Net income	102,491	$ 65,444
Adjustments to reconcile net income to net cash provided by operating activities:		
Net decrease in trading securities	118	6,709
Sale of trading securities	-	166,932
Purchase of securities held-for-trading	(53,515)	(42,668)
Unrealized loss on securities held-for-trading	572,675	-
Unrealized loss on swaps classified as held-for-trading	811	-
Realized loss (gain) on securities and swaps held-for-trading, net	3,236	(1,513)
Unrealized gain on liabilities	(667,980)	-
Earnings from subsidiary trust	(317)	(316)
Distributions from subsidiary trust	316	316
Earnings from equity investments	(2,510)	(28,982)
Distributions of earnings from equity investments	3,599	11,948
Provision for loan loss	43,942	-
Discount accretion, net	(14,362)	(9,010)
Amortization of finance costs	2,505	4,351
Loss on impairment of assets	-	7,036
Unrealized net foreign currency loss (gain)	28,528	(41,796)
Non-cash management and incentive fees	11,934	3,838
(Disbursements) proceeds from termination of interest rate swap agreements	(17,101)	17,737
Amortization of terminated interest rate swaps from OCI	4,577	928
Dedesignation of cash flow hedges	7,084	-
Increase in other assets	(8,910)	(11,074)
(Decrease) increase in other liabilities	(6,287)	6,903
Net cash provided by operating activities	10,834	156,783
Cash flows from investing activities:		
Purchase of securities	-	(505,119)
Proceeds from sale of securities	74,272	591,360
Principal payments received on securities	56,968	58,857
Funding of commercial mortgage loans	(2,286)	(687,316)
Repayments received from commercial mortgage loans	19,341	275,127
Repayments received from commercial mortgage loan pools	7,639	14,835
Decrease in restricted cash equivalents	16,086	29,254
Return of capital from equity investments	-	25,000
Investment in equity investments	(35,538)	(38,555)
Net cash provided by (used in) investing activities	136,482	(236,557)
Cash flows from financing activities:		
(Decrease) increase in borrowings under reverse repurchase agreements and credit facilities:		
Secured by pledge of subordinated CMBS	(102,998)	230,100
Secured by pledge of investment grade CMBS	(85,617)	(480,927)

Secured by pledge of commercial mortgage loans		(39,556)		234,471
Secured by pledge of equity investments		30,000		-
Secured by pledge of securities held-for-trading		-		(127,249)
Repayments of borrowings secured by commercial mortgage loan pools		(9,157)		(16,065)
Repayments of collateralized debt obligations		(44,885)		(50,018)
Issuance of collateralized debt obligations		-		23,875
Issuance costs for collateralized debt obligations		-		(1,537)
Issuance of senior convertible debt		-		80,000
Issuance costs of senior convertible debt		-		(2,419)
Issuance of senior unsecured notes		-		87,500
Issuance costs of senior unsecured notes		-		(2,456)
Issuance of junior unsecured notes		-		68,557
Issuance costs of junior unsecured notes		-		(2,113)
Dividends paid on preferred stock		(11,805)		(7,344)
Proceeds from issuance of preferred stock, net of offering costs		69,839		83,267
Proceeds from issuance of common stock, net of offering costs		59,327		66,624
Repurchase of common stock		-		(12,000)
Dividends paid on common stock		(61,141)		(52,943)
Net cash (used in) provided by financing activities		(195,993)		119,323
Effect of exchange rate changes on cash and cash equivalents		2,940		16,248
Net (decrease) increase in cash and cash equivalents		(45,737)		55,797
Cash and cash equivalents, beginning of period		91,547		66,388
Cash and cash equivalents, end of period	$	45,810	$	122,185

	For the Nine Months Ended September 30, 2008		For the Nine Months Ended September 30, 2007	
Supplemental disclosure of cash flow information:				
Cash paid for interest	$	167,624	$	168,889
Series E-3 preferred stock conversion	$	23,289	$	-
Incentive fees paid by the issuance of common stock	$	9,257	$	5,250

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

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

Note 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Anthracite Capital, Inc., a Maryland corporation (collectively with its subsidiaries, the "Company"), was incorporated in Maryland in November 1997, commenced operations on March 24, 1998 and is organized as a real estate investment trust ("REIT"). 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 yield 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 and equity.

The Company’s primary investment activities are conducted on a global basis in four investment sectors:
1) Commercial Real Estate Debt Securities
2) Commercial Real Estate Loans
3) Commercial Real Estate Equity
4) RMBS

The accompanying September 30, 2008 unaudited consolidated financial statements have been prepared in conformity with the instructions to Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (“GAAP”) for complete financial statements. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and changes in cash flows have been made. These consolidated financial statements should be read in conjunction with the annual audited financial statements and notes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2007 filed with the Securities and Exchange Commission (the “SEC”).

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

Recent Accounting Developments

Fair Value Measurements

In September 2006, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("FAS 157"). FAS 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. FAS 157 requires companies to disclose the fair value of their financial instruments according to a fair value hierarchy (i.e., Levels 1, 2 and 3, as defined). Additionally, companies are required to provide enhanced disclosure regarding instruments in the Level 3 category (which have inputs to the valuation techniques that are unobservable and require significant management judgment), including a reconciliation of the beginning and ending balances separately for each major category of assets and liabilities. FAS 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 adopted FAS 157 as of January 1, 2008. FAS 157 did not materially affect how the Company determines fair value, but resulted in certain additional disclosures.

In October 2008, the FASB issued FASB Staff Position ("FSP") FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active* ("FSP 157-3"), which became effective upon issuance, including periods for which financial statements have not been issued. FSP FAS 157-3 clarifies the application of FAS 157, which the Company adopted as of January 1, 2008, in a market that is not active and provides an example to illustrate key considerations in the determination of the fair value of a financial asset when the market for that asset is not active. The key considerations illustrated in the FSP FAS 157-3 example include the use of an entity's own assumptions about future cash flows and appropriately risk-adjusted discount rates, appropriate risk adjustments for nonperformance and liquidity risks, and the reliance that an entity should place on quotes that do not reflect the result of market transactions. The adoption by the Company of FSP FAS 157-3 did not have a material impact on its financial statements or its determination of fair values as of September 30, 2008.

Fair Value Accounting

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ("FAS 159"). FAS 159 permits entities to elect to measure eligible financial instruments at fair value. The unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. The decision to elect the fair value option is determined on an instrument-by-instrument basis, is applied to an entire instrument and is irrevocable. Assets and liabilities measured at fair value pursuant to the fair value option will be reported separately on the consolidated statement of financial condition from those instruments measured using another measurement attribute. FAS 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. The Company adopted FAS 159 as of January 1, 2008 and elected to apply the fair value option to the following financial assets and liabilities existing at the time of adoption:

(1) all securities which were previously accounted for as available-for-sale;
(2) investments in equity of subsidiary trusts;
(3) all unsecured long-term liabilities, consisting of all senior unsecured notes, senior unsecured convertible notes, junior unsecured notes and junior subordinated notes to subsidiary trust issuing preferred securities; and

(4) all CDO liabilities.

Upon adoption, with an adjustment to opening retained earnings, total stockholders' equity increased by $350,623, substantially all of which relates to applying the fair value option to the Company's long-term liabilities. The Company recorded all unamortized debt issuance costs relating to debt for which the Company elected the fair value option on January 1, 2008 as an adjustment to opening retained earnings. Subsequent to January 1, 2008, all changes in the estimated fair value of the Company's securities, CDO liabilities, senior unsecured notes, senior unsecured convertible notes, junior unsecured notes and junior subordinated notes are recorded in earnings.

Disclosures about Derivative Instruments and Hedging Activities

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* (“FAS 161”). This statement amends and expands the disclosure requirements of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* (“FAS 133”). This statement requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. FAS 161 will be effective for the Company on January 1, 2009. Management is currently evaluating the effects that FAS 161 will have on the disclosures included in the Company’s consolidated financial statements.

Reverse Repurchase Agreements

In February 2008, the FASB issued FSP FAS 140-3, *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions* ("FSP 140-3"). FSP 140-3 addresses the accounting for the transfer of financial assets and a subsequent repurchase financing and shall be effective for financial statements issued for fiscal years beginning after November 15, 2008 and interim periods within those years. FSP 140-3 focuses on the circumstances that would permit a transferor and a transferee to separately evaluate the accounting for a transfer of a financial asset and a repurchase financing under SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities* (“FAS 140”).

FSP 140-3 states that a transfer of a financial asset and a repurchase agreement involving the transferred financial asset should be considered part of the same arrangement when the counterparties to the two transactions are the same unless certain criteria are met. The criteria in FSP 140-3 are intended to identify whether (1) there is a valid and distinct business or economic purpose for entering separately into the two transactions and (2) the repurchase financing does not result in the initial transferor regaining control over the previously transferred financial assets. The FASB has stated that FSP 140-3’s purpose is to limit diversity of practice in accounting for these situations, resulting in more consistent financial reporting. FSP 140-3 shall be applied prospectively to initial transfers and repurchase financings for which the initial transfer is executed on or after the beginning of the fiscal year in which FSP 140-3 is initially applied.

Currently, the Company records such assets and the related financing gross on its consolidated statement of financial condition, and the corresponding interest income and interest expense gross on its consolidated statement of operations. However, in a transaction in which securities are acquired from and financed under a repurchase agreement with the same counterparty, the acquisition may not qualify as a sale for the seller or a purchase for the Company under the provisions of FAS 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. The Company has not completed its evaluation of the impact of FSP 140-3, but the Company may be precluded from presenting the assets gross on the Company's consolidated statement of financial condition and may be instead required to treat the Company's net investment in such assets as a derivative. If it is determined that these transactions should be treated as derivatives, the derivative instruments entered into by the Company to hedge the Company's interest rate exposure with respect to the borrowings under the associated repurchase agreements may no longer qualify for hedge accounting, and would then, as with the underlying asset transactions, also be marked to market through the consolidated statement of operations. This potential change in accounting treatment does not affect the economics of the transactions but does affect how the transactions would be reported on the Company's consolidated financial statements. The Company's cash flows and liquidity would be unchanged, and the Company does not believe its REIT taxable income or REIT status would be affected. The Company believes stockholders' equity would not be materially affected.

Investment Companies

In June 2007, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position ("SOP") 07-1, *Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies*. This SOP provides guidance for determining whether an entity is within the scope of the AICPA Audit and Accounting Guide Investment Companies (the "Guide"). Entities that are within the scope of the Guide are required, among other things, to carry their investments at fair value, with changes in fair value included in earnings. On February 14, 2008, the FASB decided to indefinitely defer the effective date of this SOP.

Variable Interest Entities

The consolidated financial statements include the financial statements of the Company and its subsidiaries, which are wholly owned or controlled by the Company or entities which are variable interest entities (“VIE”) in which the Company is the primary beneficiary under FASB Interpretation No. 46 (revised), *Consolidation of Variable Interest Entities* (“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 intercompany balances and transactions have been eliminated in consolidation.

The Company considers the CMBS where it maintains the right to control the foreclosure/workout process on the underlying loans as controlling class CMBS ("Controlling Class"). The Company has analyzed the governing pooling and servicing agreements for each of its Controlling Class CMBS and believes that the terms are industry standard and are consistent with the qualifying special-purpose entity ("QSPE") criteria. As a result, the Company does not consolidate these entities.

In April 2008, the FASB voted to eliminate QSPEs from the guidance in FAS 140 and to remove the scope exception for QSPEs from FIN 46R. This will require that VIEs previously accounted for as QSPEs to be analyzed for consolidation according to FIN 46R. The FASB also proposed that an entity review VIEs at each reporting period to reconsider whether an entity is a VIE and to determine the primary beneficiary. While the revised standards have not been finalized and the Board's proposals are subject to a public comment period, this change may affect the Company's consolidated financial statements as the Company may be required to consolidate entities that had previously been determined to qualify as QSPEs. The FASB proposed that the amendments to FAS 140 and FIN 46R be effective for new and existing transactions for fiscal years and interim periods beginning after November 15, 2009. The Company will continue to evaluate the impact of these changes on its consolidated financial statements once these changes to current GAAP become finalized.

Convertible Debt Instruments

In May 2008, FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* ("FSP APB 14-1") was issued. FSP APB 14-1 applies to convertible debt instruments that, by their stated terms, may be settled in cash (or other assets) upon conversion, including partial cash settlement of the conversion option. FSP APB 14-1 requires bifurcation of the instrument into a debt component that is initially recorded at fair value and an equity component. The difference between the fair value of the debt component and the initial proceeds from issuance of the instrument is recorded as a component of equity. The liability component of the debt instrument is accreted to par using the effective yield method; accretion is reported as a component of interest expense. The equity component is not subsequently re-valued as long as it continues to qualify for equity treatment under EITF Issue No. 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock*. FSP APB 14-1 is effective for financial statements issued for fiscal years and interim periods beginning after December 15, 2008. Early adoption is not permitted. The FSP is to be applied retrospectively to all past periods presented — even if the instrument has matured, converted, or otherwise been extinguished as of the FSP's effective date. The Company is currently evaluating the impact of adopting FSP APB 14-1 on the consolidated financial statements.

Note 2 NET INCOME PER SHARE

Net income per share is computed in accordance with SFAS No. 128, *Earnings Per Share*. Basic income per share is calculated by dividing net income available to common stockholders by the weighted average number of shares of common stock outstanding during the period. Diluted income per share is calculated using the weighted average number of shares of common stock outstanding during the period plus the additional dilutive effect of common stock equivalents. The dilutive effect of outstanding stock options is calculated using the treasury stock method, and the dilutive effect of senior unsecured convertible notes and cumulative convertible redeemable preferred stock is calculated using the "if converted" method.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
Numerator:				
Numerator for basic earnings per share	$ 10,775	$ 12,259	$ 89,753	$ 56,914
Interest expense on convertible senior notes	-	-	7,066	-
Dividends on Series E convertible preferred stock	-	-	3,343	-
Numerator for diluted earnings per share	$ 10,775	$ 12,259	$ 100,162	$ 56,914
Denominator:				
Denominator for basic earnings per share—weighted average common shares outstanding	74,365,259	63,861,985	69,099,689	60,450,020
Dilutive effect of stock options	-	1,048	-	2,133
Assumed conversion of convertible senior notes	-	-	7,416,680	-
Assumed conversion of Series E convertible preferred stock	-	-	4,952,748	-
Dilutive effect of stock based incentive fee	383,301	315,486	255,534	210,324
Denominator for diluted earnings per share—weighted average common shares outstanding and common stock equivalents outstanding	74,748,560	64,178,519	81,724,651	60,662,477
Basic net income per weighted average common share:	$ 0.14	$ 0.19	$ 1.30	$ 0.94
Diluted net income per weighted average common share and common share equivalents:	$ 0.14	$ 0.19	$ 1.23	$ 0.94

Total anti-dilutive stock options excluded from the calculation of diluted net income per share were 10,000 for the three and nine months ended September 30, 2008. Total anti-dilutive stock options excluded from the calculation of diluted net income per share were 1,362,151 for the three and nine months ended September 30, 2007.

Total anti-dilutive shares related to convertible senior notes and Series E convertible preferred stock excluded from the calculation of diluted net income per share were 7,416,680 and 6,239,323, respectively, for the three months ended September 30, 2008.

Note 3 FAIR VALUE DISCLOSURES

The Company adopted FAS 157 as of January 1, 2008, which requires, among other things, enhanced disclosures about financial instruments that are measured and reported at fair value. Financial instruments include the Company’s securities classified as held-for-trading, long-term liabilities as well as derivatives accounted for at fair value.

The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of pricing observability. Pricing observability is impacted by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established and the characteristics specific to the transaction. Financial instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of pricing observability and a lesser degree of judgment utilized in measuring fair value. Conversely, financial instruments rarely traded or not quoted will generally have less, or no, pricing observability and a higher degree of judgment utilized in measuring fair value.

FAS 157 establishes a hierarchal disclosure framework associated with the level of pricing observability utilized in measuring financial instruments at fair value. Instruments are categorized based on the lowest level input that is significant to the valuation. The three levels defined by the FAS 157 hierarchy are as follows:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities at the reporting date. Level 1 assets include highly liquid cash instruments with quoted prices such as agency securities, listed equities and money market securities, as well as listed derivative instruments.

Level 2 – Pricing inputs other than quoted prices included within Level 1 that are observable for substantially the full term of the asset or liability, either directly or indirectly. Level 2 assets include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities that are not active; and inputs other than quoted prices that are observable, such as models or other valuation methodologies. Instruments which are generally included in this category are corporate bonds and loans, mortgage whole loans, municipal bonds and OTC derivatives. The Company has determined that the following instruments are Level 2: interest rate swaps, foreign currency swaps and foreign currency forward contracts.

Level 3 – Instruments that have little to no pricing observability as of the reported date. These financial instruments do not have two-way markets and are measured using management’s best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation. Instruments in this category generally include assets and liabilities for which there is little, if any, current market activity. The Company’s investments in this category include investment grade CMBS, subordinated CMBS and all of the Company’s long-term liabilities. The fair values of certain assets are determined by references to index pricing. However, for certain assets, index prices for identical or similar assets are not available. In these cases and for CDO liabilities, management uses broker quotes as being indicative of fair values, but management ultimately determines the fair values recorded in the financial statements. Broker quotes are only indicative of fair value, and do not necessarily represent what the Company would receive in an actual trade for the applicable instrument. The Company has classified these assets and liabilities as Level 3 as of September 30, 2008 due to the lack of current market activity. The Company believes that it may be appropriate to transfer these assets and liabilities to Level 2 in subsequent periods if market activity returns to normalized levels and observable inputs become available.

The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the investment.

The following table summarizes the valuation of our financial instruments by the above FAS 157 pricing observability levels as of September 30, 2008. Assets and liabilities measured at fair value on a recurring basis are categorized below based upon the lowest level of significant input to the valuations.

	Assets at Fair Value as of September 30, 2008			
	Level 1	Level 2	Level 3	Total
Subordinated CMBS	$ -	$ -	$ 607,864	$ 607,864
Investment grade CMBS	-	-	1,005,630	1,005,630
RMBS	-	-	840	840
Derivative instruments	-	495,032	-	495,032
Investments in equity of subsidiary trusts*	-	-	1,389	1,389
Total	$ -	$ 495,032	$ 1,615,723	$ 2,110,755

* Included as a component of other assets on the consolidated statements of financial condition.

	Liabilities at Fair Value as of September 30, 2008			
	Level 1	Level 2	Level 3	Total
Senior unsecured notes	$ -	$ -	$ 47,305	$ 47,305
Senior unsecured convertible notes	-	-	58,744	58,744
Junior unsecured notes	-	-	16,641	16,641
Junior subordinated notes	-	-	37,056	37,056
CDOs	-	-	1,040,435	1,040,435
Derivative instruments	-	523,898	-	523,898
Total	$ -	$ 523,898	$ 1,200,181	$ 1,724,079

The following table presents the changes in Level 3 assets for the three months ended September 30, 2008:

	Subordinated CMBS	Investment grade CMBS	RMBS	Junior subordinated notes
Balance at July 1, 2008	$ 797,327	$ 1,104,751	$ 973	$ 2,210
Net purchases (sales)	(572)	(483)	(138)	-
Net transfers in (out)	-	-	-	-
Gains (losses) included in earnings	(177,242)	(93,790)	5	(821)
Losses included in OCI [1]	(11,649)	(4,848)	-	-
Balance at September 30, 2008	$ 607,864	$ 1,005,630	$ 840	$ 1,389
Amount of total gains (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2008 [2]	$ (161,636)	$ (88,145)	$ (51)	$ (821)
Amount of total gains (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2008 [3]	$ (15,561)	$ (8,063)	$ -	$ -

[1] The Company has a foreign subsidiary that has the Euro as its functional currency. Gains (losses) in OCI represent the currency translation adjustments for this subsidiary.

[2] Recorded in “unrealized loss on securities-held-for trading” in the consolidated statement of operations.

[3] Recorded in “foreign currency gain (loss)” in the consolidated statement of operations.

The following table presents the changes in Level 3 assets for the nine months ended September 30, 2008:

	Subordinated CMBS	Investment grade CMBS	RMBS	Junior subordinated notes
Balance at January 1, 2008	$ 1,028,153	$ 1,245,998	$ 10,183	$ 3,135
Net purchases (sales)	382	(68,804)	(9,420)	-
Net transfers in (out)	-	-	-	-
Gains (losses) included in earnings	(416,750)	(170,043)	77	(1,746)
Losses included in OCI [1]	(3,921)	(1,521)	-	-
Balance at September 30, 2008	$ 607,864	$ 1,005,630	$ 840	$ 1,389
Amount of total gains (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2008 [2]	$ (407,017)	$ (167,694)	$ 21	$ (1,746)
Amount of total gains for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2008 [3]	$ (9,689)	$ (4,767)	$ -	$ -

(1) The Company has a foreign subsidiary that has the Euro as its functional currency. Gains (losses) in OCI represent the currency translation adjustments for this subsidiary.
(2) Recorded in "unrealized loss on securities-held-for trading" in the consolidated statement of operations.
(3) Recorded in "foreign currency gain (loss)" in the consolidated statement of operations.

The following table presents the changes in Level 3 liabilities for the three months ended September 30, 2008:

	CDOs	Senior unsecured notes	Senior unsecured convertible notes	Junior unsecured notes	Junior subordinated notes
Balance at July 1, 2008	$ 1,252,224	$ 85,204	$ 71,160	$ 35,611	$ 72,829
Paydowns	(1,282)	-	-	-	-
Net transfers in (out)	-	-	-	-	-
Gains included in earnings	(165,475)	(37,899)	(12,416)	(18,970)	(35,773)
Gains included in OCI (1)	(45,032)	-	-	-	-
Balance at September 30, 2008	$ 1,040,435	$ 47,305	$ 58,744	$ 16,641	$ 37,056
Amount of total losses for the period included in earnings attributable to the change in unrealized gains relating to liabilities still held at September 30, 2008 (2)	$ (165,717)	$ (37,899)	$ (12,416)	$ (10,725)	$ (35,773)
Amount of total gains (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to liabilities still held at September 30, 2008 (3)	$ -	$ -	$ -	$ (8,245)	$ -

(1) The Company has a foreign subsidiary that has the Euro as its functional currency. Gains (losses) in OCI represent the currency translation adjustments for this subsidiary.
(2) Recorded in "unrealized gain on liabilities" in the consolidated statement of operations.
(3) Recorded in "foreign currency gain (loss)" in the consolidated statement of operations.

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The following table presents the changes in Level 3 liabilities for the nine months ended September 30, 2008:

	CDOs	Senior unsecured notes	Senior unsecured convertible notes	Junior unsecured notes	Junior subordinated notes
Balance at January 1, 2008	$ 1,598,502	$ 114,473	$ 70,186	$ 44,833	$ 103,312
Paydowns	(44,885)	-	-	-	-
Net transfers in (out)	-	-	-	-	-
Gains included in earnings	(498,057)	(67,168)	(11,442)	(28,192)	(66,256)
Gains included in OCI [1]	(15,125)	-	-	-	-
Balance at September 30, 2008	$ 1,040,435	$ 47,305	$ 58,744	$ 16,641	$ 37,056
Amount of total losses for the period included in earnings attributable to the change in unrealized gains or losses relating to liabilities still held at September 30, 2008 [2]	(498,299)	(67,168)	(11,442)	(25,322)	(66,256)
Amount of total gains (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to liabilities still held at September 30, 2008 [3]	$ -	$ -	$ -	$ (2,870)	$ -

[1] The Company has a foreign subsidiary that has the Euro as its functional currency. Gains (losses) in OCI represent the currency translation adjustments for this subsidiary.

[2] Recorded in “unrealized gain on liabilities” in the consolidated statement of operations.

[3] Recorded in “foreign currency gain (loss)” in the consolidated statement of operations.

Assets measured at fair value on a nonrecurring basis

Certain assets are measured at fair value on a nonrecurring basis, meaning that the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances (for example, when there is evidence of impairment). The following table presents the asset carried on the consolidated statement of financial condition by caption and by level within the FAS 157 valuation hierarchy as of September 30, 2008, for which a nonrecurring change in fair value has been recorded during the nine months ended September 30, 2008:

	Level 1	Level 2	Level 3	Carrying Value
Commercial mortgage loans(1)	$ -	$ -	$ -	$ 45,997
Total assets at fair value on a nonrecurring basis	-	-	-	45,997

(1) The Company recorded a provision for loan loss in the amount of $43,942 for the nine months ended September 30, 2008. This provision relates to three loans with a principal balance of $90,580 and accrued interest of $190.

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Fair Value Option

On January 1, 2008, the Company adopted FAS 159 which provides an option to elect fair value as an alternative measurement for selected financial assets or liabilities not previously recorded at fair value. The fair value option was elected for these assets and liabilities to align the measurement attributes of both the assets and liabilities while mitigating volatility in earnings from using different measurement attributes.

The following table presents information about the eligible instruments for which the Company elected the fair value option and for which a transition adjustment was recorded as of January 1, 2008:

	Carrying Value at January 1, 2008	Transition Adjustment to Retained Earnings (Distributions in Excess of Earnings)	Carrying Value at January 1, 2008 (After Adoption of FAS 159)
Securities held-for-trading (1)	$ 2,284,334	$ (227,635)	$ 2,284,334
Liability issuance costs	35,137	(35,137)	-
Senior unsecured notes	(162,500)	48,027	(114,473)
Senior unsecured convertible notes	(80,000)	9,814	(70,186)
Junior unsecured notes	(73,103)	28,269	(44,834)
Investments in equity of subsidiary trusts	5,477	(2,342)	3,135
Junior subordinated notes	(180,477)	77,165	(103,312)
CDOs	(1,823,328)	224,827	(1,598,501)
Cumulative effect of the adoption of the fair value option		$ 122,988	

(1) Prior to January 1, 2008, the majority of the Company’s securities were classified as available-for-sale and carried at fair value. Accordingly, the election of the fair value option for these securities did not change their carrying value and resulted in a reclassification from OCI to opening distributions in excess of earnings.

Valuation

Provided below is a summary of the valuation techniques employed with respect to financial instruments measured at fair value utilizing methodologies other than quoted prices in active markets:

Investments in mortgage backed securities and derivative instruments - The fair value of these assets is determined by reference to index pricing and market prices provided by certain dealers who make a market in these financial instruments, although such markets may not be active. Broker quotes are only indicative of fair value, and do not necessarily represent what the Company would receive in an actual trade for the applicable instrument. The Company performs additional analysis on prices received based on broker quotes. This process includes analyzing the securities based on vintage year, rating and asset type and converting the price received to a spread. The calculated spread is then compared to market information available for securities of similar type, vintage year and rating. The Company utilizes this process to validate the prices received from brokers and adjustments are made as deemed necessary by management to capture current market information.

Collateralized debt obligations - The fair value of these liabilities are based on market prices provided by certain dealers who make a market in this sector, although such markets may be inactive. The dealers use models that considered, among other things, (i) anticipated cash flows, (ii) current market credit spreads, (iii) known and anticipated credit issues of underlying collateral, (iv) term and reinvestment period and (v) market transactions of similar bonds. The Company performs additional analysis on prices received from the brokers. This process includes analyzing the securities based on vintage year, rating and asset type and converting the price received to a spread. The calculated spread is then compared to market information available for securities of similar type, vintage year and rating. The Company utilizes this process to validate the prices received from brokers and adjustments are made as deemed necessary by management to capture current market information.

Senior unsecured convertible notes - The Company used the mid-point of a bid/ask price obtained from a dealer in this market. The bid/ask price represented the price the counterparty was willing to transact at on the measurement date of September 30, 2008 understanding that it is an over-the-counter market that requires direct communication with the counterparty to execute the transaction. The counterparty utilizes a model to publish such price and consideration into such model include, among other things (i) anticipated cash flows, (ii) current market credit spreads and (iii) market transactions of similar bonds.

Senior and junior unsecured notes and junior subordinated notes - The estimated fair values of these liabilities were developed based on the price obtained by the Company for the senior unsecured convertible notes. The senior unsecured convertible notes are senior to the unsecured and junior subordinated notes. The Company priced the senior unsecured convertible notes without the conversion option to obtain a straight bond price, converted that price to a spread to swap curve and then applied an additional spread to account for the fact that these liabilities were junior to the senior unsecured convertible notes. The Company was able to compare the change in implied spreads for these bonds to published spreads for CMBS securities which was deemed to be a reasonable comparison for these liabilities.

Note 4 SECURITIES HELD-FOR TRADING

Upon adoption of FAS 159 as of January 1, 2008, the Company elected the fair value option for all of its securities that were previously classified as available-for-sale. As a result, all securities are now classified as held-for-trading. This reclassification adjustment did not result in a change to the Company’s intent as it relates to these securities. For the three and nine months ended September 30, 2008, respectively, $(247,348) and $(572,675) were recorded as unrealized loss on the securities and is included in loss on securities held-for-trading on the consolidated statements of operations. The estimated fair value of securities held-for-trading at September 30, 2008 is summarized as follows:

Security Description		Estimated Fair Value
U.S. Dollar Denominated:		
CMBS:		
Investment grade CMBS	$	638,163
Non-investment grade rated subordinated CMBS		359,360
Non-rated subordinated CMBS		70,329
CMBS interest only securities (“IOs”)		4,424
Credit tenant leases		22,203
Investment grade REIT debt		201,735
Multifamily agency securities		354
CDO investments - investment grade		2,600
CDO investments - non-investment grade		27,187
Total CMBS		1,326,355
RMBS:		
Residential CMOs		428
Hybrid adjustable rate mortgages (“ARMs”)		412
Total RMBS		840
Total U.S. dollar denominated		1,327,195
Non-U.S. Dollar Denominated:		
Investment grade CMBS		136,151
Non-investment grade rated subordinated CMBS		124,531
Non-rated subordinated CMBS		26,457
Total non-U.S. dollar denominated		287,139
Total securities held-for-trading	$	1,614,334

At September 30, 2008, an aggregate of $1,556,603 in estimated fair value of the Company's securities held-for-trading was pledged to secure its collateralized borrowings.

The CMBS held by the Company consist of subordinated securities collateralized by adjustable and fixed rate commercial and multifamily mortgage loans. The CMBS provide credit support to the more senior classes of the related commercial securitization. The Company generally does not own the senior classes of its below investment grade CMBS. Cash flows from the mortgages underlying the CMBS generally are 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 September 30, 2008, the anticipated reported yield based upon the adjusted cost of the Company's entire subordinated CMBS portfolio was 12.8% per annum. The anticipated reported yield of the Company's investment grade securities was 7.2%. The Company's anticipated yields to maturity on its subordinated CMBS and other securities are based upon a number of assumptions that are subject to certain business and economic uncertainties and contingencies. Examples of these uncertainties 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 in this report, will be achieved.

Note 5 COMMERCIAL MORTGAGE LOANS

The following table summarizes the Company's commercial real estate loan portfolio by property type at September 30, 2008 and December 31, 2007:

	Loan Outstanding				Weighted Average Yield	
	September 30, 2008		December 31, 2007			
Property Type	Amount	%	Amount	%	2008	2007
U.S.						
Retail	$ 52,533	5.9%	$ 52,209	5.3%	9.6%	9.6%
Office	45,393	5.1	45,640	4.6	10.3	10.3
Multifamily[1]	170,463	19.0	174,873	17.8	9.9	9.7
Storage	32,080	3.6	32,307	3.3	9.1	9.1
Land[2]	-	-	25,000	2.5	-	9.6
Hotel	12,387	1.4	12,208	1.2	13.0	10.9
Other Mixed Use	3,996	0.4	3,983	0.5	8.5	8.5
Total U.S.	316,852	35.4	346,220	35.2	9.9	9.7
Non-U.S.						
Retail	259,983	29.0	278,669	28.3	9.0	8.9
Office[3]	212,950	23.6	238,691	24.3	9.2	8.8
Multifamily	39,145	4.3	41,403	4.2	8.8	8.6
Storage	45,974	5.1	51,272	5.2	9.2	9.5
Industrial	15,340	1.7	17,274	1.8	10.3	10.6
Hotel	3,407	0.4	5,016	0.5	10.7	10.1
Other Mixed Use	4,304	0.5	4,842	0.5	10.3	9.0
Total Non-U.S.	581,103	64.6	637,167	64.8	9.1	8.9
Total	$ 897,955	100.00%	$ 983,387	100.00%	9.4%	9.2%

(1) Net of a loan loss reserve of $5,000 at September 30, 2008.
(2) Net of a loan loss reserve of $25,000 at September 30, 2008.
(3) Net of a loan loss reserve of $13,752 at September 30, 2008.

As of September 30, 2008, the Company's loans had the following maturity characteristics:

Year of initial maturity *	Number of loans maturing	Current carrying value	% of total
2008	1	$ 32,000	3.6%
2009	-	-	-
2010	3	24,818	2.8
2011	15	279,476	31.1
2012	17	228,218	25.4
Thereafter	23	333,443	37.1
Total	59	$ 897,955	100.0%

* Does not include potential extension options.

Activity for the nine months ended September 30, 2008 was as follows:

	Book Value
Balance at December 31, 2007	$ 983,387
Investments in commercial mortgage loans	2,286
Proceeds from repayment of mortgage loans	(19,341)
Provision for loan loss	(43,752)
Foreign currency translation	(30,239)
Discount accretion, net	5,614
Balance at September 30, 2008	$ 897,955

The Company recorded a provision for loan losses of $18,752 and $43,942 for the three and nine months ended September 30, 2008, respectively. This provision relates to three loans with an aggregate principal balance of $90,580 and accrued interest of $190. The first is a $25,000 loan secured by land in California which required a provision totaling $25,190 (includes accrued interest of $190). The second is a $20,500 mezzanine loan secured by a 1,802 unit apartment complex located in New York City which required a provision totaling $5,000. The third loan is a €32,094 ($45,080) junior mezzanine loan secured by a portfolio of office buildings in the Netherlands which required a provision totaling €9,790 ($13,752). The loans are in various stages of resolution and due to the estimated reduction in value of the underlying collateral below the principal balance of the loans, the Company believes the full collectibility of the loans is not probable.

Changes in the reserve for possible loan losses were as follows:

Provision for possible loan losses, December 31, 2007	$	-
Provision for loan losses		43,942
Reserve for possible loan losses, September 30, 2008	$	43,942

During the third quarter of 2008, one of the Company’s mezzanine loans with a carrying value of $32,000 (€22,781) defaulted. The borrower executed a standstill agreement which is being extended to allow time to conclude an extension agreement. As of September 30, 2008, the Company concluded that a loan loss reserve is not necessary because the value of the underlying collateral is greater than the principal balance of the loan. As such, the Company believes the collectibility of the loan is probable. At September 30, 2008, all other commercial real estate loans owned directly by the Company are performing according to their terms or have been appropriately reserved.

Note 6 COMMERCIAL MORTGAGE LOAN POOLS

During the second quarter of 2004, the Company acquired subordinated CMBS in a trust representing 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 assets, liabilities 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 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.

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 would result in an impairment recorded on the consolidated statement of operations. An increase in estimated cash flows will increase the amount of interest income recorded in future periods.

Note 7 IMPAIRMENTS - CMBS

The Company updates its estimated cash flows for securities subject to Emerging Issues Task Force Issue 99-20, *Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets* (“EITF 99-20”), on a quarterly basis. The Company compares the yields resulting from the updated cash flows to the current accrual yields. An impairment 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 these securities at their estimated fair value on its consolidated statements of financial condition.

For the nine months ended September 30, 2008, changes in timing of assumed credit loss and prepayments on the Company’s 2005 through 2007 vintage Controlling Class CMBS required an impairment totaling $456,620.

For the nine months ended September 30, 2007, changes in timing of assumed credit loss and prepayments on three CMBS required an impairment totaling $4,468. Also, the Company increased its underlying loss expectations for one below investment grade European CMBS during the nine months ended September 30, 2007, resulting in an additional impairment of $1,321. In addition, the Company incurred a charge of $1,247 related to the mark to market of its remaining high credit quality securities because similar securities were sold at a loss during the third quarter of 2007.

As a result of the adoption of FAS 159 on January 1, 2008, the Company will no longer be required to make an adjustment to OCI in stockholder’s equity for other-than-temporary impairment because the changes in fair value are recorded in the statement of operations. However, because the Company records interest income as a separate line item in the consolidated statements of operations, the Company does assess securities for other-than-temporary impairment in order to adjust the amount of interest income recorded on such securities.

Note 8 EQUITY INVESTMENTS

The following table is a summary of the Company’s equity investments for the nine months ended September 30, 2008:

	Carbon I	Carbon II	Dynamic India Fund IV *	AHR JV	AHR Int’l JV	Total
Balance at December 31, 2007	$ 1,636	$ 97,762	$ 9,350	$ -	$ -	$ 108,748
Contributions to investments	-	-	-	1,351	30,886	32,237
Equity earnings	75	1,372	-	(367)	1,430	2,510
Foreign currency translation	-	-	-	-	(3,351)	(3,351)
Distributions of earnings	-	(3,206)	-	-	(393)	(3,599)
Balance at September 30, 2008	$ 1,711	$ 95,928	$ 9,350	$ 984	$ 28,572	$ 136,545

* The Company neither controls nor has significant influence over the Dynamic India Fund IV and accounts for this investment using the cost method of accounting. The Company invested $3,300 in the Dynamic India Fund IV in the fourth quarter of 2007 that did not settle until the first quarter of 2008.

At September 30, 2008, the Company owned approximately 20% of Carbon Capital, Inc. ("Carbon I"). The Company also owned approximately 26% of Carbon Capital II, Inc. ("Carbon II", and collectively with Carbon I, the "Carbon Capital Funds"). The Company has pledged its interest in Carbon II as collateral under a revolving credit agreement (see Note 9 for further details). The Carbon Capital Funds are private commercial real estate income opportunity funds managed by the Manager (see Note 12 of the consolidated financial statements).

The Company entered into a $50,000 commitment on July 20, 2001 to acquire shares of Carbon I. On July 12, 2005, the investment period expired and Carbon I is in liquidation.

The Company entered into an aggregate commitment of $100,000 to acquire shares of Carbon II. The final obligation to fund capital of $13,346 was called on July 13, 2007.

On December 22, 2005, the Company entered into an $11,000 commitment to indirectly acquire shares of Dynamic India Fund IV. At September 30, 2008, the Company's capital commitment was $11,000, of which $9,350 had been drawn.

The Company is committed to invest up to $5,000, for up to a 10% interest, in Anthracite JV LLC ("AHR JV"). AHR JV invests in U.S. CMBS rated higher than BB. As of September 30, 2008, the Company had invested $1,351 in AHR JV. The other member in AHR JV is managed by or otherwise associated with an affiliate of Credit Suisse. AHR JV is managed by the Manager (see Note 12 of the consolidated financial statements).

On June 26, 2008, the Company invested $30,886 in RECP Anthracite International JV Limited ("AHR International JV"). AHR International JV invests in investments backed by non-U.S. real estate assets and is managed by the Manager (see Note 12 of the consolidated financial statements). The Company will invest on a deal-by-deal basis and has no committed capital obligation. The Company is utilizing the joint venture structure to increase its capacity to invest in larger and more diverse transactions given the current market's elevated level of risk. The other shareholder in AHR International JV is managed by or otherwise associated with an affiliate of Credit Suisse.

Note 9 BORROWINGS

Certain information with respect to the Company's borrowings at September 30, 2008 is summarized as follows:

Borrowing Type	Market Value	Adjusted Issuance Price	Weighted Average Borrowing Rate	Weighted Average Remaining Maturity	Estimated Fair Value of Assets Pledged
Credit facilities (1)	$ 546,704	$ 546,704	5.55%	1.17 years	$ 902,291
Commercial mortgage loan pools	1,201,019	1,201,019	4.00%	4.18 years	1,223,630
CDOs (2)	1,040,435	1,764,303	4.67%	5.19 years	1,896,427
Senior unsecured notes (2)	47,305	162,500	7.59%	8.82 years	Unsecured
Junior unsecured notes (2)	16,641	70,233	6.56%	13.84 years	Unsecured
Senior unsecured convertible notes (2)	58,744	80,000	11.75%	19.18 years	Unsecured
Junior subordinated notes (2)	37,056	180,477	7.64%	27.61 years	Unsecured
Total Borrowings	$ 2,947,904	$ 4,005,236	5.03%	5.78 years	

(1) Includes $ 4,610 of borrowings under facilities related to commercial mortgage loan pools.

(2) As a result of the adoption of FAS 159 on January 1, 2008, the Company records the above liabilities at fair value. Changes in fair value are recorded in unrealized gain (loss) on liabilities on the consolidated statement of operations. For the nine months ended September 30, 2008, the Company recorded an unrealized gain of $667,980 due to the reduction of the fair value of such liabilities.

At September 30, 2008, the Company's borrowings had the following remaining maturities, at amortized cost:

Borrowing Type	Within 30 days	31 to 59 days	60 days to less than 1 year	1 year to 3 years	3 years to 5 years	Over 5 years	Total
Credit facilities (1)	$ 0	$ -	$ 257,405	$ 289,299	$ -	$ -	$ 546,704
Commercial mortgage loan pools(2)	6,054	5,866	333,448	102,892	43,396	709,363	$ 1,201,019
CDOs(2)	829	319	52,075	222,710	775,967	712,403	1,764,303
Senior unsecured notes	-	-	-	-	-	162,500	$ 162,500
Junior unsecured notes	-	-	-	-	-	70,233	$ 70,233
Senior unsecured convertible notes	-	-	-	-	-	80,000	80,000
Junior subordinated notes	-	-	-	-	-	180,477	$ 180,477
Total Borrowings	$ 6,883	$ 6,185	$ 642,928	$ 614,901	$ 819,363	$ 1,914,976	$ 4,005,236

(1) Includes $4,610 of borrowings under facilities related to commercial mortgage loan pools.

(2) Commercial mortgage loan pools and CDOs are non-recourse borrowings and payments for these borrowings are supported solely by the cash flows from the assets in these structures.

Reverse Repurchase Agreements and Credit Facilities

As credit market conditions have permitted, the Company has entered into short-term reverse repurchase agreements to finance securities that are not financed under its credit facilities or CDOs. The reverse repurchase agreements bear interest at a LIBOR-based variable rate. At September 30, 2008, the Company did not have any reverse repurchase agreements outstanding. At December 31, 2007, the Company had $80,119 of reverse repurchase agreements outstanding.

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. See Note 15 to the consolidated financial statements for additional discussion of the Company’s exposure to potential margin calls.

The Company's credit facilities have been used to replace 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 September 30, 2008 and December 31, 2007:

		September 30, 2008			December 31, 2007		
	Maturity Date	Facility Amount	Total Borrowings	Unused Borrowing Capacity	Facility Amount	Total Borrowings	Unused Borrowing Capacity
Bank of America, N.A. (1) (5)	9/18/10	$ 275,000	$ 141,694	$ 133,306	$ 275,000	$ 211,088	$ 63,912
Deutsche Bank AG, Cayman Islands Branch (2)	7/08/10	92,166	92,166	-	200,000	174,186	25,814
Bank of America, N.A.(3)	9/18/10	100,000	55,439	44,561	100,000	87,706	12,294
Morgan Stanley Bank (3) (4)	2/07/09	300,000	227,405	72,595	300,000	198,621	101,379
BlackRock HoldCo 2, Inc. (1)	3/06/09	53,624	30,000	23,624	-	-	-
		$ 820,790	$ 546,704	$ 274,086	$ 875,000	$ 671,601	$ 203,399

(1) USD only.
(2) Multicurrency (USD and Non-USD).
(3) Non-USD only.
(4) Can be increased by an additional $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.
(5) Includes $4,610 of borrowings under facilities related to commercial mortgage loan pools.

As further detailed below, the Company is subject to financial covenants in its credit facilities. For the quarter ended September 30, 2008, the Company is not aware of any instances of non-compliance with these covenants.

On December 28, 2007, the Company received a waiver from its compliance with the tangible net worth covenant at December 31, 2007 from Bank of America, N.A., the lender under a $100,000 multicurrency secured credit facility. Without the waiver, the Company would have been required to maintain tangible net worth of at least $520,416 at December 31, 2007 pursuant to the covenant. On January 25, 2008, this lender agreed to amend the covenant so that the Company would be required to maintain tangible net worth at the end of each fiscal quarter of not less than the sum of (i) $400,000 plus (ii) an amount equal to 75% of any equity proceeds received by the Company on or after July 20, 2007.

On February 15, 2008, Morgan Stanley Bank extended its $300,000 non-USD facility until February 7, 2009. In connection with the extension, certain financial covenants were added or modified so that: (i) the Company is required to have a minimum debt service coverage ratio (as defined in the related guaranty) of 1.4 to 1.0 for any calendar quarter, (ii) on any date, the Company's tangible net worth shall not decline 20% or more from its tangible net worth as of the last business day in the third month preceding such date, (iii) on any date, the Company's tangible net worth shall not decline 40% or more from its tangible net worth as of the last business day in the twelfth month preceding such date, (iv) on any date, the Company's tangible net worth shall not be less than the sum of $400,000 plus 75% of any equity offering proceeds received from and after February 15, 2008, (v) at all times, the ratio of the Company's total recourse indebtedness to tangible net worth shall not be greater than 3:1, (vi) on any date the Company's liquid assets (as defined in the related guaranty) shall not at any time be less than 5% of its mark-to-market indebtedness (mark-to-market indebtedness is defined under the related guaranty generally to mean short-term liabilities that have a margin call feature and as of September 30, 2008 amounted to $546,704) and (vii) cumulative income cannot be less than one dollar for two consecutive quarters. Morgan Stanley Bank can require the Company to fund margin calls in the event the lender determines the value of the underlying assets have declined in value. The Company has commenced discussions with Morgan Stanley Bank to extend the maturity date of the facility beyond February 7, 2009.

On July 8, 2008, Deutsche Bank AG, Cayman Islands Branch, extended its multicurrency credit facility until July 8, 2010. In connection with the extension, certain financial covenants were added or modified to conform to the covenants in the Morgan Stanley Bank facility described above. In addition, the Company separately agreed with Deutsche Bank AG, Cayman Islands Branch, that to the extent the Company from time to time agrees to covenants that are more restrictive than those in the Deutsche Bank agreement, the covenants in the Deutsche Bank agreement will automatically be deemed to be modified to match the restrictions in such more restrictive covenants, subject to limited exceptions. The amended agreement also provides that the Company’s failure to procure an extension of any of its existing facilities with Bank of America, N.A. and Morgan Stanley Bank as of the 30th day before the maturity date (or the 15th day before the maturity date if the Company demonstrates to the satisfaction of Deutsche Bank that it is negotiating a bona fide commitment to extend or replace such facility) would constitute an event of default under such agreement; however, any such failure would not be deemed to constitute an event of default if the Company demonstrates to the satisfaction of Deutsche Bank that it has sufficient liquid assets, as defined under such agreement, to pay down the multicurrency repurchase agreement when due. Under the terms of the extension agreement, no additional borrowings are permitted under the facility. In addition, monthly amortization payments of approximately $1,600 are required under the facility. The monthly amortization payment can be increased or decreased based on a monthly repricing of all the assets that collaterize the credit facility.

On August 7, 2008, Bank of America, N.A. extended its USD and non-USD facilities until September 18, 2010. In connection with the extension, certain financial covenants were added or modified to conform to more restrictive covenants contained in other credit facilities. Also in connection with the extension, the Company (i) is required to make amortization payments totaling $31,000 on various dates through September 30, 2008, and (ii) is required to make monthly installment payments of $2,250 commencing October 15, 2008 until March 15, 2010 under the non-USD facility and $2,250 per month commencing April 15, 2010 and ending at maturity under the USD facility. Bank of America, N.A, can require the Company to fund margin calls in the event the lender determines the value of the underlying collateral has declined.

To satisfy a margin call of $11,582 made in October 2008 by Bank of America under its credit facilities, the Company agreed with Bank of America to increase the Company's monthly installment payments from $2,250 to $3,250 commencing November 15, 2008 through March 15, 2010 under its non-USD facility and commencing April 15, 2010 through September 18, 2010 under its USD facility.

On February 29, 2008, the Company entered into a binding loan commitment letter (the "Commitment Letter") with BlackRock HoldCo 2, Inc. ("HoldCo 2"), pursuant to the terms of which HoldCo 2 or its affiliates (together, the "Lender") committed to provide a revolving credit loan facility (the "BlackRock Facility") to the Company for general working capital purposes. HoldCo 2 is a wholly-owned subsidiary of BlackRock, Inc., the parent of BlackRock Financial Management, Inc., the Manager of the Company.

On March 7, 2008, the Company and HoldCo 2 entered into the BlackRock Facility. The BlackRock Facility has a term of 364 days with two 364-day extension periods, subject to the Lender's approval. The BlackRock Facility is collateralized by a pledge of equity shares that the Company holds in Carbon II. The maximum principal amount of the BlackRock Facility is the lesser of $60,000 or a number determined in accordance with a borrowing base calculation equal to 60% of the fair market value of the shares of Carbon II that are pledged to secure the BlackRock Facility. At September 30, 2008, based on the value of the Carbon II shares on a mark-to-market basis, the maximum principal amount of the BlackRock Facility has declined to $53,624 and the Company has remaining unused borrowing capacity of $23,624. As of October 31, 2008, unused borrowing capacity from the BlackRock Facility declined to $16,835 due to a decline in the fair market value of the shares of Carbon II that are pledged to secure the BlackRock Facility.

The BlackRock Facility bears interest at a variable rate equal to LIBOR plus 2.5%. The fee letter, dated February 29, 2008, between the Company and HoldCo 2, sets forth certain terms with respect to fees. Amounts borrowed under the BlackRock Facility may be repaid and reborrowed from time to time. The Company, however, has agreed to use commercially reasonable efforts to obtain other financing to replace the BlackRock Facility and reduce the outstanding balance.

The terms of the BlackRock Facility give the Lender the option to purchase from the Company the shares of Carbon II that serve as collateral for the BlackRock Facility, up to the BlackRock Facility commitment amount, at a price equal to the fair market value (as determined by the terms of the BlackRock Facility agreement) of those shares, unless the Company elects to prepay outstanding loans under the BlackRock Facility in an amount equal to the Lender's desired share purchase amount and reduce the BlackRock Facility's commitment amount accordingly, which may require termination of the BlackRock Facility. Upon the consummation of the purchase, the BlackRock Facility’s commitment amount shall be reduced by the share purchase amount and the share purchase amount paid shall be applied to repay any outstanding loans under the BlackRock Facility as if the Company had prepaid the loans. The balance of the share amount available after such repayment, if any, shall be paid to the Company.

On April 8, 2008, the Company repaid $52,500 to HoldCo 2, representing all then-outstanding borrowings under the BlackRock Facility. On July 28, 2008, the Company reborrowed $30,000 under the BlackRock Facility which was still outstanding at September 30, 2008.

Failure to meet a margin call or required amortization payment under any of the five aforementioned facilities would constitute an event of default under the applicable facility. An event of default would allow the lender to accelerate all facility obligations under such agreement.

Each of the five facilities contains cross default provisions that provide that any default by the Company under any loan, guaranty or similar agreement that permits acceleration of the balance due under such agreement would constitute an event of default under such facility.

Note 10 CONVERTIBLE REDEEMABLE PREFERRED STOCK

On April 4, 2008, the Company issued $70,125 of 12% Series E-1 Cumulative Convertible Redeemable Preferred Stock, 12% Series E-2 Cumulative Convertible Redeemable Preferred Stock and 12% Series E-3 Cumulative Convertible Redeemable Preferred Stock (collectively, the “Series E Preferred Stock”). Net proceeds to the Company were $69,839. Dividends are payable on the Series E Preferred Stock at a 12% coupon and the holder has the right to convert the preferred stock into common stock at $7.49 per share (a 12% premium to the closing price of the Company's common stock on March 28, 2008, the pricing date).

On or after April 4, 2012, each holder of Series E-1 Preferred Stock has the right to require, at its option, the Company to repurchase all of such holder's shares of Series E-1 Preferred Stock, in whole but not in part, for cash, at a repurchase price equal to the liquidation preference of $1,000 per share, plus all accumulated but unpaid dividends thereon.

On or after April 4, 2013, each holder of Series E-2 Preferred Stock has the right to require, at its option, the Company to repurchase all of such holder's shares of Series E-2 Preferred Stock, in whole but not in part, for cash, at a repurchase price equal to the liquidation preference of $1,000 per share, plus all accumulated but unpaid dividends thereon.

On June 20, 2008, the holder of the outstanding 12% Series E-3 Cumulative Convertible Redeemable Preferred Stock exercised its right to convert its shares into 3,119,661 shares of common stock.

The holder is a subsidiary of a fund managed by an affiliate of Credit Suisse. Whenever dividends on the Series E Preferred Stock are in arrears for six or more quarterly periods (whether or not consecutive), then the holder, together with the holders of the Company's Series C and Series D Preferred Stock which rank equally with the Series E Preferred Stock, shall be entitled to elect a total of two additional directors to the Company’s Board of Directors in addition to the one director appointed to the Board at consummation of this transaction.

Note 11 COMMON STOCK

The following table summarizes Common Stock issued by the Company for the nine months ended September 30, 2008, net of offering costs:

	Shares	Net Proceeds
Dividend Reinvestment and Stock Purchase Plan	152,332	$ 1,071
Sales agency agreement	5,226,800	35,012
Management and incentive fees*	1,065,818	7,013
Incentive fee – stock based*	316,320	2,116
Series E-3 preferred stock conversion	3,119,661	23,289
Private transaction (see details below)	3,494,021	23,244
Director compensation	21,256	128

Total	13,396,208	$ 91,873

*See Note 12 to the consolidated financial statements, Transactions with the Manager and Certain Other Parties, for a further description of the Company's Management Agreement.

In conjunction with the Company’s issuance of the Series E Preferred Stock on April 4, 2008, the Company also issued 3,494,021 shares of Common Stock, for $6.69 per share, resulting in net proceeds of $23,244.

On March 12, 2008, the Company declared dividends to its common stockholders of $0.30 per share, which were paid on April 30, 2008 to stockholders of record on March 30, 2008. For U.S. federal income tax purposes, the dividends are expected to be ordinary income to the Company’s stockholders.

On May 15, 2008, the Company declared dividends to its common stockholders of $0.31 per share, which were paid on July 31, 2008 to stockholders of record on June 30, 2008. For U.S. federal income tax purposes, the dividends are expected to be ordinary income to the Company’s stockholders.

On September 10, 2008, the Company declared dividends to its common stockholders of $0.31 per share, which were paid on October 31, 2008 to stockholders of record on September 30, 2008. For U.S. federal income tax purposes, the dividends are expected to be ordinary income to the Company’s stockholders.

Note 12 TRANSACTIONS WITH THE MANAGER AND CERTAIN OTHER PARTIES

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.

On March 31, 2008, the Company’s unaffiliated directors approved an amended investment advisory agreement with the Manager. The amended Management Agreement will expire on March 31, 2009, unless extended. For the full one-year term of the renewed contract, the Manager has agreed to receive 100% of the management fees and any incentive fees in the Company's Common Stock. The stock issued to the Manager under this plan will be restricted from sale until six months after it is received.

Other significant changes pursuant to the amended Management Agreement include a reduction in the quarterly base management fee from 0.50% of stockholders' equity to 0.375% for the first $400 million in average total stockholders' equity; 0.3125% for the next $400 million of average total stockholders' equity and 0.25% for the average total stockholders' equity in excess of $800 million. Under the terms of the prior Management Agreement, the Company paid the Manager a base management fee equal to 0.5% of the quarterly average total stockholders’ equity for the applicable quarter. The amended Management Agreement continues to provide that the Company will grant the Manager Common Stock equal to one-half of one percent (0.5%) of the total number of shares of the Company's Common Stock outstanding as of a specified date in the fourth quarter of each year.

The amended Management Agreement also provides for the Manager to receive a quarterly incentive fee equal to 25% of the amount by which the applicable quarter’s Operating Earnings (as defined in the Management Agreement) of the Company (before incentive fee) plus realized gains, net foreign currency gains and decreases in expense associated with reversals of credit impairments on commercial mortgage loans; less realized losses, net foreign currency losses and increases in expense associated with credit impairments on commercial mortgage loans exceeds the weighted average issue price per share of the Company's Common Stock ($10.76 per common share at September 30, 2008) multiplied by the ten-year Treasury note rate plus 4.0% per annum (expressed as a quarterly percentage), multiplied by the weighted average number of shares of the Company's Common Stock outstanding during the applicable quarterly period. The Management Agreement continues to provide that the incentive fee payable to the Manager shall be subject to a rolling four-quarter high watermark.

Under the terms of the prior Management Agreement, the Manager was entitled to receive an incentive fee 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. Additionally, up to 30% of the incentive fees earned in 2007 or after were 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 2007.

The following is a summary of management and incentive fees incurred for the three and nine months ended September 30, 2008 and 2007:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
Management fee	$ 3,050	$ 3,473	$ 9,286	$ 10,862
Incentive fee	-	-	11,879	5,645
Incentive fee - stock based	382	497	1,426	2,145
Total management and incentive fees	$ 3,432	$ 3,970	$ 22,591	$ 18,652

At September 30, 2008 and 2007, management and incentive fees of $11,077 and $5,434, respectively, remain payable to the Manager and are 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 $(175) and $75 for certain expenses (accrual adjustments) during the three and nine months ended September 30, 2008 and $184 and $486 for the three and nine months ended September 30, 2007, respectively.

The Company also has administration and accounting services agreements with the Manager. Under the terms of the administration services 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 three and nine months ended September 30, 2008, the Company recorded administration and investment accounting service fees of $250 and $735, respectively, which are included in general and administrative expense on the accompanying consolidated statements of operations. For the three and nine months ended September 30, 2007, the Company recorded administration and investment accounting service fees of $181 and $544, respectively, which are included in general and administrative expense on the accompanying consolidated statements of operations.

The special servicer on 33 of the Company's 39 Controlling Class trusts is Midland Loan Services, Inc. ("Midland"), a wholly owned indirect subsidiary of The PNC Financial Services Group, Inc. (“PNC Bank”). Midland therefore may be presumed to be an affiliate of the Manager. The Company's fees for Midland’s services are at market rates.

On March 7, 2008, the Company entered into a credit facility with a subsidiary of BlackRock, Inc. BlackRock, Inc. is the parent of the Company’s manager, BlackRock Financial Management, Inc. (See Note 9).

During 2001, the Company entered into a $50,000 commitment to acquire shares of Carbon I, a private commercial real estate income opportunity fund managed by the Manager. The Company’s investment in Carbon I at September 30, 2008 was $1,711. The Company does not incur any additional management or incentive fees to the Manager related to its investment in Carbon I. At September 30, 2008, the Company owned approximately 20% of the outstanding shares of Carbon I.

The Company entered into an aggregate commitment of $100,000 to acquire shares of Carbon II, a private commercial real estate income opportunity fund managed by the Manager. The Company’s investment in Carbon II at September 30, 2008 was $95,928. The Company does not incur any additional management or incentive fees to the Manager related to its investment in Carbon II. On September 30, 2008, the Company owned approximately 26% of the outstanding shares of Carbon II.

The Company is committed to invest up to $5,000, for up to a 10% interest, in Anthracite JV LLC (“AHR JV”). AHR JV invests in U.S. CMBS rated higher than BB. As of September 30, 2008, the Company had invested $1,351 in AHR JV. AHR JV is managed by the Manager. The other member in AHR JV is managed by or otherwise associated with an affiliate of Credit Suisse.

On June 26, 2008, the Company invested $30,886 in RECP Anthracite International JV Limited (“AHR International JV”). AHR International JV invests in investments backed by non-U.S. real estate assets and is managed by the Manager. The Company will invest on a deal-by-deal basis and has no committed capital obligation. The other shareholder in AHR International JV is managed by or otherwise associated with an affiliate of Credit Suisse.

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 September 30, 2008, the Installment Payment would be $2,000 payable over two years. The Company is not required to accrue for this contingent liability because it is not probable.

Note 13 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company accounts for its derivative investments under FAS 133, 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 in 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 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, credit facilities and the floating rate debt of its CDOs. On the date in which the derivative contract is entered into, the Company designates the derivative as either a cash flow hedge or a trading derivative.

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 either other assets, other liabilities or restricted cash. Should the counterparty fail to return deposits paid, the Company would be at risk for the estimated fair value of that asset. At September 30, 2008, the balance of such net deposits pledged to counterparties as collateral under these agreements totaled $20,266 and is recorded as a component of other assets on the consolidated statement of financial condition.

At September 30, 2008, the Company had interest rate swaps with notional amounts aggregating $88,493 designated as cash flow hedges of borrowings under credit facilities. Cash flow hedges with an estimated fair value of $229 were included in derivative assets in the consolidated statement of financial condition and cash flow hedges with an estimated fair value of $307 were included in derivative liabilities in the consolidated statement of financial condition. For the three months ended September 30, 2008, the net change in the estimated fair value of the interest rate swaps was a decrease of $1,780, of which $769 was deemed ineffective and is included as an increase of interest expense and $1,011 was recorded as a reduction of OCI. For the nine months ended September 30, 2008, the net change in the estimated fair value of the interest rate swaps was a decrease of $5,685, of which $534 was deemed ineffective and is included as a decrease of interest expense and $6,219 was recorded as a reduction of OCI. At September 30, 2008, the $88,493 of notional swaps designated as cash flow hedges had a weighted average remaining term of 3.2 years.

During the nine months ended September 30, 2008, the Company terminated five of its interest rate swaps with a notional amount of $168,500 that were designated as cash flow hedges of borrowings under reverse repurchase agreements and credit facilities. Prior to the dedesignation discussed below, the Company expected to reclassify the $18,253 loss in value from OCI to interest expense over approximately 7.6 years, which was the weighted average remaining term of the swaps at the time they were closed out.

During the third quarter of 2008, the Company extended two of its credit facilities. In connection with the extension of the credit facilities, there was a reduction in the balance of the Company’s 90-day repurchase agreements and the forecasted transactions related to certain balances in OCI for interest rate swaps that had been hedging 90-day repurchase agreements were no longer probable of occurring. As a result, the Company reclassified $(7,084) out of OCI which is included in dedesignation of derivative instruments on the consolidated statements of operations. This amount was previously being reclassified to interest expense over the weighted average remaining term of the swaps at the time the swaps were closed. At September 30, 2008, the Company had, in aggregate, $12,209 of net losses related to terminated swaps recorded in OCI. For the quarter ended September 30, 2008, $639 was reclassified as an increase to interest expense and $2,557 is expected to be reclassified as an increase to interest expense over the next twelve months.

In connection with the adoption of FAS 159 on January 1, 2008, the Company dedesignated CDO interest rate swaps with notional amounts aggregating $875,548 as trading derivatives. The Company will reclassify the $25,410 loss in value from OCI to interest expense over 8.3 years. For the quarter ended September 30, 2008, $1,238 was reclassified as an increase to interest expense and $5,204 will be reclassified as an increase to interest expense over the next twelve months.

At September 30, 2008, the Company had interest rate swaps with notional amounts aggregating $1,209,731 designated as trading derivatives. Trading derivatives with an estimated fair value of $497 were included in derivative assets on the consolidated statement of financial condition and trading derivatives with an estimated fair value of $30,295 were included in derivative liabilities on the consolidated statement of financial condition. For the nine months ended September 30, 2008, the change in estimated fair value for these trading derivatives was a decrease of $1,426 which is included as a component of gain (loss) on securities held-for-trading on the consolidated statement of operations. At September 30, 2008, the $1,209,731 notional of swaps designated as trading derivatives had a weighted average remaining term of 5.0 years.

At September 30, 2008, the Company had a forward LIBOR cap with a notional amount of $85,000 and an estimated fair value at September 30, 2008, of $277 which is included in derivative assets, and the change in estimated fair value related to this derivative of $18 and $82 for the three and nine months ended September 30, 2008, respectively is included as a component of gain (loss) in securities held-for-trading on the consolidated statement 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 statements of operations. These contracts are recorded at their estimated fair value at September 30, 2008 and are included in derivative instruments on the consolidated statement of financial conditions. The Company recorded foreign currency gains (losses) of $7,273 and $(2,913) for the three and nine months ended September 30, 2008 and $775 and $3,631 for the three and nine months ended September 30, 2007, respectively.

Foreign currency agreements at September 30, 2008 consisted of the following:

	Estimated Fair Value	Unamortized Cost	Weighted Average Remaining Term
Currency swaps	$ (15,474)	$ -	7.7 years
CDO currency swaps	$ 13,437	$ -	9.1 years
Forwards	$ 2,770	$ -	49 days

Consistent with SFAS No. 52, *Foreign Currency Translation* ("FAS 52"), FAS 133 allows hedging of the foreign currency risk of a net investment in a foreign operation. The Company may use foreign currency forward contracts to manage the foreign exchange risk associated with the Company's investment in its non-U.S. dollar functional currency foreign subsidiary. In accordance with FAS 52, the Company records the change in the carrying amount of this investment in the cumulative translation adjustment account within OCI. For the nine months ended September 30, 2008, the foreign currency translation loss included in accumulated OCI was $8,010. Simultaneously, the effective portion of the hedge of this exposure is also recorded in the cumulative translation adjustment account and any ineffective portion of net investment hedges is recorded in income.

Note 14 NET INTEREST INCOME

The following is a presentation of the Company's net interest income for the three and nine months ended September 30, 2008 and 2007:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
Interest Income:				
Interest from securities	$ 53,387	$ 49,560	$ 156,261	$ 147,195
Interest from commercial mortgage loans	22,674	20,494	69,506	49,942
Interest from commercial mortgage loan pools	12,779	12,985	38,445	39,119
Interest from cash and cash equivalents	558	1,784	2,540	3,648
Total interest income	89,398	84,823	266,752	239,904
Interest Expense:				
Interest – securities	56,652	62,525	164,189	178,450
Total interest expense	56,652	62,525	164,189	178,450
Net interest income	$ 32,746	$ 22,298	$ 102,563	$ 61,454

Note 15 CURRENT AND SUBSEQUENT EVENTS IN THE CREDIT MARKETS

The Company does not currently know the full extent to which the current market disruption will affect it or the markets in which it operates, and the Company is unable to predict its length or ultimate severity. The values of real estate debt securities and loans are subject to changes in credit spreads. Credit spreads measure the yield demanded on debt securities and loans by the market based on credit relative to a specific benchmark. The ongoing weaknesses in the subprime mortgage sector and in the broader mortgage market have resulted in reduced liquidity and demand for mortgage-backed securities and have caused the credit spreads to widen substantially since the beginning of 2007. Under these conditions, the values of real estate securities and loans have declined, and such decline has resulted in margin calls. The Company's credit facilities (including its repurchase agreements) allow the lender, to varying degrees, to revalue the collateral to values that the lender considers to reflect market value. If a lender determines that the value of the collateral has decreased, it may initiate a margin call requiring the Company to repay a portion of the outstanding borrowings to cover the decrease or to post additional collateral with minimal notice.

During 2007, the Company paid $82,570 related to margin calls. During the period from January 1, 2008 through November 10, 2008, the Company paid $189,352 ($84,733 since July 1, 2008) related to margin calls and amortization payments (including payments the Company made to lenders upon their determination that the value of collateral declined and fixed payments the Company made to lenders pursuant to the terms of the facilities). Of the $84,733 paid since July 1, 2008, $41,223 represented contractual payments negotiated upon the extension of two of the Company's credit facilities. The Company will fund an additional margin call of approximately $6,600 on November 11, 2008. It has also agreed to make increased monthly installment payments to one of its lenders in full satisfaction of a margin call of $11,582 originally scheduled to be paid in October 2008.

Additional margin calls as a result of the widening of credit spreads or otherwise could harm the Company’s liquidity, results of operations, financial condition and business prospects in a number of ways. In order to obtain cash to satisfy a margin call and absent other capital resources becoming available, the Company would be required to liquidate assets at a disadvantageous time, which would cause the Company to incur losses and consequently adversely affect the Company’s results of operations and financial condition. Posting additional collateral would decrease available cash limiting the Company’s ability to satisfy other obligations, including future margin calls or to make additional investments. In addition, the Company may need to hold increased levels of cash or cash equivalents in anticipation of potential margin calls which could also limit the Company’s ability to make additional investments. If the Company did not have sufficient cash available or was unable to sell sufficient assets to satisfy margin calls, the Company would be in default under its facilities which would trigger cross default provisions in each of the Company’s five credit facilities. In such an event, the Company would be required to repay outstanding indebtedness under its credit facilities immediately. (As of September 30, 2008, the Company had $546,704 of indebtedness outstanding under its credit facilities.) Absent other capital resources becoming available, the Company will not have sufficient liquid assets to repay such indebtedness and will be unable to fund its operations and continue its business.

The aforementioned market factors could adversely affect one or more of the Company's credit facilities (including repurchase agreement) counterparties which provide funding for the Company's portfolio and thereby could cause one or more of the Company's counterparties to be unwilling or unable to provide the Company with additional financing or to extend current credit facilities on the maturity date. If one or more of the Company's counterparties were unwilling or unable to extend the current credit facilities at the maturity date and the Company were unable to replace such facilities, the Company’s liquidity would be reduced, which could have a material adverse effect on the Company's financial condition and business. The Company could be forced to sell its investments at a time when prices are depressed, which could adversely affect the Company's ability to comply with REIT asset and income tests and maintain its qualification as a REIT. Moreover, the Company may not be able to sell those investments at all under current market conditions. In addition, the failure to extend certain of the Company’s credit facilities as of the 30th day before the maturity date (or the 15th day before the maturity date if the Company demonstrates to the satisfaction of Deutsche Bank AG, Cayman Islands Branch that it is negotiating a bona fide commitment to extend or replace such facility) will constitute an event of default under the Company’s credit facility with Deutsche Bank AG.

If one or more major market participants that provide financing for mortgage-backed or other fixed income securities fails or decides to withdraw from the market, it could negatively affect the marketability of all fixed income securities, including the value of the securities in the Company's portfolio, thus reducing the Company's liquidity. In addition, distribution requirements under the REIT provisions of the Code limit the Company's ability to retain earnings and thereby replenish or increase capital for its operations thereby further reducing the Company’s liquidity.

To date, the credit performance of the majority of the Company's investments remains consistent both with the Company's expectations and with the broader commercial real estate finance industry experience; nevertheless, during the first nine months of 2008, the capital markets have been marking down the value of all credit-sensitive securities regardless of performance.

In addition to the covenants under the Company’s secured facilities, certain of the Company’s seven CDOs contain compliance tests which, if violated, could trigger a diversion of cash flows from the Company to bondholders. The Company's first three CDOs contain certain interest coverage and overcollateralization tests. At September 30, 2008, all such tests are passing by a wide margin. The Company’s three CDOs designated as its high yield (“HY”) series do not have any compliance tests. The Euro-denominated CDO's ("Euro CDO") most significant test is the weighted average rating test which is affected by credit rating agency downgrades to underlying CDO collateral. The Company can actively manage the Euro CDO collateral pool to maintain compliance with those tests. At September 30, 2008, the Company is meeting all such tests.

During the first nine months of 2008, the Company raised $35,012 of capital by issuing common shares under its sales agency agreement. On April 4, 2008, in a privately negotiated transaction, the Company issued $70,125 of Series E Preferred Stock and 3,494,021 shares of Common Stock, resulting in combined net proceeds of $93,128. The Company repaid $52,500 of its loan from HoldCo 2 on April 8, 2008. On July 28, 2008, the Company subsequently reborrowed $30,000 from HoldCo 2.

In the event of a further reduction in market liquidity, the Company’s short-term (one year or less) liquidity needs will be met primarily with $45,810 of unrestricted cash and cash equivalents (of which $20,501 must be retained under the provisions of the Company’s financial debt covenants and would not be available to fund operations) held as of September 30, 2008, potential common stock issuances under the Company’s sales agency agreement, and $23,624 of unused borrowing capacity from HoldCo 2 as of September 30, 2008. As of October 31, 2008, unused borrowing capacity from the BlackRock Facility declined to $16,835 due to a decline in the fair market value of the shares of Carbon II that are pledged to secure the BlackRock Facility.

The Company believes it has sufficient sources of liquidity to fund operations for the next twelve months (November 1, 2008 to October 31, 2009). This analysis is based on a number of assumptions. The following are the most critical:

1) The Company will be successful in renewing the facility with Morgan Stanley Bank prior to January 23, 2009 and will have no amortization payments under the terms of the renewal.
2) The Company will have sufficient available cash to meet its periodic loan amortization payments to Deutsche Bank and Bank of America, N.A.
3) The Company does not receive any significant margin calls from its lenders.
4) The Company will be successful in renewing the facility with HoldCo 2 prior to March 6, 2009 and will not have any required paydowns under the terms of the renewal.

Based on current projections of cash for the next twelve months, the Company expects it will have cash resources to pay quarterly cash dividends on its common stock at the current rate for the dividend typically payable in the first quarter of 2009 and, if the Company raises additional capital, obtains additional financing and/or receives cash proceeds from the future sale of assets or asset repayments, thereafter. However, no decision has been made by the Company with respect to the declaration or payment of any future dividend, including the rate or time of declaration and payment of any such dividend. The Company may consider payment of dividends on its common stock all or partially in common stock and intends to continue to comply with REIT dividend requirements.

The Company's ability to meet its long-term (greater than twelve months) liquidity requirements is also subject to obtaining additional long-term 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.

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

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

I. General

Anthracite Capital, Inc., a Maryland corporation (collectively with its subsidiaries, the "Company"), is a specialty finance company that invests in commercial real estate assets on a global basis. The Company commenced operations on March 24, 1998 and is organized as a real estate investment trust ("REIT"). 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 and equity.

The Company's primary investment activities are conducted on a global basis in four investment sectors:

1) Commercial Real Estate Debt Securities
2) Commercial Real Estate Loans
3) Commercial Real Estate Equity
4) RMBS

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). 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 may consider investing in RMBS given their current relative value and liquidity.

The Company's common stock, par value $0.001 per share ("Common Stock"), is traded on the New York Stock Exchange ("NYSE") under the symbol "AHR". The Company's primary long-term objective is to generate sufficient earnings to support a dividend at a level which provides an attractive return to stockholders. 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 more than $1.27 trillion of assets under management at September 30, 2008. The Manager provides an operating platform that incorporates significant asset origination, risk management, and operational capabilities.

The Company's fixed income investment activity continues to be managed to maintain a positive, though controlled, exposure to both long- and short-term interest rates through its active hedging strategies. See "Item 3 - Quantitative and Qualitative Disclosures About Market Risk" for a discussion of interest rates and their effect on earnings and book value.

The following table illustrates the mix of the Company's asset types at September 30, 2008 and December 31, 2007:

	Carrying Value at			
	September 30, 2008		December 31, 2007	
	Amount	%	Amount	%
Commercial real estate securities(1)	$ 1,614,478	41.7%	$ 2,274,151	49.3%
Commercial real estate loans(2)	1,024,166	26.4	1,082,785	23.5
Commercial mortgage loan pools(3)	1,223,630	31.6	1,240,793	26.9
Commercial real estate equity(4)	9,350	0.3	9,350	0.2
Total commercial real estate assets	3,871,624	100.0	4,607,079	99.9
Residential mortgage-backed securities	840	-	10,183	0.1
Total	$ 3,872,464	100.0%	$ 4,617,262	100.0%

(1) Includes equity investment in AHR JV.

(2) Includes equity investments in the Carbon Capital funds and AHR International JV.

(3) Represents a Controlling Class CMBS that is consolidated for accounting purposes. See Note 6 of the consolidated financial statements.

(4) Represents equity investment in Dynamic India Fund IV.

During the nine months ended September 30, 2008, the Company purchased $53,515 of non-U.S. dollar denominated securities in order to continue to increase geographic diversification. Also during the first nine months of 2008, the Company sold the majority of its remaining multifamily agency securities and CMBS IOs to increase its liquidity position. In addition, the dislocation in the capital markets during 2008 caused CMBS spreads to widen significantly. This development resulted in a significant decline in the market value of the Company's CMBS portfolio during the nine months ended September 30, 2008.

Summary of Commercial Real Estate Assets by Local Currency

A summary of the Company's commercial real estate assets with estimated fair values in local currencies at September 30, 2008 is as follows:

	Commercial Real Estate Securities[2]	Commercial Real Estate Loans [1]	Commercial Real Estate Equity	Commercial Mortgage Loan Pools	Total Commercial Real Estate Assets	Total Commercial Real Estate Assets (USD)	% of Total
USD	$ 1,327,339	$ 414,490	-	$ 1,223,630	$ 2,965,459	$ 2,965,459	76.6%
GBP	£ 22,824	£ 43,975	-	-	£ 66,799	119,066	3.1%
EURO	€ 97,724	€ 358,813	-	-	€ 456,537	641,273	16.6%
Canadian Dollars	C$77,045	C$6,281	-	-	C$83,326	78,373	2.0%
Japanese Yen	¥ 3,898,669	-	-	-	¥ 3,898,669	36,723	0.9%
Swiss Francs	-	CHF 23,972	-	-	CHF 23,972	21,380	0.6%
Indian Rupees	-	-	Rs 434,308	-	Rs 434,308	9,350	0.2%
Total USD Equivalent	$ 1,614,478	$ 1,024,166	$ 9,350	$ 1,223,630	$ 3,871,624	$ 3,871,624	100.0%

(1) Includes the Company's investments in the Carbon Capital Funds of $97,639 and AHR International JV of $28,572 at September 30, 2008.

(2) Includes the Company's investment in AHR JV of $984 at September 30, 2008.

A summary of the Company's commercial real estate assets with estimated fair values in local currencies at December 31, 2007 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 (USD)	% of Total
USD	$ 1,881,328	$ 445,618	$ -	$ 1,240,793	$ 3,567,739	$ 3,567,739	77.4%
GBP	£ 35,247	£ 45,944	-	-	£81,191	161,618	3.5%
Euro	€ 131,645	€ 354,458	-	-	€486,103	710,707	15.4%
Canadian Dollars	C$89,805	C$6,249	-	-	C$96,054	97,324	2.1%
Japanese Yen	¥ 4,378,759	-	-	-	¥4,378,759	39,196	0.9%
Swiss Francs	-	CHF23,939	-	-	CHF23,939	21,145	0.5%
Indian Rupees	-	-	Rs 368,483	-	Rs 368,483	9,350	0.2%
Total USD Equivalent	$ 2,274,151	$ 1,082,785	$ 9,350	$ 1,240,793	$ 4,607,079	$ 4,607,079	100.0%

(1) Includes the Company's investments of $99,398 in the Carbon Capital Funds at December 31, 2007.

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The Company has foreign currency rate exposure related to its non-U.S. dollar denominated assets. The Company's primary foreign currency exposures are the Euro, British pound and Canadian dollar. Changes in currency rates can adversely impact the estimated fair value and earnings of the Company's non-U.S. dollar investments. The Company mitigates this impact by utilizing local currency-denominated financing on its foreign investments and foreign currency forward contracts and swaps to hedge the net exposure.

Commercial Real Estate Assets Portfolio Activity

The following table details the par value, carrying value, adjusted purchase price, and expected yield of the Company's commercial real estate securities included in as well as outside of the Company's CDOs at September 30, 2008. 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 outside CDOs	Par	Carrying Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Expected Yield
Investment grade CMBS	$ 205,776	$ 127,026	$ 61.73	$ 174,342	$ 84.72	7.54%
Investment grade REIT debt	121	116	95.51	123	101.41	5.27
CMBS rated BB+ to B	551,008	161,252	29.26	220,319	39.98	9.60
CMBS rated B- or lower	512,802	94,106	18.16	109,385	21.07	14.00
CDO Investments	329,718	27,186	8.25	17,384	5.41	66.62
CMBS Interest Only securities ("IOs")	88,686	4,425	4.99	1,873	2.11	22.45
Multifamily agency securities	347	354	102.00	516	148.66	6.75
Total commercial real estate assets outside CDOs	1,688,458	414,465	24.49	524,392	30.98	11.81
Commercial real estate loans and equity outside CDOs						
Commercial real estate loans	588,652	577,957		579,789		
Commercial mortgage loan pools	1,189,528	1,223,630	102.87	1,223,630	102.87	4.15
Commercial real estate	9,350	9,350		9,350		
Total commercial real estate loans and equity outside CDOs	1,787,530	1,810,937	102.87	1,812,769	102.87	
Commercial real estate assets included in CDOs						
Investment grade CMBS	797,569	647,288	81.16	734,888	92.14	7.58
Investment grade REIT debt	210,624	201,619	95.72	211,697	100.51	5.48
CMBS rated BB+ to B	583,464	290,222	49.72	384,578	65.91	11.18
	199,962	36,080	18.04	45,439	22.72	17.56

CMBS rated B- or lower						
CDO Investments	4,000	2,600	65.00	2,600	65.00	7.81
Credit tenant lease	22,795	22,203	97.40	23,406	102.68	5.66
Commercial real estate loans	457,745	446,210	97.48	430,885	92.12	8.97
Total commercial real estate assets included in CDOs	2,276,159	1,646,222	72.32	1,833,493	80.15	8.63%
Total commercial real estate assets	$ 5,752,147	$ 3,871,624		$ 2,947,024		

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 of the Company's CDOs at December 31, 2007:

Commercial real estate securities outside CDOs	Par	Carrying Value	Dollar Price	Adjusted Purchase Price	Dollar Price	Expected Yield
Investment grade CMBS	$ 179,638	$ 149,856	$ 83.42	$ 158,216	$ 88.07	6.56%
Investment grade REIT debt	23,121	20,034	86.65	22,995	99.45	5.49
CMBS rated BB+ to B	546,299	316,210	57.88	417,204	76.37	8.71
CMBS rated B- or lower	513,189	144,797	28.21	166,381	32.42	10.73
CDO Investments						