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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED: MARCH 31, 2000

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: 1-13759

REDWOOD TRUST, INC.
(Exact name of Registrant as specified in its Charter)

MARYLAND	68-0329422
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

591 REDWOOD HIGHWAY, SUITE 3100 MILL VALLEY, CALIFORNIA	94941
(Address of principal executive offices)	(Zip Code)

(415) 389-7373
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all documents and 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 [ ]

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of stock, as of the last practicable date.

Class B Preferred Stock ($.01 par value)	902,068 as of May 10, 2000
Common Stock ($.01 par value)	8,789,376 as of May 10, 2000

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REDWOOD TRUST, INC.
FORM 10-Q

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PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

REDWOOD TRUST, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

<TABLE>
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	March 31, 2000	December 31, 1999
	(Unaudited)	
<S>	<C>	<C>
ASSETS		
Mortgage loans		
Residential: held-for-sale	$ 13,040	$ 415,880
Residential: held-for-investment, net	1,316,508	968,709
Commercial: held-for-sale	16,865	8,437
	1,346,413	1,393,026
Mortgage securities		
Residential: trading	1,004,862	946,373
Residential: available-for-sale, net	36,994	28,006
	1,041,856	974,379
Cash and cash equivalents	12,539	19,881
Restricted cash	2,445	5,384
Interest rate agreements	1,189	2,037
Accrued interest receivable	14,920	13,244
Investment in RWT Holdings, Inc.	2,822	3,391

Loans to RWT Holdings, Inc.	1,400	6,500
Receivable from RWT Holdings, Inc.	573	472
Other assets	3,446	1,614
	-----------	-----------
Total Assets	$ 2,427,603	$ 2,419,928
	===========	===========
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Short-term debt	$ 922,405	$ 1,253,565
Long-term debt, net	1,282,756	945,270
Accrued interest payable	5,715	5,462
Accrued expenses and other liabilities	3,270	2,819
Dividends payable	3,757	2,877
	-----------	-----------
Total Liabilities	2,217,903	2,209,993
	-----------	-----------
Commitments and contingencies (See Note 13)		
STOCKHOLDERS' EQUITY		
Preferred stock, par value $0.01 per share; Class B 9.74% Cumulative Convertible 902,068 shares authorized, issued and outstanding ($28,645 aggregate liquidation preference)	26,517	26,517
Common stock, par value $0.01 per share; 49,097,932 and 49,090,482 shares authorized; 8,783,341 and 11,251,556 issued and outstanding	88	88
Additional paid-in capital	242,139	242,094
Accumulated other comprehensive income	(3,835)	(3,348)
Cumulative earnings	12,104	8,140
Cumulative distributions to stockholders	(67,313)	(63,556)
	-----------	-----------
Total Stockholders' Equity	209,700	209,935
	-----------	-----------
Total Liabilities and Stockholders' Equity	$ 2,427,603	$ 2,419,928
	===========	===========

</TABLE>

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

REDWOOD TRUST, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share data)
(Unaudited)

<TABLE>
<CAPTION>

	Three Months Ended March 31,	
	2000	1999

<S>	<C>	<C>
INTEREST INCOME		
Mortgage loans		
Residential: held-for-sale	$ 6,520	$ 4,287
Residential: held-for-investment	17,218	16,285
Commercial: held-for-sale	211	76
	------------	------------
	23,949	20,648
Mortgage securities		
Residential: trading	17,060	18,974
Residential: available-for-sale	1,615	803
	------------	------------
	18,675	19,777
U.S. Treasury securities: trading	--	533
Cash and cash equivalents	314	773
	------------	------------
Total interest income	42,938	41,731
INTEREST EXPENSE		
Short-term debt	(19,164)	(14,750)
Long-term debt	(15,359)	(18,741)
	------------	------------
Total interest expense	(34,523)	(33,491)
Net interest rate agreements expense	(408)	(333)
	------------	------------
NET INTEREST INCOME	8,007	7,907
Net unrealized and realized market value gains (losses)		
Loans and securities	(1,077)	2,990
Interest rate agreements	(147)	(821)
	------------	------------
	(1,224)	2,169
Provision for credit losses	(119)	(345)
	------------	------------
NET REVENUES	6,664	9,731
Operating expenses	(2,147)	(714)
Other income	15	8
Equity in earnings (losses) of RWT Holdings, Inc.	(568)	(2,484)
	------------	------------
Net income before preferred dividend	3,964	6,541
Less cash dividends on Class B preferred stock	(681)	(687)
	------------	------------
NET INCOME AVAILABLE TO COMMON STOCKHOLDERS	$ 3,283	$ 5,854
	============	

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EARNINGS PER SHARE:		
Basic	$ 0.37	$ 0.54
Diluted	$ 0.37	$ 0.54
Weighted average shares of common stock and common stock equivalents:		
Basic	8,785,017	10,778,159
Diluted	8,844,606	10,861,774

</TABLE>

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

REDWOOD TRUST, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands, except share data)
(Unaudited)

<TABLE>
<CAPTION>

	Class B Preferred stock		Common stock		Additional paid-in
	Shares	Amount	Shares	Amount	capital
Balance, December 31, 1999	902,068	$ 26,517	8,783,341	$ 88	$ 242,094
Comprehensive income:					
Net income before preferred dividend	--	--	--	--	--
Net unrealized loss on assets available-for-sale	--	--	--	--	--
Total comprehensive income	--	--	--	--	--
Issuance of common stock	--	--	--	--	45
Dividends declared:					
Preferred	--	--	--	--	--
Common	--	--	--	--	--
Balance, March 31, 2000	902,068	$ 26,517	8,783,341	$ 88	$ 242,139

</TABLE>

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	Accumulated other comprehensive income	Cumulative earnings	Cumulative distributions to stockholders	Total
Balance, December 31, 1999	$ (3,348)	$ 8,140	$ (63,556)	$ 209,935
Comprehensive income:				
Net income before preferred dividend	--	3,964	--	3,964
Net unrealized loss on assets available-for-sale	(487)	--	--	(487)
Total comprehensive income	--	--	--	3,477
Issuance of common stock	--	--	--	45
Dividends declared:				
Preferred	--	--	(681)	(681)
Common	--	--	(3,076)	(3,076)
Balance, March 31, 2000	$ (3,835)	$ 12,104	$ (67,313)	$ 209,700

</TABLE>

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

REDWOOD TRUST, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

<TABLE>
<CAPTION>

	Three Months Ended March 31, 2000	1999
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income before preferred dividend	$ 3,964	$ 6,541
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,131	2,521
Provision for credit losses	119	345
Equity in (earnings) losses of RWT Holdings, Inc.	568	2,484
Net unrealized and realized market value (gains) losses	1,224	(2,169)
Purchases of mortgage loans: held-for-sale	(25,734)	(6,412)
Proceeds from sales of mortgage loans: held-for-sale	405,616	42,629
Principal payments on mortgage loans: held-for-sale	14,287	35,249
Purchases of mortgage securities: trading	(165,264)	--
Proceeds from sales of mortgage securities: trading	49,372	--
Principal payments on mortgage securities: trading	56,014	168,982
Purchases of U.S. Treasury securities: trading	--	(45,844)
Proceeds from sales of U.S. Treasury securities: trading	--	58,442
Purchases of interest rate agreements	(222)	(409)
Proceeds from sales of interest rate agreements	339	--
(Increase) decrease in accrued interest receivable	(1,676)	3,070
Increase in other assets	(1,896)	(987)
Increase (decrease) in accrued interest payable	253	(5,125)
Increase (decrease) in accrued expenses and other liabilities	451	(1,411)
Net cash provided by operating activities	338,546	257,906
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of mortgage loans: held-for-investment	(384,328)	--
Principal payments on mortgage loans: held-for-investment	35,876	107,362
Purchases of mortgage securities: available-for-sale	(9,151)	--
Principal payments on mortgage securities: available-for-sale	243	58
Net decrease in restricted cash	2,939	1,366
(Loans) to RWT Holdings, Inc., net of repayments	5,100	(7,200)
(Increase) decrease in receivable from RWT Holdings, Inc.	(101)	

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Net cash provided by (used in) investing activities	(349,422)	101,889
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net repayments on short-term debt	(331,160)	(223,928)
Proceeds from issuance of long-term debt	375,844	--
Repayments on long-term debt	(38,318)	(134,136)
Net proceeds from issuance of common stock	45	1
Repurchases of common stock	--	(16,035)
Dividends paid	(2,877)	(686)
Net cash provided by (used in) financing activities	3,534	(374,784)
Net decrease in cash and cash equivalents	(7,342)	(14,989)
Cash and cash equivalents at beginning of period	19,881	55,627
Cash and cash equivalents at end of period	$ 12,539	$ 40,638
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	$ 34,270	$ 38,616

</TABLE>

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

REDWOOD TRUST, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2000
(UNAUDITED)

NOTE 1. THE COMPANY

Redwood Trust, Inc. ("Redwood Trust") was incorporated in Maryland on April 11, 1994 and commenced operations on August 19, 1994. During 1997, Redwood Trust formed Sequoia Mortgage Funding Corporation ("Sequoia"), a special-purpose finance subsidiary. Redwood Trust acquired an equity interest in RWT Holdings, Inc. ("Holdings"), a taxable affiliate of Redwood Trust, during the first quarter of 1998. For financial reporting purposes, references to the "Company" mean Redwood Trust, Sequoia, and Redwood Trust's equity interest in Holdings. Redwood Trust, together with its affiliates, is a finance company specializing in the mortgage portfolio spread lending business. The Company's primary activity is the acquisition, financing, and management of high-quality residential mortgage loans with funds raised through long-term debt issuance. The Company also acquires, finances, and manages residential mortgage securities and originates and sells commercial mortgage loans.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION
The accompanying interim consolidated financial statements are unaudited. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the quarter ended March 31, 2000 are not necessarily indicative of the results that may be expected for the year ending December 31, 2000. The accompanying consolidated financial statements should be read in conjunction

with the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 1999.

The consolidated financial statements include the accounts of Redwood Trust and Sequoia. Substantially all of the assets of Sequoia are pledged or subordinated to support long-term debt in the form of collateralized mortgage bonds ("Long-Term Debt") and are not available for the satisfaction of general claims of the Company. The Company's exposure to loss on the assets pledged as collateral for Long-Term Debt is limited to its net equity investment in Sequoia, as the Long-Term Debt is non-recourse to the Company. All significant inter-company balances and transactions with Sequoia have been eliminated in the consolidation of the Company. Certain amounts for prior periods have been reclassified to conform to the 2000 presentation.

During March 1998, the Company acquired an equity interest in Holdings, which originates and sells commercial mortgage loans. The Company owns all of the preferred stock and has a non-voting, 99% economic interest in Holdings. As the Company does not own the voting common stock of Holdings or control Holdings, its investment in Holdings is accounted for under the equity method. Under this method, original equity investments in Holdings are recorded at cost and adjusted by the Company's share of earnings or losses and decreased by dividends received.

USE OF ESTIMATES

The preparation of financial statements in conformity with Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of certain revenues and expenses during the reported period. Actual results could differ from those estimates. The primary estimates inherent in the accompanying consolidated financial statements are discussed below.

Fair Value. Management estimates the fair value of its financial instruments using available market information and other appropriate valuation methodologies. The fair value of a financial instrument, as defined by Statement

of Financial Accounting Standards ("SFAS") No. 107, Disclosures about Fair Value of Financial Instruments, is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced liquidation sale. Management's estimates are inherently subjective in nature and involve matters of uncertainty and judgement to interpret relevant market and other data. Accordingly, amounts realized in actual sales may differ from the fair valueS presented in Notes 3, 7 and 10.

Reserve for Credit Losses. A reserve for credit losses is maintained at a level deemed appropriate by management to provide for known losses, as well as potential losses inherent in its mortgage loan portfolio. The reserve is based upon management's assessment of various factors affecting its mortgage loans, including current and projected economic conditions, delinquency status, and credit protection. In determining the reserve for credit losses, the Company's credit exposure is considered based on its credit risk position in the mortgage pool. These estimates are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known. The reserve is increased by provisions, which are charged to income from operations. When a loan or portions of a loan are determined to be uncollectible, the portion deemed uncollectible is charged against the reserve and subsequent recoveries, if any, are credited to the reserve. The Company's actual credit losses may differ from those estimates used to establish the reserve. Summary information regarding the Reserve for Credit Losses is presented in Note 4.

MORTGAGE ASSETS

The Company's mortgage assets consist of mortgage loans and mortgage securities ("Mortgage Assets"). Interest is recognized as revenue when earned according to the terms of the loans and securities and when, in the opinion of management, it is collectible. Discounts and premiums relating to Mortgage Assets are amortized into interest income over the lives of the Mortgage Assets using methods that approximate the effective yield method. Gains or losses on the sale of Mortgage Assets are based on the specific identification method.

Mortgage Loans: Held-for-Sale

The Company classifies certain short-funded mortgage loans as held-for-sale. These mortgage loans are carried at the lower of original cost or market value ("LOCOM"). Realized and unrealized gains and losses on these loans are recognized in "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

Some of the mortgage loans purchased by the Company for which securitization or sale is contemplated are committed for sale by the Company to Holdings, or a subsidiary of Holdings, under a Master Forward Commitment Agreement. As the forward commitment is entered into on the same date that the Company commits to purchase the loans, the price which Holdings will pay to purchase the loans under the forward commitment is the same as the price that the Company paid for the mortgage loans, as established by the external market. Fair value is therefore equal to the commitment price, which is the carrying value of the mortgage loans. Accordingly, no gain or loss is recognized on the subsequent sales of these mortgage loans to Holdings or subsidiaries of Holdings.

Mortgage Loans: Held-for-Investment
All of the assets of Sequoia that are pledged or subordinated to support the Long-Term Debt are classified as held-for investment. Mortgage loans classified as held-for-investment are carried at their unpaid principal balance adjusted for net unamortized premiums or discounts, and net of the related allowance for credit losses.

Mortgage Securities: Trading
The Company classifies all of its mortgage securities with a rating of AA or higher as trading. Mortgage securities classified as trading are accounted for in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. Accordingly, such securities are recorded at their estimated fair market value. Unrealized and realized gains and losses on these securities are recognized as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

Mortgage Securities: Available-for-Sale
The Company classifies all mortgage securities rated A or lower as available-for-sale. All mortgage securities classified as available-for-sale are carried at their estimated fair value. Current period unrealized gains and losses are excluded from net income and reported as a component of Other Comprehensive Income in Stockholders' Equity with cumulative unrealized gains and losses classified as Accumulated Other Comprehensive Income in Stockholders' Equity.

Unrealized losses on mortgage securities classified as available-for-sale that are considered other-than-temporary, are recognized in income and the carrying value of the mortgage security is adjusted. Other-than-temporary unrealized losses are based on management's assessment of various factors affecting the expected cash flow from the mortgage securities, including an other-than-temporary deterioration of the credit quality of the underlying mortgages and/or the credit protection available to the related mortgage pool and a significant change in the prepayment characteristics of the underlying collateral.

U.S. TREASURY SECURITIES
U.S. Treasury securities include notes issued by the U.S. Government. Interest is recognized as revenue when earned according to the terms of the Treasury securities. Discounts and premiums are amortized into interest income over the life of the security using the effective yield method. U.S. Treasury securities are classified as trading and, accordingly, are recorded at their estimated fair market value with unrealized gains and losses recognized as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

CASH AND CASH EQUIVALENTS
Cash and cash equivalents include cash on hand and highly liquid investments with original maturities of three months or less.

RESTRICTED CASH
Restricted cash of the Company includes principal and interest payments on mortgage loans held as collateral for the Company's Long-Term Debt, and cash pledged as collateral on certain interest rate agreements.

INTEREST RATE AGREEMENTS
The Company maintains an overall interest-rate risk-management strategy that incorporates the use of derivative interest rate agreements to minimize significant unplanned fluctuations in earnings that are caused by interest-rate volatility. Interest rate agreements that are used as part of the Company's interest-rate risk management strategy include interest rate options, swaps, options on swaps, futures contracts, options on futures contracts, forward sales of fixed-rate Agency mortgage securities ("MBS"), and options on forward purchases or sales of MBS' (collectively "Interest Rate Agreements"). On the date an Interest Rate Agreement is entered into, the Company designates the Interest Rate Agreement as (1) a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment ("fair value" hedge), (2) a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge), or (3) held for trading ("trading" instruments). Since the adoption of SFAS No. 133, the Company has elected to designate all of its Interest Rate Agreements as trading instruments. Accordingly, such instruments are recorded at their estimated fair market value with changes in their fair value reported in current-period earnings in "Net unrealized and realized market value gains

(losses)" on the Consolidated Statements of Operations.

Net premiums on interest rate options are amortized as a component of net interest income over the effective period of the interest rate option using the effective interest method. The income and/or expense related to interest rate options and swaps are recognized on an accrual basis.

DEBT

Short-Term and Long-Term Debt are carried at their unpaid principal balances, net of any unamortized discount or premium and any unamortized deferred bond issuance costs. The amortization of any discount or premium is recognized as an adjustment to interest expense using the effective interest method based on the maturity schedule of the related borrowings. Bond issuance costs incurred in connection with the issuance of Long-Term Debt are

deferred and amortized over the estimated lives of the Long-Term Debt using the interest method adjusted for the effects of prepayments.

INCOME TAXES

The Company has elected to be taxed as a Real Estate Investment Trust ("REIT") under the Internal Revenue Code (the "Code") and the corresponding provisions of State law. In order to qualify as a REIT, the Company must annually distribute at least 95% of its taxable income to stockholders and meet certain other requirements. If these requirements are met, the Company generally will not be subject to Federal or state income taxation at the corporate level with respect to the taxable income it distributes to its stockholders. Because the Company believes it meets the REIT requirements and also intends to distribute all of its taxable income, no provision has been made for income taxes in the accompanying consolidated financial statements.

Under the Code, a dividend declared by a REIT in October, November or December of a calendar year and payable to shareholders of record as of a specified date in such month, will be deemed to have been paid by the Company and received by the shareholders on the last day of that calendar year, provided the dividend is actually paid before February 1st of the following calendar year, and provided that the REIT has any remaining undistributed taxable income on the record date. Therefore, the dividends declared in December 1999 which were paid in January 2000 are considered taxable income to shareholders in 1999, the year declared.

NET INCOME (LOSS) PER SHARE

Net income per share for the three months ended March 31, 2000 and 1999 is shown in accordance with SFAS No. 128, Earnings Per Share. Basic net income per share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing the net income available to common stockholders by the weighted average number of common shares and common equivalent shares outstanding during the period. The common equivalent shares are calculated using the treasury stock method, which assumes that all dilutive common stock equivalents are exercised and the funds generated by the exercise are used to buy back outstanding common stock at the average market price during the reporting period.

The following tables provide reconciliations of the numerators and denominators of the basic and diluted net income per share computations.

(IN THOUSANDS, EXCEPT SHARE DATA)

<TABLE>
<CAPTION>

	THREE MONTHS ENDED MARCH 31, 2000	THREE MONTHS ENDED MARCH 31, 1999
<S>	<C>	<C>
NUMERATOR:		
Numerator for basic and diluted earnings per share--		
Net income before preferred dividend	$ 3,964	$ 6,541
Cash dividends on Class B preferred stock	(681)	(687)
Basic and Diluted EPS - Net income available to common stockholders	$ 3,283	$ 5,854
DENOMINATOR:		
Denominator for basic earnings per share--		
Weighted average number of common shares outstanding during the period	8,785,017	10,778,159
Net effect of dilutive stock options	59,589	83,615
Denominator for diluted earnings per share--	8,844,606	10,861,774

	============	============
Net income per share - basic	$ 0.37	$ 0.54
	============	============
Net income per share - diluted	$ 0.37	$ 0.54
	============	============

</TABLE>

COMPREHENSIVE INCOME
SFAS No. 130, Reporting Comprehensive Income, requires the Company to classify items of "other comprehensive income" by their nature in a financial statement and display the accumulated balance of other

comprehensive income separately from retained earnings and additional paid-in capital in the equity section of the balance sheet. In accordance with SFAS No. 130, current period unrealized gains and losses on assets available-for-sale are reported as a component of Comprehensive Income on the Consolidated Statements of Stockholders' Equity with cumulative unrealized gains and losses classified as Accumulated Other Comprehensive Income in Stockholders' Equity. At March 31, 2000 and December 31, 1999, the only component of Accumulated Other Comprehensive Income was net unrealized gains and losses on assets available-for-sale.

RECENT ACCOUNTING PRONOUNCEMENT
During March 2000, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 44, Accounting for Certain Transactions involving Stock Compensation - an interpretation of APB Opinion No. 25 ("FIN 44"). FIN 44 clarifies the application of APB Opinion No. 25 by expanding upon a number of issues not specifically addressed in the Opinion such as the definition of an employee for purposes of applying APB Opinion No. 25 and the accounting for modifications to a previously fixed stock option award. FIN 44 is effective July 1, 2000. The impact on the Company of adopting FIN 44 has not yet been determined.

NOTE 3. MORTGAGE ASSETS

At March 31, 2000 and December 31, 1999, investments in Mortgage Assets consisted of interests in adjustable-rate, hybrid, or fixed-rate mortgage loans on residential and commercial properties. The hybrid mortgages have an initial fixed coupon rate for three to ten years followed by annual adjustments. Agency mortgage securities ("Agency Securities") represent securitized interests in pools of adjustable-rate mortgages from the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association. The Agency Securities are guaranteed as to principal and interest by these United States government-sponsored entities. The original maturity of the majority of the Mortgage Assets is thirty years; the actual maturity is subject to change based on the prepayments of the underlying mortgage loans.

At March 31, 2000 and December 31, 1999, the annualized effective yield after taking into account the amortization expense due to prepayments on the Mortgage Assets was 7.29% and 7.00%, respectively, based on the reported cost of the assets. At March 31, 2000, 82% of the Mortgage Assets owned by the Company were adjustable-rate mortgages, 16% were hybrid mortgages, and 2% were fixed-rate mortgages. At December 31, 1999, 81% of the Mortgage Assets owned by the Company were adjustable-rate mortgages, 17% were hybrid mortgages, and 2% were fixed-rate mortgages. At March 31, 2000 and December 31, 1999, the coupons on 62% and 61% of the adjustable-rate Mortgage Assets were limited by periodic caps (generally interest rate adjustments are limited to no more than 1% every six months or 2% every year), respectively. The majority of the coupons on the adjustable-rate and hybrid Mortgage Assets owned by the Company are limited by lifetime caps. At March 31, 2000 and December 31, 1999, the weighted average lifetime cap on the adjustable-rate Mortgage Assets was 11.65% and 11.64%, respectively.

At March 31, 2000 and December 31, 1999, Mortgage Assets consisted of the following:

MORTGAGE LOANS: RESIDENTIAL

<TABLE>
<CAPTION>

	MARCH 31, 2000			DECEMBER 31, 1999		
(IN THOUSANDS)	HELD-FOR-SALE	HELD-FOR-INVESTMENT	TOTAL	HELD-FOR-SALE	HELD-FOR-INVESTMENT	TOTAL
	-----------	-----------	-----------	-----------	-----------	-----------
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Current Face	$ 13,340	$ 1,305,963	$ 1,319,303	$ 412,456	$ 960,928	$

						1,373,384
Unamortized Discount	(325)	--	(325)	(305)	--	(305)
Unamortized Premium	25	15,789	15,814	3,729	12,906	16,635
Amortized Cost	13,040	1,321,752	1,334,792	415,880	973,834	1,389,714
Reserve for Credit Losses	--	(5,244)	(5,244)	--	(5,125)	(5,125)
Carrying Value	$ 13,040	$ 1,316,508	$ 1,329,548	$ 415,880	$ 968,709	$ 1,384,589

</TABLE>

The Company recognized losses of $0.1 million during both the quarters ended March 31, 2000 and 1999, as a result of LOCOM adjustments on residential mortgage loans held-for-sale. The LOCOM adjustments are reflected as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations. During the three months ended March 31, 2000, the Company sold to Holdings $380.5 million participation agreement on residential mortgage loans for proceeds of $380.5 million (see Note 12). Additionally, during the three months ended March 31, 2000, the Company sold residential mortgage loans to Redwood Residential Funding ("RRF"), a subsidiary of Holdings, for proceeds of $16.7 million. Pursuant to the terms of the Master Forward Commitment Agreement, the mortgage loans are sold to RRF at the same price for which the Company acquires the commercial mortgage loans (see Note 12). Accordingly, there were no LOCOM adjustments or gains on sales related to the RRF sales transactions. During the three months ended March 31, 1999, the Company sold residential mortgage loans held-for-sale for proceeds of $34.3 million.

There were no sales of residential mortgage loans held-for-investment during the three months ended March 31, 2000 and 1999.

MORTGAGE LOANS: COMMERCIAL

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 2000 HELD-FOR-SALE	DECEMBER 31, 1999 HELD-FOR-SALE
Current Face	$ 16,899	$ 8,450
Unamortized Discount	(34)	(13)
Carrying Value	$ 16,865	$ 8,437

</TABLE>

During the three months ended March 31, 2000 and 1999, the Company sold commercial mortgage loans to Redwood Commercial Funding ("RCF"), a subsidiary of Holdings, for proceeds of $8.4 million and 8.3 million, respectively. To date, pursuant to the Master Forward Commitment Agreement, all commercial mortgage loans purchased by the Company are sold to RCF at the same price for which the Company acquires or originates the commercial mortgage loans (see Note 12). Accordingly, there are no LOCOM adjustments or gains on sales related to commercial mortgage loans.

MORTGAGE SECURITIES: RESIDENTIAL

<TABLE>
<CAPTION>

	MARCH 31, 2000			DECEMBER 31, 1999		
(IN THOUSANDS)	TRADING	AVAILABLE-FOR-SALE	TOTAL	TRADING	AVAILABLE-FOR-SALE	TOTAL
Current Face	$ 995,442	$ 60,878	$ 1,056,320	$ 938,943	$ 48,627	$ 987,570
Unamortized Discount	(2,789)	(19,363)	(22,152)	(3,548)	(16,444)	(19,992)
Unamortized Premium	12,209	--	12,209	10,978	--	10,978

Amortized Cost	1,004,862	41,515	1,046,377	946,373	32,183	978,556
Reserve for Credit Losses	--	(686)	(686)	--	(829)	(829)
Gross Unrealized Gains	--	352	352	--	166	166
Gross Unrealized Losses	--	(4,187)	(4,187)	--	(3,514)	(3,514)
Carrying Value	$ 1,004,862	$ 36,994	$ 1,041,856	$ 946,373	$ 28,006	$ 974,379
Agency	$ 671,395	--	$ 671,395	$ 580,958	--	$ 580,958
Non-Agency	333,467	$ 36,994	370,461	365,415	$ 28,006	393,421
Carrying Value	$ 1,004,862	$ 36,994	$ 1,041,856	$ 946,373	$ 28,006	$ 974,379

</TABLE>

For the three months ended March 31, 2000 and 1999, the Company recognized a market value loss of $0.9 million and a market value gain of $4.9 million on mortgage securities classified as trading, respectively. The market value adjustments are reflected as a component of "Net unrealized and realized market value gains

(losses)" on the Consolidated Statements of Operations. The Company also sold mortgage securities classified as trading for proceeds of $49 million during the quarter ended March 31, 2000.

There were no sales of available-for-sale mortgage securities during the three months ended March 31, 2000 and 1999. Any gains and losses on the sales and write-downs of mortgage securities available-for-sale are reflected as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

NOTE 4. RESERVE FOR CREDIT LOSSES

The Reserve for Credit Losses is reflected as a component of Mortgage Assets on the Consolidated Balance Sheets. The following table summarizes the Reserve for Credit Losses activity:

<TABLE>
<CAPTION>

	THREE MONTHS ENDED MARCH 31,	
(IN THOUSANDS)	2000	1999
<S>	<C>	<C>
Balance at beginning of period	$ 5,954	$ 4,973
Provision for credit losses	119	345
Charge-offs	(143)	(121)
Balance at end of period	$ 5,930	$ 5,197

</TABLE>

NOTE 5. U.S. TREASURY SECURITIES

The Company did not hold any U.S. Treasury securities at March 31, 2000 or December 31, 1999. During the three months ended March 31, 1999, the Company recognized a market value loss of $1.9 million on U.S. Treasury securities and received proceeds of $58.4 million on sales of U.S. Treasury securities. The market value adjustments are reflected as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

NOTE 6. COLLATERAL FOR LONG-TERM DEBT

The Company has pledged collateral in order to secure the Long-Term Debt issued in the form of collateralized mortgage bonds ("Bond Collateral"). This Bond Collateral consists primarily of adjustable-rate and hybrid, conventional, 30-year mortgage loans secured by first liens on one- to four-family residential properties. All Bond Collateral is pledged to secure repayment of the related Long-Term Debt obligation. All principal and interest (less servicing and related fees) on the Bond Collateral is remitted to a trustee and is available for payment on the Long-Term Debt obligation. The Company's exposure to loss on the Bond Collateral is limited to its net investment, as the Long-Term Debt is non-recourse to the Company.

The components of the Bond Collateral are summarized as follows:

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 2000	DECEMBER 31, 1999
<S>	<C>	<C>
Mortgage loans		
Residential: held-for-investment, net	$1,316,508	$ 968,709
Restricted cash	1,881	4,791
Accrued interest receivable	6,229	5,633
	$1,324,618	$ 979,133

</TABLE>

For presentation purposes, the various components of the Bond Collateral summarized above are reflected in their corresponding line items on the Consolidated Balance Sheets.

NOTE 7. INTEREST RATE AGREEMENTS

At March 31, 2000 and December 31, 1999, all of the Company's Interest Rate Agreements were classified as trading, and therefore, reported at fair value.

For the three months ended March 31, 2000 and 1999, the Company recognized market value losses of $0.1 million and $0.8 million on Interest Rate Agreements classified as trading, respectively. The market value gains and losses are reflected as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations. The Company sold Interest Rate Agreements classified as trading for proceeds of $0.3 million during the quarter ended March 31, 2000.

The following table summarizes the aggregate notional amounts of all of the Company's Interest Rate Agreements as well as the credit exposure related to these instruments.

<TABLE>
<CAPTION>

	NOTIONAL AMOUNTS		CREDIT EXPOSURE (a)	
(IN THOUSANDS)	MARCH 31, 2000	DECEMBER 31, 1999	MARCH 31, 2000	DECEMBER 31, 1999
<S>	<C>	<C>	<C>	<C>
Interest Rate Options				
Purchased	$2,210,800	$2,960,900	--	--
Interest Rate Swaps	--	250,000	$ 2,390	$ 2,632
Interest Rate Futures and Forwards	843,000	630,000	524	593
Total	$3,053,800	$3,840,900	$ 2,914	$ 3,225

</TABLE>

(a) Reflects the fair market value of all cash and collateral of the Company held by counterparties.

Interest Rate Options purchased (sold), which may include caps, floors, call and put corridors, options on futures, options on MBS forwards, and swaption collars (collectively, "Options"), are agreements which transfer, modify or reduce interest rate risk in exchange for the payment (receipt) of a premium when the contract is initiated. Purchased interest rate cap agreements provide cash flows to the Company to the extent that a specific interest rate index exceeds a fixed rate. Conversely, purchased interest rate floor agreements produce cash flows to the Company to the extent that the referenced interest rate index falls below the agreed upon fixed rate. Purchased call (put) corridors will cause the Company to incur a gain to the extent that the yield of the specified index is below (above) the strike rate at the time of the option expiration. The maximum gain or loss on a purchased call (put) corridor is equal to the up-front premium. Call (put) corridors that are sold will cause the Company to incur a loss to the extent that the yield of the specified index is below (above) the strike rate at the time of the option expiration. Such loss, if any, will, in part, be offset by upfront premium received. The maximum gain or loss on a call (put) corridor sold is determined at the time of the transaction by establishing a minimum (maximum) index rate. The Company will receive cash on the purchased options on futures/forwards if the futures/forward price exceeds (is below) the call (put) option strike price at the expiration of the option. For the written options on futures/forwards, the Company receives an up-front premium for selling the option, however, the Company will incur a loss on the written option if the futures/forward price exceeds (is below) the call (put) option strike price at the expiration of the option. Purchased receiver (payor) swaption collars will cause the Company to incur a gain (loss) should the index rate be below (above) the strike rate as of the expiration date. The maximum gain or loss on a receiver (payor) swaption is established at the time of the transaction by establishing a minimum (maximum) index rate. The Company's credit risk on the purchased Options is limited to the carrying value of the Options agreements. The credit risk on options on futures is limited due to the fact that the exchange and its members are required to satisfy the obligations of any member that fails to perform.

Interest Rate Swaps ("Swaps") are agreements in which a series of interest rate flows are exchanged over a prescribed period. The notional amount on which the interest payments are based is not exchanged. Most of the Company's Swaps involve the exchange of one floating interest payment for another floating interest payment based on a different index. Most of the Swaps require that the Company provide collateral, such as mortgage securities, to the counterparty. Should the counterparty fail to return the collateral, the Company would be at risk for the fair market value of that asset.

Interest Rate Futures and Forwards ("Futures and Forwards") are contracts for the purchase or sale of securities or cash in which the seller (buyer) agrees to deliver (purchase) on a specified future date, a specified instrument (or the cash equivalent), at a specified price or yield. Under these agreements, if the Company has sold (bought) the futures/forwards, the Company will generally receive additional cash flows if interest rates rise (fall). Conversely, the Company will generally pay additional cash flows if interest rates fall (rise). The credit risk inherent in futures and forwards arises from the potential inability of counterparties to meet the terms of their contracts, however, the credit risk on futures is limited by the requirement that the exchange and its members make good on obligations of any member that fails to perform.

In general, the Company has incurred credit risk to the extent that the counterparties to the Interest Rate Agreements do not perform their obligations under the Interest Rate Agreements. If one of the counterparties does not perform, the Company would not receive the cash to which it would otherwise be entitled under the Interest Rate Agreement. In order to mitigate this risk, the Company has only entered into Interest Rate Agreements that are either a) transacted on a national exchange or b) transacted with counterparties that are either i) designated by the U.S. Department of the Treasury as a "primary government dealer", ii) affiliates of "primary government dealers", or iii) rated BBB or higher. Furthermore, the Company has entered into Interest Rate Agreements with several different counterparties in order to diversify the credit risk exposure.

NOTE 8. SHORT-TERM DEBT

The Company has entered into repurchase agreements, bank borrowings, and other forms of collateralized short-term borrowings (collectively, "Short-Term Debt") to finance acquisitions of a portion of its Mortgage Assets. This Short-Term Debt is collateralized by a portion of the Company's Mortgage Assets.

At March 31, 2000, the Company had $0.9 billion of Short-Term Debt outstanding with a weighted-average borrowing rate of 6.19% and a weighted-average remaining maturity of 83 days. This debt was collateralized with $1.0 billion of Mortgage Assets. At December 31, 1999, the Company had $1.3 billion of Short-Term Debt outstanding with a weighted-average borrowing rate of 6.22% and a weighted-average remaining maturity of 96 days. This debt was collateralized with $1.3 billion of Mortgage Assets.

At March 31, 2000 and December 31, 1999, the Short-Term Debt had the following remaining maturities:

(IN THOUSANDS)	MARCH 31, 2000	DECEMBER 31, 1999
Within 30 days	$ 257,383	$ 163,394
30 to 90 days	197,267	385,729
Over 90 days	467,755	704,442
Total Short-Term Debt	$ 922,405	$1,253,565

For the three months ended March 31, 2000 and 1999, the average balance of Short-Term Debt was $1.2 billion with a weighted-average interest cost of 6.25% and 5.12%, respectively. The maximum balance outstanding during both the three months ended March 31, 2000 and 1999 was $1.3 billion.

In July 1999, the Company entered into a one-year, $90 million revolving mortgage warehousing credit facility with two banks. The facility was primarily intended to finance newly acquired residential mortgage loans. At the Company's request, this line was cancelled during the first quarter of 2000. Therefore, there were no outstanding borrowings at March 31, 2000 under this facility. At December 31, 1999, the Company had outstanding borrowings of $6.4 million under this facility, which were reflected as a component of Short-Term Debt. Holdings had no outstanding borrowings under this facility at December 31, 1999. Borrowings under this facility bore interest based on a specified margin over the London Interbank Offered Rate ("LIBOR"). At December 31, 1999, the weighted-average borrowing rate under this facility was 6.87%. The Company and Holdings were in

compliance with all material representations, warranties, and covenants under this credit facility at December 31, 1999.

In July 1999, the Company entered into a one-year, $350 million master loan and security agreement with a Wall Street firm. The facility is primarily intended to finance newly originated commercial and acquisitions of residential mortgage loans. At March 31, 2000 and December 31, 1999, the Company had outstanding borrowings of $4.3 million and $119.9 million, respectively, under this facility, which are reflected as a component of Short-Term Debt. Holdings may borrow under this facility as a co-borrower. At March 31, 2000 and December 31, 1999, Holdings had outstanding borrowings of $11.6 million and $19.8 million under this facility, respectively. Borrowings under this facility bear interest based on a specified margin over LIBOR. At March 31, 2000 and December 31, 1999, the weighted-average borrowing rate under this facility was 6.61% and 5.72%, respectively. The Company and Holdings were in compliance with all material representations, warranties, and covenants under this credit facility at March 31, 2000 and December 31, 1999.

In March 2000, the Company established a $50 million revolving commercial mortgage loan warehouse facility with Residential Funding Corporation. The committed facility provides additional financing for RCF's commercial mortgage loan origination business. At March 31, 2000, the Company had outstanding borrowings of $8.0 million under this facility, which are reflected as a component of Short-Term Debt. RCF may borrow under this facility as a co-borrower. At March 31, 2000, RCF had outstanding borrowings of $2.4 million under this facility. Borrowings under this facility bear interest based on a specified margin over LIBOR. At March 31, 2000, the weighted-average borrowing rate under this facility was 8.01%. The Company and Holdings were in compliance with all material representations, warranties, and covenants under this credit facility at March 31, 2000.

NOTE 9. LONG-TERM DEBT

Long-Term Debt in the form of collateralized mortgage bonds is secured by a pledge of Bond Collateral. As required by the indentures relating to the Long-Term Debt, the Bond Collateral is held in the custody of trustees. The trustees collect principal and interest payments on the Bond Collateral and make corresponding principal and interest payments on the Long-Term Debt. The obligations under the Long-Term Debt are payable solely from the Bond Collateral and are otherwise non-recourse to the Company.

Each series of Long-Term Debt consists of various classes of bonds at variable rates of interest. The maturity of each class is directly affected by the rate of principal prepayments on the related Bond Collateral. Each series is also subject to redemption according to the specific terms of the respective indentures. As a result, the actual maturity of any class of a Long-Term Debt series is likely to occur earlier than its stated maturity.

The components of the Long-Term Debt at March 31, 2000 and December 31, 1999 along with selected other information are summarized below:

(IN THOUSANDS)	MARCH 31, 2000	DECEMBER 31, 1999
Long-Term Debt	$ 1,283,026	$ 944,225
Unamortized premium on Long-Term Debt	3,655	3,881
Deferred bond issuance costs	(3,925)	(2,836)
Total Long-Term Debt	$ 1,282,756	$ 945,270
Range of weighted-average coupon rates, by series	6.34% to 6.46%	6.21% to 6.88%
Stated maturities	2017 - 2029	2017 - 2029
Number of series	4	3

For the three months ended March 31, 2000 and 1999, the average effective interest cost for Long-Term Debt, as adjusted for the amortization of bond premium, deferred bond issuance costs, and other related expenses, was 6.32% and 6.03%, respectively. At March 31, 2000 and December 31, 1999, accrued interest payable on Long-Term Debt was $3.5 million and $3.0 million, respectively, and is reflected as a component of Accrued Interest Payable on the Consolidated Balance Sheets.

NOTE 10. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the carrying values and estimated fair values of the Company's financial instruments at March 31, 2000 and December 31, 1999.

	MARCH 31, 2000		DECEMBER 31, 1999	
(IN THOUSANDS)	CARRYING VALUE	FAIR VALUE	CARRYING VALUE	FAIR VALUE
Assets				
Mortgage Loans				
Residential: held-for-sale	$ 13,040	$ 13,040	$ 415,880	$ 415,880
Residential: held-for-investment, net	$1,316,508	$1,301,787	$ 968,709	$ 955,653
Commercial: held-for-sale	$ 16,865	$ 16,865	$ 8,437	$ 8,437
Mortgage Securities				
Residential: trading	$1,004,862	$1,004,862	$ 946,373	$ 946,373
Residential: available-for-sale, net	$ 36,994	$ 36,994	$ 28,006	$ 28,006
Interest Rate Agreements	$ 1,189	$ 1,189	$ 2,037	$ 2,037
Investment in RWT Holdings, Inc.	$ 2,822	$ 3,060	$ 3,391	$ 3,675
Liabilities				
Long-Term Debt	$1,282,756	$1,265,560	$ 945,270	$ 928,449

The carrying values of all other balance sheet accounts as reflected in the financial statements approximate fair value because of the short-term nature of these accounts.

NOTE 11. STOCKHOLDERS' EQUITY

CLASS B 9.74% CUMULATIVE CONVERTIBLE PREFERRED STOCK On August 8, 1996, the Company issued 1,006,250 shares of Class B Preferred Stock ("Preferred Stock"). Each share of the Preferred Stock is convertible at the option of the holder at any time into one share of Common Stock. Effective October 1, 1999, the Company can either redeem or, under certain circumstances, cause a conversion of the Preferred Stock. The Preferred Stock pays a dividend equal to the greater of (i) $0.755 per share, per quarter or (ii) an amount equal to the quarterly dividend declared on the number of shares of the Common Stock into which the Preferred Stock is convertible. The Preferred Stock ranks senior to the Company's Common Stock as to the payment of dividends and liquidation rights. In the event of a liquidation or dissolution of the Company, the liquidation preference entitles the holders of the Preferred Stock to receive $31.00 per share plus any accrued dividends before any distribution is made on the Common Stock. As of March 31, 2000 and December 31, 1999, 96,732 shares of the Preferred Stock have been converted into 96,732 shares of the Company's Common Stock.
In March 1999, the Company's Board of Directors approved the repurchase of up to 150,000 shares of the Company's Preferred Stock. There were no preferred stock repurchases during the three months ended March 31, 2000 and 1999. At March 31, 2000 and December 31, 1999, there were 142,550 shares available for repurchase.

STOCK OPTION PLAN
The Company has adopted a Stock Option Plan for executive officers, employees, and non-employee directors (the "Plan"). The Plan authorizes the Board of Directors (or a committee appointed by the Board of Directors) to

grant "incentive stock options" as defined under Section 422 of the Code ("ISOs"), options not so qualified ("NQSOs"), deferred stock, restricted stock, performance shares, stock appreciation rights, limited stock appreciation rights ("Awards"), and dividend equivalent rights ("DERs") to such eligible recipients other than non-employee directors. Non-employee directors are automatically provided annual grants of NQSOs with DERs pursuant to a formula under the Plan.

The number of shares of Common Stock available under the Plan for options and Awards, subject to certain anti-dilution provisions, is 15% of the Company's total outstanding shares of Common Stock. The total outstanding shares are determined as the highest number of shares outstanding prior to any stock repurchases. At March 31, 2000 and December 31, 1999, 413,644 and 283,975 shares of Common Stock, respectively, were available for grant. Of the shares of Common Stock available for grant, no more than 500,000 shares of Common Stock shall be cumulatively available for grant as ISOs. At March 31, 2000 and December 31, 1999, 382,305 and 389,942 ISOs had been granted, respectively. The exercise price for ISOs granted under the Plan may not be less than the fair market value of shares of Common Stock at the time the ISO is granted. All stock options granted under the Plan vest no earlier than ratably over a four-year period from the date of grant and expire within ten years after the date of grant.

The Company's Plan permits certain stock options granted under the plan to accrue stock DERs. Stock DERs represent shares of stock which are issuable to holders of stock options when the holders exercise the underlying stock options. The number of stock DER shares accrued is based on the level of the Company's dividends and on the price of the stock on the related dividend payment date. For the three months ended March 31, 2000, the stock DERs accrued on NQSOs that had a stock DER feature resulted in charges to operating expenses of $0.1 million. There were no such charges for the three months ended March 31, 1999.

A summary of the status of the Company's Plan as of March 31 and changes during the periods ending on that date is presented below.

<TABLE>
<CAPTION>

	2000		1999	
(IN THOUSANDS, EXCEPT SHARE DATA)	SHARES	WEIGHTED AVERAGE EXERCISE PRICE	SHARES	WEIGHTED AVERAGE EXERCISE PRICE
<S>	<C>	<C>	<C>	<C>
Outstanding options at January 1	1,713,836	$ 21.97	1,739,787	$ 23.68
Options granted	11,000	$ 12.55	42,000	$ 14.43
Options exercised	(6,035)	$ 3.02	(12,361)	$ 0.11
Options canceled	(144,225)	$ 14.04	(141,520)	$ 28.96
Stock dividend equivalent rights earned	3,556	--	--	--
Outstanding options at March 31	1,578,132	$ 22.66	1,627,906	$ 23.16

</TABLE>

COMMON STOCK REPURCHASES
Since September 1997, the Company's Board of Directors has approved the repurchase of 7,455,000 shares of the Company's Common Stock. At March 31, 2000 and December 31, 1999, there were 1,000,000 shares authorized for repurchase. The repurchased shares have been returned to the Company's authorized but unissued shares of Common Stock.

NOTE 12. RELATED PARTY TRANSACTIONS

PURCHASES AND SALES OF MORTGAGE LOANS
During December 1999, Holdings purchased $390 million of residential mortgage loans and subsequently sold a participation agreement on the mortgage loans to the Company. Pursuant to the terms of the Mortgage Loan Participation Purchase Agreement, the Company purchased a 99% interest in the mortgage loans, and assumed all related risks of ownership. Holdings did not recognize any gain or loss on this transaction. During March 2000, the Company sold the participation agreement back to Holdings for proceeds of $380.5 million. Holdings

simultaneously sold $384 million of residential mortgage loans to Sequoia for proceeds of $384 million. Sequoia pledged these loans as collateral for a new issue of Long-Term Debt.

During the three months ended March 31, 2000 and 1999, the Company sold $8.4 million and $8.3 million of commercial mortgage loans to RCF, respectively. Pursuant to the Master Forward Commitment Agreement, the Company sold the mortgage loans to RCF at the same price for which the Company acquired the mortgage loans. At March 31, 2000 and December 31, 1999, under the terms of the Master Forward Commitment Agreement, the Company had committed to sell $16.9 million and $8.4 million of commercial mortgage loans to RCF for settlement during the first half of 2000, respectively.

During the three months ended March 31, 2000, the Company sold $16.7 million of residential mortgage loans to Redwood Residential Funding ("RRF"), a subsidiary of Holdings. Pursuant to the Master Forward Commitment Agreement, the Company sold the mortgage loans to RRF at the same price for which the Company acquired the mortgage loans. There were no such sales during the three months ended March 31, 1999. At March 31, 2000 and December 31, 1999, under the terms of the Master Forward Commitment Agreement, the Company had committed to sell $0.4 million and $16.7 million of residential mortgage loans to RRF during the first half of 2000, respectively.

OTHER

Under a revolving credit facility arrangement, the Company may loan funds to Holdings to finance Holdings' operations. These loans are unsecured, subordinated, and are repaid within six months. Such loans bear interest at a rate of 3.50% over the LIBOR interest rate. At March 31, 2000 and December 31, 1999, the Company had loaned $1.4 million and $6.5 million to Holdings, respectively, in accordance with the provisions of this arrangement. During the three months ended March 31, 2000 and 1999, the Company earned $0.1 million and $0.2 million, respectively, in interest on loans to Holdings.

The Company shares many of the operating expenses of Holdings, including personnel and related expenses, subject to full reimbursement by Holdings. During the years three months ended March 31, 2000 and 1999, $0.1 million and $0.6 million, respectively, of Holdings' operating expenses were paid by the Company, and were subject to reimbursement by Holdings.

The Company may provide credit support to Holdings to facilitate Holdings' financings from third-party lenders and/or hedging arrangements with counterparties. As part of this arrangement, Holdings is authorized as a co-borrower under some of the Company's Short-Term Debt agreements subject to the Company continuing to remain jointly and severally liable for repayment. Accordingly, Holdings pays the Company credit support fees on borrowings subject to this arrangement. At March 31, 2000 and December 31, 1999, the Company was providing credit support on $13.9 million and $22.4 million of Holdings' Short-Term Debt. During both the three months ended March 31, 2000 and 1999, the Company recognized approximately $0.1 million in credit support fee income. Credit support fees are reflected as a component of "Other Income" on the Consolidated Statements of Operations.

NOTE 13. COMMITMENTS AND CONTINGENCIES

At March 31, 2000, the Company had entered into commitments to purchase $0.1 million of interest rate agreements for settlement in April 2000. At March 31, 2000, the Company had also entered into commitments to sell $16.9 million of commercial mortgage loans to RCF and $0.4 million of residential mortgage loans to RRF for settlement during the second quarter of 2000.

At March 31, 2000, the Company is obligated under non-cancelable operating leases with expiration dates through 2003. The total future minimum lease payments under these non-cancelable leases is $582,893 and is expected to be recognized as follows: 2000 - $259,891; 2001 - $171,856; 2002 - $53,546; 2003 - $43,601.

RWT HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

<TABLE>
<CAPTION>

	March 31, 2000	December 31, 1999
-	(Unaudited)	
<S>	<C>	<C>
ASSETS		

Mortgage loans: held-for sale		
Commercial	$ 17,636	$ 29,605
Residential	--	4,399
	17,636	34,004
Cash and cash equivalents	3,624	1,999
Restricted cash	92	50
Accrued interest receivable	155	1,520
Property, equipment and leasehold improvements, net	102	299
Other assets	18	1,081
Total Assets	$ 21,627	$ 38,953
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Short-term debt	$ 13,936	$ 22,427
Loans from Redwood Trust, Inc.	1,400	6,500
Payable to Redwood Trust, Inc.	573	472
Accrued interest payable	10	831
Accrued restructuring charges	2,285	4,039
Accrued expenses and other liabilities	572	1,259
Total Liabilities	18,776	35,528
Commitments and contingencies (See Note 10)		
STOCKHOLDERS' EQUITY		
Series A preferred stock, par value $0.01 per share; 10,000 shares authorized; 5,940 issued and outstanding ($5,940 aggregate liquidation preference)	29,700	29,700
Common stock, par value $0.01 per share; 10,000 shares authorized; 3,000 issued and outstanding	--	--
Additional paid-in capital	300	300
Accumulated deficit	(27,149)	(26,575)
Total Stockholders' Equity	2,851	3,425
Total Liabilities and Stockholders' Equity	$ 21,627	$ 38,953

</TABLE>

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

RWT HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)
(Unaudited)

<TABLE>
<CAPTION>

	Three Months Ended March 31,	
	2000	1999
<S>	<C>	<C>
REVENUES		
Interest income		
Mortgage loans: held-for-sale		
Commercial	$ 500	$ 126
Residential	67	53
	567	179
Mortgage securities: trading	--	207
Cash and cash equivalents	32	108
Total interest income	599	494
Interest expense		
Short-term debt	(300)	(107)
Credit support fees	(15)	(8)
Loans from Redwood Trust, Inc.	(89)	(159)
Total interest expense	(404)	(274)

Net interest income	195	220
Net unrealized and realized market value gains (losses)	92	478
Other income	--	57
Net revenues	287	755
EXPENSES		
Compensation and benefits	(585)	(2,259)
General and administrative	(276)	(1,005)
Total expenses	(861)	(3,264)
NET LOSS	$ (574)	$(2,509)

</TABLE>

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

RWT HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands, except share data)
(Unaudited)

<TABLE>
<CAPTION>

	Series A Preferred stock		Common stock		Additional paid-in capital	Accumulated deficit	Total
	Shares	Amount	Shares	Amount			
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, December 31, 1999	5,940	$ 29,700	3,000	$ --	$ 300	$(26,575)	$ 3,425
Comprehensive income:							
Net loss	--	--	--	--	--	(574)	(574)
Issuance of preferred stock	--	--	--	--	--	--	0
Issuance of common stock	--	--	--	--	--	--	0
Balance, March 31, 2000	5,940	$ 29,700	3,000	$ --	$ 300	$(27,149)	$ 2,851

</TABLE>

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

RWT HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

<TABLE>
<CAPTION>

	Three Months Ended March 31,	
	2000	1999
<S>	<C>	<C>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (574)	$ (2,509)
Adjustments to reconcile net loss to net cash used in operating activities:		

Depreciation and amortization	8	103
Net unrealized and realized market value (gains) losses	(92)	(478)
Purchases of mortgage loans: held for sale	(406,583)	(102,343)
Proceeds from sales of mortgage loans: held for sale	422,869	17,841
Principal payments on mortgage loans: held for sale	179	30
Proceeds from sales of mortgage securities: trading	--	10,502
Principal payments on mortgage securities: trading	--	518
(Increase) decrease in accrued interest receivable	1,365	(115)
(Increase) decrease in other assets	1,058	(1,235)
Increase (decrease) in amounts due to Redwood Trust	101	(303)
Increase (decrease) in accrued interest payable	(821)	113
Decrease in accrued restructuring charges	(1,754)	--
Increase (decrease) in accrued expenses and other liabilities	(687)	102
Net cash provided by (used in) operating activities	15,069	(77,774)
CASH FLOWS FROM INVESTING ACTIVITIES:		
(Purchases) sales of property, equipment and leasehold improvements, net	189	(830)
Net increase in restricted cash	(42)	--
Net cash provided by (used in) investing activities	147	(830)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from issuance of short-term debt (net of repayments)	(8,491)	72,313
Loans from Redwood Trust, Inc. (net of repayments)	(5,100)	7,200
Net cash provided by (used in) financing activities	(13,591)	79,513
Net increase in cash and cash equivalents	1,625	909
Cash and cash equivalents at beginning of period	1,999	9,711
Cash and cash equivalents at end of period	$ 3,624	$ 10,620
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest expense	$ 2,994	$ 2,518

</TABLE>

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

RWT HOLDINGS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2000
(UNAUDITED)

NOTE 1. THE COMPANY

RWT Holdings, Inc. ("Holdings") was incorporated in Delaware on February 13, 1998 and commenced operations on April 1, 1998. Holdings originates and sells commercial mortgage loans. Redwood Trust, Inc. ("Redwood Trust") owns all of the preferred stock and has a non-voting, 99% economic interest in Holdings. The consolidated financial statements include the three wholly-owned subsidiaries of Holdings. Redwood Commercial Funding, Inc. ("RCF") originates commercial mortgage loans for sale to institutional investors. Redwood Residential Funding, Inc. ("RRF") and Redwood Financial Services, Inc. ("RFS") were start-up ventures that ceased operations in 1999. Holdings and its subsidiaries currently utilize both debt and equity to finance acquisitions. References to Holdings in the following footnotes refer to Holdings and its subsidiaries.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The accompanying interim consolidated financial statements are unaudited. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the quarter ended March 31, 2000 are not necessarily indicative of the results that may be expected for the year ending December 31, 2000. The accompanying consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Annual Report on Form 10-K filed by Redwood Trust for the year ended December 31, 1999.

The consolidated financial statements include the accounts of Holdings and its subsidiaries. All significant intercompany balances and transactions with Holdings' consolidated subsidiaries have been eliminated.

USE OF ESTIMATES

The preparation of financial statements in conformity with Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results could differ from those estimates. The primary estimates inherent in the accompanying consolidated financial statements are discussed below.

Fair Value. Management estimates the fair value of its financial instruments using available market information and other appropriate valuation methodologies. The fair value of a financial instrument, as defined by Statement of Financial Accounting Standards ("SFAS") No. 107, Disclosures about Fair Value of Financial Instruments, is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced liquidation sale. Management's estimates are inherently subjective in nature and involve matters of uncertainty and judgement to interpret relevant market and other data. Accordingly, amounts realized in actual sales may differ from the fair values presented in Note 6.

MORTGAGE ASSETS

Holdings' mortgage assets consist of mortgage loans and mortgage securities ("Mortgage Assets"). Interest is recognized as revenue when earned according to the terms of the loans and when, in the opinion of management, it is collectible.

Mortgage Loans: Held-for-Sale

Mortgage loans are recorded at the lower of cost or market value ("LOCOM"). Cost generally consists of the loan principal balance net of any unamortized premium or discount and net loan origination fees. Interest income

is accrued based on the outstanding principal amount of the mortgage loans and their contractual terms. Realized and unrealized gains or losses on the loans are based on the specific identification method and are recognized in "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

Some of the mortgage loans purchased by Redwood Trust for which securitization or sale is contemplated are committed for sale by Redwood Trust to Holdings, or a subsidiary of Holdings, under a Master Forward Commitment Agreement. As the forward commitment is entered into on the same date that Redwood Trust commits to purchase the loans, the price which Holdings will pay to purchase the loans under the forward commitment is the same as the price Redwood Trust paid for the mortgage loans, as established by the external market.

Mortgage Securities: Trading

Mortgage securities classified as trading are accounted for in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. Accordingly, such securities are recorded at their estimated fair market value. Unrealized and realized gains and losses on these securities are recognized as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations.

LOAN ORIGINATION FEES

Loan fees, discount points, and certain direct origination costs are recorded as an adjustment to the cost of the loan and are recorded in earnings when the loan is sold.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash on hand and highly liquid investments with original maturities of three months or less.

INTEREST RATE AGREEMENTS

During 1999 and the first quarter of 2000, Holdings utilized interest rate agreements to mitigate the risks that a change in interest rates would result in a change in the value of the Mortgage Assets. Holdings designated all interest rate agreements as trading instruments. Accordingly, such instruments were recorded at their estimated fair market value with unrealized and realized gains and losses on these instruments recognized as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations. At March 31, 2000, there were no outstanding interest rate agreements. At December 31, 1999, Holdings had entered into $1 million notional value of forward contracts for the sale of mortgage loans.

INCOME TAXES

Taxable earnings of Holdings are subject to state and federal income taxes at the applicable statutory rates. Holdings provides for deferred income taxes if any, to reflect the estimated future tax effects under the provisions of SFAS

No. 109, Accounting for Income Taxes. Under this pronouncement, deferred income taxes, if any, reflect the estimated future tax effects of temporary differences between the amount of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws and regulations.

COMPREHENSIVE INCOME
SFAS No. 130, Reporting Comprehensive Income, requires Holdings to classify items of "other comprehensive income" by their nature in a financial statement and display the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in capital in the equity section of the balance sheet. As of March 31, 2000, there was no other comprehensive income.

RECENT ACCOUNTING PRONOUNCEMENT
During March 2000, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 44, Accounting for Certain Transactions involving Stock Compensation - an interpretation of APB Opinion No. 25 ("FIN 44"). FIN 44 clarifies the application of APB Opinion No. 25 by expanding upon a number of issues not specifically addressed in the Opinion such as the definition of an employee for purposes of applying APB Opinion No. 25 and the accounting for modifications to a previously fixed stock option award. FIN 44 is effective July 1, 2000. The impact on the Holdings of adopting FIN 44 has not yet been determined.

NOTE 3. MORTGAGE ASSETS

At March 31, 2000 and December 31, 1999 Mortgage Assets consisted of the following:

MORTGAGE LOANS: HELD-FOR-SALE

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 2000 COMMERCIAL	DECEMBER 31, 1999 RESIDENTIAL	DECEMBER 31, 1999 COMMERCIAL	DECEMBER 31, 1999 TOTAL
<S>	<C>	<C>	<C>	<C>
Current Face	$ 18,547	$ 4,995	$ 30,324	$ 35,319
Unamortized Premium (Discount)	(911)	(596)	(719)	(1,315)
Carrying Value	$ 17,636	$ 4,399	$ 29,605	$ 34,004

</TABLE>

Holdings recognized gains of $0.1 million and losses of $0.1 million during the quarters ended March 31, 2000 and 1999, respectively, as a result of LOCOM adjustments on mortgage loans held-for-sale. The LOCOM adjustments are reflected as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations. Additionally, during the three months ended March 31, 2000, Holdings sold residential mortgage loans to Sequoia Mortgage Funding Corporation, a subsidiary of Redwood Trust ("Sequoia"), for proceeds of $384 million. Holdings also sold other residential and commercial mortgage loans for proceeds of $39 million during the three months ended March 31, 2000. During the three months ended March 31, 1999, Holdings sold mortgage loans held-for-sale for proceeds of $18 million.

MORTGAGE SECURITIES: TRADING

Holdings did not own any mortgage securities at March 31, 2000 and December 31, 1999. For the three months ended March 31, 1999, Holdings recognized market value gains of $0.6 million on mortgage securities classified as trading. This gain is reflected as a component of "Net unrealized and realized market value gains (losses)" on the Consolidated Statements of Operations. Also during the three months ended March 31, 1999, Holdings sold mortgage securities classified as trading for proceeds of $10.5 million.

NOTE 4. SHORT-TERM DEBT

Holdings has entered into reverse repurchase agreements and other forms of collateralized short-term borrowings (collectively, "Short-Term Debt") to finance acquisitions of a portion of its Mortgage Assets. This Short-Term Debt is collateralized by a portion of Holdings' mortgage loans.

At March 31, 2000, and December 31, 1999, Holdings had $13.9 million and $22.4 million of Short-Term Debt outstanding with a weighted-average borrowing rate of 7.70% and 7.02%, respectively. The average balance of Short-Term Debt outstanding during the quarters ended March 31, 2000 and 1999 was $17 million and $8 million with a weighted-average interest cost of 7.23% and 5.28%, respectively. The maximum balance outstanding during the three months ended

March 31, 2000 and 1999 was $22 million and $88 million, respectively.

In July 1999, Redwood Trust entered into a one-year, $350 million master loan and security agreement with a Wall Street firm. The facility is primarily intended to finance newly originated commercial and residential mortgage loans. Holdings may borrow under this facility as a co-borrower. At March 31, 2000 and December 31, 1999, Holdings had outstanding borrowings of $11.6 million and $19.8 million, respectively, under this facility. Borrowings under this facility bear interest based on a specified margin over the London Interbank Offered Rate ("LIBOR"). At March 31, 2000 and December 31, 1999, the weighted-average borrowing rate under this facility was 7.63% and 7.23%, respectively. Redwood Trust and Holdings were in compliance with all material representations, warranties, and covenants under this credit facility at March 31, 2000 and December 31, 1999.

In March 2000, Redwood Trust established a $50 million revolving commercial mortgage loan warehouse facility with Residential Funding Corporation. This committed facility provides additional financing for RCF's commercial mortgage loan origination business. RCF may borrow under this facility as a co-borrower. At March 31, 2000, RCF had outstanding borrowings of $2.4 million under this facility. Borrowings under this facility bear interest based on a specified margin over LIBOR. At March 31, 2000, the weighted-average borrowing rate under this facility was 8.01%. The Company and Holdings were in compliance with all material representations, warranties, and covenants under this credit facility at March 31, 2000

Redwood Trust may provide credit support to Holdings to facilitate Holdings' financings from third-party lenders and/or hedging arrangements with counterparties. As part of this arrangement, Holdings is authorized as a co-borrower under some of Redwood Trust's Short-Term Debt agreements subject to Redwood Trust continuing to remain jointly and severally liable for repayment. Accordingly, Holdings pays Redwood Trust credit support fees on borrowings subject to this arrangement. At March 31, 2000 and December 31, 1999, Redwood Trust was providing credit support on $13.9 million and $22.4 million of Holdings' Short-Term Debt, respectively. These expenses are reflected as "Credit support fees" on the Consolidated Statements of Operations (see Note 9).

NOTE 5. RESTRUCTURING CHARGE

During the year ended December 31, 1999, Holdings recognized $8.4 million in restructuring charges as a result of the closure of two of its subsidiaries, RRF and RFS. Restructuring charges were determined in accordance with the provisions of Staff Accounting Bulletin No. 100 "Restructuring and Impairment Charges", Emerging Issues Task Force No. 94-3 "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity", and other relevant accounting guidance. The restructuring accrual includes costs associated with existing contractual and lease arrangements at both subsidiaries which have no future value. In addition, as a result of the closure of the two subsidiaries, certain assets utilized in these businesses were determined to have little or no realizable value, resulting in impairment losses. These assets included software developed for use at RRF and certain fixed assets at both subsidiaries. The following table provides a summary of the primary components of the restructuring liability.

<TABLE>
<CAPTION>

	TOTAL REMAINING LIABILITY	
(IN THOUSANDS)	MARCH 31, 2000	DECEMBER 31, 1999
<S>	<C>	<C>
Payroll, severance, and termination benefits	$1,309	$2,431
Asset impairments	--	--
Lease and other commitments	931	1,068
Other	45	540
Total	$2,285	$4,039

</TABLE>

Holdings expects to pay the majority of the remaining restructuring costs during the year 2000. The remaining liability for restructuring costs is reflected as "Accrued restructuring charges" on the Consolidated Balance Sheets.

NOTE 6. INCOME TAXES

The provision for income taxes for both the quarters ended March 31, 2000 and 1999 was $3,200 and represents minimum California franchise taxes. No tax provision was recorded for the quarters ended March 31, 2000 and 1999, as

Holdings reported a loss for the period. Due to the uncertainty of realization of net operating losses, no tax benefit has been provided against the loss for the period. In addition, a valuation allowance has been provided to eliminate the deferred tax asset related to net operating loss carryforwards at March 31, 2000 and December 31, 1999. At both March 31, 2000 and December 31, 1999, the valuation allowance was approximately $8.0 million. At December 31, 1999 Holdings had net operating loss carryforwards of approximately $21 million for federal tax purposes, and $11 million for state tax purposes. The federal loss carryforwards and a portion of the

state loss carryforwards expire through 2019, while the largest portion of the state loss carryforwards expire through 2004.

NOTE 7. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the carrying values and estimated fair values of Holdings' financial instruments at March 31, 2000 and December 31, 1999.

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 2000		DECEMBER 31, 1999	
	CARRYING VALUE	FAIR VALUE	CARRYING VALUE	FAIR VALUE
<S>	<C>	<C>	<C>	<C>
Assets				
Mortgage loans:				
held-for-sale				
Commercial	$17,636	$17,876	$29,605	$29,876
Residential	--	--	$ 4,399	$ 4,415

</TABLE>

The carrying amounts of all other balance sheet accounts as reflected in the financial statements approximate fair value because of the short-term nature of these accounts.

NOTE 8. STOCKHOLDERS' EQUITY

The authorized capital stock of Holdings consists of Series A Preferred Stock ("Preferred Stock") and Common Stock. Holdings is authorized to issue 10,000 shares of Common Stock, each having a par value of $0.01, and 10,000 shares of Preferred Stock, each having a par value of $0.01. All voting power is vested in the common stock.

Holdings has issued a total of 5,940 shares of Preferred Stock to Redwood Trust. The Preferred Stock entitles Redwood Trust to receive 99% of the aggregate amount of any such dividends or distributions made by Holdings. The holders of the Common Stock are entitled to receive the remaining 1% of the aggregate amount of such dividends or distributions. The Preferred Stock ranks senior to the Common Stock as to the payment of dividends and liquidation rights. The liquidation preference entitles the holders of the Preferred Stock to receive $1,000 per share liquidation preference before any distribution is made on the Common Stock. After the liquidation preference, the holders of Preferred Stock are entitled to 99% of any remaining assets.

NOTE 9. RELATED PARTY TRANSACTIONS

PURCHASES AND SALES OF MORTGAGE LOANS

During December 1999, Holdings purchased $390 million of residential mortgage loans and subsequently sold a participation agreement on the mortgage loans to Redwood Trust. Pursuant to the terms of the Mortgage Loan Participation Purchase Agreement, Redwood Trust purchased a 99% interest in the mortgage loans, and assumed all related risks of ownership. Holdings did not recognize any gain or loss on this transaction. During March 2000, Redwood Trust sold the participation agreement back to Holdings for proceeds of $380.5 million. Holdings simultaneously sold $384 million of residential mortgage loans to Sequoia for proceeds of $384 million.

During both the three months ended March 31, 2000 and 1999, RCF purchased $8.4 million of commercial mortgage loans from Redwood Trust. Pursuant to the Master Forward Commitment Agreement, RCF purchased the mortgage loans from Redwood Trust at the same price for which Redwood Trust acquired the mortgage loans. At March 31, 2000 and December 31, 1999, under the terms of the Master Forward Commitment Agreement, Redwood Trust had committed to sell $16.9 million and $8.4 million of commercial mortgage loans to RCF for settlement during the first half of 2000, respectively.

During the three months ended March 31, 2000, RRF purchased $16.7 million of residential mortgage loans from Redwood Trust. Pursuant to the Master Forward Commitment Agreement, RRF purchased the mortgage loans from Redwood Trust at the same price for which Redwood Trust acquired the mortgage loans. There were no such purchases during the three months ended March 31, 1999. At March 31, 2000 and December 31, 1999, under the terms of the Master Forward Commitment Agreement, Redwood Trust had committed to sell $0.4 million and $16.7 million of residential mortgage loans to RRF during the first half of 2000, respectively.

OTHER

Under a revolving credit facility arrangement, Redwood Trust may loan funds to Holdings to finance Holdings' operations. These loans are unsecured, subordinated, and are repaid within six months. Such loans bear interest at a rate of 3.50% over the LIBOR interest rate. At March 31, 2000 and December 31, 1999, Holdings had borrowed $1.4 million and $6.5 million from Redwood Trust, respectively, in accordance with the provisions of this arrangement. During the three months ended March 31, 2000 and 1999, Holdings incurred $0.1 million and $0.2 million, respectively, in interest expense on loans from Redwood Trust.

Redwood Trust shares many of the operating expenses of Holdings, including personnel and related expenses, subject to full reimbursement by Holdings. During the years three months ended March 31, 2000 and 1999, $0.1 million and $0.6 million, respectively, of Holdings' operating expenses were paid by Redwood Trust, and were subject to reimbursement by Holdings.

Redwood Trust may provide credit support to Holdings to facilitate Holdings' financings from third-party lenders and/or hedging arrangements with counterparties. As part of this arrangement, Holdings is authorized as a co-borrower under some of Redwood Trust's Short-Term Debt agreements subject to Redwood Trust continuing to remain jointly and severally liable for repayment. Accordingly, Holdings pays Redwood Trust credit support fees on borrowings subject to this arrangement. At March 31, 2000 and December 31, 1999, Redwood Trust was providing credit support on $13.9 million and $22.4 million of Holdings' Short-Term Debt. During both the three months ended March 31, 2000 and 1999, Holdings recognized approximately $0.1 million in credit support fee expense.

NOTE 10. COMMITMENTS AND CONTINGENCIES

At March 31, 2000, RCF is obligated under non-cancelable operating leases with expiration dates through 2006. The total future minimum lease payments under these non-cancelable leases is $419,821 and is expected to be recognized as follows: 2000- $56,341; 2001 - $85,240; 2002 - $87,472; 2003 - $89,772; 2004 through 2006 - $83,388.

At March 31, 2000, RCF had entered into commitments to purchase $16.9 million of commercial mortgage loans from Redwood Trust for settlement during the second quarter of 2000.

At March 31, 2000, RRF had entered into commitments to purchase $0.4 million of residential mortgage loans from Redwood Trust for settlement during the second quarter of 2000.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the Consolidated Financial Statements and Notes.

SAFE HARBOR STATEMENT

"Safe Harbor" Statement under the Private Securities Litigation Reform Act of 1995: Statements in this discussion regarding Redwood Trust, Inc., or "Redwood Trust", and our business which are not historical facts are "forward-looking statements" that involve risks and uncertainties. For a discussion of such risks and uncertainties, which could cause actual results to differ from those contained in the forward-looking statements, we refer you to "Company Business and Strategy" beginning on Page 4 and "Risk Factors" commencing on Page 13 of our 1999 Form 10-K included in our 1999 Annual Report.

OVERVIEW

Redwood Trust is a finance company specializing in the mortgage portfolio lending business. Our primary activity is the acquisition, financing, and management of high-quality jumbo residential mortgage loans. We fund our loans chiefly through the issuance of long-term debt. We also manage a portfolio of residential mortgage securities and, through our affiliates, originate commercial mortgage loans for sale to other financial institutions.

Our core business of mortgage finance is conducted through Redwood Trust, Inc., which is a qualified real estate investment trust ("REIT"). In general, our REIT status allows us to avoid corporate income taxes by distributing to our shareholders an amount equal to at least 95% of taxable income.

We also own a 99% economic interest in a taxable affiliate company, RWT Holdings, Inc. ("Holdings"). Our investment in Holdings is accounted for under the equity method. Holdings originates commercial mortgage loans for sale to institutional investors through its Redwood Commercial Funding, Inc. ("RCF") subsidiary. RCF typically originates shorter-term floating-rate commercial mortgage loans to borrowers who require more flexible borrowing arrangements than are usually offered by life insurance companies or commercial mortgage conduit lending programs.

For more information, please visit our Web site at: www.redwoodtrust.com.

SIGNIFICANT ACTIVITY DURING THE QUARTER

During March 2000, we issued $377 million of long-term debt through our special-purpose finance subsidiary, Sequoia Mortgage Funding Corporation ("Sequoia"). This issuance is the fourth series in our on-going program of issuing AAA-rated, non-recourse, callable, long-term debt to finance our high-quality residential mortgage loan portfolio. The debt certificates are supported by a $381 million pool of high-quality adjustable-rate residential mortgage loans. The proceeds from this debt issuance were used to reduce short-term debt.

FINANCIAL CONDITION

Our balance sheet presents our mortgage finance assets and liabilities. It also includes, as one line item, our net investment in Holdings. Holdings' balance sheet and financial condition are presented separately with discussion and analysis beginning on Page 44.

At March 31, 2000, we owned $1.4 billion mortgage loans and $1.0 billion mortgage securities. We owned similar amounts at December 31, 1999. Our mix of debt changed over this period, as we financed these mortgage assets with $0.9 billion of short-term debt, $1.3 billion of long-term debt, and $210 million of equity at March

31, 2000, as compared to $1.3 billion of short-term debt, $0.9 billion of long-term debt, and $210 million of equity at December 31, 1999. This increase in long-term debt and reduction in short-term debt was the result of our issuance of long-term debt in the first quarter of 2000.

Our exposure to credit loss from our mortgage loans is limited, to some degree, by the methods we use to finance these loans. The long-term debt we issue is non-recourse to us; as a result, our credit exposure to our long-term debt financed loans is limited to our net investment remaining after the issuance of such debt. A total of $1.3 billion of non-recourse assets and liabilities are owned by trusts created by Sequoia. The trusts are "bankruptcy-remote" with respect to Redwood Trust. Although the net earnings of the trusts accrue to Redwood Trust, Redwood Trust is not responsible for the repayment of Sequoia debt and Sequoia has no call on the liquidity of Redwood Trust. Likewise, the assets of these trusts are pledged to secure the related debt of each trust and accordingly, are not available for general creditors of Redwood Trust. Our recourse exposure to Sequoia's mortgage assets is limited to our equity investments in these trusts. At March 31, 2000, these equity investments had a reported net value of $41 million.

At March 31, 2000, the portion of our balance sheet that was subject to recourse was $1.1 billion of assets, $0.9 billion of borrowings, and $0.2 billion of equity. The ratio of equity-to-recourse-assets was 18.4%. The ratio of recourse-debt-to-equity was 4.4 to 1.0.

At December 31, 1999, we reported $2.4 billion in assets, of which $1.5 billion were recourse, and $2.6 billion of liabilities, of which $1.3 billion were recourse. Equity capital was $0.2 billion. The ratio of equity-to-recourse-assets was 14.8% and the ratio of recourse-debt-to-equity was 6.0 to 1.0. The improvement in our debt-based ratios during the first quarter of 2000 was due to our issuance of long-term debt.

EARNING ASSETS

At March 31, 2000 and December 31, 1999, we owned $2.4 billion of earning assets. During the first quarter of 2000, we acquired $204 million in assets and sold $75 million in assets. We received $106 million in mortgage principal paydowns during the quarter.

MORTGAGE LOANS

At March 31, 2000, $953 million carrying value, or 40% of our total mortgage asset portfolio, were high-quality residential mortgage loans with adjustable-rate coupons with a principal value of $942 million. Our carrying value of these loans, after $2.9 million of credit reserves, was 101.18% of the face or principal value of the loans. At December 31, 1999, we owned $993 million carrying value of these loans, or 42% of our portfolio, at a carrying value of 101.21% of the $981 million principal value (net of a $2.8 million credit reserve). Seriously delinquent loans (over 90 days delinquent, in foreclosure, or REO) in this portion of our portfolio were $4.6 million at March 31, 2000 and $3.4 million at December 31, 1999.

At March 31, 2000, $377 million carrying value and principal value, or 16% of our total mortgage asset portfolio, were high-quality residential mortgage loans with hybrid coupons. Our hybrid mortgage loans have an initial fixed coupon rate for three to ten years followed by annual coupon adjustments. On average, these loans become floating-rate in December 2002. Our carrying value of these loans, after $2.2 million of credit reserves, was 99.81% of face value. At December 31, 1999 we owned $391 million carrying value of these loans, or 17% of our portfolio, at a carrying value of 99.84% of the $392 million principal value (net of a $2.3 million credit reserve). Seriously delinquent loans in this portion of our portfolio were $0.7 million at March 31, 2000 and $1.3 million at December 31, 1999. This portion of our portfolio is matched to the $368 million of long-term debt we have issued that is fixed-rate debt until December 2002.

At March 31, 2000, $16.9 million carrying value, or 0.7% of our total mortgage asset portfolio, were commercial mortgage loans originated by our affiliate, RCF. Our carrying value of these loans was 99.80% of principal value. At December 31, 1999, we owned $8.4 million carrying value of these loans, or 0.4% of our portfolio, at a carrying value of 99.85% of principal value. All of these loans were current at March 31, 2000 and December 31, 1999. The amount of commercial loans on our balance sheet will vary over time as RCF originates and sells

commercial mortgage loans, and will depend on the amount of RCF's warehouse that we finance at Redwood as opposed to at Holdings.

We own residential mortgage loans on real estate properties located throughout the United States. At March 31, 2000 and December 31, 1999, the geographic distribution of our mortgage loan portfolio was as follows: California 26%; Florida 9%; New York 8%; New Jersey 5%; Texas 5%; Georgia 5%. The remaining 42% of our investments were in states located throughout the country, with no one state greater than 5%. At March 31, 2000, our loan portfolio consisted of 4,207 loans, with an average loan size of $313,600. At December 31, 1999, we owned 4,366 loans with an average loan size of $315,700.

At March 31, 2000, the geographic distribution of our commercial mortgage loan portfolio was as follows: California 82%; New York 8%. At December 31, 1999, 100% of our commercial loans were secured by properties located in California. At March 31, 2000, our commercial loan portfolio consisted of 6 loans, with an average loan size of $2.8 million. At December 31, 1999, we owned 3 loans with an average loan size of $2.8 million.

For presentation purposes, the $1.3 billion at March 31, 2000 and the $1.0 billion at December 31, 1999 of residential mortgage loans that are financed with long-term debt in Sequoia trusts are classified as "Mortgage Loans: held-for investment" on our balance sheets and are carried at amortized cost. The remaining residential and commercial mortgage loans that are funded with short-term debt and equity ($30 million at March 31, 2000 and $424 million at December 31, 1999) are classified as "Mortgage Loans: held-for-sale" on our balance sheets and are carried at the lower-of-cost-or-market, with any related market value adjustments recorded through the income statement.

MORTGAGE SECURITIES

At March 31, 2000, 28% of our total mortgage asset portfolio, or $671 million carrying value with a principal value of $660 million, consisted of residential mortgage securities issued and credit-enhanced by Fannie Mae or Freddie Mac and effectively rated "AAA". The majority of these securities, $654 million or 99%, were adjustable-rate securities with the remaining 1% fixed-rate securities. The carrying value of these securities was 101.72% of principal value. At December 31, 1999, we owned $575 million carrying value of these securities, or 24% of our portfolio, at a carrying value of 101.73% of the $565 million principal value.

At March 31, 2000, 12% of our total mortgage asset portfolio, or $284 million carrying and principal value, consisted of adjustable-rate residential mortgage securities issued by private-label security issuers. These securities were credit-enhanced through subordination or other means and were rated "AAA" or "AA". The carrying value of these securities was 100.03% of face value. At December 31, 1999, we owned $291 million carrying value and principal value of these securities, or 12% of our portfolio, at a carrying value of 99.86%.

At March 31, 2000, 2% of our mortgage asset portfolio, or $37 million carrying value with a principal value of $61 million, consisted of lower-rated, residential mortgage securities issued by private-label security issuers. Due to their subordinated status, these securities bore some degree of credit risk and were rated "A" or below. The loans underlying these securities were, with minor exceptions, high-quality loans. The carrying value of these securities, after $0.8 million of credit reserves, was 60.77% of face value. At December 31, 1999, we owned $28 million carrying value of these securities, or 1% of our portfolio, at a carrying value, after credit reserves, of 57.85% of the $49 million face value. We intend to continue to increase our investment in lower-rated, subordinated residential mortgage securities backed by high-quality loans in the future.

At March 31, 2000, 1% of our total mortgage asset portfolio, or $23 million carrying value and principal value, consisted of residential floating-rate mortgage securities rated "AAA" or "AA" which were backed by home equity loans, or "HEL". The carrying value of these securities was 99.50% of face value. At December 31, 1999, we owned $47 million carrying value of these securities, or 2% of our portfolio, at a carrying value of 98.79% of the $48 million principal value.

At March 31, 2000, 1% of our mortgage asset portfolio, or $15 million carrying and principal value, consisted of fixed-rate, private-label mortgage securities. These are commonly called "CMOs". They were rated "AAA" or "AA" and had average lives of 1 to 2 years. The carrying value of these securities was 95.91% of principal value. At December 31, 1999, we owned $16 million carrying value and principal value of these securities, or 1% of our portfolio, at a carrying value of 97.28% of principal value.

At March 31, 2000, 0.5% of our mortgage asset portfolio, or $12 million carrying value with a principal value of $13 million, consisted of fixed-rate, credit-enhanced private-label mortgage securities rated "AA" and backed by residential mortgage loans with loan-to-value ratios in excess of 100%. The carrying value of these securities was 89.88% of face value. At December 31, 1999, we owned $12 million carrying value of these securities, or 0.5% of our portfolio, at a carrying value of 91.00% of the $13 million principal value. The average life of these assets was 7.9 years at March 31, 2000 and 8.2 years at December 31, 1999

At March 31, 2000, 0.3% of our total mortgage asset portfolio, or $6 million carrying and face value, consisted of floating-rate CMO mortgage securities issued by Fannie Mae or Freddie Mac and effectively rated "AAA". The carrying value of these securities was 99.03% of principal value. At December 31, 1998, we owned $6 million carrying value and principal value of these securities, or 0.3% of our portfolio, at a carrying value of 99.88% of the principal value.

At March 31, 2000, 0.003% of our mortgage asset portfolio, or $0.1 million carrying value with no principal value, consisted of interest-only mortgage securities rated "AAA" or "AA". At December 31, 1998, we owned $0.1 million carrying value of these securities, or 0.005% of our portfolio.

For presentation purposes, all of the mortgage securities except for the lower-rated securities are classified as "Mortgage Securities - trading" on our balance sheets and are carried at their estimated fair market value, with any related market value adjustments recorded through the income statement. The $37 million at March 31, 2000 and $28 million at December 31, 1999, of lower-rated mortgage securities are classified as "Mortgage Securities - available-for-sale" on our balance sheets and are also carried at their estimated fair market value. Market value adjustments on these securities, however, are not recorded through the income statement but are included in "accumulated other comprehensive income" in the equity portion of the balance sheet.

CASH

We had $13 million of unrestricted cash at March 31, 2000 and $20 million at year-end 1998.

Sequoia held cash totaling $2 million at December 31, 1999 and $5 million at year-end 1999. In consolidating Sequoia assets on our balance sheet, we reflect this cash as "Restricted Cash" since it will be used for the specific purpose of making payments to Sequoia bondholders and is not available for general corporate purposes.

The amount of liquidity we maintain is only measured in part by the amount of cash we show on our balance sheet at the end of each reporting period. Please refer to the discussion regarding our liquidity beginning on page 41.

INTEREST RATE AGREEMENTS

Our interest rate agreements are carried on our balance sheet at estimated market value, which was $1.2 million at March 31, 2000 and $2.5 million at December 31, 1999. Please see "Note 2. Summary of Significant Accounting Policies", "Note 7. Interest Rate Agreements" and "Note 10. Fair Value of Financial Instruments" in the Notes to Consolidated Financial Statements for more information.

INVESTMENT IN RWT HOLDINGS, INC.

We do not consolidate the assets and liabilities of Holdings on our balance sheet. We reflect the net book value of our investment in one line item on our balance sheet labeled "Investment in RWT Holdings, Inc." We refer you to Holdings' "Consolidated Financial Statements and Notes" and Holdings' "Management's Discussion and Analysis" below for more information on Holdings.

The carrying value of our equity investment in Holdings was $2.8 million at March 31, 2000 and $3.4 million at December 31, 1999.

At March 31, 2000, our assets also included loans to Holdings of $1.4 million and a receivable from Holdings of $0.6 million. We expect that we will continue to provide liquidity to Holdings. At December 31, 1999, loans to Holdings totaled $6.5 million and receivables from Holdings were $0.5 million.

OTHER ASSETS

Our other assets include accrued interest receivables, other receivables, fixed assets, leasehold improvements and prepaid expenses. These totaled $18.2 million at March 31, 2000 and $14.9 million at December 31, 1999.

SHORT-TERM DEBT

Short-term borrowings totaled $0.9 billion at March 31, 2000, or 42% of our total debt. At December 31, 1999, short-term borrowings were $1.3 billion, or 57% of our total debt. The level of short-term borrowings was reduced in the first quarter of 2000 as we issued long-term debt and used the proceeds to reduce short-term debt. We pledge a portion of our mortgage securities portfolio, mortgage loan portfolio, and other assets to secure our short-term debt. Maturities on this debt typically range from one month to one year. The interest rate on most of this debt adjusts monthly to a spread over or under the one-month LIBOR interest rate, with some of it adjusting daily based on the Fed Funds interest rate.

LONG-TERM DEBT

At March 31, 2000, we owned $1.3 billion of residential mortgage loans that were financed with long-term debt through trusts owned by our financing subsidiary, Sequoia. The amount of outstanding Sequoia long-term debt amortizes as the underlying mortgages pay down. As the equity owner of these trusts, we are entitled to distributions of the net earnings of the trusts, which principally consist of the interest income earned from mortgages in each trust less the interest expense of the debt of each trust. Sequoia debt is non-recourse to Redwood Trust. The debt is consolidated on our balance sheet and is reflected as long-term debt, which is carried at historical amortized cost. The original scheduled maturity of this debt was approximately thirty years. Since these debt balances are retired over time as principal payments are received on the underlying mortgages, the expected average life of this debt is two to six years.

At March 31, 2000, 58% of our total debt, or $1.3 billion, was long-term mortgage-backed debt. Of this long-term debt, $577 million had a floating-rate based on one-month LIBOR and $338 million had a floating-rate based on the twelve-month average of the one-year Treasury rate. An additional $368 million was fixed-rate until December 2002 with a floating-rate coupon thereafter; this debt is matched to our portfolio of hybrid fixed/floating residential mortgage loans.

At December 31, 1999, 43% of our total debt, or $945 million, was long-term mortgage-backed debt. Of this long-term debt, $212 million had a floating-rate based on one-month LIBOR, $351 had a floating-rate based on the twelve-month average of the one-year Treasury rate, and $382 million had a fixed-rate until December 2002 with a floating-rate coupon thereafter.

OTHER LIABILITIES

Our other liabilities include accrued interest payable, accrued expenses, and dividends payable. The net balance of these accounts totaled $12.7 million at December 31, 1999 and $11.2 million at December 31, 1999.

STOCKHOLDERS' EQUITY

At March 31, 2000, total equity capital was $210 million, preferred stock equity was $27 million, and reported common equity totaled $183 million, or $20.84 per common share outstanding.

In reporting equity, we mark-to-market all earning assets and interest rate agreements except mortgage loans that were financed to maturity (Sequoia). In accordance with Generally Accepted Accounting Principles ("GAAP"), no liabilities were marked-to-market.

If we had marked-to-market all of our assets and liabilities, total equity capital would have been reported as $212 million at March 31, 2000. After subtracting out the preference value of the preferred stock, common equity on a full mark-to-market basis was $184 million and the net mark-to-market value, or "intrinsic" value, per common share was $20.89.

At December 31, 1999, reported equity capital was $210 million, preferred stock equity was $27 million, and reported common equity was $183 million, or $20.88 per common share outstanding. Mark-to-market common equity was $185 million, or $21.07 intrinsic value per common share.

During the first quarter of 2000, our equity, book value per share, and intrinsic value per share declined slightly after accruing for our $0.35 common dividend. Despite a rising interest rate environment, we had a relatively small net market valuation adjustment on all our assets and liabilities, with the average net decline in our assets being 0.12% of principal value.

RESULTS OF OPERATIONS

Our operating results include all of the reported income of our mortgage finance operations plus, as one line item on our income statement, our share of the after-tax results of operations at Holdings. Detailed results at Holdings are discussed separately below. Please see "RWT Holdings, Inc. - Management Discussion and Analysis of Financial Condition and Results of Operations" commencing on page 44 of this Form 10-Q for further discussion of Holdings' financial position and performance.

INTEREST INCOME

For the quarter ended March 31, 2000, interest income generated by our mortgage finance operations was $43 million. Our portfolio had average earning assets of $2.4 billion and earned an average yield of 7.24%. During this quarter, the average coupon rate, or the cash-earning rate on mortgage principal, was 7.35%. The average value of assets included a net unamortized premium of 0.25% of mortgage principal totaling $6 million. We write off this net premium balance as an expense over the life of our assets. Net premium amortization expense for the quarter was $0.5 million, which reduced our earning asset yield by 0.08%. The annualized prepayment rate on our mortgage assets, which drives the rate at which we write off net premium balances, was 17% Conditional Prepayment Rate ("CPR") during the quarter. Other factors reduced the earning asset yield by 0.03%.

For the preceding quarter (ended December 31, 1999), interest income was $35 million. Our portfolio had average earning assets of $2.0 billion and earned an average yield of 6.88%. The average coupon rate was 7.01%. The average reported value of assets included a 0.33% net premium, or $7 million. Net premium amortization expense was $0.5 million, which reduced earning asset yield by 0.10%. Prepayments during the quarter averaged 19% CPR. Other factors reduced the earning asset yield by 0.03%.

From the fourth quarter of 1999 to the first quarter of 2000, our yield on assets rose by 0.36%, from 6.88% to 7.24%, due to rising short-term interest rates. Most of our mortgage assets are adjustable rate mortgages and the coupons rise as the underlying indices rise. Short-term interest rates have risen by 1.00% to 1.50% since the beginning of 1999, and as our loans reset, our coupon rates are increasing. In addition, prepayment speeds slowed from quarter to quarter, further benefiting our yield. Total interest income increased on a successive quarter basis due to higher yields and a larger average portfolio size in the first quarter of 2000.

For the quarter ended March 31, 1999, interest income was $42 million. Our portfolio had average earning assets of $2.5 billion and earned an average yield of 6.55%. The average coupon rate was 6.99%. The reported value of assets included a 0.71% net premium, or $18 million. Net premium amortization expense was $2.2 million, which reduced earning asset yield by 0.37%. Prepayments during the quarter were 33% CPR. Other factors reduced the earning asset yield by 0.07%.

Total interest income increased from the first quarter of 1999 to the first quarter of 2000, despite a decrease in average portfolio size, as our yields increased. Year-over-year yields increased by 0.69%, from 6.55% in the first quarter of 1999 to 7.24% in the first quarter of 2000. This increase was a result of higher coupon rates on our loans (due to rising short-term interest rates) and slower prepayment speeds.

INTEREST EXPENSE

Interest expense for the quarter ended March 31, 2000 was $35 million. We funded our mortgage portfolio and other assets with an average of $210 million of equity and $2.2 billion of borrowings. We paid an average cost of funds of 6.29% for these borrowings. Short-term debt averaged 56% of total debt and cost us 6.25%. Long-term debt averaged 44% of total debt and cost us 6.32%.

In the previous quarter (the fourth quarter of 1999), interest expense was $28 million. We funded our mortgage portfolio with an average of $219 million of equity and $1.8 billion of borrowings. We paid an average cost of funds of 5.89% for these borrowings. Short-term debt averaged 47% of total debt and cost us 5.68%. Long-term debt averaged 53% of total debt and cost us 6.13%.

Total interest expense was higher in the first quarter of 2000 than in the previous quarter due to an increase in borrowings needed to fund our larger portfolio of assets and due to a higher cost of funds. Our cost of funds rose from quarter to quarter by 0.40%, from 5.89% to 6.29%. This was primarily a result of increases in one-month LIBOR, our main borrowing rate.

For the quarter ended March 31, 1999, interest expense was $33 million. We funded our mortgage portfolio with an average of $250 million of equity and $2.4 billion of borrowings. We paid an average cost of funds of 5.59% for these borrowings. Short-term debt averaged 48% of total debt and cost us 5.12%. Long-term debt averaged 52% of total debt and cost us 6.03%.

The increase in interest expense from year to year is the result of increases in one-month LIBOR and other short-term interest rates during this time. Interest expense increased even though average borrowings declined.

INTEREST RATE AGREEMENTS EXPENSE

We use interest rate agreements in order to strengthen our balance sheet, increase liquidity, and dampen potential earnings volatility. In the third quarter of 1998, as a result of early adopting SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, we elected to classify all of our interest rate agreements as trading instruments. Total interest rate agreement expense (hedging expense) may change over time as the mix of our assets and liabilities changes. We refer you to "Note 7. Interest Rate Agreements" in the Notes to Consolidated Financial Statements for additional details.

Net interest rate agreements expense, before any market value adjustments which are reflected in the Statement of Operations line item "Realized and Unrealized Market Value Gains (Losses)", was $0.4 million for the quarter ended March 31, 2000, $0.5 million for the quarter ended December 31, 1999, and $0.3 million for the quarter ended March 31, 1999. As a percent of average borrowings, net interest rate agreements expense was 0.07% during the first quarter of 2000, 0.11% during the fourth quarter of 1999, and 0.06% during the first quarter of 1999. Net hedging expenses vary as a result of various asset/liability strategies we employ.

NET INTEREST INCOME

Net interest income, which equals interest income less interest expense less interest rate agreements expense, was $8.0 million for the quarter ended March 31, 2000. Our interest rate spread, which equals the yield on earning assets less the cost of funds and hedging, was 0.88%. Our net interest margin, which equals net interest income divided by average assets, was 1.32%. Our net interest income as a percent of average equity was 15.2% during this quarter.

For the fourth quarter of 1999, net interest income was $6.7 million, our interest rate spread was 0.88%, and our net interest margin was 1.28%. Net interest income as a percent of average equity was 12.1%.

Net interest income increased from the fourth quarter of 1999 to the first quarter of 2000 primarily due to an increase in assets as we more fully utilized our capital during the later period. In addition, with higher asset yields, we earned a greater return on that portion of our balance sheet that is funded with equity rather than debt.

For the quarter ended March 31, 1999, net interest income was $7.9 million, our interest rate spread was 0.90%, and our net interest margin was 1.19%. Net interest income as a percent of average equity was 12.7%.

We earned more net interest income in the first quarter of 2000 ($8.0 million) than we did in the first quarter of 1999 ($7.9 million). This is despite the fact that in the earlier period we had more equity ($250 million in 1999 versus $210 million in 2000), more assets ($2.5 billion versus $2.4 billion), and a wider spread (0.90% versus 0.88%). The key factor is asset yield, which was 7.24% in the first quarter of 2000 and 6.55% in the first quarter of 1999. With a higher asset yield, we earn a greater amount on that portion of our balance sheet that is funded with equity rather than debt. As a result of this factor, and better utilization of our equity base, our net interest margin increased from 1.19% in the first quarter of 1999 to 1.32% in the first quarter of 2000 and our net interest income increased despite a smaller balance sheet.

NET UNREALIZED AND REALIZED MARKET VALUE GAINS AND LOSSES

We report many of our mortgage assets and all of our interest rate agreements at market value, with any market valuation adjustments being recognized as a gain or loss in our income statements. Please see "Note 2. Summary of Significant Accounting Policies", "Note 3. Mortgage Assets", and "Note 7. Interest Rate Agreements" in the Notes to Consolidated Financial Statements for more information.

During the first quarter of 2000, our portfolio of assets that were marked-to-market for income statement purposes decreased in estimated market value by $1.2 million. This net loss consisted of $1.1 million market value loss on mortgage assets and $0.1 million market value loss on interest rate agreements. Market values for our mortgage assets fell as interest rates rose. Since most of these assets are adjustable rate, the coupon rates will reset to higher levels. The market values may, in the future, adjust accordingly. Losses in our interest rate agreements portfolio were due to falling volatility and other factors. The net combined market valuation adjustment loss of $1.1 million represents 0.12% of our portfolio of assets that is marked to market.

Total net realized losses on assets during the quarter ended December 31, 1999 were $1.2 million. This net loss consisted of $1.1 million realized losses on mortgage assets and $0.1 million realized losses on interest rate agreements.

The net gain on our portfolio of assets that were marked-to-market in the first quarter of 1999 was $2.2 million. This net gain consisted of $3.0 million market value gain on mortgage assets and other securities and $0.8 million market value loss on interest rate agreements.

As a result of changes in accounting methodologies instituted in 1998, we record both realized and unrealized market value gains and losses on many of our mortgage securities, short-term funded mortgage loans, and interest rate agreements as an item in our income statement. We believe it is beneficial to show shareholders the changes in the market values of our liquid portfolio assets. In addition, our freedom to manage and hedge our portfolio is enhanced by the use of these accounting techniques.

However, very few other financial institutions use these accounting methods; as a result, direct comparisons of our reported earnings with those of other companies on an apples-to-apples basis may be more difficult.

Relatively small changes in portfolio market values can have a significant impact on our reported earnings per share. In our opinion, quarter-to-quarter fluctuations in mark-to-market earnings adjustments are probably of less import than would be a cumulative positive or negative adjustment established over a longer period of time that was large relative to our asset base. For example, our cumulative mark-to-market earnings adjustment since the beginning of 1999 is negative $0.9 million ($0.11 per share). This is a minor amount compared to the size of our portfolio.

Excluding these mark-to-market adjustments, our total earnings were $4.5 million ($0.51 per share) in the first quarter of 2000, negative $4.4 million (negative $0.50 per share) in the fourth quarter of 1999, and $3.7 million ($0.34 per share) in the first quarter of 1999.

PROVISION FOR CREDIT LOSSES

We take credit provision expenses on our mortgage loans held for investment, which are those loans financed with long-term debt and accounted for on an amortized cost basis. During the quarter ended March 31, 2000, credit provisions were $0.1 million. In the quarter ended December 31, 1999, credit provisions were $0.2 million. In the first quarter of 1999, credit provisions were $0.3 million. Credit provisions have decreased over time as the credit performance outlook of our loans continues to improve. We have reduced our provision rates on older loans. We have not incurred any credit losses on our mortgage loans over the last two quarters. However, credit provision expense will increase in the future as we acquire additional mortgage loans that are held for investment and may increase if credit conditions deteriorate. In addition, in the second quarter of 2000 we will begin taking credit provisions for the $384 million of loans underlying our most recent Sequoia long-term debt issuance.

Prior to 1998, we also expensed credit provisions on a portfolio of subordinated mortgage securities. We stopped taking credit provisions on this pool of securities in December 1997 when we restructured and reduced our credit risk on these securities through a resecuritization transaction ("SMFC re-REMIC securities"). The existing reserve for the SMFC re-REMIC securities is $0.7 million at March 31, 2000. Actual realized taxable credit losses against these securities were $0.1 million in the first quarter of 2000, $0.1 million in the fourth quarter of 1999, and $0.1 million in the first quarter of 1999. We continually monitor the credit performance of these assets and will make appropriate changes to our credit provision policy should the need arise.

We have purchased, and intend to continue to purchase, mortgage-backed securities that have risk of credit loss. In acquiring such assets, we project cash flows and resulting yields under a variety of potential loss scenarios as well as other factors (e.g., interest rates, prepayment speeds.) These securities are purchased at a discount, in part because of the credit risk inherent in these assets. We anticipate a yield on such assets after factoring in anticipated losses. Thus, we do not plan to build a credit reserve for such assets, as such losses are already imbedded in the price paid and resulting yields on such assets. The amount of discount amortized into income is based on the projected future cash flows, after credit losses, on such asset. Once acquired, we continue to review the projected losses on each asset. Should projected credit losses change (which can occur for a variety of reasons), the effective yield earned over the remaining life of the asset will change accordingly.

OPERATING EXPENSES

Total operating expenses recognized at Redwood were $2.1 million in the first quarter of 2000, $1.2 million in the fourth quarter of 1999, and $0.7 million in the first quarter of 1999. Due to changes in amounts of expense allocated and recognized between Redwood and Holdings, a more useful number for understanding trends in operating expenses is the total operating expenses of Redwood and Holdings combined. Combined operating expenses were $3.0 million in the first quarter of 2000, $3.6 million in the fourth quarter of 1999, and $4.0 million in the first quarter of 1999.

Some of these expenses were associated with business units that have been closed. Combined operating expenses for on-going operations -- Redwood portfolio lending and RCF -- were $2.8 million in the first quarter of 2000, $1.9 million in the fourth quarter of 1999, and $1.6 million in the first quarter of 1999. We have expanded our residential whole loan operations, increased dividend equivalent rights payments to employees as a result of our increasing dividend, and built origination and sales staff at RCF.

NET EARNINGS FROM MORTGAGE FINANCE OPERATIONS

Net earnings from mortgage finance operations include all revenue and expense items except for the losses from Holdings and preferred dividends. For the quarter ended March 31, 2000, net earnings from mortgage finance operations were $4.5 million, or $0.51 per share. Net earnings from mortgage finance operations were $4.1 million for the quarter ended December 31, 1999, or $0.46 per share. For the quarter ended March 31, 1999, net earnings were $9.0 million, or $0.83 per share.

Net earnings per share increased in the first quarter of 2000 over the fourth quarter of 1999 due to larger portfolio size and higher yields. These gains were partially offset by higher operating expenses. From the first quarter of 1999 to the first quarter of 2000, net earnings per share from mortgage finance operations decreased primarily due to the differences in market valuation adjustments. In the first quarter of 1999, the market value adjustment was positive $2.2 million as compared to a negative $1.2 million market valuation adjustment for the same period in 2000.

EQUITY IN EARNINGS (LOSSES) OF RWT HOLDINGS, INC.

In the first quarter of 2000, our share of the losses generated by Holdings was $0.6 million. This included $0.1 million of net expense for the shut down of Redwood Residential Funding, Inc. We shut down this operation in December 1999 and accounted for many of the costs as a restructuring charge in 1999. However, under GAAP, some operating expenses could not be included in the restructuring charge accrual and are being expensed as incurred in 2000. The remaining loss at Holdings represents losses reported at RCF. The accounting loss at Holdings' subsidiary RCF is not representative of the profitability of our overall commercial operations because it does not include related income recorded at Redwood Trust.

In the fourth quarter of 1999, we recognized losses from Holdings of $9.0 million, which included $6.2 million of restructuring charges at RRF. In the first quarter of 1999, we recognized losses from Holdings of $2.5 million representing start-up expenses from the three business units operating at Holdings at that time.

We refer you to Holdings' "Consolidated Financial Statements and Notes" and Holdings' "Management's Discussion and Analysis" below for more information on

Holdings.

NET INCOME

For the quarter ended March 31, 2000, net income for all of our operations was $4.0 million. After preferred dividends of $0.7 million, net income available to common stockholders was $3.3 million. For the quarter ended December 31, 1999, net losses for all of our operations were $4.9 million. After preferred dividends of $0.7 million, net income available to common stockholders was negative $5.6 million. For the quarter ended March 31, 1999, net income for all of our operations was $6.6 million. After preferred dividends of $0.7 million, net income available to common stockholders was $5.9 million.

EARNINGS PER SHARE

Average diluted common shares outstanding were 8.8 million for the quarter ended March 31, 2000, 9.0 million for the fourth quarter of 1999, and 10.9 million for the first quarter of 1999. Earnings per share were positive $0.37 for first quarter of 2000, negative $0.64 for fourth quarter of 1999, and positive $0.54 for the first quarter of 1999.

Shares outstanding declined over the past year as a result of our common stock repurchase program. We repurchased 2.5 million shares during 1999. We did not acquire any of our own shares in the first quarter of 2000.

DIVIDENDS

We declared common stock dividends of $0.35 per share for the quarter ended March 31, 2000 and $0.25 per share for the quarter ended December 31, 1999. No common stock dividend was declared for the quarter ended March 31, 1999.

We continue to pay $0.755 per share in quarterly preferred stock dividends.

RISK MANAGEMENT

We seek to manage the interest rate, market value, liquidity, prepayment, and credit risks inherent in all financial institutions in a prudent manner designed to insure our longevity. At the same time, we endeavor to provide our shareholders an opportunity to realize an attractive total rate of return through stock ownership in our company.

We do not seek to avoid risk. We do seek, to the best of our ability, to assume risk that can be quantified from historical experience, to actively manage such risk, to earn sufficient compensation to justify the taking of such risks, and to maintain capital levels consistent with the risks we do undertake.

Our strategy for managing some of these risks includes the use of derivative interest rate agreements. Please see "Note 2. Summary of Significant Accounting Policies" for additional discussions on our use of interest rate agreements and their designation as "trading" instruments.

In April and May of 2000, short-term interest rates continued to rise, and debt markets signaled that expectations for further increases in short-term interest rates in 2000 and 2001 are continuing to increase. As we have frequently noted, rapid and sustained increases in short-term interest rates are likely to reduce our net interest income for some period of time following such increases. Such interest rate increases, if they occur, would also likely cause negative mark-to-market adjustments to our reported earnings. Mark-to-market adjustments on all our assets, if negative, would reduce our capital base, book value per share, intrinsic value per share, and our liquidity reserve.

MARKET VALUE RISK

The market value of our assets can fluctuate due to changes in interest rates, prepayment rates, liquidity, financing, supply and demand, credit, and other factors. These fluctuations affect our earnings.

At March 31, 2000, we owned mortgage securities and loans totaling $1.0 billion that we account for on a mark-to-market basis or, in the case of mortgage loans, on a lower-of-cost-or-market basis, for purposes of determining reported earnings. Of these assets, 98% had adjustable-rate coupons and 2% had fixed-rate coupons.

Our interest rate agreements hedging program may offset some asset market value fluctuations due to interest rate changes, or, in some cases, may exacerbate such fluctuations. All of our $3.1 billion in notional amounts of interest rate agreements are marked-to-market for income statement purposes.

Market value fluctuations of assets and interest rate agreements, especially to the extent assets are funded with short-term borrowings, can also affect our access to liquidity.

INTEREST RATE RISK

At March 31, 2000, we owned $2.4 billion of assets and had $2.2 billion of liabilities. The majority of the assets were adjustable-rate, as were a majority of the liabilities.

On average, our cost of funds has the ability to rise or fall more quickly as a result of changes in short-term interest rates than does the earning rate on our assets. In addition, in the case of a large increase in short-term interest rates, periodic and lifetime caps for a portion of our assets could limit increases in interest income. The risk of reduced earnings in a rising interest rate environment may be mitigated to some extent by our interest rate agreements hedging program and by any concurrent slowing of mortgage prepayment rates that may occur.

Hybrid mortgage assets (with fixed-rate coupons for 3 to 7 years and adjustable-rate coupons thereafter) totaled $0.4 billion. We had debt with interest rate reset characteristics matched to the hybrid mortgages totaling $0.4 billion.

Our net income may vary somewhat as the yield curve between one-month interest rates and six- and twelve-month interest rates vary. At March 31, 2000, we effectively owned $0.6 billion of adjustable-rate mortgage assets with interest rates that adjust every six months as a function of six-month LIBOR interest rates funded with equity and debt that had an interest rate that adjusts monthly as a function of one-month LIBOR interest rates.

At March 31, 2000, we owned $0.6 billion of adjustable-rate mortgage assets that adjust monthly as a function of one-month LIBOR interest rates, funded with equity and debt that also adjusts monthly as a function of one-month LIBOR interest rates.

Adjustable-rate assets with earnings rates dependent on one-year U.S. Treasury rates with annual adjustments totaled $0.8 billion at March 31, 2000. These Treasury-based assets were effectively funded with equity and $0.3 billion of liabilities with a cost of funds dependent on one-year U.S. Treasury rates with annual adjustments, and the remainder funded with liabilities with a cost of funds dependent on one month LIBOR rates or the daily Fed Funds rate. To the extent our Treasury-based assets are not funded with Treasury-based liabilities, we incur basis risk. Such risk arises because changes in Treasury rates may differ significantly from changes in the Fed Funds, LIBOR, or Euro-dollar interest rates.

Interest rates and related factors can affect our spread income and our mark to market results. Changes in interest rates also affect prepayment rates (see below) and influence other factors that may affect our results.

LIQUIDITY RISK

Our primary liquidity risk arises from financing long-maturity mortgage assets with short-term debt. Even if the interest rate adjustments of these assets and liabilities are well matched, maturities may not be matched. In addition, trends in the liquidity of the U.S. capital markets in general may affect our ability to rollover short-term debt.

The assets that we pledge to secure short-term borrowings are generally high-quality, liquid assets. As a result, we have not had difficulty refinancing our short-term debt as it matures, even during the financial market liquidity crisis in late 1998. Still, changes in the market values of our assets, in our perceived credit worthiness, in lender over-collaterization requirements, and in the capital markets can impact our access to liquidity.

At March 31, 2000, we had $75 million of highly liquid assets which were unpledged and available to meet margin calls on short-term debt that could be caused by asset value declines or changes in lender over-collateralization requirements. These assets consisted of unrestricted cash and unpledged "AAA" rated mortgage securities. Total available liquidity, including unrestricted cash, equaled 8% of our short-term debt balances.

We currently have two committed lines of short-term financing, one for residential and commercial mortgage loans and one solely for commercial. There are certain restrictions regarding the collateral for which these lines can be used, but they generally allow us to fund whole loan acquisitions for the term of the commitments. There is no assurance that we will be able to renew or wish to renew such lines upon expiration.

We will continue to pursue additional sources of financing in order to enhance the liquidity of our portfolio.

PREPAYMENT RISK

As we receive repayments of mortgage principal, we amortize into income our mortgage premium balances as an expense and our mortgage discount balances as income. Mortgage premium balances arise when we acquire mortgage assets at a price in excess of the principal value of the mortgages. Premium balances are also created when an asset appreciates and is marked-to-market at a price above par. Mortgage discount balances arise when we acquire mortgage assets at a price below the principal value of the mortgages, or when an asset depreciates in market value and is marked-to-market at a price below par. At March 31, 2000, mortgage premium balances were $28.0 million and mortgage discount balances were $22.5 million. Net mortgage premium was $5.5 million. Since the prepayment characteristics of our premium and discount mortgage assets may vary, gross premium levels, net premium levels, and other factors may influence our earnings.

Sequoia's long-term debt has associated deferred bond issuance costs. These capitalized costs are amortized as an expense as the bonds are paid off with mortgage principal receipts. These deferred costs totaled $3.9 million at March 31, 2000. In addition, premium received from the issuance of bonds at prices over principal value is amortized as income as the bond issues pay down. These balances totaled $3.6 million at March 31, 2000. The combined effect of these two items was to increase our effective mortgage-related premium by $0.3 million.

Our net premium at March 31, 2000 for assets and liabilities affected by the rate of mortgage principal receipts was $5.8 million. This net premium equaled 3.2% of common equity. Amortization expense and income will vary as prepayment rates on mortgage assets vary. In addition, changes in prepayment rates will effect the market

value of our assets and our earnings. Changes in the value of our assets, to the extent they are incorporated into the basis of our assets, will also affect future amortization expense.

CREDIT RISK

Our principal credit risk comes from mortgage loans owned by Sequoia, mortgage loans held in portfolio, and our lower-rated mortgage securities. We also have credit risk with counter-parties with whom we do business.

Not including mortgage loans owned by Sequoia, we owned $13 million in residential mortgage loans at March 31, 2000. Of these, $0.3 million were seriously delinquent (delinquent over 90 days, in foreclosure, in bankruptcy, or real estate owned). We also owned $17 million in commercial mortgage loans. These commercial mortgage loans were all current at March 31, 2000.

The four Sequoia trusts owned $1.3 billion in residential mortgage loans at March 31, 2000. Our total credit risk from these trusts is limited to our equity investment in these trusts. These equity investments had a reported value of $41 million, net of related credit reserves, at March 31, 2000. At that time, $5.0 million of the underlying loans, or 0.38%, were seriously delinquent.

At March 31, 2000, we had $5.1 million of credit reserves to provide for potential future credit losses from our mortgage loans held for investment by the Sequoia trusts. The reserve is based upon our assessment of various factors affecting our mortgage loans, including current and projected economic conditions, delinquency status, and credit protection. Total seriously delinquent loans had a loan balance of $5.3 million. To date, our realized credit losses from defaulted residential mortgage loans have averaged 9% of the loan balance of the defaulted loans. Delinquencies, defaults, and loss severities may increase in the future, however, particularly if real estate values decline or the general U.S. economy weakens. We believe our current level of reserve and credit provision policy is reasonable.

At March 31, 2000, we also had $0.7 million credit reserves for our SMFC re-REMIC securities. Our total potential credit exposure from these securities (after this credit reserve) is our net cost basis of $6.6 million.

It should be noted that the establishment of a credit reserve for GAAP purposes does not reduce our taxable income or our dividend payment obligations as a REIT. For taxable income, credit expenses are recognized as incurred, and will have the effect of reducing dividends at that point.

CAPITAL RISK

Our capital levels, and thus our access to borrowings and liquidity, may be tested, particularly if the market value of our assets securing short-term borrowings declines.

Through our risk-adjusted capital policy, we assign a guideline capital adequacy amount, expressed as a guideline equity-to-assets ratio, to each of our mortgage assets. For short-term funded assets, this ratio will fluctuate over time, based on changes in that asset's credit quality, liquidity characteristics, potential for market value fluctuation, interest rate risk, prepayment risk, and the over-collateralization requirements for that asset set by our collateralized short-term lenders. Capital requirements for residential mortgage securities rated below AA and commercial mortgage whole loans are generally higher than for higher-rated residential securities and residential whole loans. Capital requirements for these less-liquid assets depend chiefly on our access to secure funding for these assets, the number of sources of such funding, the funding terms, and on the amount of extra capital we decide to hold on hand to protect against possible liquidity events with these assets. Capital requirements for equity interests in Sequoia generally equal our net investment. The sum of the capital adequacy amounts for all of our mortgage assets is our aggregate guideline capital adequacy amount.

Generally, our total guideline equity-to-assets ratio capital amount has declined over the last few years as we have eliminated some of the risks of short-term debt funding through issuing long-term debt. In the most recent quarters, however, the guideline ratio has increased as we have acquired new types of assets such as commercial mortgage loans and lower-rated mortgage securities. This increase was partially offset in the first quarter of 2000 by the issuance of new long-term debt replacing short-term debt.

We do not expect that our actual capital levels will always exceed the guideline amount. If interest rates were to rise in a significant manner, our capital guideline amount may rise, as the potential interest rate risk of our mortgages would increase, at least on a temporary basis, due to periodic and life caps and slowing prepayment rates. We measure all of our mortgage assets funded with short-term debt at estimated market value for the purpose of making risk-adjusted capital calculations. Our actual capital levels, as determined for the risk-adjusted capital policy, would likely fall as rates increase as the market values of our mortgages, net of mark-to-market gains on hedges, decreased. (Such market value declines may be temporary as well, as future coupon adjustments on adjustable-rate mortgage loans may help to restore some of the lost market value.)

In this circumstance, or any other circumstance in which our actual capital levels decreased below our capital adequacy guideline amount, we would generally cease the acquisition of new mortgage assets until capital balance was restored through prepayments, interest rate changes, or other means. In certain cases prior to a planned equity offering or other circumstances, the Board of Directors has authorized management to acquire mortgage assets in a limited amount beyond the usual constraints of our risk-adjusted capital policy.

Growth in assets and earnings may be limited when our access to new equity capital is limited. Holdings can benefit over time from the re-investment of retained earnings at Holdings. Our mortgage finance operation, however, is generally required to distribute at least 95% of taxable income as dividends due to its REIT status.

INFLATION RISK

Virtually all of our assets and liabilities are financial in nature. As a result, interest rates, changes in interest rates and other factors drive our performance far more than does inflation. Changes in interest rates do not necessarily correlate with inflation rates or changes in inflation rates.

Our financial statements are prepared in accordance with Generally Accepted Accounting Principles and our dividends must equal at least 95% of our net income as calculated for tax purposes. In each case, our activities and balance sheet are measured with reference to historical cost or fair market value without considering inflation.

RWT HOLDINGS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

OVERVIEW

RWT Holdings, Inc. ("Holdings") was incorporated in Delaware in February 1998 and commenced operations on April 1, 1998. Holdings' start-up operations have been funded by Redwood Trust, which has a significant investment in Holdings through the ownership of all of Holdings' non-voting preferred stock, and by Redwood Trust's senior management, who own Holding's voting common stock. We refer you to "Note 1. The Company" in the Notes to the Consolidated Financial Statements of RWT Holdings, Inc. and Subsidiaries for additional information on Holdings' initial capitalization.

Holdings originates commercial mortgage loans for sale to institutional investors through its Redwood Commercial Funding, Inc. ("RCF") subsidiary.

Holdings had two other operating businesses, Redwood Financial Services, Inc. ("RFS") and Redwood Residential Funding ("RRF"). Due to a variety of start-up difficulties with these units, operations were closed at RFS in the third quarter of 1999 and at RRF in the fourth quarter of 1999. These closures resulted in restructuring charges of $8.4 million during the year ended December 31, 1999, and a significant reduction in the headcount and ongoing operating expenses at Holdings.

FINANCIAL CONDITION

At March 31, 2000, Holdings owned $17.6 million of commercial mortgage loans. Holdings also had $3.7 million in cash, $0.2 million of accrued interest receivable, and $0.1 million in other assets, for total assets of $21.6 million. Holdings had commitments to acquire $16.9 million of commercial mortgage loans from Redwood Trust for settlement during the second quarter of 2000. Holdings intends to sell these loans in 2000.

The loans owned by Holdings were funded with short-term borrowings and equity. Short-term debt was $13.9 million, loans from Redwood Trust were $1.4 million, receivables due Redwood Trust totaled $0.6 million, accrued restructuring charges were $2.3 million, and other liabilities totaled $0.6 million, for total liabilities of $18.8 million. Redwood Trust expects to continue to provide liquidity to Holdings, when necessary, during the year 2000. Total equity at March 31, 2000 was $2.9 million.

At December 31, 1999, Holdings owned $4.4 million of residential mortgage loans, $29.6 million of commercial mortgage loans, $2.0 million in cash, and $1.3 million in other assets, for total assets of $39.0 million. Short-term debt totaled $22.4 million, loans from Redwood Trust totaled $6.5 million, receivables due Redwood Trust were $0.5 million, accrued restructuring charges totaled $4.0 million, other liabilities were $2.1 million, and total equity totaled $3.4 million.

RESULTS OF OPERATIONS

For the quarter ended March 31, 2000, net interest income for Holdings was $0.2 million, including interest income of $0.6 million and interest expense of $0.4 million. Holdings also had net gains as a result of commercial and residential mortgage loan sales and market value adjustments of $0.1 million during the first quarter of 2000, resulting in net revenues of $0.3 million. Operating expenses at Holdings totaled $0.9 million for the first three months of 2000. Holdings' net loss for the quarter ended March 31, 2000 was $0.6 million.

In the first quarter of 2000, RCF originated $8 million of commercial mortgage loans and sold $12 million. In the first quarter of 1999, RCF originated $2.9 million of commercial mortgage loans. Total 1999 commercial loan originations were $42 million; total 1999 sales were $11.3 million. At March 31, 2000, commercial mortgage

loans originated or acquired by RCF that had not yet been sold totaled $35 million, of which $17 million were held by Redwood Trust and $18 million were held at Holdings. These loans are all held for future sale.

RCF recorded net revenue for the first three months of 2000 of $0.2 million. Net interest income at RCF does not include interest on loans that RCF has a commitment to purchase from Redwood. For the quarter ended March 31, 2000, direct RCF operating expenses were $0.5 million and operating expenses reimbursable by RCF to Redwood Trust totaled $0.1 million. RCF expects to recognize sale revenues upon the sale of the commercial loan portfolio.

For the quarter ended December 31, 1999, net interest income for Holdings was $0.3 million, including interest income of $2.1 million and interest expenses of $1.8 million. Holdings also had net losses as a result of mortgage asset sales and market value adjustments of $0.9 million during the fourth quarter of 1999, resulting in net revenues of negative $0.6 million. Operating expenses at Holdings totaled $2.3 million for this quarter. Restructuring charges related to the closure of RRF totaled $6.2 million. Holdings' net loss for the quarter ended December 31, 1999 was $9.1 million.

The net operating expense, including on-going operating expenses and restructuring charges, relating to closed operations was $0.9 million in the first quarter of 2000 and $8.5 million in the fourth quarter of 1999. This explains the large improvement in Holdings' results from quarter to quarter. Net losses recognized at Holdings attributable to the on-going operations of RCF were $0.5 million in the first quarter of 2000 and $0.6 million in the fourth quarter of 1999. This does not represent the profit or loss of the combined commercial mortgage operations of Redwood and Holdings, as some of the income on the loans during this period accrued to Redwood.

For the quarter ended March 31, 1999, net interest income for Holdings was $0.2

million, including interest income of $0.5 million and interest expense of $0.3 million. Holdings also had net gains as a result of commercial and residential mortgage loan sales and market value adjustments of $0.6 million during the first quarter of 1999, resulting in net revenues of $0.8 million. Operating expenses at Holdings totaled $3.3 million for the first three months of 1999. Holdings' net loss for the quarter ended March 31, 1999 was $2.5 million.

Holdings' losses in the first quarter of 2000 were much lower than in the first quarter of 1999 due to the shut down of operations at RRF and RFS during 1999. In the first quarter of 1999, these operations were incurring significant operating expenses. These operations were subsequently closed and the net loss associated with these operations in the first quarter of 2000 was minor.

At March 31, 2000, Holdings had net operating loss carryforwards of approximately $21 million for federal tax purposes and $11 million for state income tax purposes. The federal carryforwards expire through 2018 and the state carryforwards expire through 2004.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

At March 31, 2000, there were no pending legal proceedings to which the Company as a party or of which any of its property was subject.

Item 2. Changes in Securities

Not applicable

Item 3. Defaults Upon Senior Securities

Not applicable

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

Not applicable

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit 3.3.2 - Amended and Restated Bylaws, amended March 9, 2000 (Incorporated by reference to the Form 8-K filed March 14, 2000 referred to below).

Exhibit 4.4.3 - Pooling and Servicing Agreement, dated as of March 1, 2000, among Merrill Lynch Mortgage Investors, Inc., Sequoia Mortgage Funding Corporation, Merrill Lynch Credit Corporation and Norwest Bank Minnesota, N.A. (Incorporated by reference to the Form 8-K filed by Merrill Lynch Mortgage Investors, Inc. (333-81429) on April 4, 2000).

Exhibit 10.14 - Employment Agreement, dated March 13, 2000, between the Company and Harold F. Zagunis.

Exhibit 11.1 to Part I - Computation of Earnings Per Share for the three months ended March 31, 2000 and March 31, 1999.

Exhibit 27 - Financial Data Schedule

(b) Reports

Form 8-K filed by the Company on March 14, 2000, attaching Amended and Restated Bylaws, amended March 9, 2000.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

REDWOOD TRUST, INC.

Dated: May 10, 2000 By: /s/ Douglas B. Hansen

Douglas B. Hansen
President
(authorized officer of registrant)

Dated: May 10, 2000 By: /s/ Harold F. Zagunis

Harold F. Zagunis
Vice President, Chief Financial Officer
Secretary, Treasurer and Controller
(principal financial and accounting officer)

REDWOOD TRUST, INC.
INDEX TO EXHIBIT

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EXHIBIT 10.14

EMPLOYMENT AGREEMENT

This Employment Agreement (hereinafter referred to as "Agreement") is entered into this 13th day of March, 2000, by Harold Zagunis (hereinafter referred to as "Executive") and Redwood Trust, Inc., a Maryland Corporation located in Mill Valley, California (hereinafter referred to as the "Company") (hereinafter jointly referred to as the "parties") who wish to enter into this Agreement, superseding and replacing terms and conditions that previously existed.

WHEREAS, the Company wishes to employ Executive under the terms and conditions set forth below, and Executive wishes to accept such employment under the terms and conditions set forth below, and

WHEREAS, Executive acknowledges that Executive has read and is fully familiar with the terms of this Agreement, that Executive has had a reasonable opportunity to consider this Agreement and to seek legal counsel,

NOW, THEREFORE, for and in consideration of the above stated premises, and the mutual promises and agreements set forth herein, the parties agree as follows:

1. EMPLOYMENT AGREEMENT

The Company hereby employs Executive, and Executive hereby accepts employment with the Company, under the terms and conditions described in this Agreement. This Agreement shall take effect on March 13, 2000 and shall remain in effect subject to being terminated pursuant to Section 5 of this Agreement.

2. DUTIES

a. RESPONSIBILITIES

Subject to the terms of this Agreement, Executive is hereby employed to perform services and function as Vice-President, reporting to Doug Hansen, the President of Redwood Trust, Inc. (hereinafter referred to as "President"). The essential functions of Executive's position are more particularly set forth in Appendix A hereto, which is incorporated herein by reference. The President may, from time to time, at his sole discretion, modify, reassign and/or augment Executive's responsibilities. Any such modification, reassignment or augmentation of responsibilities shall be in writing. Executive fully and completely understands and accepts the nature and extent of Executive's obligations and duties under this Agreement.

b. LOYAL AND FULL-TIME PERFORMANCE OF DUTIES

Executive shall faithfully devote the whole of his professional time, attention, energies and best efforts to the performance of Executive's duties and shall not, either directly or indirectly, alone or in partnership, consult with, advise, work for or have any interest in any other business or enterprise that directly or indirectly compete with the Company during his employment hereunder. Any modification of this subparagraph 2(b) shall be made only by an agreement in writing signed by Executive and the Company.

c. COMPANY POLICIES

Executive agrees to abide by the Company's rules, regulations, policies and practices, written and unwritten, as they may from time to time be adopted or modified and issued by the Company at its sole discretion. The Company's written rules, issued policies, practices and procedures shall be binding on Executive unless superseded by or in conflict with this Agreement, in which case this Agreement shall govern.

3. COMPENSATION

a. BASE COMPENSATION RATE

As consideration for the services and covenants described in this Agreement, the Company agrees to pay Executive a 2000 and 2001 base annual salary of Two Hundred Thousand Dollars ($200,000), subject to payroll deductions required by law or authorized by Executive. Payments shall be made in equal installments in accordance with the Company's procedures, as from time to time may be amended at its sole discretion, regarding the payment of compensation to management personnel.

b. INCENTIVE BONUS

Executive may, at the President's prerogative, be eligible for consideration to receive an incentive bonus based upon a percentage of his base salary. For year 2000 and 2001, the Executive's target incentive bonus will be 50% of eligible annual base salary, and such discretionary bonus payment will depend on overall Company performance and other factors. For year 2000 and 2001, the Executive will also be eligible for an additional incentive bonus in the range of $0 to the maximum of $25,000, and such discretionary bonus payment will be based on the Executive's demonstrated leadership abilities and effectiveness as senior manager and leader of the Company, with specific performance criteria to be determined by the President. The issuance (if any), timing and amount of any incentive bonus shall be within the sole discretion of the President. Executive's eligibility to receive any such incentive bonus shall be expressly conditioned on, among other

things, Executive remaining employed with the Company up through any designated distribution date set by the President.

c. ANNUAL REVIEW

Executive's performance shall be reviewed at least annually. The performance evaluations shall consider and assess Executive's performance of his duties and responsibilities, the timely accomplishment of existing performance objectives, his level of efficiency and overall effectiveness and/or other factors or criteria that the Company, in its sole discretion, may deem relevant. The frequency of performance evaluations may vary depending upon, among other things, length of service, past performance, changes in job duties or performance levels. Positive performance evaluations do not guarantee salary increases or incentive bonuses. Salary increases and incentive bonus awards are solely within the discretion of the Company and may depend upon many factors other than Executive's performance.

d. BENEFITS PLANS

Executive shall be entitled to participate in any benefit adopted from time to time by the Company for the benefit generally of its executive employees, and Executive shall be entitled to receive such other fringe benefits as may be granted to him from time to time by the President.

The Executive shall be entitled to participate in any benefit plans relating to paid time off, stock options, stock purchases, retirement, thrift, life insurance, medical coverage, education or other employee benefits that may, from time to time, be made available generally to other employees of the Company, subject to and in accordance with any provisions and restrictions (including applicable waiting periods) specified in such plans.

4. BUSINESS EXPENSES

The Company shall pay Executive's reasonable and necessary business expenses, incurred by Executive on behalf of the Company, in accordance with the customary and usual practice and policies of the Company as may be adopted or amended from time to time in the Company's sole discretion. If Executive incurs business expenses hereunder, he shall submit to the Company a request for reimbursement together with supporting documentation and receipts in accordance with Company policy. Reimbursement for legitimate business expenses shall be made within a reasonable period of time.

5. TERMINATION AND SEVERANCE PAY

a. TERMINATION FOR CAUSE BY THE COMPANY

Executive's employment hereunder may be terminated immediately by the Company for cause upon occurrence of any of the following:

1. Gross negligence or willful misconduct by Executive in

the performance of his duties hereunder;

2. The habitual or repeated neglect of his duties by Executive;

3. A material breach of this Agreement;

4. Executive's death;

5. Executive's permanent total disability, which shall be defined as Executive being unable to adequately perform the essential functions of their current position, as defined by the Company, due to a medically determinable mental or physical illness or injury which can be expected to result in death or can be reasonably expected to last for a continuous period of not less than six (6) months. Any determination of such inability to perform shall be made only by the Company based on professional medical advice provided by a medical professional mutually agreeable to Executive, or his representative, and the Company;

6. Conviction of a felony;

7. Theft or embezzlement, or attempted theft or embezzlement, of money or tangible or intangible assets or property of the Company or its employees, customers, clients, etc.;

8. Any act of moral turpitude by Executive injurious to the interest, property, operations, business or reputation of the Company;

9. Unauthorized use or disclosure of trade secrets or confidential or proprietary information pertaining to Company business.

Upon the Company learning of a material breach of this Agreement by Executive, the Company may permit Executive a 30-day period to cure such a breach if, in the judgment of the Company, the breach may be cured and it is in the Company's best interest to allow an opportunity to do so. Any termination under this Section shall be without prejudice as to any other remedy to which the Company may be entitled either under this Agreement or at law. Upon such termination, the Company shall have no further obligations to make payments of any kind to Executive, except as required by law.

b. TERMINATION WITHOUT CAUSE BY THE COMPANY

The Company may terminate Executive's employment hereunder at any time without cause upon 30 days written notice to Executive or pay in lieu thereof.

c. TERMINATION BY EXECUTIVE

Executive may terminate his employment with the Company under this Agreement for any reason by giving 30 days written notice to the Company.

The Executive shall also have the right to terminate this Agreement for good reason. "Good Reason" shall mean the occurrence, without Executive's express written consent of the following:

(i) Failure by the Company to make payment to Executive as required by this Agreement;

(ii) Change of Control - Change of control is defined in this Agreement as the sale of all or substantially all of the assets of the Company or the transfer of all or substantially all of the management control or ownership of the Company to an entity which is not affiliated with the Company. In the event that a Change of Control occurs and Executive thereafter resigns after three months but within six (6) months of the Change of Control for the stated reason(s) that the Company (or its successor) have reduced his base salary or caused a substantial and material diminution of his responsibilities as Vice-President.

(iii) A significant reduction in Executive's responsibilities or base salary, that is not accompanied or caused by a Change of Control, except as may result in connection with the Company's termination of Executive's employment or accommodation of a disability of the Executive, in accordance with this Agreement.

d. NO SEVERANCE PAYMENTS/INCENTIVE BONUS

No severance payment shall be payable to Executive in the event of termination of this Agreement by the Company for cause, due to the Executive's death or in the event Executive terminates his employment without Good Reason. Executive shall not be entitled to any incentive bonus, or any portion of such bonus, where the distribution date as established by the President is subsequent to the date of termination; eligibility for any such incentive bonus is conditioned upon Executive actively working until the established distribution date.

6. SEVERANCE.

If Executive's employment is terminated (i) by the Company without cause (Section 5b, above), or (ii) by the Executive for Good Reason (Section 5c), and Executive signs a release discharging the Company and all its respective officers, agents, directors, supervisors, employees, representatives and their successors and assigns and all persons acting by, through, under, or in concert with any of them from any and all charges, complaints, claims, and liabilities of any kind of nature whatsoever, known or unknown, suspected or unsuspected, arising out of Executive's Employment and/or this Agreement, Executive shall be entitled to the following benefits:

a. SEVERANCE PAYMENT

Severance payment shall be the greater of (i) fifty percent (50%) of current year annual base salary; or (ii) the equivalent gross amount of fifty percent (50%) of 1999 annual base salary plus 1999 incentive bonus, total of which is equivalent to One Hundred Six Thousand Two Hundred and Thirty-two Dollars ($106,232). Severance payment shall be paid in six equal installments over a six-month period, subject to the Executive executing a Release of all claims; provided, should Executive violate any provision of Section 7 and/or 8 of this Agreement, such payments shall immediately terminate and Executive shall be entitled to no further monies or benefits. Calculation of severance payment excludes any and all DERs (Dividend Equivalent Rights payments as noted in the Company's standard ISO or non-qualified stock option grant agreement). In addition, Executive shall not be eligible to receive DER payments for which the record date for the dividend is subsequent to the Executive's termination date. Severance eligibility is expressly conditioned and dependent upon, Executive's compliance with the terms and conditions of Sections 7 and 8 of this Agreement.

b. CONTINUATION OF FRINGE BENEFITS

Continued health benefits as set forth in Section 3(d) as if Executive's employment under the Agreement had not been terminated until the earlier of the following: (i) severance obligations owed by the Company to Executive, as provided under Section 6(a), expire or terminate, or (ii) Executive shall find alternative employment (Executive shall be required to notify the Company immediately upon obtaining alternative employment). Notwithstanding the foregoing, should Executive not be coverable under the Company plans, or should the Company exercise its prerogative to reduce and/or terminate such benefits to Executive, the Company may instead compensate Executive in lieu of his receiving coverage by paying Executive directly, for each month that Executive would be eligible to receive such benefits, the monthly dollar amount the Company would have expended for premiums for such benefits for the Executive, and for any dependents or beneficiaries covered at the time of termination, less any monthly amount Executive would have paid had he remained employed.

c. CHANGE OF CONTROL REQUIREMENTS

Notwithstanding the provisions of Paragraph 5(c), Executive shall not be eligible for any severance if: a) Executive resigns within six (6) months following a Change of Control and there has been no reduction of his base salary or substantial and material diminution of his responsibilities as Vice-President following the Change of Control; or b) Executive resigns within three months of a Change of Control even if their has been a reduction of his base salary or substantial and material diminution of his responsibilities as Vice-President following the Change of Control.

7. COMPETITION, CONFIDENTIALITY, TRADE SECRETS AND INVENTIONS.

a. NON-COMPETITION

During the term of this contract, and for six months following the termination of this Agreement, Executive shall not engage in any other business, commercial or professional activity or capacity that is or may be competitive with the Company or a subsidiary or affiliate of the Company that might create a conflict of interest with the Company, or that otherwise might interfere directly or indirectly with the business of the Company, without the prior written consent of the Doug Hansen or the President of the Company. Executive further agrees that during this time he shall not solicit any employee of the Company, directly or indirectly, to leave the employ of the Company.

b. DUTY TO AVOID CONFLICT OF INTEREST

During his employment by the Company, Executive agrees not to engage or participate in, directly or indirectly, any activities in conflict with the best interests of the Company. The Company shall be the final decision-maker with regard to any conflict of interest issue.

c. CONFIDENTIAL AND PROPRIETARY INFORMATION

(1) It is hereby acknowledged that Executive has and shall gain knowledge of trade secrets and confidential information owned by or related to the Company and/or its affiliates including but not limited to the following: (i) the names, lists, buying habits and practices of their customers, clients or vendors, (ii) their marketing and related information, (iii) relationships between them and the persons and entities with whom and which they have contracted, (iv) their products, designs, software, developments, improvements and methods of operation, (v) their financial condition, profit performance and financial requirements, (vi) the compensation paid to their employees, (vii) business plans and the information contained therein, and (viii) all other confidential information of, about or

concerning the Company, the manner of operation of the Company and other confidential data of any kind, nature or description relating to the Company (collectively the "Confidential Information"). Confidential Information does not include information which (ix) is or becomes generally available to the public other than as a result of a disclosure by Executive; or (x) becomes available to Executive on a non-confidential basis after the termination or expiration of Executive's obligations under this Agreement from a source other than the Company, provided that such source is not bound by a confidentiality agreement with or other contractual, legal or fiduciary obligation of confidentiality to the Company or any other party with respect to such information; or (xi) is independently developed after the termination or expiration of Executive's obligations under this agreement without reference to the Confidential Information, provided such independent development can reasonably be proven by Executive by written records.

(2) The parties hereby acknowledge that the Confidential Information constitutes important, unique, material and confidential trade secrets which affect the successful activities of the Company, and constitute a substantial part of the assets and goodwill of the Company. In view of the foregoing, Executive agrees that he will not at any time whether during or after the term of this Agreement, except as required in the course of Executive's employment by Company and at its direction and for its sole benefit, in any fashion, form or

manner, directly or indirectly (i) use or divulge, disclose, communicate or provide or permit access to any person, firm, partnership, corporation or other entity, any Confidential Information of any kind, nature or description, or (ii) remove from Company's premises any notes or records relating thereto, or copies or facsimiles thereof (whether made by electronic, electrical, magnetic, optical, laser, acoustic or other means).

(3) Promptly upon the request of Company, and immediately upon the termination of Executive's employment, Executive shall not transfer and shall deliver to Company all Confidential Information, and other property belonging to the Company, including all copies thereof, in the possession of Executive.

(4) Executive represents that the performance of all the terms of this Agreement will not conflict with, and will not breach, any other invention assignment agreement, confidentiality agreement, employment agreement or non-competition agreement to which Executive is or has been a party. To the extent that Executive has confidential information or

materials of any former employer, Executive acknowledges that the Company has directed Executive to not disclose such confidential information or materials to the Company or any of its employees, and that the Company prohibits Executive from using said confidential information or materials in any work that Executive may perform for the Company. Executive agrees that Executive will not bring with Executive to the Company, and will not use or disclose any confidential, proprietary information, or trade secrets acquired by Executive prior to his employment with the Company. Executive will not disclose to the Company or any of its employees, or induce the Company or any of its employees to use, any confidential or proprietary information or material belonging to any previous employers or others, nor will Executive bring to the Company or use in connection with Executive's work for the Company copies of any software, computer files, or any other copyrighted or trademarked materials except those owned by or licensed to the Company. Executive represents that he is not a party to any other agreement that will interfere with his full compliance with this Agreement. Executive further agrees not to enter into any agreement, whether written or oral, in conflict with the provisions of this Agreement.

d. INVENTIONS

Any and all inventions, discoveries or improvements that Executive has conceived or made or may conceive or make during the period of employment relating to or in any way pertaining to or connected with the systems, products, computer programs, software, apparatus or methods employed, manufactured or constructed by the Company or to systems, products, apparatus or methods with respect to which the Company engages in, requests or anticipates research or development, shall be promptly and fully disclosed and described by Executive to the Company and shall be the sole and exclusive property of the Company, and Executive shall assign, and hereby does assign to the Company Executive's entire right, title and interest in and to all such inventions, discoveries or improvements as well as any modifications or improvements thereto that may be made. The parties agree that any inventions, discoveries or ideas that Executive has created or possesses prior to his employment by the Company are specified in Appendix B attached to this Agreement and will not be considered to be the property of the Company.

The obligations outlined in this Section 7, except for the requirements as to disclosure, do not apply to any invention that qualifies fully under California Labor Code section 2870 or to any rights Executive may have acquired in connection with an invention, discovery or improvement that was developed entirely on Executive's own time for which no equipment, supplies, facilities or trade secret information of the Company was used and (a) that does not relate directly or indirectly to the business of the Company or to the Company's actual or demonstrable anticipated research or development, or (b) that does not result from any work performed by Executive for the Company.

e. BREACH

It is expressly agreed that each breach of this Section 7 is a distinct and material breach of this Agreement and that solely a monetary remedy would be inadequate, impracticable and extremely difficult to prove, and that each such breach would cause the Company irreparable harm. It is further agreed that, in addition to any and all remedies available at law or equity (including money damages), either party shall be entitled to temporary and permanent injunctive relief to enforce the provisions of this Section, without the necessity of proving actual damages. It is further agreed that the either party shall be entitled to seek such equitable relief in any forum, including a court of law, notwithstanding the provisions of Section 8 and the Alternative Dispute Resolution Agreement incorporated therein. Either party may pursue any of the remedies described herein concurrently or consecutively in any order as to any such breach or violation, and the pursuit of one of such remedies at any time will not be deemed an election of remedies or waiver of the right to pursue any of the other such remedies. Any breach of this Section shall immediately terminate any obligations by the Company to provide Executive with severance and continued benefits pursuant to Section 6 of this Agreement.

f. UNENFORCEABILITY

Should any portion of this Section 7 be deemed unenforceable because of its scope, duration or effect, and only in such event, then the parties expressly consent and agree to such limitation on scope, duration or effect as may be finally adjudicated as enforceable, to give this Section its maximum permissible scope, duration and effect.

8. SUBMISSION TO ARBITRATION

In the event there is any dispute arising out of Executive's employment, the termination of that employment, or arising out of this Agreement, the Company and Executive agree to submit such dispute, except as to those matters specifically exempt per Section 7, to binding arbitration in accordance with the terms of the Alternative Dispute Agreement set forth in Appendix C to this Agreement and incorporated herein.

9. GOVERNING LAW

This Agreement shall be construed in accordance with and governed by the laws of the State of California, excluding its choice of law rules.

10. INTERPRETATION

This Agreement shall be interpreted in accordance with the plain meaning of its terms and not strictly for or against either party.

11. ENTIRE AGREEMENT

This Agreement, together with Appendices A, B, C and D, embodies the complete agreement and understanding of the parties related to Executive's employment by the Company, superseding any and all other prior or contemporaneous oral or written agreements between the parties hereto with respect to the employment of Executive by the Company, and contains all of the covenants and agreements of any kind whatsoever between the parties with respect to such employment. Each party acknowledges that no representations, inducements, promises or agreements, whether oral or written, express or implied, have been made by either party or anyone acting on behalf of a party, that are not incorporated herein and that no other agreement or promise not contained herein shall be valid or binding. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

12. MODIFICATION

This Agreement may be amended only by an agreement in writing signed by the parties hereto.

13. WAIVER

Failure to insist upon strict compliance with any of the terms, covenants, or conditions hereof shall not be deemed a waiver of such term, covenant, or condition, nor shall any waiver or relinquishment of, or failure to insist upon strict compliance with, any right or power hereunder at any one or more times be deemed a waiver or relinquishment of such right or power at any other time or times. This Agreement shall not be modified in any respect except by a writing executed by the parties.

14. INVALIDITY

Each term, clause and provision of this Agreement is separate and independent, and should any term, clause or provision of this Agreement be found to be invalid or unenforceable, the validity of the remaining terms, clauses, and provisions shall not be affected.

15. NOTICES

Any notice provided for in this Agreement shall be in writing and shall be either personally delivered, mailed first class mail (postage prepaid), or sent by facsimile or reputable overnight courier service (charges prepaid) to the recipient at the following addresses (or at such address as the recipient party has specified by prior written notice to the sending party):

To the Company: Doug Hansen
President

Redwood Trust, Inc.,
591 Redwood Highway, Suite 3100,
Mill Valley, CA 94941

To Executive: Harold Zagunis
408 San Andreas Drive
Novato, CA 94945

Each party shall be responsible for keeping such party's address current. Notices shall be deemed to have been given hereunder when delivered personally, three business days after deposit in the U.S. mail, on the date of delivery by facsimile (if transmitted before 5:00 p.m. local time), and/or one day after deposit with a reputable overnight courier service.

16. VOLUNTARY AGREEMENT

Executive and the Company represent and agree that each has reviewed all aspects of this Agreement, has carefully read and fully understands all provisions of this Agreement, and is voluntarily entering into this Agreement. Each party represents and agrees that such party has had the opportunity to review any and all aspects of this Agreement with the legal, tax or other advisor(s) of such party's choice before executing this Agreement.

17. SUCCESSORS AND ASSIGNS

This Agreement shall be binding upon and inure to the benefit of and shall be enforceable against Executive's heirs, beneficiaries and legal representatives. It is agreed that the rights and obligations of Executive may not be delegated or assigned except as specifically set forth in this Agreement. In the event of a sale of all or substantially all of the Company's assets, including the stock of the Company, or consolidation or merger of the Company with or into another corporation or entity or individual, the Company may assign its rights and obligations under this Agreement to its successor-in-interest, and such successor-in-interest shall be deemed to have acquired all rights and assumed all obligations of the Company hereunder, including those set forth in Section 7 of this Agreement.

18. COUNTERPARTS

This Agreement may be executed in several counterparts, each of which shall be deemed to be an original but all of which together will constitute one and the same instrument.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day, month and year first above written.

DATED: March 13, 2000 /s/ Harold Zagunis
Harold Zagunis

REDWOOD TRUST, INC.

DATED: March 13, 2000 By: /s/ Doug Hansen
Doug Hansen

Title: President

APPENDIX A

ESSENTIAL RESPONSIBILITIES

APPENDIX B

PRIOR INVENTIONS

APPENDIX C

ALTERNATIVE DISPUTE RESOLUTION POLICY

I. AGREEMENT TO ARBITRATE

In the event that any employment dispute arises between Redwood Trust, Inc. ("Company") and Harold Zagunis ("Executive"), the parties involved will make all efforts to resolve any such dispute through informal means. If these informal attempts at resolution fail and if the dispute arises out of or is related to the parties' Employment Agreement, the termination of Executive's employment or alleged unlawful discrimination, including but not limited to unlawful harassment, the Company and Executive will submit the dispute to final and binding arbitration, except as set forth in Section 7 of the Employment Agreement.

The parties expressly understand and agree that arbitration is the exclusive remedy for all such arbitrable disputes; with respect to such disputes, no other action may be brought in court or any other forum (except actions to compel arbitration hereunder). THIS ALTERNATIVE DISPUTE RESOLUTION ("ADR") AGREEMENT IS A WAIVER OF THE PARTIES' RIGHTS TO A CIVIL COURT ACTION FOR A DISPUTE RELATING TO BREACH OF THE PARTIES' EMPLOYMENT AGREEMENT, TERMINATION OF THAT EMPLOYMENT OR ALLEGED UNLAWFUL DISCRIMINATION, WHICH INCLUDES RETALIATION OR SEXUAL OR OTHER UNLAWFUL HARASSMENT; ONLY AN ARBITRATOR, NOT A JUDGE OR JURY, WILL DECIDE THE DISPUTE.

To the fullest extent permitted by the law of the jurisdiction, employment disputes arising out of or related to termination of employment or alleged unlawful discrimination, including retaliation or sexual or other unlawful harassment, shall include, but not be limited to, the following: alleged violations of federal, state and/or local constitutions, statutes or regulations; claims based on any purported breach of contractual obligation, including breach of the covenant of good faith and fair dealing; and claims based on any purported breach of duty arising in tort, including violations of public policy. Disputes related to workers' compensation and unemployment insurance is not arbitrable hereunder. Claims for benefits covered by a separate benefit plan that provides for arbitration are not covered by this ADR Agreement. Also, nothing in Employment Agreement or in the ADR Policy shall be construed as precluding Employee from filing a charge with the Equal Employment Opportunity Commission ("EEOC"), the National Labor

Relations Board ("NLRB") or other federal, state or local agencies, seeking administrative assistance in resolving claims. Claims that are filed with or are being processed by the EEOC or that are brought under Title VII of the Civil Rights Act of 1964, as amended ("Title VII), are not arbitrable under this Agreement, except that the

parties may agree in writing to do so with respect to each such dispute that may arise. The EEOC is the federal agency which enforces laws prohibiting employment discrimination. Title VII is the federal statute which prohibits discrimination on the basis of race, color, religion, sex, national origin, retaliation.

II. REQUEST FOR ARBITRATION

A. ATTEMPT AT INFORMAL RESOLUTION OF DISPUTES

Prior to submission of any dispute to arbitration, Executive and the Company shall attempt to resolve the dispute informally as set forth below.

Executive and the Company will select a mediator from a list provided by the Federal Mediation and Conciliation Service or other similar agency who will assist the parties in attempting to reach a settlement of the dispute. The mediator may make settlement suggestions to the parties but shall not have the power to impose a settlement upon them. If the dispute is resolved in mediation, the matter shall be deemed closed. If the dispute is not resolved in mediation and goes to the next step (binding arbitration), any proposals or compromises suggested by either of the parties or the mediator shall not be referred to in or have any bearing on the arbitration procedure. The mediator cannot also serve as the arbitrator in the subsequent proceeding unless all parties expressly agree in writing.

B. ARBITRATION PROCEDURES

The party desiring arbitration, whether Executive or the Company, must submit a "Request For Arbitration" in writing to the other party within the time period required by the law that applies to the claim under the applicable statute of limitations. If the "Request for Arbitration" is not submitted in accordance with the aforementioned time limitations, the party failing to do so will not be able to bring his claims to this or any other forum. The requesting party may use a "Request for Arbitration" form supplied by the Company (Appendix D). Alternatively, the requesting party may create a "Request For Arbitration" form that, unless otherwise required by law, clearly states "Request For Arbitration" at the beginning of the first page and includes the following information:

1. A factual description of the dispute in sufficient detail to advise the other party of the nature of the dispute;

2. The date when the dispute first arose;

3. The names, work locations and telephone numbers of any individuals, including employees or supervisors, with knowledge of the dispute; and

4. The relief requested by requesting party.

The responding party may submit counterclaim(s) in accordance with applicable law.

C. SELECTION OF THE ARBITRATOR

All disputes will be resolved by a single Arbitrator, the Arbitrator will be mutually selected by the Company and the Executive. If the parties cannot agree on an Arbitrator, then a list of seven (7) arbitrators, experienced in employment matters, shall be provided by the Federal Mediation and Conciliation Service. The Arbitrator will be selected by the parties who will alternately strike names from the list. The last name remaining on the list will be the Arbitrator selected to resolve the dispute. Upon selection, the Arbitrator shall set an appropriate time, date and place for the arbitration, after conferring with the parties to the dispute.

D. THE ARBITRATOR'S AUTHORITY

The Arbitrator shall have the powers enumerated below:

1. Ruling on motions regarding discovery, and ruling on procedural

and evidentiary issues arising during the arbitration.

2. Ruling on motions to dismiss and/or motions for summary judgment applying the standards governing such motions under the Federal Rules of Civil Procedure.

3. Issuing protective orders on the motion of any party or third party witness. Such protective orders may include, but are not limited to, sealing the record of the arbitration, in whole or in part (including discovery proceedings and motions, transcripts, and the decision and award), to protect the privacy or other constitutional or statutory rights of parties and/or witnesses.

4. Determining only the issue(s) submitted to him/her. The issue(s) must be identifiable in the "Request For Arbitration" or counterclaim(s). Except as required by law, any issue(s) not identifiable in those documents is outside the scope of the Arbitrator's jurisdiction and any award involving such issue(s), upon motion by a party, shall be vacated.

E. DISCOVERY

The discovery process shall proceed and be governed, consistent with the standards of the Federal Rules of Civil Procedure, as follows:

1. Unless otherwise required by law, parties may obtain discovery by any of the following methods:

    a. Depositions of non-expert witnesses upon oral examination, three (3) per side as of right, with more permitted if leave is obtained from the Arbitrator;

    b. Written interrogatories, up to a maximum combined total of twenty (20), with the responding party having twenty (20) days to respond;

    c. Request for production of documents or things or permission to enter upon land or other property for inspection, with the responding party having twenty (20) days to produce the documents and allow entry or to file objections to the request;

    d. Physical and mental examination, in accordance with Federal Rule of Civil Procedure 35(a); and

    e. Any motion to compel production, answers to interrogatories or entry onto land or property must be made to the Arbitrator within fifteen (15) days of receipt of objections.

2. To the extent permitted by the Federal Arbitration Act or applicable California law, each party shall have the right to subpoena witnesses and documents during discovery and for the arbitration.

3. All discovery requests shall be submitted no less than sixty (60) days before the hearing date.

4. The scope of discoverable evidence shall be in accordance with Federal Rule of Civil Procedure 26(b) (1).

5. The Arbitrator shall have the power to enforce the aforementioned discovery rights and obligations by the imposition of the same terms, conditions, consequences, liabilities, sanctions and penalties as can or may be imposed in like circumstances in a civil action by a federal court under the Federal Rules of Civil Procedure, except the power to order the arrest or imprisonment of a person.

F. HEARING PROCEDURE

The hearing shall be held at a location mutually agreed upon by the parties, or as determined by the Arbitrator in the absence of an agreement, and shall proceed according to the American Arbitration Association's "National Rules for the Resolution of Employment Disputes" as amended and effective June 1, 1997, with the following amendments:

    1. The Arbitrator shall rule at the outset of the arbitration on procedural issues that bear on whether the arbitration is allowed to proceed.

2. Each party has the burden of proving each element of its claims or counterclaims, and each party has the burden of proving any of its affirmative defenses.

3. In addition to, or in lieu of closing argument, either party shall have the right to present a post-hearing brief, and the due date for exchanging any post-hearing briefs shall be mutually agreed on by the parties and the Arbitrator, or determined by the Arbitrator in the absence of agreement.

G. SUBSTANTIVE LAW

1. The parties agree that they will be afforded the identical legal equitable and statutory remedies as would be afforded them were they to bring an action in a court of competent jurisdiction.

2. The applicable substantive law shall be the law of the State of California or federal law. Choice of substantive law in no way affects the procedural aspects of the arbitration, which are exclusively governed by the provisions of this ADR Agreement.

H. OPINION AND AWARD

The Arbitrator shall issue a written opinion and award, in conformance with the following requirements:

1. The opinion and award must be signed and dated by the Arbitrator.

2. The Arbitrator's opinion and award shall decide all issues submitted.

3. The Arbitrator's opinion and award shall set forth the legal principles supporting each part of the opinion.

4. The Arbitrator shall have the same authority to award remedies, damages and costs as provided to a judge and/or jury under parallel circumstances.

I. ENFORCEMENT OF ARBITRATOR'S AWARD

Following the issuance of the Arbitrator's decision, any party may petition a court to confirm, enforce, correct or vacate the Arbitrator's opinion and award under the Federal Arbitration Act, and/or applicable California law.

J. FEES AND COSTS

Unless otherwise required by law, fees and costs shall be allocated in the following manner:

1. Each party shall be responsible for its own attorneys' fees, except as otherwise provided by law for the particular claim(s) at issue.

2. The Company shall pay the entire cost of the arbitrator's services, the facility in which the arbitration is to be held, and any similar costs, except that Executive shall contribute toward these costs an amount equal to the then-current filing fee in California Superior Court charged for filing a complaint or for first appearing, whichever is lower.

3. The Company shall pay the entire cost of a court reporter to transcribe the arbitration proceedings. Each party shall advance the cost for said party's transcript of the proceedings. Each party shall advance its own costs for witness fees, service and subpoena charges, copying, or other incidental costs that each party would bear during the course of a civil lawsuit.

4. Each party shall be responsible for its costs associated with discovery, except as required by law or court order.

III. SEVERABILITY

Each term, clause and provision of this ADR Agreement is separate and independent, and should any term, clause or provision of this ADR Agreement be found to be invalid or unenforceable, the validity of the remaining terms, clauses, and provisions shall not be affected. As to those terms, clauses and provisions found to be invalid or unenforceable, they shall be replaced with valid and enforceable terms, clauses or provisions or shall be modified, in order to achieve, to the fullest extent possible, the economic, business and other purposes of the invalid or unenforceable terms, clauses or provisions.

Dated: March 13, 2000

/s/ Harold Zagunis

Harold Zagunis

REDWOOD TRUST, INC.

Dated: March 13, 2000

By: /s/ Doug Hansen

Doug Hansen

Title: President

APPENDIX D

REQUEST FOR ARBITRATION FORM

ALTERNATIVE DISPUTE RESOLUTION POLICY

- --

Submission - This form (or, alternatively, a form that includes the information Requirement below) must be submitted by the individual claimant or the Redwood Trust, Inc. (to the President) within the time period required by the law that applies to the claim.

- If Redwood Trust, Inc. requests arbitration, the form must also be served on the individual within the appropriate time period.

- --

1. State the nature of the claim in detail:

- --

- --

- --

- --

(Continue on reverse and add pages if necessary)

Enter the date of termination or date(s) of alleged incident(s) (i.e., date of last instance of unlawful discrimination, sexual or other unlawful harassment):
_______/________/_______

Month Day Year

2. Provide the names and work locations of any individuals, including employees or supervisors, with knowledge of the dispute:

Name	Job Title	Work Location
- ----------------------	---------------------	--------------------
- ----------------------	---------------------	--------------------
- ----------------------	---------------------	--------------------
- ----------------------	---------------------	--------------------

3. Describe the relief requested (i.e., what you want done):

- --

- --

- --

(Please attach any documents relevant to the dispute.)

Signature of Party Requesting arbitration:

Redwood Trust, Inc.

__________________________ Date: ___________________

Signature of Executive:

__________________________ Date: ___________________

EXHIBIT 11.1

REDWOOD TRUST, INC.
STATEMENT RE: COMPUTATION OF PER SHARE EARNINGS

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	Three Months Ended March 31, 2000	Three Months Ended March 31, 1999
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Basic:		
Average common shares outstanding	8,785,017	10,778,159
Total	8,785,017	10,778,159
Net Income	$ 3,283,791	$ 5,854,817
Per Share Amount	$ 0.37	$ 0.54
DILUTED:		
Average common shares outstanding	8,785,017	10,778,159
Net effect of dilutive stock options outstanding during the period -- based on the treasury stock method	.59,589	83,615
Total	8,844,606	10,861,774
Net Income	$ 3,283,791	$ 5,854,817
Per Share Amount	$ 0.37	$ 0.54

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