==

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, 1997

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: 0-26436

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 ($.01 par value)	999,638 as of May 9, 1997
Common Stock ($.01 par value)	13,021,846 as of May 9, 1997

==

REDWOOD TRUST, INC.
FORM 10-Q

INDEX

<TABLE>
<CAPTION>

<S>	<C>	Page <C>
PART I.	FINANCIAL INFORMATION	
Item 1.	Consolidated Financial Statements	
	Consolidated Balance Sheets at March 31, 1997 and December 31, 1996..........	3
	Consolidated Statements of Operations for the three months ended March 31, 1997 and March 31, 1996......................................	4
	Consolidated Statements of Stockholders' Equity for the three months ended March 31, 1997 and March 31, 1996......................................	5
	Consolidated Statements of Cash Flows for the three months	

	ended March 31, 1997 and March 31, 1996	6
	Notes to Consolidated Financial Statements	7
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	18
PART II.	OTHER INFORMATION	
Item 1.	Legal Proceedings	50
Item 2.	Changes in Securities	50
Item 3.	Defaults Upon Senior Securities	50
Item 4.	Submission of Matters to a Vote of Security Holders	50
Item 5.	Other Information	50
Item 6.	Exhibits and Reports on Form 8-K	50
SIGNATURES		51

</TABLE>

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

REDWOOD TRUST, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

<TABLE>
<CAPTION>

<S>	March 31, 1997 <C>	December 31, 1996 <C>
ASSETS		
Cash and cash equivalents	$ 12,985	$ 11,068
Mortgage assets	2,604,714	2,153,428
Interest rate agreements	5,773	2,601
Accrued interest receivable	19,251	15,537
Other assets	341	1,563
	$ 2,643,064	$ 2,184,197
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Short-term borrowings	$ 2,373,279	$ 1,953,103
Accrued interest payable	14,962	14,060
Accrued expenses and other liabilities	1,262	761
Dividends payable	7,899	5,268
	2,397,402	1,973,192
Commitments and contingencies (See Note 10)		
STOCKHOLDERS' EQUITY		
Preferred stock, par value $0.01 per share; Class B 9.74% Cumulative Convertible 999,638 and 1,006,250 shares authorized; 999,638 and 1,006,250 shares issued and outstanding ($31,744 aggregate liquidation preference)	29,383	29,579
Common stock, par value $0.01 per share; 49,000,362 and 48,993,750 shares authorized; 11,905,957 and 10,996,572 issued and outstanding	119	110
Additional paid-in capital	219,461	187,507
Net unrealized gain/(loss) on assets available for sale	118	(3,460)
Dividends in excess of net income	(3,419)	(2,731)

	245,662	211,005
	$ 2,643,064	$ 2,184,197

</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)

<TABLE>
<CAPTION>

<S>	Three Months Ended March 31, 1997 <C>	1996 <C>
INTEREST INCOME		
Mortgage assets	$ 38,406	$ 8,914
Cash and investments	162	217
	38,568	9,131
INTEREST EXPENSE	28,900	6,202
INTEREST RATE AGREEMENTS		
Interest rate agreements expense	595	151
NET INTEREST INCOME	9,073	2,778
Provision for credit losses	695	332
Net interest income after provision for credit losses	8,378	2,446
Operating expenses	1,167	492
NET INCOME	7,211	1,954
Less cash dividends on Class B preferred stock	755	--
NET INCOME AVAILABLE TO COMMON STOCKHOLDERS	$ 6,456	$ 1,954
NET INCOME PER SHARE		
Primary	$ 0.53	$ 0.32
Fully diluted	$ 0.53	$ 0.32
Weighted average shares of common stock and common stock equivalents:		
Primary	12,116,867	6,129,587
Fully diluted	12,133,742	6,132,648
Dividends declared per Class B preferred share	$ 0.755	$ --
Dividends declared per common share	$ 0.600	$ 0.460

</TABLE>

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

REDWOOD TRUST, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

For the three months ended March 31, 1997
(In thousands, except share data)

<TABLE>
<CAPTION>

	Class B Preferred Stock		Common Stock		Additional Paid-in Capital	Net Unrealized Gain/(Loss) on Assets Available for Sale	Dividends in Excess of Net Income	Total
	Shares	Amount	Shares	Amount				
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, December 31, 1996	1,006,250	$ 29,579	10,996,572	$110	$187,507	($3,460)	($2,731)	$211,005
Net income	--	--	--	--	--	--	7,211	7,211
Conversion of Class B preferred stock into common stock	(6,612)	(196)	6,612	1	195	--	--	0
Issuance of common stock	--	--	902,773	8	31,759	--	--	31,767
Dividends declared:								
Class B Preferred	--	--	--	--	--	--	(755)	(755)
Common	--	--	--	--	--	--	(7,144)	(7,144)
Fair value adjustment on assets available for sale	--	--	--	--	--	3,578	--	3,578
Balance, March 31, 1997	999,638	$ 29,383	11,905,957	$119	$219,461	$ 118	($3,419)	$245,662

</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, except share data)

<TABLE>
<CAPTION>

	Three Months Ended March 31, 1997	Three Months Ended March 31, 1996
<S>	<C>	<C>

CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 7,211	$ 1,954
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of mortgage asset premium and discount, net	3,818	530
Depreciation and amortization	26	17
Provision for credit losses on mortgage assets	695	332
Amortization of interest rate cap agreements	311	151
Increase in accrued interest receivable	(3,714)	(1,226)
(Increase) decrease in other assets	1,196	(66)
Increase in accrued interest payable	902	326
Increase in accrued expenses and other	501	63
Net cash provided by operating activities	10,946	2,081
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of mortgage assets	(627,075)	(166,852)
Principal payments on mortgage assets	173,362	32,814
Purchases of interest rate cap agreements	(1,991)	(165)
Net cash used in investing activities	(455,704)	(134,203)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net borrowings from reverse repurchase agreements	420,176	138,405
Net proceeds from issuance of common stock	31,767	31
Dividends paid	(5,268)	(1,434)
Net cash provided by financing activities	446,675	137,002
Net increase in cash and cash equivalents	1,917	4,880
Cash and cash equivalents at beginning of period	11,068	4,825
Cash and cash equivalents at end of period	$ 12,985	$ 9,705
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 28,068	$ 5,876

</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, 1997

NOTE 1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Redwood Trust, Inc. ("Redwood Trust" or the "Company") was incorporated in Maryland on April 11, 1994 and commenced operations on August 19, 1994. The Company completed its initial public offering of 3,593,750 shares of Common Stock on August 4, 1995 at a price of $15.50 per share. On April 19, 1996 the Company completed its second public offering of 2,875,000 shares of Common Stock at a price of $20.25 per share. On August 8, 1996 the Company completed its public offering of 1,006,250 shares of Class B 9.74% Cumulative Convertible Preferred Stock ("Class B Preferred Stock") at a price of $31.00 per share. On November 19, 1996 the Company completed its third public offering of 1,250,000 shares of Common Stock at a price of $31.75 per share. On January 24, 1997 the Company completed its fourth public offering of 750,000 shares of Common Stock at a price of $39.50 per share.

The Company's principal source of earnings is net interest income, or interest income generated from its Mortgage Assets less the cost of borrowed funds and hedging. The Company acquires Mortgage Assets that are secured by single-family real estate properties throughout the United States, with a special emphasis on properties located in the State of California.

The consolidated financial statements include the accounts of Redwood Trust, Inc. and its special-purpose finance subsidiary, Sequoia Mortgage Funding Corporation. Inter-company balances have been eliminated.

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 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.

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

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and highly liquid investments with original maturities of three months or less. The carrying amount of cash equivalents approximates their fair value.

Mortgage Assets

The Company's mortgage assets ("Mortgage Assets") may consist of mortgage loans, mortgage loans which have been securitized by the Company following acquisition, mortgage loans which have been securitized by others prior to acquisition by the Company and interest only strips ("IO's").

Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities ("SFAS 115"), requires the Company to classify its mortgage loans which have been securitized and IO's as either trading investments, available-for-sale investments or held-to-maturity investments. Although the Company generally intends to hold most of these Mortgage Assets until maturity, it may, from time to time, sell any of these Mortgage Assets as part of its overall management of its balance sheet. Accordingly, to maintain flexibility, the Company currently classifies all of its Mortgage Assets which have been securitized and its IO's as available-for-sale. All assets classified as available-for-sale are reported at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity.

Unrealized losses on Mortgage Assets that are considered other-than-temporary, as measured by the amount of decline in fair value attributable to factors other than temporary, are recognized in income and the cost basis of the Mortgage Asset is adjusted. Other-than-temporary unrealized losses are based on management's assessment of various factors affecting the expected cash flow from the Mortgage Assets, 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.

Mortgage Assets held in the form of mortgage loans are carried at their unpaid principal balance, net of unamortized discount or premium.

Interest income is accrued based on the outstanding principal amount of the Mortgage Assets and their contractual terms. 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.

IO's are accounted for under the prospective method. Under this method, income is amortized over the asset's estimated life based on a method which provides a constant yield. At the end of each quarter, the yield over the remaining life of the asset is recalculated based on expected future cash flows. This new yield is then used to calculate the subsequent quarter's financial statement income.

Under certain extended high interest rate periods, or in the event of extremely high prepayment rates on the collateral, the return on the Company's investment in an IO could be zero

or negative. In the event that the projected return on an investment in an IO falls below a risk free rate, the Company would record a write down of such investment to its fair value.

Interest Rate Agreements

The rate the Company pays on its short-term and variable borrowings will rise and fall without limit as short-term market interest rates fluctuate. The rate the Company earns on its adjustable rate assets, however, is limited by periodic and lifetime caps.

Under the Company's hedging policy the Company does not hedge specific assets or liabilities, but rather the Company hedges the risk of overall limitations to its interest income. To utilize hedge accounting, the policy requires risk reduction and that there be at least a 50% correlation between changes in the estimated fair value of the assets or liabilities hedged and the hedge instruments. Currently, the Company invests in "Interest Rate Agreements." Interest Rate Agreements, which include interest rate cap agreements (the "Cap Agreements"), interest rate swap agreements (the "Swap Agreements"), interest rate collar agreements (the "Collar Agreements") and interest rate futures agreements (the "Futures Agreements"), entered into by the Company are intended to provide income to offset potential reduced net interest income under certain rising interest rate scenarios. The Company periodically evaluates the effectiveness of these hedges under various interest rate scenarios.

The Company accounts for the Interest Rate Agreements as hedges. Because the hedged Mortgage Assets are carried at fair value, the Company's Interest Rate Agreements are carried at fair value, with unrealized gains and losses reported as a separate component of equity.

The cost of each Cap Agreement and the net cost or payment received on each Collar Agreement is amortized over the effective period of that Cap or Collar Agreement using the effective interest method. The income and expense related to each Swap Agreement is recognized on an accrual basis. Gains and losses on early termination of Interest Rate Agreements are amortized as a component of net interest income over the remaining term of the original Interest Rate Agreement, or, if shorter, over the remaining term of associated Mortgage Assets as adjusted for estimated future principal prepayments.

Unrealized losses on Interest Rate Agreements that are considered other-than-temporary are recognized in income and the cost basis of the Interest Rate Agreement is adjusted. The other-than-temporary decline is measured as the amount of the decline in fair value attributable to factors that are other-than-temporary. Other-than-temporary unrealized losses are based on management's assessment of various factors affecting the Interest Rate Agreements, for example, a serious deterioration of the ability of the counterparty to perform under the terms of the Interest Rate Agreement.

Premises, Furniture and Equipment

Leasehold improvements are stated at cost and are amortized on a straight-line basis over the life of the lease. Furniture and equipment is stated at cost and depreciated on an accelerated basis over its estimated useful life. Expenditures for repairs and maintenance are charged to expense when incurred. Premises and equipment totaled $285,197 at March 31, 1997 and $257,493 at December 31, 1996. Depreciation expense and leasehold improvements amortization for the three months ended March 31, 1997 and March 31, 1996 totaled $17,111 and $4,059, respectively. Accumulated depreciation and leasehold improvement amortization totaled $107,165 at March 31, 1997 and $90,053 at December 31, 1996.

Income Taxes

The Company has elected to be taxed as a Real Estate Investment Trust ("REIT") and intends to comply with the REIT provisions of the Internal Revenue Code (the "Code") and the corresponding provisions of State law. Accordingly, the

Company will not be subject to Federal or state income tax to the extent of its distributions to stockholders. In order to maintain its status as a REIT, the Company is required, among other requirements, to distribute at least 95% of its taxable income.

Earnings Per Share

Earnings per share are based on the weighted average shares of common stock outstanding plus common equivalent shares using the treasury stock method. The treasury stock method calculation assumes 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, for primary earnings per share, or at the end of period market price if higher, for fully diluted earnings per share.

In February 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 128, "Earning Per Share" ("SFAS 128"). SFAS 128 is designed to improve the earnings per share ("EPS") information provided in the financial statements by simplifying the existing computational guidelines, revising the disclosure requirements, and increasing the comparability of EPS data on an international basis. SFAS 128 is effective for financial statements issued for periods ending after December 15, 1997, including interim periods. The Company will implement SFAS 128 in its December 31, 1997 financial statements. The following table reflects the impact that SFAS 128 would have had on the current financial statements.

	Three Months Ended March 31, 1997	Three Months Ended March 31, 1996
As Reported:		
Primary Earnings Per Share	$0.53	$0.32
Fully Diluted Earnings Per Share	$0.53	$0.32
Under SFAS No. 128:		
Basic Earnings Per Share	$0.56	$0.35
Fully Diluted Earnings Per Share	$0.53	$0.32

Credit Risk

The majority of the Company's Mortgage Assets have protection from some degree of credit loss either through subordination, insurance, third party guarantees, or other means. Many of the Company's Privately-Issued Mortgage Assets have received ratings from one or more of the four nationally recognized credit rating agencies. Based on these ratings, and on credit criteria similar to those used by rating agencies, the Company assigns a "rating equivalent" to each Mortgage Asset. For purposes of assigning a rating equivalent to unrated pools of whole loans or unrated securitized pools of mortgage loans, the Company assigns a series of ratings to different portions of the pool according to the Company's estimation of how the pool would currently be structured and rated if it were newly securitized. At March 31, 1997, the Privately-Issued Mortgage Assets held by the Company had rating equivalents ranging from AAA to unrated, with a weighted average of AA+; the weighted average rating equivalent of all the Company's Mortgage Assets was AA+. At December 31, 1996, the Privately-Issued Mortgage Assets held by the Company had rating equivalents ranging from AAA to unrated, with a weighted average of AA+; the weighted average rating equivalent of all the Company's Mortgage Assets was AA+.

An allowance for credit losses is maintained at a level deemed appropriate by management to provide for known losses as well as unidentified potential losses in its Mortgage Asset portfolio. The allowance is based upon management's assessment of various factors affecting its Privately-Issued Mortgage Assets, including current and projected economic conditions, delinquency status and credit protection. In determining the

allowance 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 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 allowance and subsequent recoveries, if any, are credited to the allowance. During the three months ended March 31, 1997 the Company provided for $695,469 in credit losses and incurred $42,236 in charge-offs, resulting in a reserve balance of $2,832,783 at March 31, 1997. During the three months ended March 31, 1996 the Company provided for $331,516 in credit losses and incurred no charge-offs, resulting in a reserve balance of $821,229 at March 31, 1996. The reserve balance at December 31, 1996 was $2,179,550.

Reclassifications

Certain amounts for prior years have been reclassified to conform with the 1997 presentation.

Recent Accounting Pronouncements

In June 1996 the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" ("SFAS 125"). SFAS 125 provides accounting and reporting standards for all types of securitization transactions involving the transfer of financial assets including repurchase agreements and collateralized borrowing arrangements. The Company has adopted this pronouncement effective January 1, 1997. The adoption of SFAS 125 does not have a material impact on the Company's financial statements.

NOTE 2. MORTGAGE ASSETS

Mortgage Assets Excluding IO's

At March 31, 1997, Mortgage Assets, excluding IO's, consisted of the following:

(IN THOUSANDS)	FEDERAL HOME LOAN MORTGAGE CORPORATION	FEDERAL NATIONAL MORTGAGE ASSOCIATION	NON-AGENCY MORTGAGE ASSETS	TOTAL
Mortgage Assets, Gross	$ 321,354	$ 660,388	$ 1,574,115	$ 2,555,857
Unamortized Discount	0	(214)	(15,427)	(15,641)
Unamortized Premium	10,381	20,611	31,714	62,706
Amortized Cost	331,735	680,785	1,590,402	2,602,922
Allowance for Credit Losses	0	0	(2,833)	(2,833)
Gross Unrealized Gains	1,476	3,592	2,637	7,705
Gross Unrealized Losses	(200)	(274)	(4,633)	(5,107)
Carrying Value	$ 333,011	$ 684,103	$ 1,585,573	$ 2,602,687

At December 31, 1996, Mortgage Assets, excluding IO's, consisted of the following:

(IN THOUSANDS)	FEDERAL HOME LOAN MORTGAGE CORPORATION	FEDERAL NATIONAL MORTGAGE ASSOCIATION	NON-AGENCY MORTGAGE ASSETS	TOTAL
Mortgage Assets, Gross	$ 304,668	$ 635,268	$ 1,177,309	$ 2,117,245
Unamortized Discount	0	(234)	(15,859)	(16,093)

Unamortized Premium	9,287	17,652	24,839	51,778
Amortized Cost	313,955	652,686	1,186,289	2,152,930
Allowance for Credit Losses	0	0	(2,180)	(2,180)
Gross Unrealized Gains	1,091	2,082	2,746	5,919
Gross Unrealized Losses	(185)	(688)	(4,477)	(5,350)
Carrying Value	$ 314,861	$ 654,080	$ 1,182,378	$ 2,151,319

</TABLE>

At March 31, 1997 and December 31, 1996, all investments in Mortgage Assets consisted of interests in adjustable-rate mortgages on residential properties. A majority of the Non-Agency Mortgage Asset properties are located in the State of California. The securitized interests in pools of adjustable-rate mortgages from the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association are guaranteed as to principal and interest by those US government agencies. The original maturity of the vast 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, 1997, the average annualized effective yield on the Mortgage Assets was 6.85% based on the amortized cost of the assets and 6.85% based on the fair value of the assets. At December 31, 1996, the average annualized effective yield was 7.10% based on the amortized cost of the assets and 7.11% based on the fair value of the assets.

Most of the adjustable-rate mortgage securities and loans are limited by periodic caps (generally interest rate adjustments are limited to no more than 1% every six months or 2% every year) and lifetime caps. At March 31, 1997 and December 31, 1996, the weighted average lifetime cap was 11.91% and 11.73%, respectively.

IO's

The amortized cost and fair value of the Company's IO's are summarized as follows:

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 1997	DECEMBER 31, 1996
<S>	<C>	<C>
Amortized Cost	$ 2,400	$ 2,539
Gross Unrealized Gains	49	45
Gross Unrealized Losses	(422)	(475)
Estimated Fair Value	$ 2,027	$ 2,109

</TABLE>

The average annualized effective yield at March 31, 1997 on the IO's was 11.47% based on the amortized cost of the assets and 13.58% based on the fair value of the assets. The average annualized effective yield at December 31, 1996 on the IO's was 11.24% based on the amortized cost of the assets and 13.53% based on the fair value of the assets.

NOTE 3. INTEREST RATE AGREEMENTS

The amortized cost and fair value of the Company's Interest Rate Agreements are summarized as follows:

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 1997	DECEMBER 31, 1996
<S>	<C>	<C>
Amortized Cost	$ 7,879	$ 6,200
Gross Unrealized Gains	734	156
Gross Unrealized Losses	(2,840)	(3,755)
Carrying Value	$ 5,773	$ 2,601

</TABLE>

The sum of the notional amounts of all of the Company's Interest Rate Agreements in effect was $2,192,200,000 at March 31, 1997 and $1,128,000,000 at December 31, 1996, respectively.

Cap Agreements

The Company had seventy-one outstanding Cap Agreements at March 31, 1997 and fifty-seven outstanding Cap Agreements at December 31, 1996. Potential future earnings from each of these Cap Agreements are based on variations in the London Inter-Bank Offered Rate ("LIBOR"). The sum of the notional amounts of the Company's Cap Agreements in effect was $1,767,200,000 and $703,000,000 at March 31, 1997 and December 31, 1996, respectively. The weighted average cap strike rate during the three months ended March 31, 1997 and March 31, 1996 was 7.63% and 7.35%, respectively. Under these Cap Agreements the Company will receive cash payments should an agreed-upon reference rate, either one-month or three-month LIBOR, increase above the strike rates of the Cap Agreements.

Information on Cap Agreements outstanding at March 31, 1997 is summarized below.

<TABLE>
<CAPTION>

(DOLLARS IN THOUSANDS) YEAR	AVERAGE CAP NOTIONAL FACE AMOUNT	AVERAGE CAP STRIKE RATE	LOW CAP STRIKE RATE	HIGH CAP STRIKE RATE	EXPECTED CAP EXPENSE AMORTIZATION
<S>	<C>	<C>	<C>	<C>	<C>
1997 (last 9 months)	1,719,796	7.37%	5.50%	12.00%	1,985
1998	983,191	8.47%	5.50%	12.00%	1,753
1999	1,022,088	9.47%	6.30%	12.00%	1,727
2000	739,720	9.95%	7.50%	12.00%	1,231
2001	441,164	10.11%	7.50%	11.00%	714
2002	49,274	8.39%	8.00%	11.00%	169
2003	22,634	8.67%	8.00%	9.00%	145
2004	21,834	8.67%	8.00%	9.00%	135
2005	5,216	8.53%	8.50%	9.00%	20
Total					$7,879

</TABLE>

Collar Agreement

At March 31, 1997, the Company had entered into one outstanding collar agreement, consisting of the purchase of a cap agreement subsidized by the sale of a floor agreement. On the cap portion, the Company will receive net hedge income to the extent that three month LIBOR exceeds 7.50%. On the floor portion, the Company will incur a net hedge expense to the extent that three month LIBOR falls below 5.91%

Information on the Collar Agreement outstanding at March 31, 1997 is summarized below.

<TABLE>
<CAPTION>

EFFECTIVE PERIOD:	NOTIONAL FACE AMOUNT (IN THOUSANDS)	INDEX	CAP STRIKE RATE	FLOOR STRIKE RATE	EXPECTED COLLAR EXPENSE AMORTIZATION
<S>	<C>	<C>	<C>	<C>	<C>
April 1997 to July 1999	$20,000	3 mo LIBOR	7.50%	5.91%	$0

</TABLE>

Swap Agreements

The Company has entered into three types of Interest Rate Swap Agreements summarized as follows:

Fixed vs. Floating Rate Swap Agreements:
The Company had six outstanding fixed vs. floating rate Swap Agreements ("Fixed Pay Rate Swaps") at March 31, 1997 and December 31, 1996. The sum of the notional amounts of the Company's Fixed Pay Rate Swaps in effect was $135,000,000 at March 31, 1997 and December 31, 1996. Under these Swap Agreements, the Company receives the 3 month LIBOR rate and pays the agreed upon fixed rate.

Information on Fixed Pay Rate Swaps outstanding at March 31, 1997 is summarized below.

<TABLE>
<CAPTION>

(DOLLARS IN THOUSANDS) YEAR	AVERAGE SWAP NOTIONAL FACE AMOUNT	AVERAGE PAY RATE	LOW PAY RATE	HIGH PAY RATE
1997 (last 9 months)	101,418	6.29%	6.01%	7.18%
1998 (first 5 months)	25,828	6.59%	6.40%	7.18%

Periodic Swap Agreements:
As of March 31, 1997, the Company had entered into three Periodic Swap Agreements designed to produce income to the Company in the event that the three month LIBOR rate rises sharply. In each of these swaps, the Company receives income on the notional face at a rate equal to three month LIBOR less 0.230% to 0.265% and

pays income on the notional face on the lesser of (a) three month LIBOR or (b) the prior period's LIBOR plus 0.50%. The average notional face of these swaps is $110,000,000, with $90,000,000 maturing in August 1999 and $20,000,000 maturing in September 1999.

Information on the Periodic Swap Agreements outstanding at March 31, 1997 is summarized below.

(DOLLARS IN THOUSANDS) YEAR	AVERAGE SWAP NOTIONAL FACE AMOUNT	AVERAGE SPREAD RECEIVED	LOW SPREAD RECEIVED	HIGH SPREAD RECEIVED
1997 (last 9 months)	110,000	-0.255%	-0.265%	-0.230%
1998	110,000	-0.255%	-0.265%	-0.230%
1999 (first 9 months)	98,242	-0.257%	-0.265%	-0.230%

Basis Swap Agreements:
As of March 31, 1997, the Company had entered into five LIBOR/Treasury bill Basis Swap Agreements totaling $160 million in notional value. These Basis Swap Agreements, in conjunction with the Company's other Swap and Cap Agreements, are designed to reduce the potential risks in that portion of the Company's balance sheet wherein Treasury-based assets are funded with LIBOR-based liabilities. The Basis Swap Agreements will produce net hedge income for the Company to the extent that three month LIBOR exceeds the average three month Treasury bill rate by 0.440% to 0.465% and will produce a net hedge expense for the Company to the extent that the spread between these two indices is narrower than 0.440% to 0.465%. The maturities of these Basis Swap Agreements are as follows: $30,000,000 in June 1998, $50,000,000 in December 1998, $30,000,000 in June 1999 and $50,000,000 in December 1999. Information on Basis Swap Agreements outstanding at December 31, 1996 is summarized below.

(DOLLARS IN THOUSANDS) YEAR	AVERAGE SWAP NOTIONAL FACE AMOUNT	AVERAGE SPREAD PAID	LOW SPREAD PAID	HIGH SPREAD PAID
1997 (last 9 months)	160,000	0.453%	0.440%	0.465%
1998	144,877	0.455%	0.440%	0.465%
1999	64,712	0.464%	0.460%	0.465%

The Company has incurred credit risk to the extent that the counter-parties to the Interest Rate Agreements do not perform their obligations under the Interest Rate Agreements. Potential credit write-offs are limited to the amortized cost of the Cap Agreements. In addition, for Cap, Swap and Collar Agreements, if one of the counter-parties 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 entered into Interest Rate Agreements only with counter-parties rated A or better and has entered into Interest Rate Agreements with fifteen different counter-parties in order to reduce the risk of credit exposure to any one counter-party.

NOTE 4. SHORT-TERM BORROWINGS

The Company has entered into reverse repurchase agreements, notes payable and a revolving line of credit (together "Short-Term Borrowings") to finance acquisitions of a portion of its Mortgage Assets. These Short-Term Borrowings are collateralized by a portion of the Company's Mortgage Assets.

At March 31, 1997, the Company had $2,373,279,000 of Short-Term Borrowings outstanding with a weighted average borrowing rate of 5.82% and a weighted average maturity of 79 days. These borrowings were collateralized with $2,478,190,951 of Mortgage Assets. At December 31, 1996, the Company had $1,953,103,000 of Short-Term Borrowings outstanding with a weighted average borrowing rate of 5.83% and a weighted average remaining maturity of 98 days. These borrowing were collateralized with $2,050,813,000 of Mortgage Assets.

In September 1996, the Company entered into a $20,000,000, one-year revolving line of credit agreement with a financial institution. The agreement requires that the Company maintain certain financial ratios. The Company is in compliance with all requirements. Interest rates on borrowings under this facility are based on LIBOR. At March 31, 1997, borrowings under this facility totaled $19,191,000 and were committed through April 16, 1997. At December 31, 1996, borrowings under this facility totaled $19,302,000. These borrowings are reflected in the $2,373,279,000 and $1,953,103,000 of Short-Term Borrowings outstanding at March 31, 1997 and December 31, 1996.

At March 31, 1997 and December 31, 1996, the Short-Term Borrowings had the following remaining maturities:

<TABLE>
<CAPTION>

(IN THOUSANDS)	MARCH 31, 1997	DECEMBER 31, 1996
<S>	<C>	<C>
Within 30 days	$ 588,937	$ 268,042
30 to 90 days	622,985	667,567
Over 90 days	1,161,357	1,017,494
Total Borrowings	$2,373,279	$1,953,103

</TABLE>

For the three months ended March 31, 1997 and March 31, 1996, the average balance of Short-Term Borrowings was $2,056,051,000 and $435,978,990 with a weighted average interest cost of 5.62% and 5.69%, respectively. The maximum balances outstanding during the three months ended March 31, 1997 and March 31, 1996 were $2,373,279,000 and $508,721,000, respectively.

NOTE 5. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the carrying amounts and estimated fair values of the Company's financial instruments at March 31, 1997 and December 31, 1996. FASB Statement No. 107, Disclosures about Fair Value of Financial Instruments, defines the fair value of a financial instrument as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced liquidation sale.

<TABLE>
<CAPTION>

	MARCH 31, 1997		DECEMBER 31, 1996	
(IN THOUSANDS)	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE
<S>	<C>	<C>	<C>	<C>
Assets				
Mortgage Assets	$2,602,687	$2,602,212	$2,151,319	$2,151,319
IO's	2,027	2,027	2,109	2,109
Interest Rate Agreements	5,773	5,773	2,601	2,601

</TABLE>

Management bases its fair value estimates primarily on third party bid price indications, such as bid indications provided by dealers who make markets in these assets and asset valuations made by collateralized lenders, when such indications are available. However, the fair value reported reflects estimates and may not necessarily be indicative of the amounts the Company could realize in a current market exchange.

Cash and cash equivalents, interest receivable, short-term borrowings, accrued interest payable, accrued expenses and other liabilities are reflected in the financial statements at their costs, which approximates their fair value because of the short-term nature of these instruments.

NOTE 6. CLASS B 9.74% CUMULATIVE CONVERTIBLE PREFERRED STOCK

On August 8, 1996, the Company issued 1,006,250 shares of Class B Preferred Stock. Each share of the Class B Preferred Stock is convertible at the option of the holder at any time into one share of Common Stock. After September 30, 1999, the Company can either redeem or cause a conversion of the Class B Preferred Stock. The Class B Preferred Stock pays a dividend equal to the greater of (i) $0.755 per quarter or (ii) an amount equal to the quarterly dividend declared on the number of shares of the Common Stock into which the Class B Preferred Stock is convertible. The Class B Preferred Stock ranks senior to the Company's Common Stock as to the

payment of dividends and liquidation rights. The liquidation preference entitles the holders of the Class B Preferred Stock to receive $31 per share plus any accrued dividends before any distribution is made on the Common Stock.

As of March 31, 1997, a total of 6,612 shares of the Class B Preferred Stock has been converted into 6,612 shares of the Company's Common Stock. At March 31, 1997 and December 31, 1996, there were 999,638 and 1,006,250 shares of the Class B Preferred Stock outstanding, respectively.

NOTE 7. STOCK PURCHASE WARRANTS

At March 31, 1997 and December 31, 1996, there were 272,304 and 412,894 Warrants outstanding, respectively. Each Warrant entitles the holder to purchase 1.000667 shares of the Company's common stock at an exercise price of $15.00 per share. The Warrants remain exercisable until December 31, 1997.

NOTE 8. STOCK OPTION PLAN

The Company has adopted a Stock Option Plan for executive officers, employees and non-employee directors (the "Stock Option Plan"). The Stock Option 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 and limited stock appreciation rights ("Awards") and stock dividend equivalent rights ("stock DERs") to such eligible recipients other than non-employee directors. Non-employee directors are automatically provided annual grants of NQSOs with stock DERs pursuant to a formula under the Stock Option Plan.

The number of shares of Common Stock available under the Stock Option Plan for options and Awards, subject to certain anti-dilution provisions, is 15% of the Company's total outstanding shares of Common Stock. At March 31, 1997 and December 31, 1996, 1,022,241 and 1,138,743 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, 1997 and December 31, 1996, 299,633 ISOs had been granted. The exercise price for ISOs granted under the Stock Option 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 Stock Option 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 Stock Option Plan permits stock options granted under the plan to accrue stock DERs. For the three months ended March 31, 1997 and March 31, 1996, the stock DERs accrued on NQSOs that had a stock DER feature resulted in non-cash charges to operating expenses of $123,859 and $84,919, respectively. 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 are based on the level of the Company's dividends and on the price of the stock on the related dividend payment date.

Information with respect to stock option and DER activity is as follows:

<TABLE>

<CAPTION>

	THREE MONTHS ENDED MARCH 31, 1997	YEAR ENDED DECEMBER 31, 1996
Outstanding options at beginning of period:	421,577	310,857
Options granted	250,000	141,300
Options exercised	--	(42,083)
Dividend equivalent rights earned	2,910	11,503
Outstanding options at end of period	674,487	421,577
Exercise price per share:		
For options exercised during period	--	$0.10 - $0.11
For options outstanding end of period	$0.10 - $42.50	$0.10 - $36.88

</TABLE>

NOTE 9. DIVIDENDS

The Company declared and paid the following dividends for the three months ended March 31, 1997 and for the year ended December 31, 1996:

<TABLE>
<CAPTION>

Declaration Date	Record Date	Payable Date	Total Dividends	Dividends Per Share: Class B Preferred Stock	Dividends Per Share: Common Stock
3/5/97	3/31/97	4/21/97	$7,898,301	$0.755	$0.600
12/16/96	12/31/96	1/21/97	$5,268,314	$0.755	$0.410
9/16/96	9/30/96	10/21/96	$4,016,274	$0.386	$0.400
6/14/96	6/28/96	7/18/96	$3,408,046	--	$0.400
3/11/96	3/29/96	4/19/96	$2,539,833	--	$0.460

</TABLE>

Under the Internal Revenue Code of 1986, a dividend declared by a REIT in December of a calendar year, payable to shareholders of record as of a specified date in December, will be deemed to have been paid by the Company and received by the shareholders on that record date if the dividend is actually paid before February 1st of the following calendar year. Therefore, the dividend declared in December 1996 which was paid in January 1997 is considered taxable income to shareholders in the year declared. The Company's dividends are not eligible for the dividends received deduction for corporations.

NOTE 10. COMMITMENTS AND CONTINGENCIES

As of March 31, 1997, the Company had entered into a commitment to purchase $4.9 million of Mortgage Assets for settlement in April 1997. The Company had also entered into a commitment to purchase one Interest Rate Agreement for a premium of $25,125. At March 31, 1997, the Company had no other outstanding commitments to purchase or sell Mortgage Assets or to purchase, sell or terminate Interest Rate Agreements. The Company also had no commitments to enter into additional reverse repurchase agreements or other borrowings.

Rental expense for office properties under operating leases for the three months ended March 31, 1997 and March 31, 1996, was $30,813 and $24,062, respectively.

Future minimum rental commitments as of March 31, 1997 under non-cancelable operating leases with initial or remaining terms of more than one year, are as follows:

<TABLE>
<CAPTION>

YEAR ENDING DECEMBER 31,	MINIMUM RENTAL COMMITMENT AS OF MARCH 31, 1997 (IN THOUSANDS)
1997	143
1998	191
1999	191
2000	191
2001	64

Total	$524

</TABLE>

Effective January 1, 1997, the Company is bearing 100% of all expenses. Prior to 1997, the Company shared certain office expenses, such as lease payments and utilities, on a pro rata basis with GB Capital. GB Capital was owned by certain officers of the Company and ceased operations effective March 31, 1997. For the year ended December 31, 1996, the Company was bearing 95% of the lease expenses and GB Capital was bearing 5%.

ITEM 7. 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. (the "Company") and its 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, see "Risk Factors" commencing on Page 26 of the Company's 1996 Form 10-K.

OVERVIEW

Redwood Trust, Inc. is a mortgage finance company which acquires mortgages and seeks to earn spread income while holding and managing the mortgages to maturity. The Company uses both its equity and borrowed funds to acquire mortgages. The Company's source of earnings is net interest income, or the interest income earned on mortgages less interest expense paid on borrowed funds and hedging costs. The Company believes its primary competitors are other financial institutions, such as banks and savings and loan institutions, which seek to earn spread income from managing mortgage assets. Compared to most of its competitors, the Company believes it benefits from a lower cost of operations and from its status as a Real Estate Investment Trust ("REIT"). As a REIT, the Company does not pay corporate Federal income taxes on its taxable income it pays out as dividends.

The Company has sought to structure its business to achieve operational efficiencies and to minimize fixed costs. Instead of maintaining an in-house mortgage origination staff, the Company acquires mortgage assets from mortgage origination companies, savings and loans, banks and from the secondary mortgage market. The Company out-sources mortgage servicing functions. Rather than build a retail branch banking system to gather deposits (which would require the Company to obtain a bank or savings and loan charter, pay taxes and be regulated), the Company accesses borrowed funds in the capital markets. This strategy enables the Company to keep its operating costs low. In the first quarter of 1997, the Company's operating expenses to assets ratio was 0.20% and its efficiency ratio (operating expenses to net interest income) was 13%.

As of March 31, 1997, all of the Company's mortgage assets consisted of adjustable-rate, first-lien mortgages on single-family properties or mortgage securities evidencing an interest in such mortgages. In the future the Company may acquire fixed-rate single-family mortgage loans as well as mortgage loans on multi-family or commercial properties.

The Company is an "A" quality mortgage lending company: the Company does not own mortgages originated to "B", "C", or "D" quality origination or documentation standards except in limited circumstances when the Company has a degree of credit protection sufficient to eliminate most of the potential credit risk from such loans.

The Company acquires high quality individual whole mortgage loans (28% of total mortgage assets as of March 31, 1997), mortgage securities evidencing an interest in pools of mortgage loans which have been fully insured against credit losses by one of the government-sponsored mortgage entities such as GNMA, FHLMC and FNMA (39% of total), mortgage securities which have partial private-sector credit-enhancement through insurance, subordination, or other means sufficient to warrant an investment-grade credit rating from one of the nationally-recognized credit rating firms (32% of total), and mortgage securities which are

subordinated and have higher levels of credit risk such that they have received a rating below BBB (1% of total). The average credit rating equivalent of the Company's mortgage assets is AA+.

The Company seeks to acquire "A" quality single-family mortgage assets consisting of "jumbo" mortgages which, in general, have loan balances greater than $214,600. Because of their size, these jumbo loans are not eligible to be acquired or guaranteed by the government-sponsored mortgage entities. The Company also acquires FNMA and

FHLMC mortgage securities and smaller balance "A" quality whole loans when such acquisitions are deemed attractive by management.

As of March 31, 1997, 41% of the whole mortgage loans owned by the Company were secured by single-family residential properties located in California. In addition, 70% of the properties underlying the mortgage pools in which the Company owned an interest that was rated less than AA were located in California. Management believes that the economy and the trend of residential housing values in California were generally stable to improving in 1996 and the first quarter of 1997.

The coupon rate the Company earns on its adjustable-rate mortgage assets (100% of all mortgage assets as of March 31, 1997) increases or falls in conjunction with changes in short-term interest rates, as does the rate the Company pays on its borrowings. The coupon rate on each mortgage generally adjusts on a one, six or twelve month cycle; approximately 2% of the Company's assets are "hybrid" adjustable rate mortgages that have an extended period to the first coupon change (averaging 30 months from March 31, 1997) and thereafter adjust on a regular 12 month schedule. The average term-to-next-adjustment for all of the Company's mortgage assets was five months as of March 31, 1997. Borrowings have maturities ranging from one to twelve months; the average maturity at March 31, 1997 was 79 days. Some of these borrowings have adjustable rates; the term-to-next-interest-rate-adjustment for these borrowings was 43 days as of March 31, 1997. The Company's interest rate agreement hedging program is designed to reduce the impact of negative effects that could occur in a rising interest rate environment as a result of mismatches between the adjustment dates of the Company's assets and liabilities. Such mismatches, before hedging, averaged 3.5 months at March 31, 1997. Changes in the coupon rates earned on the Company's mortgages are limited by periodic and lifetime caps; the Company's hedging program also seeks to mitigate the negative effects such mortgage coupon caps may have on spread income should short-term interest rates increase rapidly. Because the Company's adjustable-rate earning assets exceed its liabilities, the Company believes that rising short-term interest rates may lead to higher net earnings after a lag period, all other factors being equal. Similarly, falling short-term interest rates may lead to reduced net earnings after a lag period.

The Company seeks to generate secular growth in earnings and dividends per share in a variety of ways, including through (i) issuing new equity and increasing the size of the balance sheet when opportunities in the mortgage market are likely to allow growth in earnings per share, (ii) seeking to improve productivity by increasing the size of the balance sheet at a rate faster than operating expenses increase, (iii) changing the mix of mortgage asset types on the balance sheet in an effort to improve risk-adjusted returns, (iv) seeking to benefit by an increased market value of assets and lower borrowing costs should mortgage asset quality improve with seasoning, mortgage principal repayments, and improvements in real estate markets and the general economy, and (v) increasing the efficiency with which the Company utilizes its equity capital over time by increasing the Company's use of debt when prudent and by issuing subordinated debt, preferred stock or other forms of debt and equity.

The Company has grown rapidly by issuing new capital and acquiring new mortgage assets. While the Company believes such growth has significantly increased its long-term earnings per share potential, the near-term effect has been a reduction in reported earnings per share as compared to what earnings likely would have been without such growth. The Company intends to continue to pursue additional growth in the future when management believes that growth is likely to be additive to earnings per share potential.

RESULTS OF OPERATIONS: FIRST QUARTER 1997 VS. FIRST QUARTER 1996

CHANGE IN CLASSIFICATION FOR CERTAIN ASSETS AND CHANGE IN CALCULATION METHOD FOR CERTAIN PREVIOUSLY REPORTED YIELDS AND RATIOS

Through December 31, 1996, the Company classified all of its mortgage assets and interest rate agreements as "available-for-sale" and, as a result, carried these assets on its balance sheet at fair market value (estimated liquidation value). Starting in 1997, the Company has reclassified certain assets as "held-to-maturity". Accordingly, such assets are now carried on the Company's balance sheet at a carrying value that will be adjusted over time from the market value at the time of reclassification towards historical amortized cost. Neither the use of this different type of balance

sheet classification nor the change from one type of balance sheet classification to the other will effect in any way the manner in which the Company manages its business or calculates its net income.

As a result of this change, the stockholders' equity numbers reported by the Company on its balance sheet have become, in the opinion of management, more difficult to interpret as stockholders' equity includes a valuation account which incorporates mark-to-market adjustments on some mortgage assets and interest rate agreements, but not on other assets or on any liabilities. In addition, the valuation account includes the adjustment factor described above designed to move the carrying value of reclassified assets towards historical amortized cost over time. Thus stockholders' equity and the valuation account will not represent a full mark-to-market presentation nor will it reflect a historical amortized cost presentation.

Since information regarding market values of assets and liabilities is a very important input into the management of the operations of the Company, and because management believes that these market values are a source of potentially valuable information for its shareholders, the Company will continue to fully disclose mark-to-market figures for all of its earning assets, interest rate agreements and liabilities in this "Management's Discussion and Analysis" section of its financial reports. See "Financial Condition -- Stockholders' Equity" below.

In accordance with these changes, the Company has changed its method of calculating certain previously reported yields and ratios. Unless indicated otherwise, all such measures have now been calculated using historical amortized cost figures for all assets and liabilities; mark-to-market effects are excluded. For example, historical return on equity ("ROE") figures have been adjusted downwards slightly from previously reported ROE numbers as the Company's equity base on a historical amortized cost basis has, in the past, exceeded its equity base as calculated including unrealized market value losses on assets. These changes effect certain balance sheet and yield calculations, but do not effect the calculation of income. These changes are not material. Management has made these changes in an effort to make the presentation of these figures more useful and consistent.

TOTAL NET INCOME

Total net income to common and preferred shareholders, as calculated according to Generally Accepted Accounting Principles ("GAAP"), increased by 269%, from $2.0 million in the first quarter of 1996 to $7.2 million in the first quarter of 1997. Total net income available to common shareholders after preferred dividends increased by 230%, from $2.0 million in the first quarter of 1996 to $6.5 million in the first quarter of 1997. Growth in total net income was driven primarily by growth in average assets. From the first quarter of 1996 to the first quarter of 1997, average assets grew by 350% to $2.3 billion, interest income revenue grew by 322% to $38.6 million, net interest income grew by 227% to $9.1 million, credit provision expenses rose by 110% to $0.7 million and operating expenses grew by 137% to $1.2 million. Average total equity grew by 219% to $237.2 million.

Growth in revenues and net interest income have lagged average asset growth somewhat as the Company has changed its asset mix towards lower credit risk assets with narrower spreads and as the Company has utilized a higher percentage of debt rather than equity to fund its mortgage assets. Credit provision expenses have not increased pro-rata with growth in average assets as the Company has not added to its portfolio of securitized mortgages rated less than AA since 1995. On average, the Company has moved towards an asset mix that, through March 31, 1997, has required a lower average level of credit provisions. Growth in operating expenses has lagged asset growth as the Company has become more efficient in its operations.

The Company's primary income and expense categories are shown in Table 1.

TABLE 1
NET INCOME

<TABLE>
<CAPTION>

	REVENUES OR INTEREST INCOME	INTEREST EXPENSE	INTEREST RATE AGREEMENT EXPENSE	NET INTEREST INCOME	CREDIT PROVISION EXPENSE	OPERATING EXPENSES	NET INCOME BEFORE PREFERRED DIVIDENDS	PREFERRED DIVIDENDS	INCOME AFTER PREFERRED DIVIDENDS
	(DOLLARS IN THOUSANDS)								
Fiscal 1994	$ 1,296	$ 760	$ 8	$ 528	$ 0	$ 146	$ 382	$ 0	$ 382
1995, Quarter 1	2,170	1,533	16	621	19	201	401	0	401
1995, Quarter 2	2,960	2,190	82	688	40	198	450	0	450
1995, Quarter 3	3,986	2,432	112	1,442	84	364	994	0	994
1995, Quarter 4	6,610	4,453	129	2,028	350	368	1,310	0	1,310
1996, Quarter 1	9,131	6,202	151	2,778	331	493	1,954	0	1,954
1996, Quarter 2	12,901	9,075	255	3,571	477	594	2,500	0	2,500
1996, Quarter 3	19,371	14,447	350	4,574	516	671	3,387	388	2,999
1996, Quarter 4	25,881	19,467	402	6,012	372	796	4,844	760	4,084
1997, Quarter 1	38,568	28,900	595	9,073	695	1,167	7,211	755	6,456

</TABLE>

SHARES OUTSTANDING

Table 2 below shows the number of common shares (which includes Class A preferred shares which were converted into common shares in 1995), preferred shares, and warrants outstanding at the end of each reporting period. The table also shows the average number of primary common shares (common shares outstanding increased by an amount based on potential future dilution due to warrants and options) used to calculate the Company's reported earnings per share. From the first quarter of 1996 to the first quarter of 1997, the average number of primary common shares outstanding increased by 98%.

TABLE 2
NUMBER OF SHARES

<TABLE>
<CAPTION>

	COMMON SHARES OUTSTANDING AT PERIOD END	PREFERRED SHARES OUTSTANDING AT PERIOD END	WARRANTS OUTSTANDING AT PERIOD END	AVERAGE NUMBER OF COMMON SHARES OUTSTANDING	POTENTIAL DILUTION DUE TO WARRANTS AND OPTIONS	AVERAGE NUMBER OF PRIMARY COMMON SHARES	AVERAGE NUMBER OF COMMON AND PREFERRED SHARES OUTSTANDING
Fiscal 1994	1,874,395	0	1,666,063	1,676,080	240,766	1,916,846	1,676,080
1995, Quarter 1	1,874,395	0	1,666,063	1,874,395	240,766	2,115,161	1,874,395
1995, Quarter 2	1,874,395	0	1,666,063	1,874,395	188,699	2,063,094	1,874,395
1995, Quarter 3	5,516,313	0	1,666,063	3,944,129	239,009	4,183,138	3,944,129
1995, Quarter 4	5,517,299	0	1,665,063	5,516,310	563,197	6,079,507	5,516,310
1996, Quarter 1	5,521,376	0	1,665,063	5,521,376	608,211	6,129,587	5,521,376
1996, Quarter 2	8,520,116	0	1,563,957	7,813,974	786,258	8,600,232	7,813,974
1996, Quarter 3	9,069,653	1,006,250	1,076,431	8,732,326	783,848	9,516,174	9,246,389
1996, Quarter 4	10,996,572	1,006,250	412,894	9,705,138	747,334	10,452,472	10,711,388
1997, Quarter 1	11,905,957	999,638	272,304	11,605,171	511,696	12,116,867	12,610,686

</TABLE>

EARNINGS PER PRIMARY SHARE (EPS)

Reported earnings per primary common share (EPS) in the first quarter of 1997 were $0.53. This was an increase of 66% from the $0.32 earned in the first quarter of 1996. As shown in Table 3, the two primary components of this increase in EPS were an 18% increase in the return on equity earned by the Company and a 33% increase in book value per share (the amount of equity per share the Company has available with which to generate earnings).

TABLE 3
PRIMARY COMPONENTS OF EARNINGS PER SHARE
(HISTORICAL AMORTIZED COST BASIS)

<TABLE>
<CAPTION>

<S>	AVERAGE COMMON EQUITY PER SHARE <C>	RETURN ON AVERAGE COMMON EQUITY <C>	EARNINGS PER AVERAGE COMMON SHARE OUTSTANDING <C>	ADJUSTMENT FOR POTENTIAL FUTURE DILUTION <C>	EARNINGS PER PRIMARY COMMON SHARE ("EPS") <C>
Fiscal 1994	$12.01	5.25%	$0.23	$0.03	$0.20
1995, Quarter 1	12.36	6.94%	0.21	0.02	0.19
1995, Quarter 2	12.27	7.82%	0.24	0.02	0.22
1995, Quarter 3	13.37	7.54%	0.25	0.01	0.24
1995, Quarter 4	13.38	7.10%	0.24	0.02	0.22
1996, Quarter 1	13.49	10.50%	0.35	0.03	0.32
1996, Quarter 2	15.05	8.50%	0.32	0.03	0.29
1996, Quarter 3	15.16	9.06%	0.34	0.02	0.32
1996, Quarter 4	15.99	10.53%	0.42	0.03	0.39
1997, Quarter 1	17.89	12.44%	0.56	0.03	0.53

</TABLE>

Return on equity increased as a result of increasing operational and capital efficiencies at the Company. As shown in Table 4, the return on total equity (including common and preferred equity) earned by the Company rose from 10.50% in the first quarter of 1996 to 12.16% in the first quarter of 1997 Net interest income per dollar of total equity increased from 14.92% to 15.30% as the Company increased its capital utilization efficiency. Credit expenses as a percentage of total equity dropped from 1.78% to 1.17% as the result of the shift the Company has been making since mid-1995 towards the acquisition of lower-credit-risk assets. Operating expenses as a percentage of total equity dropped from 2.64% to 1.97% as the Company became more productive. See "Earning Asset Yield and Interest Rate Spread", "Net Interest Income", "Credit Expenses" and "Operating Expenses" below.

TABLE 4
PRIMARY COMPONENTS OF RETURN ON TOTAL EQUITY
(HISTORICAL AMORTIZED COST BASIS)

<TABLE>
<CAPTION>

<S>	NET INTEREST INCOME RETURN ON AVERAGE TOTAL EQUITY <C>	CREDIT PROVISIONS/ AVERAGE TOTAL EQUITY <C>	OPERATING EXPENSE/ AVERAGE TOTAL EQUITY <C>	RETURN ON AVERAGE TOTAL EQUITY <C>	RETURN ON AVERAGE COMMON EQUITY <C>	RETURN ON AVERAGE ASSETS <C>	RATIO OF AVERAGE ASSETS TO TOTAL EQUITY <C>
Fiscal 1994	7.27%	0.00%	2.01%	5.25%	5.25%	1.81%	2.90x
1995, Quarter 1	10.73%	0.32%	3.48%	6.94%	6.94%	1.26%	5.48x
1995, Quarter 2	11.96%	0.70%	3.44%	7.82%	7.82%	1.10%	7.13x
1995, Quarter 3	10.94%	0.64%	2.76%	7.54%	7.54%	1.85%	4.08x
1995, Quarter 4	10.99%	1.90%	1.99%	7.10%	7.10%	1.40%	5.06x
1996, Quarter 1	14.92%	1.78%	2.64%	10.50%	10.50%	1.52%	6.89x
1996, Quarter 2	12.14%	1.62%	2.02%	8.50%	8.50%	1.30%	6.56x
1996, Quarter 3	12.40%	1.40%	1.82%	9.18%	9.06%	1.17%	7.83x
1996, Quarter 4	13.01%	0.81%	1.72%	10.48%	10.53%	1.25%	8.39x
1997, Quarter 1	15.30%	1.17%	1.97%	12.16%	12.44%	1.25%	9.74x

</TABLE>

The Company's equity per share (on a historical amortized cost basis excluding the mark-to-market valuation adjustments that have been made on a portion of the Company's assets) has increased due to accretive stock offerings priced at levels in excess of book value per share. In addition, in the first quarter of 1997, the Company's equity per share as reported increased due to market value

appreciation of Company assets. Equity

per share growth has been offset to some degree by the exercise of warrants and options, the payment of dividends (which are based on taxable income) in excess of GAAP income, and other factors. As shown in Table 24, total equity per share (excluding mark-to-market valuation adjustments) increased by 44% from $13.26 at March 31, 1996 to $19.03 at March 31, 1997. Table 5 shows how each of the Company's public stock offerings increased the Company's total equity per share (and thus its earnings per share potential).

TABLE 5
ACCRETIVE STOCK OFFERINGS
(HISTORICAL AMORTIZED COST BASIS)

<TABLE>
<CAPTION>

SECURITY	DATE	NUMBER OF SHARES	PRICE PER SHARE	NET PROCEEDS	% INCREASE IN NUMBER OF SHARES	% INCREASE IN TOTAL EQUITY	% INCREASE IN EQUITY PER SHARE
		(DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)					
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Common Stock - IPO	08/04/95	3,593,750	$ 15.50	$ 51,281	187%	224%	13%
Common Stock	04/19/96	2,875,000	20.25	54,730	52%	74%	15%
Class B Preferred Stock	08/17/96	1,006,250	31.00	29,712	12%	23%	10%
Common Stock	11/19/96	1,250,000	31.75	39,171	12%	23%	10%
Common Stock	01/24/97	750,000	39.50	29,223	6%	14%	7%

</TABLE>

TAXABLE INCOME

In order to determine its dividend levels, the Company must first determine its pre-tax, or taxable, income as calculated according to IRS guidelines. As a REIT, the Company deducts its dividend distributions from taxable income and is required to pay Federal taxes on any remaining undistributed taxable income. Since the Company intends to distribute 100% of its taxable income as dividends (and as a REIT is required to distribute at least 95%), the Company is not generally subject to Federal income tax. As a result of these REIT issues, the Company's total dividends will reflect its taxable income rather than its total net GAAP income.

Taxable income differs from GAAP because (i) taxable income credit expense equals actual credit losses rather than credit provisions (actual credit losses through March 31, 1997 have been minor), (ii) amortization methods differ for discount that has been created when mortgages have been acquired at a price below principal value, (iii) stock dividend equivalent rights which accrue on some stock options are deducted from GAAP income as an operating expense but are not deducted from taxable income until the stock is issued, and (iv) operating expenses differ in certain other aspects. Management believes taxable income is a closer approximation of current cash flow generation than is GAAP income.

Taxable income (before preferred dividends) in the first quarter of 1997 was $7.9 million and was 10% higher than GAAP net income (before preferred dividends) of $7.2 million during the same period. The table below presents the major differences between GAAP and taxable income for the Company.

TABLE 6
TAXABLE INCOME

<TABLE>
<CAPTION>

	GAAP NET INCOME BEFORE PREFERRED DIVIDENDS	GAAP CREDIT PROVISIONS IN EXCESS OF REALIZED CREDIT LOSSES	TAXABLE OPERATING EXPENSES AND MORTGAGE AMORTIZATION DIFFERENCES	TAXABLE INCOME BEFORE PREFERRED DIVIDENDS	TAXABLE INCOME AFTER PREFERRED DIVIDENDS	TAXABLE RETURN ON AVERAGE COMMON EQUITY	TAXABLE RETURN ON AVERAGE TOTAL EQUITY
			(DOLLARS IN THOUSANDS)				
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 382	$ 0	$ (28)	$ 354	$ 354	4.86%	4.86%
1995, Quarter 1	401	19	(12)	408	408	7.05%	7.05%

1995, Quarter 2	450	40	38	528	528	9.19%	9.19%
1995, Quarter 3	994	84	5	1,083	1,083	8.21%	8.21%
1995, Quarter 4	1,310	347	156	1,813	1,813	9.83%	9.83%
1996, Quarter 1	1,954	331	264	2,549	2,549	13.69%	13.69%
1996, Quarter 2	2,500	477	165	3,142	3,142	10.69%	10.69%
1996, Quarter 3	3,387	516	145	4,048	3,660	11.06%	10.97%
1996, Quarter 4	4,844	365	220	5,429	4,669	12.03%	11.75%
1997, Quarter 1	7,211	653	48	7,912	7,157	13.79%	13.34%

</TABLE>

DIVIDENDS

The Company declared a dividend of $0.60 per common share in the first quarter of 1997 resulting in a total dividend distribution (including preferred dividends) of $7.9 million, or 99.8% of taxable income earned during the quarter. Through March 31, 1997, cumulative taxable income exceeded cumulative dividends paid or declared by $0.4 million; the Company intends to distribute this excess taxable income as part of the Company's future dividends.

The first quarter common stock dividend of $0.60 per share represented a 46% increase over the $0.41 per common share declared in the fourth quarter of 1996 and an increase of 30% over the $0.46 declared for the first quarter of 1996.

The Company's Class B Preferred stock outstanding at period end receives a quarterly dividend of $0.755 per share or, if greater, the common stock dividend. There were 999,638 shares of Class B Preferred stock outstanding at March 31, 1997. Dividends for the first quarter of 1997 equaled the minimum level of $0.755 per share.

TABLE 7
DIVIDENDS

<TABLE>
<CAPTION>

(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)

	COMMON SHARES OUTSTANDING EARNING DIVIDEND	TAXABLE INCOME AFTER PREFERRED DIVIDENDS PER COMMON SHARE OUTSTANDING	COMMON DIVIDEND DECLARED PER SHARE	TOTAL COMMON DIVIDEND	PREFERRED SHARES OUTSTANDING EARNING DIVIDEND	PREFERRED DIVIDEND DECLARED PER SHARE	TOTAL PREFERRED DIVIDEND	TOTAL COMMON AND PREFERRED DIVIDENDS DECLARED
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	1,401,904	$ 0.25	$ 0.25	$ 350	0	$ 0.000	$ 0	$ 350
1995, Quarter 1	1,666,063	0.25	0.20	333	0	0.000	0	333
1995, Quarter 2	1,666,063	0.32	0.30	500	0	0.000	0	500
1995, Quarter 3	5,516,313	0.20	0.20	1,103	0	0.000	0	1,103
1995, Quarter 4	5,517,299	0.33	0.26	1,434	0	0.000	0	1,434
1996, Quarter 1	5,521,376	0.46	0.46	2,540	0	0.000	0	2,540
1996, Quarter 2	8,520,116	0.37	0.40	3,408	0	0.000	0	3,408
1996, Quarter 3	9,069,653	0.40	0.40	3,628	1,006,250	0.386	388	4,016
1996, Quarter 4	10,996,572	0.42	0.41	4,508	1,006,250	0.755	760	5,268
1997, Quarter 1	11,905,957	0.60	0.60	7,144	999,638	0.755	755	7,899

</TABLE>

EARNING ASSET YIELD AND INTEREST RATE SPREAD

The yield on the Company's earning assets (mortgages plus cash) declined from 7.34% in the first quarter of 1996 to 6.87% in the first quarter of 1997, a decline of 47 basis points. Over the same period, the Company's cost of funds declined by 7 basis points from 5.69% to 5.62% and the Company's cost of hedging declined by 2 basis points from 0.14% to 0.12%. As a result of these changes, the spread the Company earned between the yield on its assets and its cost of borrowed funds and hedging declined from 1.51% in the first quarter of 1996 to 1.13% in the first quarter of 1997.

The asset mix of the Company, and therefore the earning asset yield and the spread the Company earned, changed from the first quarter of 1996 to first quarter of 1997. Beginning in 1995, the Company ceased the acquisition of higher-yielding, wider-spread, higher-credit-risk assets such as mortgage securities rated below AA and focused on the acquisition of lower-yielding, narrower-spread, lower-credit-risk assets such as high-quality whole loans and mortgage securities rated AAA and AA. A competitive return on equity can be achieved by the Company on these new higher-quality assets, despite a lower yield and a narrower interest rate spread, as the Company makes a smaller internal capital allocation to these assets and expenses a lower level of credit

provisions.

Rapid asset growth has also led, on a temporary basis, to lower asset yields and a narrower spread for the Company. Newly acquired adjustable-rate mortgages typically have lower initial mortgage coupon rates than the Company earns on its existing mortgage portfolio. Typically the coupon rates on newly acquired mortgages are lower than average for six to twelve months. Thus the Company's average spread has been narrower on a temporary basis during periods of rapid balance sheet growth.

TABLE 8
EARNING ASSET YIELD AND INTEREST RATE SPREAD

<TABLE>
<CAPTION>

	AVERAGE COUPON RATE DURING PERIOD	AVERAGE COST BASIS	AVERAGE COUPON YIELD	EFFECT OF NET DISCOUNT/ (PREMIUM) AMORTIZATION	NET MORTGAGE YIELD	CASH YIELD	EARNING ASSET YIELD	COST OF FUNDS	COST OF HEDGING	INTEREST RATE SPREAD
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	6.09%	100.0%	6.09%	0.45%	6.54%	4.73%	6.33%	5.55%	0.06%	0.72%
1995, Quarter 1	6.32%	99.5%	6.35%	0.70%	7.05%	4.96%	7.03%	5.96%	0.06%	1.01%
1995, Quarter 2	6.82%	98.5%	6.92%	0.51%	7.43%	5.57%	7.41%	6.26%	0.23%	0.92%
1995, Quarter 3	7.29%	98.7%	7.39%	0.30%	7.69%	5.53%	7.66%	6.09%	0.28%	1.29%
1995, Quarter 4	7.59%	99.3%	7.64%	(0.25%)	7.39%	5.48%	7.34%	6.04%	0.18%	1.12%
1996, Quarter 1	7.73%	98.8%	7.82%	(0.44%)	7.38%	5.93%	7.34%	5.69%	0.14%	1.51%
1996, Quarter 2	7.47%	100.0%	7.48%	(0.56%)	6.92%	5.61%	6.90%	5.57%	0.16%	1.17%
1996, Quarter 3	7.52%	101.0%	7.44%	(0.52%)	6.92%	5.30%	6.90%	5.78%	0.14%	0.98%
1996, Quarter 4	7.58%	101.4%	7.48%	(0.59%)	6.89%	5.31%	6.87%	5.76%	0.12%	0.99%
1997, Quarter 1	7.70%	101.8%	7.56%	(0.68%)	6.88%	5.69%	6.87%	5.62%	0.12%	1.13%

</TABLE>

The Company's earning asset yield and spread were also diminished in the first quarter of 1997 due to an increase in the rate of mortgage principal repayments on those assets for which the Company paid a premium price. As shown in Table 9, the Company wrote off its premium balances at an annual rate of 25% in the first quarter of 1996 and 29% in the first quarter of 1997. The Company writes off premium as an amortization expense at a rate equal to or greater than the actual monthly rate of principal repayment on those assets, so increases in principal repayment rates cause an increase in amortization expense. The mortgages the Company acquired at a discount also had rapid rates of mortgage principal repayment; the Company does not amortize its discount balances into income at a correspondingly rapid rate, however, as the discount balance acts as a form of credit reserve for these assets. See "Credit Reserves" below.

The average annualized rate of principal repayment of the Company's mortgage assets was 32% in the first quarter of 1997. This measure includes scheduled principal payments, prepayments of principal, and the effects of returns of principal caused by certain calls imbedded in securitized mortgage interests. It represents the rate at which the Company must acquire new mortgage assets in order to maintain its current size. A significant and increasing portion of the Company's mortgage assets represent senior interests in pools of mortgage loans; such senior interests typically receive principal repayments at an accelerated rate relative to the rate of principal pay down of the underlying mortgage pool. The Company's rate of mortgage principal repayment has increased, in part, because of this change in asset mix. The weighted average Conditional Prepayment Rate ("CPR") of the Company's mortgage loans and for the pools of mortgages underlying the Company's securitized interests was 23% in the first quarter of 1997; CPR is a standard mortgage industry calculation which measures mortgage prepayments but does not include scheduled mortgage principal repayments or the effects of accelerated payments or calls. The adjustable-rate mortgages the Company has acquired have generally been of a type that should be expected to experience faster rates of principal repayment and higher CPRs than many other types of adjustable-rate and fixed-rate mortgages. At acquisition, the Company assumes that these mortgages will pay down at rapid rates; the Company adjusts its bids for mortgage assets accordingly.

TABLE 9
AMORTIZATION ON MORTGAGE ASSETS

<TABLE>

<CAPTION>

	AVERAGE DISCOUNT BALANCE	DISCOUNT AMORT.	ANNUAL RATE OF DISCOUNT AMORT.	AVERAGE PREMIUM BALANCE	PREMIUM AMORT.	ANNUAL RATE OF PREMIUM AMORT.	NET AMORT. INCOME/ (EXPENSE)	NET MORTGAGE PRINCIPAL REPAYMTS RECEIVED	NET MORTGAGE PRINCIPAL REPAYMT RATE	EST. AVE. CONDITIONAL PREPYMNT RATE "CPR"
	(DOLLARS IN THOUSANDS)									
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 440	$ 101	63%	$ 450	$ 19	12%	$ 82	$ 1,244	7%	9%
1995, Quarter 1	1,440	234	65%	785	19	10%	215	2,673	9%	8%
1995, Quarter 2	3,528	237	27%	1,175	34	12%	203	2,934	7%	11%
1995, Quarter 3	6,017	280	19%	3,351	123	15%	157	8,319	16%	21%
1995, Quarter 4	10,889	210	8%	8,314	429	21%	(219)	24,898	28%	25%
1996, Quarter 1	16,941	177	4%	11,299	707	25%	(530)	32,814	27%	26%
1996, Quarter 2	16,739	245	6%	16,402	1,268	31%	(1,023)	53,058	29%	29%
1996, Quarter 3	16,471	271	7%	27,233	1,707	25%	(1,436)	76,942	28%	24%
1996, Quarter 4	16,236	217	5%	36,977	2,425	26%	(2,208)	95,610	26%	23%
1997, Quarter 1	15,927	272	7%	56,374	4,090	29%	(3,818)	173,362	32%	23%

</TABLE>

The Company's earning asset yield and interest rate spread also declined during the first quarter of 1997 as prospective yields and spreads available from newly acquired mortgages declined throughout 1996 and thus far in 1997. Mortgage prices have risen over the past year relative to expected future cash flows. Management believes mortgage prices have risen due to strong demand from banks, savings and loans, and other financial institutions (stemming from a continued state of over-capitalization), an increase in the price of financial assets in general, a decrease in interest rate volatility, and other factors. The effect on the Company's earnings of this increase in mortgage prices for new assets was offset to some degree by a reduced cost of hedging.

As noted, the Company's spread has narrowed over the past year for a variety of reasons (some of which are temporary); at the same time, however, the Company has significantly improved its operating and capital efficiencies. These efficiencies have allowed the Company to increase return on equity over this period despite lower yields and spreads.

As compared to the spread of 0.99% the Company earned in the fourth quarter of 1996, the 1.13% earned in the first quarter of 1997 was an improvement. The Company's earning asset yield remained flat at 6.87% while the Company lowered its cost of funds by 0.14%.

NET INTEREST INCOME

Net interest income, or interest income revenues less the cost of funds and hedging, increased from $2.8 million in the first quarter of 1996 to $9.1 million in the first quarter of 1997.

As a percentage of average total equity, net interest income increased from 14.92% in the first quarter of 1996 to 15.30% in the first quarter of 1997. There were three primary factors affecting profitability at the net interest income level. First, the earning asset yield decreased from 7.34% to 6.87% over this period, thus reducing the rate of net interest income the Company earned from its mortgage assets funded directly with equity proceeds. In addition, as discussed above, the spread the Company earned between its asset yield and its cost of borrowed funds decreased from 1.51% to 1.13%. As an offsetting positive factor, however, the Company was able to reduce risk on its balance sheet and thereby lower its target equity-to-assets ratio. This combined with better coordination of the timing of receipt of new equity and its employment in earning assets allowed the Company to utilize more leverage and increase returns. The target equity-to-assets ratio dropped from 12.8% to 10.1% and the average actual equity-to-asset ratio dropped from 14.5% to 10.3%. (Balance sheet capacity utilization increased from 88% to 98%).

From the fourth quarter of 1996 to the first quarter of 1997, net interest income as a percentage of equity increased from 13.01% to 15.30%. The earning asset yield in both quarters was 6.87%, so earnings from

equity-funded assets were similar. The interest rate spread earned increased from 0.99% to 1.13%. In addition, the Company was able to make greater use of leverage due to continued risk reduction (the target equity-to-assets ratio dropped from 10.2% to 10.1%) and due to an increase in balance sheet capacity utilization from 86% to 98% (the average actual equity-to-asset ratio dropped from 11.9% to 10.3%).

TABLE 10
NET INTEREST INCOME

<TABLE>
<CAPTION>

	NET INTEREST INCOME RETURN ON AVERAGE TOTAL EQUITY	EARNING ASSET YIELD	INTEREST RATE SPREAD	AVERAGE EQUITY TO ASSETS RATIO DURING PERIOD	AVERAGE TARGET EQUITY TO ASSETS RATIO	PERCENT OF CAPITAL EMPLOYED DURING PERIOD	RATIO OF SPREAD FUNDED ASSETS TO EQUITY	NET INTEREST MARGIN
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	7.27%	6.33%	0.72%	34.5%	10.6%	31%	1.88x	2.50%
1995, Quarter 1	10.73%	7.03%	1.01%	18.2%	12.9%	71%	4.44x	1.96%
1995, Quarter 2	11.96%	7.41%	0.92%	14.0%	13.2%	94%	6.09x	1.68%
1995, Quarter 3	10.94%	7.66%	1.29%	24.5%	13.6%	55%	3.03x	2.68%
1995, Quarter 4	10.99%	7.34%	1.12%	19.8%	13.6%	69%	4.00x	2.17%
1996, Quarter 1	14.92%	7.34%	1.51%	14.5%	12.8%	88%	5.86x	2.17%
1996, Quarter 2	12.14%	6.90%	1.17%	15.2%	11.4%	75%	5.54x	1.85%
1996, Quarter 3	12.40%	6.90%	0.98%	12.8%	10.7%	84%	6.77x	1.58%
1996, Quarter 4	13.01%	6.87%	0.99%	11.9%	10.2%	86%	7.31x	1.55%
1997, Quarter 1	15.30%	6.87%	1.13%	10.3%	10.1%	98%	8.67x	1.57%

</TABLE>

The net interest margin is net interest income divided by assets. This ratio changes as a function of the leverage ratio and other factors. As shown in Table 10, due to improving spreads and other efficiencies the net interest margin has remained steady in a narrow range over the last three quarters even though the Company has made greater use of leverage.

CREDIT LOSSES AND PROVISIONS

Realized actual credit losses were $0 in the first quarter of 1996 and were $42,713 in the first quarter of 1997. The losses reduced taxable income and dividends by the indicated amounts for those quarters, but did not impact reported GAAP net income as they were previously provided for. The Company expects to realize credit losses throughout 1997.

The Company reduced reported net income by $695,470 in the first quarter of 1997 to provide for possible future credit losses. As shown in Table 11, this provision represented 0.12% of average assets and 1.17% of total average equity. The credit provision in the first quarter of 1996 was $331,516, or 0.26% of assets and 1.78% of equity. The Company has been able to reduce its credit provision rate as its reduces the average level of credit risk on its balance sheet (below-BBB-rated mortgage securities have declined from 4.9% of assets at March 31, 1996 to 1.1% of assets at March 31, 1997).

The Company recently changed its policy regarding credit provisions for whole mortgage loans. Formerly, the Company took a provision for "A" quality whole loans at the time of acquisition equal to 0.30% of the principal value of the mortgages. In the fourth quarter of 1996, the Company started taking whole loan credit provisions on an on-going, rather than a one-time, basis in order to avoid large unwarranted swings in reported income that could be caused by acquisitions of bulk loan portfolios. Under the new policy, the Company takes on-going credit provisions at an annual rate of 0.15% of the principal value of "A" quality whole loans. The increase in credit provisions from the fourth quarter of 1996 to the first quarter of 1997 is primarily the result of this change in provision method and of a large bulk whole loan acquisition at the end of 1996.

TABLE 11
CREDIT PROVISIONS AND ACTUAL CREDIT LOSSES

<TABLE>
<CAPTION>

	TOTAL CREDIT PROVISIONS	TOTAL ACTUAL CREDIT LOSSES	ANNUALIZED CREDIT PROVISIONS TO AVERAGE ASSETS	ANNUALIZED CREDIT PROVISIONS TO AVERAGE TOTAL EQUITY
	(DOLLARS IN THOUSANDS)			
<S>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 0	$ 0	0.00%	0.00%
1995, Quarter 1	19	0	0.06%	0.32%
1995, Quarter 2	40	0	0.10%	0.70%
1995, Quarter 3	84	0	0.16%	0.64%

1995, Quarter 4	350	4	0.38%	1.90%
1996, Quarter 1	331	0	0.26%	1.78%
1996, Quarter 2	477	0	0.25%	1.62%
1996, Quarter 3	516	0	0.18%	1.40%
1996, Quarter 4	372	7	0.10%	0.81%
1997, Quarter 1	695	42	0.12%	1.17%

</TABLE>

OPERATING EXPENSES

The Company has been able to improve its operating efficiency over time. As shown in Table 12, total operating expenses rose from $0.5 million in the first quarter of 1996 to $1.2 million in the first quarter of 1997. As a percentage of average assets, however, annualized operating expenses dropped from 0.38% to 0.20% and as a percentage of total average equity annualized operating expenses dropped from 2.64% to 1.97%. Thus, the improvement in return on equity over this period due to increasing operational efficiencies was 0.67%.

From the fourth quarter of 1996 to the first quarter of 1997, operating expenses rose by 47%, although most measures of operational efficiency remained the same or improved. The Company significantly increased the accrual rates it uses for cash compensation in anticipation of moving to a market-based salary and bonus system for all employees except the Chairman/CEO and the President. Following a third-party analysis of compensation practices at comparable companies, the management and the Board of Directors decided that the Company and its shareholders would best be served by increasing salaries and materially increasing potential bonus awards for some employees in order to reflect market rates of compensation. In order to maintain the current close alignment between shareholders' interests and the compensation of the top employees, however, the Board of Directors decided that the two senior executives will continue to be compensated primarily with stock options and related dividend equivalent rights and anticipates, given current information, that these two executives will continue to receive salary and annual bonus awards which will be substantially below market-based rates.

TABLE 12
OPERATING EXPENSES

<TABLE>
<CAPTION>

<S>	COMPENSATION AND BENEFITS EXPENSE <C>	OTHER OPERATING EXPENSE <C>	TOTAL OPERATING EXPENSE <C>	EFFICIENCY RATIO (OPERATING EXPENSE/ NET INTEREST INCOME) <C>	OPERATING EXPENSE/ AVERAGE ASSETS <C>	OPERATING EXPENSE/ AVERAGE TOTAL EQUITY <C>	AVERAGE ASSETS PER AVE. # OF EMPLOYEES ($MM) <C>
	(DOLLARS IN THOUSANDS)						
Fiscal 1994	$ 63	$ 83	$ 146	28%	0.69%	2.01%	$ 12
1995, Quarter 1	81	120	201	32%	0.63%	3.48%	25
1995, Quarter 2	81	117	198	29%	0.48%	3.44%	33
1995, Quarter 3	204	160	364	25%	0.68%	2.76%	39
1995, Quarter 4	151	217	368	18%	0.39%	1.99%	53
1996, Quarter 1	319	174	493	18%	0.38%	2.64%	70
1996, Quarter 2	384	210	594	17%	0.31%	2.02%	84
1996, Quarter 3	390	281	671	15%	0.23%	1.82%	115
1996, Quarter 4	480	316	796	13%	0.21%	1.72%	155
1997, Quarter 1	732	435	1,167	13%	0.20%	1.97%	221

</TABLE>

PER SHARE TRENDS

Table 13 below shows the Company's assets, equity, and income statement components on a per average share outstanding basis (including both common and preferred shares). From the first quarter of 1996 to the first quarter of 1997, the Company was able to increase its average assets per average share by 97%, from $93 to $183. This increase was due to reduced equity-to-assets ratio targets attributable to risk reductions in the balance sheet, rising capital efficiencies resulting in greater balance sheet capacity utilization, and increasing equity per share values. Revenues per share increased by 85% and net interest income per share increased by 44% over the one year period from first quarter 1996 to first quarter 1997. Per share costs of credit expenses and operating expenses remained stable. Total net income per share (including preferred and common shares) rose 63% from $0.35 to $0.57.

TABLE 13
PER SHARE INFORMATION

	AVERAGE ASSETS PER AVERAGE COMMON AND PREFERRED SHARE	AVERAGE TOTAL EQUITY PER AVERAGE COMMON AND PREFERRED SHARE	REVENUES PER AVERAGE COMMON AND PREFERRED SHARE	NET INTEREST INCOME PER AVERAGE COMMON AND PREFERRED SHARE	CREDIT PROVISIONS PER AVERAGE COMMON AND PREFERRED SHARE	OPERATING EXPENSES PER AVERAGE COMMON AND PREFERRED SHARE	NET INCOME PER AVERAGE COMMON AND PREFERRED SHARE
Fiscal 1994	$ 34.85	$12.01	$0.77	$0.31	$0.00	$0.09	$0.22
1995, Quarter 1	67.77	12.36	1.16	0.33	0.01	0.11	0.21
1995, Quarter 2	87.54	12.27	1.58	0.37	0.02	0.11	0.24
1995, Quarter 3	54.54	13.37	1.01	0.37	0.02	0.09	0.26
1995, Quarter 4	67.72	13.38	1.20	0.37	0.06	0.07	0.24
1996, Quarter 1	92.87	13.49	1.65	0.50	0.06	0.09	0.35
1996, Quarter 2	98.76	15.05	1.65	0.45	0.06	0.07	0.32
1996, Quarter 3	124.97	15.96	2.10	0.50	0.06	0.07	0.37
1996, Quarter 4	144.83	17.26	2.42	0.55	0.03	0.07	0.45
1997, Quarter 1	183.09	18.81	3.06	0.72	0.06	0.09	0.57

FINANCIAL CONDITION

SUMMARY

Management believes the Company is well capitalized for the levels of risks undertaken. The Company's assets are single-family mortgage assets. A majority of these assets are further credit-enhanced beyond the inherent value of a mortgage secured by a first lien on a residential property. The liquidity of a majority of the Company's assets has been enhanced through the securitization and credit rating process. The interest rate risks of the Company's assets and liabilities are well matched; all mortgages have adjustable-rate coupons after an initial period and are financed with equity and with variable-rate borrowings. Interest rate risks which remain on the balance sheet after this matching program are mitigated through the Company's interest rate hedging program. The Company has uncommitted borrowing facilities in excess of its needs. The Company only takes credit risk on mortgages underwritten to "A" quality standards. The Company takes credit provisions to reserve for potential future credit losses. The Company has low operating expenses and a high percentage of its equity invested in earning assets. The Company's capital base is tangible capital. Nevertheless, the Company maintains an equity-to-assets ratio that is higher than that of many banks, savings and loans, insurance companies, and REITs that act as mortgage portfolio lenders.

END OF PERIOD BALANCE SHEET

The Company's assets consist primarily of earning assets (mortgage assets and cash). As shown in the table below, total assets increased by $0.5 billion, or 21%, from December 31, 1996 to March 31, 1997. The figures in the table below present the balance sheet on a historical amortized cost basis and therefore exclude the mark-to-market valuation account from balances shown for mortgage assets, interest rate agreements, and stockholders' equity. This is the presentation the Company would report if it had classified all of its assets as "held-to-maturity".

TABLE 14
END OF PERIOD BALANCE SHEET
(HISTORICAL AMORTIZED COST BASIS)

(DOLLARS IN THOUSANDS)

END OF PERIOD	CASH	MORTGAGE ASSETS	CREDIT RESERVE	INTEREST RATE AGRMNTS	RCVBLES AND OTHER ASSETS	TOTAL ASSETS	BORROWINGS	PAYABLES	PREFERRED EQUITY	COMMON EQUITY	TOTAL EQUITY
Fiscal 1994	$ 1,027	$ 120,135	$ (0)	$ 1,791	$ 1,132	$ 124,085	$ 100,376	$ 872	$ 0	$ 22,837	$ 22,837
1995, Quarter 1	953	141,793	(19)	2,069	1,193	145,989	121,998	1,090	0	22,901	22,901

1995, Quarter 2	1,620	174,415	(59)	2,025	1,634	179,635	155,881	907	0	22,847	22,847
1995, Quarter 3	1,150	298,894	(143)	2,394	2,650	304,944	228,826	2,095	0	74,023	74,023
1995, Quarter 4	4,825	436,235	(490)	2,521	3,941	447,032	370,316	2,951	0	73,765	73,765
1996, Quarter 1	9,705	569,744	(821)	2,534	5,216	586,378	508,721	4,447	0	73,210	73,210
1996, Quarter 2	10,407	1,011,846	(1,298)	2,835	9,092	1,032,882	896,214	7,821	0	128,847	128,847
1996, Quarter 3	14,599	1,377,332	(1,814)	3,286	12,136	1,405,539	1,225,094	14,867	29,712	135,866	165,578
1996, Quarter 4	11,068	2,155,469	(2,180)	6,200	17,100	2,187,657	1,953,103	20,089	29,579	184,886	214,465
1997, Quarter 1	12,985	2,605,323	(2,833)	7,879	19,592	2,642,946	2,373,279	24,123	29,383	216,161	245,544

</TABLE>

AVERAGE DAILY BALANCE SHEET

Table 15 presents the estimated average daily balances of the major components of the Company's balance sheet as presented on a historical amortized cost basis.

TABLE 15
AVERAGE DAILY BALANCE SHEET
(HISTORICAL AMORTIZED COST BASIS)

<TABLE>
<CAPTION>

(DOLLARS IN THOUSANDS)

END OF PERIOD	CASH	MORTGAGE ASSETS	CREDIT RESERVE	INTEREST RATE AGRMNTS	RCVBLES AND OTHER ASSETS	TOTAL ASSETS	BORROWINGS	PAYABLES	PREFERRED EQUITY	COMMON EQUITY	TOTAL EQUITY
Fiscal 1994	$ 6,627	$ 50,081	$ (0)	$ 759	$ 947	$ 58,414	$ 37,910	$ 367	$ 0	$ 20,137	$ 20,137
1995, Quarter 1	1,217	122,181	(6)	1,684	1,958	127,034	102,894	978	0	23,162	23,162
1995, Quarter 2	1,466	158,183	(31)	1,916	2,559	164,093	139,979	1,111	0	23,003	23,003
1995, Quarter 3	3,597	204,672	(82)	2,120	4,819	215,126	159,794	2,585	0	52,747	52,747
1995, Quarter 4	10,709	349,676	(249)	2,428	11,000	373,564	295,089	4,654	0	73,821	73,821
1996, Quarter 1	14,639	483,102	(594)	2,503	12,094	512,762	435,979	2,324	0	74,459	74,459
1996, Quarter 2	14,402	734,010	(1,002)	2,737	21,566	771,713	651,643	2,472	0	117,598	117,598
1996, Quarter 3	18,854	1,104,844	(1,491)	3,185	30,129	1,155,521	999,229	8,728	15,179	132,385	147,564
1996, Quarter 4	16,137	1,490,985	(1,952)	4,681	41,430	1,551,281	1,351,510	14,898	29,671	155,202	184,873
1997, Quarter 1	12,147	2,233,410	(2,394)	6,899	58,856	2,308,918	2,056,051	15,691	29,545	207,631	237,176

</TABLE>

MORTGAGE ASSET ACQUISITIONS

The two principal criteria the Company uses when acquiring mortgage assets are: (i) the mortgages must be "A" quality in terms of underwriting and documentation standards, or, if the loans in a securitized pool of mortgages have not been underwritten to "A" quality standards, the interest in that pool acquired by the Company must be credit-enhanced through insurance, subordination or other means to such a degree that the interest has been rated AAA or AA by the credit rating agencies, and (ii) the risk-adjusted returns on equity the Company anticipates earning on such assets must be attractive across a variety of economic scenarios relative to the Company's cost of capital and relative to other available mortgage assets. Assets which are lower-risk, lower-yield, narrower-spread and higher-priced may produce higher returns on equity across a variety of scenarios for the Company than riskier assets due to a lower capital allocation to the lower-risk asset.

The Company acquired $627 million of mortgage assets in the first quarter of

1997. A majority of these asset acquisitions did not close until late March, so the income from these new assets will not have a significant effect on the Company's income until the second quarter of 1997.

As shown in Table 16, an increasing percentage of the Company's acquisitions have consisted of whole mortgage loans. The Company has also continued to acquire adjustable-rate mortgage securities rated AAA and AA, but has not acquired mortgage securities rated below AA since 1995.

TABLE 16
MORTGAGE ASSET ACQUISITIONS

<TABLE>
<CAPTION>

	ASSET ACQUISITIONS AT COST	AVERAGE PRICE AS % OF PRINCIPAL VALUE	AVERAGE INITIAL COUPON	"A" QUALITY WHOLE LOANS	FHLMC & FNMA GUARANTEED MORTGAGES	AAA &AA RATED MORTGAGE SECURITIES	A & BBB RATED MORTGAGE SECURITIES	BELOW BBB RATED MORTGAGE SECURITIES
				(DOLLARS IN THOUSANDS)				
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 121,297	99.53%	5.87%	0.0%	64.8%	28.1%	4.3%	2.8%
1995, Quarter 1	24,116	94.80%	6.78%	0.0%	15.1%	49.1%	25.6%	10.2%
1995, Quarter 2	35,355	93.11%	6.42%	0.0%	65.8%	13.1%	0.0%	21.1%
1995, Quarter 3	132,640	103.14%	7.40%	0.0%	59.0%	32.3%	3.8%	4.9%
1995, Quarter 4	162,461	95.78%	7.39%	16.5%	52.4%	20.1%	5.5%	5.5%
1996, Quarter 1	166,852	102.60%	7.60%	0.0%	47.6%	52.4%	0.0%	0.0%
1996, Quarter 2	496,184	102.36%	7.30%	9.9%	71.5%	18.6%	0.0%	0.0%
1996, Quarter 3	443,860	102.74%	7.53%	14.4%	69.9%	15.7%	0.0%	0.0%
1996, Quarter 4	875,968	102.86%	7.81%	47.3%	17.5%	35.2%	0.0%	0.0%
1997, Quarter 1	627,075	102.46%	7.45%	40.0%	19.9%	40.1%	0.0%	0.0%

</TABLE>

SUMMARY OF MORTGAGE ASSET CHARACTERISTICS

All the Company's mortgage assets acquired through March 31, 1997 were single-family, adjustable-rate, first-lien mortgages or securitized interests in pools of such loans. The average credit rating equivalent has been maintained at AA+. At March 31, 1997, $1.8 billion principal value of the Company's mortgage assets (72%) were classified as "available-for-sale" and were carried on its balance sheet at estimated bid-side market value. The remaining $0.7 billion principal value of the Company's mortgages (28%) were recently re-classified as "held-to-maturity". Over time, the carrying value of these re-classified mortgage assets will be adjusted towards historical amortized cost through quarterly adjustments to the valuation account. At March 31, 1997, the estimated liquidation value of all of the Company's mortgage assets was $2.604 billion; net unrealized gains on all mortgage assets were 0.7% of the historical amortized cost before credit reserve.

TABLE 17
MORTGAGE ASSET SUMMARY

<TABLE>
<CAPTION>

END OF PERIOD	MORTGAGE PRINCIPAL VALUE	UNAMORTIZED PREMIUM	UNAMORTIZED DISCOUNT	HISTORICAL AMORTIZED COST	CREDIT RESERVE	GAAP VALUATION ACCOUNT	CARRYING VALUE	ESTIMATED LIQUIDATION VALUE	UNREALIZED GAINS/ (LOSSES) AS % OF AMORTIZED COST OF MORTGAGE ASSETS
					(DOLLARS IN THOUSANDS)				
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>

Fiscal 1994	$ 120,627	$ 827	$ 1,319	$ 120,135	$ (0)	$(2,658)	$ 117,477	$ 117,477	(2.21%)
1995, Quarter 1	143,393	914	2,515	141,792	(19)	87	141,860	141,860	0.06%
1995, Quarter 2	178,429	1,409	5,423	174,415	(59)	886	175,242	175,242	0.51%
1995, Quarter 3	298,718	7,498	7,322	298,894	(143)	34	298,785	175,242	0.01%
1995, Quarter 4	443,625	9,643	17,032	436,236	(490)	(3,502)	432,244	432,244	(0.80%)
1996, Quarter 1	573,807	12,790	16,853	569,744	(821)	(3,764)	565,159	565,159	(0.66%)
1996, Quarter 2	1,005,765	22,691	16,609	1,011,847	(1,298)	(3,069)	1,007,480	1,007,480	(0.30%)
1996, Quarter 3	1,361,062	32,607	16,338	1,377,331	(1,814)	353	1,375,870	1,375,870	0.03%
1996, Quarter 4	2,117,245	54,317	16,039	2,155,469	(2,180)	139	2,153,428	2,153,428	0.01%
1997, Quarter 1	2,555,857	65,106	15,641	2,605,322	(2,833)	2,225	2,604,714	2,604,240	0.07%

</TABLE>

The following table shows the average characteristics of the Company's mortgage assets at the end of each reporting period. The index level is the weighted average rate of the various short-term interest rate indices which determine coupon adjustments. Unless limited by periodic or lifetime caps, the mortgage coupons adjust at the end of each adjustment period to the level of the index plus the net margin. The fully-indexed rate is the current index

plus the net margin: this is the maximum level to which the coupon could adjust over time should interest rates remain unchanged. The rate of adjustment of the current coupon to the fully-indexed rate is determined by the length of the adjustment periods and the periodic caps of the mortgage loans. Due to increases in short-term interest rates in March 1997, the Company's average mortgage coupon of 7.70% was 0.49% below the full potential coupon rate of the mortgages of 8.19% at March 31, 1997.

TABLE 18
AVERAGE MORTGAGE ASSET CHARACTERISTICS

<TABLE>
<CAPTION>

END OF PERIOD	MORTGAGE COUPON RATE	INTEREST RATE INDEX LEVEL	MORTGAGE NET MARGIN	MORTGAGE FULLY-INDEXED RATE	COUPON RATE VS. FULLY-INDEXED RATE	AVERAGE NUMBER OF MONTHS TO NEXT ADJUSTMENT	LIFETIME CAP
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	6.00%	6.94%	2.25%	9.19%	(3.19%)	3	11.48%
1995, Quarter 1	6.53%	6.47%	2.24%	8.71%	(2.18%)	3	11.57%
1995, Quarter 2	6.94%	5.99%	2.21%	8.20%	(1.26%)	3	11.54%
1995, Quarter 3	7.35%	5.86%	2.20%	8.06%	(0.71%)	4	11.56%
1995, Quarter 4	7.50%	5.44%	2.08%	7.52%	(0.02%)	3	11.54%
1996, Quarter 1	7.59%	5.47%	2.11%	7.58%	0.01%	3	11.53%
1996, Quarter 2	7.42%	5.72%	2.21%	7.93%	(0.51%)	4	11.71%
1996, Quarter 3	7.55%	5.70%	2.21%	7.91%	(0.36%)	4	11.69%
1996, Quarter 4	7.75%	5.58%	2.24%	7.82%	(0.07%)	5	11.73%
1997, Quarter 1	7.70%	5.98%	2.21%	8.19%	(0.49%)	5	11.91%

</TABLE>

As shown in Table 19, over the course of 1996 and through the first quarter of 1997, the Company increased its percentage of mortgage assets which had coupon rates adjusting as a function of short-term U.S. Treasury interest rate indices. Such assets represented 60% of all mortgage assets as of March 31, 1997 while 40% of Company assets adjusted off of LIBOR, CD, or other indices. Since changes in the cost of the Company's liabilities are generally correlated with changes in LIBOR rates, the Company's spread income will be diminished should LIBOR rates rise relative to U.S. Treasury rates. Management expects that this effect, should it occur, would be offset to some degree by the interest rate agreements (caps, swaps, and basis swaps) owned by the Company.

TABLE 19
MORTGAGE ASSETS BY INDEX

<TABLE>
<CAPTION>

	SIX-MONTH	ONE-MONTH	SIX-MONTH BANK	HYBRID 3/1 ONE-YEAR	STANDARD ONE-YEAR	SIX-MONTH

	LIBOR INDEX	LIBOR INDEX	CD INDEX	TREASURY INDEX	TREASURY INDEX	TREASURY INDEX	OTHER
Period of Initial Coupon Set	6 months	3 months	6 months	36 months	12 months	6 months	various
Subsequent Adjust Frequency	6 months	1 month	6 months	12 months	12 months	6 months	various
Average Next Adjustment	3 months	1 month	3 months	30 months	6 months	3 months	various
Annualized Periodic Cap	2%	none	2%	2%	2%	2%	various
			% OF TOTAL MORTGAGE ASSETS AT PERIOD END				
Fiscal 1994	78.3%	3.8%	17.9%	0.0%	0.0%	0.0%	0.0%
1995, Quarter 1	78.7%	3.1%	17.3%	0.0%	0.9%	0.0%	0.0%
1995, Quarter 2	83.1%	2.5%	13.7%	0.0%	0.7%	0.0%	0.0%
1995, Quarter 3	66.9%	1.4%	11.5%	0.0%	11.5%	7.5%	1.2%
1995, Quarter 4	60.0%	7.5%	12.5%	0.0%	12.5%	5.0%	2.5%
1996, Quarter 1	63.1%	6.5%	8.8%	0.0%	14.8%	3.6%	3.2%
1996, Quarter 2	54.2%	3.2%	3.3%	0.0%	33.2%	4.4%	1.7%
1996, Quarter 3	45.6%	2.2%	2.4%	0.0%	45.6%	3.0%	1.2%
1996, Quarter 4	35.9%	1.4%	2.5%	0.0%	56.1%	2.0%	2.1%
1997, Quarter 1	34.0%	2.6%	1.9%	2.4%	55.8%	1.6%	1.7%

</TABLE>

The table below shows the balance of the Company's whole mortgage loans and the Company's securitized mortgage assets segregated by credit rating equivalent. Due to the "A" quality underwriting and documentation standards of the Company's whole loans, management believes that over 90% of the balance of these loans would receive a credit rating of AAA or AA should the Company securitize these loans and seek a credit rating from the credit rating agencies in the future. As a result, management believes that percentage of the Company's balance sheet which had the equivalent of a AAA or AA rating was 94% or greater at both December 31, 1996 and March 31, 1997.

TABLE 20
MORTGAGE ASSETS BY CREDIT RATING EQUIVALENT

<TABLE>
<CAPTION>

END OF PERIOD	WHOLE MORTGAGE LOAN AMORTIZED COST	AAA/ AA RATING EQUIV. AMORTIZED COST	A/ BBB RATING EQUIV. AMORTIZED COST	BB/ OTHER RATING EQUIV. AMORTIZED COST	WHOLE LOAN PERCENT OF TOTAL	AAA/ AA RATING EQUIV. PERCENT OF TOTAL	A/ BBB RATING EQUIV. PERCENT OF TOTAL	BB/ OTHER RATING EQUIV. PERCENT OF TOTAL	AVERAGE CREDIT RATING EQUIVALENT
		(DOLLARS IN THOUSANDS)							
Fiscal 1994	$ 0	$ 111,274	$ 5,208	$ 3,376	0.0%	92.9%	4.3%	2.8%	AA+
1995, Quarter 1	0	124,556	11,398	5,839	0.0%	87.9%	8.0%	4.1%	AA+
1995, Quarter 2	0	149,645	11,418	13,352	0.0%	85.8%	6.5%	7.7%	AA+
1995, Quarter 3	0	262,418	16,505	19,971	0.0%	87.8%	5.5%	6.7%	AA+
1995, Quarter 4	26,449	355,500	25,417	28,869	6.1%	81.5%	5.8%	6.6%	AA+
1996, Quarter 1	24,851	490,611	26,231	28,051	4.4%	86.1%	4.6%	4.9%	AA+

1996, Quarter 2	69,680	887,888	25,422	28,858	6.9%	87.7%	2.5%	2.9%	AA+
1996, Quarter 3	127,809	1,195,188	25,429	28,906	9.3%	86.8%	1.8%	2.1%	AA+
1996, Quarter 4	527,280	1,573,868	25,385	28,935	24.5%	73.0%	1.2%	1.3%	AA+
1997, Quarter 1	731,957	1,819,100	25,311	28,955	28.1%	69.8%	1.0%	1.1%	AA+

</TABLE>

WHOLE MORTGAGE LOANS

The Company significantly increased the size of its whole mortgage loan portfolio (mortgage loans which have not been securitized) in 1996 and in the first quarter of 1997. The table below presents selected characteristics of the Company's whole mortgage loans.

At March 31, 1997, the Company owned 2,795 whole mortgage loans with a total principal balance of $716 million; these loans had an amortized cost before credit reserve of $732 million, a balance sheet carrying value of $730 million, and an estimated bid-side market value of $730 million. The whole loan credit reserve was $0.6 million. At December 31, 1996 the Company owned 2,172 whole mortgage loans with a total principal balance of $515 million; these loans had an amortized cost before credit reserve of $527 million, a balance sheet carrying value of $525 million, and an estimated bid-side market value of $525 million. The whole loan credit reserve at December 31, 1996 was $0.4 million.

All of these whole loans were adjustable-rate, single-family loans underwritten to "A" quality standards. At March 31, 1997, the average whole loan size was $256,221. California loans represent 41% of the total outstanding balance. Loans with original loan-to-value ratios (LTV) in excess of 80% represent 24% of the total outstanding balance; a substantial majority of these higher-LTV loans are credit-enhanced with primary mortgage insurance or other forms of credit support serving to bring the effective original LTV ratio on each of those loans to 75% or less. After giving effect to this mortgage insurance, the average original LTV ratio of the Company's whole loans was 68% at March 31, 1997. The ratio of the current loan balance to original home value is lower than the original LTV ratios detailed here due to pay downs of mortgage principal over time.

TABLE 21
WHOLE MORTGAGE LOAN SUMMARY

<TABLE>
<CAPTION>

(ALL RATIOS BASED ON % OF TOTAL PRINCIPAL VALUE UNLESS NOTED)	AT MARCH 31, 1997	AT DECEMBER 31,1996
	(ALL DOLLARS IN THOUSANDS)	
<S>	<C>	<C>
Face or Principal Value	$716,137	$515,033
Amortized Cost	731,957	527,280
Market Value	729,561	525,475
Adjustable-Rate	100%	100%
Single-Family	100%	100%
"A" Quality Underwriting	100%	100%
First Lien	100%	100%
Primary Residence (owner-occupied)	94%	94%
Second Home	4%	4%
Investment Property	2%	2%
Property Located in Northern California	17%	18%
Property Located in Southern California	24%	26%
Top Ten States as of 3/31/97		
California	41.3%	43.5%
Maryland	6.4%	8.0%
Florida	4.6%	4.2%
Illinois	4.0%	3.8%
New York	3.8%	3.1%
Texas	3.4%	2.3%
Virginia	3.4%	4.3%
Connecticut	3.2%	3.0%
New Jersey	3.2%	2.8%
Massachusetts	2.7%	3.4%
Number of Loans	2,795	2,172
Average Loan Size	$ 256	$ 237
Loan Balance less than $214,600	20%	23%
Loan Balance greater than $500,000	14%	8%
Average Original Loan-to-Value Ratio (LTV)	74%	77%
Original LTV > 80%	24%	25%
% of Original LTV > 80% with Primary Mortgage Insurance	94%	97%
Effective Original LTV including Primary Mortgage	68%	73%

Insurance		
1989 and Prior Years Origination	6%	9%
1990 Origination	3%	4%
1991 Origination	1%	2%
1992 Origination	3%	4%
1993 Origination	9%	14%
1994 Origination	41%	52%
1995 Origination	4%	7%
1996 Origination	30%	8%
1997 Origination	2%	0%
Average Seasoning in Months	33	37
Non-Performing Assets (90+ days delinquent + f/c + REO)	$ 1,220	$ 1,249
Number of Non-Performing Loans (NPAs)	6	7
Non-Performing Assets as % of Total Loan Balances	0.2%	0.2%
Non-Performing Assets as % of Total Assets	0.05%	0.06%
Real Estate Owned Assets (REO)	$ 128	$ 196
Number of Real Estate Owned Assets	1	1
Real Estate Owned Assets as % of Total Loan Balances	0.02%	0.04%

</TABLE>

The Company defines non-performing assets ("NPAs") as whole loans which are delinquent more than 90 days, in foreclosure or real estate owned (REO). As of March 31, 1997, the Company's NPAs were $1.2 million, with two loans 90+ days delinquent, three loans in foreclosure and one real estate owned. At December 31, 1996, the Company had seven non-performing assets totaling $1.2 million. Through March 31, 1997, the Company

experienced a credit loss on one whole loan. The loss severity on this loan (total credit loss divided by the loan balance) was 7% for a total actual credit loss of $12,995. Management eventually expects its whole loan credit losses to mirror the experience of the "A" quality single-family residential mortgage market as a whole. The Company is building a reserve for potential future credit losses; see "Credit Reserves".

SECURITIZED MORTGAGES RATED AAA TO BBB

At March 31, 1997, 71% of the Company's mortgage assets were securitized interests in pools of single-family mortgage loans which had an investment-grade credit rating of AAA through BBB from one or more of the nationally-recognized rating agencies, or, if not rated, had equivalent credit quality in the view of management. At December 31, 1996, these types of mortgage securities represented 74% of the Company's mortgage assets.

Each of these investment-grade mortgage securities has credit-enhancement from a third-party which provides the Company with full or partial protection from credit losses in addition to the protection afforded by the value of the properties underlying the individual mortgages and any primary mortgage insurance on individual loans. Given the quality of the mortgage loans in these pools and the levels of additional credit-enhancement, management believes the level of credit risk for these mortgage assets is low. In the event, however, that credit losses in these pools exhaust the credit-enhancement or in the event of default of FNMA, FHLMC or another third party guarantor, credit losses to the Company could result. Through March 31, 1997, the Company has experienced no actual credit losses from these mortgage assets.

At March 31, 1997, the principal value of these mortgage assets was $1.80 billion, the historical amortized cost was $1.84 billion, the balance sheet carrying value was $1.85 billion, and the estimated bid-side market value was $1.85 billion. At December 31, 1996, the principal value of these mortgage assets was $1.56 billion, the historical amortized cost was $1.60 billion, the balance sheet carrying value was $1.60 billion, and the estimated bid-side market value was $1.60 billion.

SECURITIZED MORTGAGES RATED BELOW BBB

In 1994 and 1995, the Company acquired a limited amount of securitized mortgage assets with a credit rating equivalent of less than BBB. A majority of the mortgages in the pools underlying these securities were underwritten to "A" quality standards. The Company may acquire additional such assets when management believes that the cash flow and return on average equity over the life of the asset, net of expected credit losses, will be attractive. These assets have high potential yields but also have higher levels of credit risk, are costly to finance and require a large allocation of capital under the Company's risk-adjusted capital system. Approximately 70% of the mortgage loans in the pools underlying these securities at the time of issue of these securities were located in California. As of March 31, 1997, these assets had a principal, or face, value of $40.5 million, an amortized cost before credit reserve of $29.0 million and an estimated bid-side market value (which equaled carrying value) of $25.5 million. The credit reserve at March 31, 1997 was $2.2

million. At December 31, 1996, these assets had a principal value of $40.8 million, an amortized cost before credit reserve of $28.9 million and an estimated bid-side market value (which equaled carrying value) of $25.6 million. The credit reserve at December 31, 1996 was $1.8 million.

These assets may be highly beneficial to the Company over their life, although any such benefits are likely to be realized chiefly in later years. Future benefits may include possible credit rating upgrades and market value improvements as the mortgage interests senior to the Company's position prepay. This would lead to lower borrowing costs, an expanded equity base for the Company and a lower internal risk-adjusted capital allocation. Another potential benefit is the eventual return of principal (net of credit losses) which was purchased at a discount. This would tend to increase the Company's earnings as it amortizes these discount balances into income.

Approximately 98% of the Company's securitized assets with a credit rating equivalent below BBB are credit-enhanced to some degree. These assets are credit-enhanced to a lesser degree than higher-rated assets. Credit losses will not be incurred by the Company on these assets until total credit losses in the related mortgage pool exhaust the credit-enhancement. At that point, however, the rate of loss to the Company's interest is likely to be

significant as these interests are subordinated to and provide credit-enhancement for other, more senior, interests issued from the same mortgage pool. In effect, the Company is providing a form of mortgage credit insurance to the senior interests in each of these pools and therefore the Company would bear the credit risk of the entire pool (which would be many times the size of the Company's interest) in the event that the credit-enhancement junior to the Company's interest is exhausted. Total potential credit losses to the Company are limited to the Company's cost basis in these assets.

In some of the mortgage pools underlying these securities, delinquencies currently exceed management's original expectations. Delinquency levels in most of these pools appear to have stabilized during 1996 and thus far in 1997.

Actual pool credit losses which have reduced the credit-enhancement protection to the Company's below BBB-rated interests have occurred, but most of the aggregate credit enhancement in these pools that existed at the time of acquisition was still intact at March 31, 1997. Through the first quarter of 1997, the Company has experienced no credit losses from these credit-enhanced, below-BBB-rated assets.

In 1995, the Company acquired two "first loss" assets. These are subordinated interests with no credit-enhancement and with leveraged credit risk. At both December 31, 1996 and March 31, 1997, the estimated market value of these assets was approximately $0.3 million; their historical amortized cost was $0.2 million. All credit losses in the related pools of mortgages will reduce the principal value of these first loss assets and will be recognized as an actual credit loss by the Company. As the Company's cost basis in its first loss assets is low relative to the mortgage principal value, the Company's realized credit loss will equal only 10-20% of the principal value of any mortgage credit losses in the pools. The limit of the Company's potential credit losses on these assets is equal to the amortized cost of $0.2 million. Total actual credit losses realized by the Company on these first loss assets were $3,997 in 1995, $6,520 in 1996 and $29,718 in the first quarter of 1997.

CREDIT RESERVES

The Company has been building a credit reserve for future potential credit losses through taking quarterly credit provisions. These credit provisions reduce reported GAAP earnings (but only future actual credit losses will reduce taxable earnings and dividends). The first step the Company takes in its on-going review of the adequacy of its credit reserve is to assess potential credit risk arising from whole loans and loans in the mortgage pools underlying the Company's securitized mortgage assets which are seriously delinquent (90+ days delinquent, in foreclosure and real estate owned). Future credit losses from these loans will depend on the number of these loans actually defaulting, the loss severity experienced on default of the loan (net of recoveries from any individual loan private mortgage insurance), the level of credit-enhancement at the pool level, and the Company's amortized cost basis in that asset. The table below shows the credit losses that could be incurred by the Company if all the seriously delinquent mortgage loans in the Company's whole loan and mortgage securities portfolios at the end of the respective quarter were to default and result in a loss. For example, if 100% of the seriously delinquent loans as of March 31, 1997 were to default and the loss severity experienced was 25% of the loan balance, credit losses to the Company would be $2,014,000 (71% of the current credit reserve). If such losses happen, most of them would likely occur over the next twelve months (during which time the Company will continue to take credit provisions and build its reserve). The amount of actual credit losses that will be incurred from these loans is unknown. This table below addresses

the potential credit risk arising from serious delinquencies as the end of the respective quarters only; it does not purport to reflect potential losses that may occur over the life of these assets. In order to complete the evaluation of the adequacy of its reserve levels, the Company also considers additional credit losses that may arise from future delinquencies. See also "Results of Operations - -- Credit Provisions".

TABLE 22
POTENTIAL FUTURE CREDIT LOSSES ESTIMATED BASED ON
CURRENT 90+ DAY DELINQUENCIES ONLY

<TABLE>
<CAPTION>

END OF PERIOD	CREDIT LOSS RESERVE	CUMULATIVE LOSS SEVERITY EXPERIENCE	POTENTIAL FUTURE LOSSES ASSUMING LOSS SEVERITY OF 10%	POTENTIAL FUTURE LOSSES ASSUMING LOSS SEVERITY OF 15%	POTENTIAL FUTURE LOSSES ASSUMING LOSS SEVERITY OF 20%	POTENTIAL FUTURE LOSSES ASSUMING LOSS SEVERITY OF 25%	POTENTIAL FUTURE LOSSES ASSUMING LOSS SEVERITY OF 30%	POTENTIAL FUTURE LOSSES ASSUMING LOSS SEVERITY OF 35%
				(DOLLARS IN THOUSANDS)				
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 0	0%	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
1995, Quarter 1	19	0%	0	0	0	0	0	0
1995, Quarter 2	59	0%	0	0	0	0	0	0
1995, Quarter 3	143	0%	0	0	0	0	0	0
1995, Quarter 4	490	9%	15	22	29	37	103	435
1996, Quarter 1	821	10%	39	58	78	227	655	1,280
1996, Quarter 2	1,298	16%	68	102	147	715	1,449	2,215
1996, Quarter 3	1,814	22%	102	154	205	703	1,254	2,196
1996, Quarter 4	2,180	27%	190	285	861	1,601	2,420	3,440
1997, Quarter 1	2,833	25%	204	370	1,040	2,014	3,217	4,486

</TABLE>

As of March 31, 1997 the mortgage securities rated below BBB owned by the Company had a historical amortized cost basis on the Company's books which was $14.8 million below the principal value (or face value) of such mortgage interests. While this $14.8 million is not a credit reserve per se, the discount basis of these assets should serve to offset a portion of any actual losses of principal due to credit that may occur in these assets in the future. To the extent such losses are not incurred, this $14.8 million discount will be amortized into the Company's reported income over time as the mortgage principal of these assets pay down. Due to their subordinated status, many of these below-BBB-rated assets are not currently receiving significant principal pay downs; unless impacted by poor credit performance, the Company should start to receive a reasonable flow of principal pay downs from these assets during the next ten years and thus may be able to recognize an increased amortization of its discount balances into income at that time.

INTEREST RATE AGREEMENTS

The Company's interest rate agreements are described in detail in "Note 3. Interest Rate Agreements" in the Notes to Consolidated Financial Statements. These assets had a historical amortized cost basis of $7.9 million at March 31, 1997, an estimated bid-side market value of $5.8 million and a balance sheet carrying value of $5.8 million. There is no credit reserve for these assets. At December 31, 1996, the Company's interest rate agreements had a historical amortized cost basis of $6.4 million, an estimated bid-side market value of $2.6 million and a balance sheet carrying value of $2.6 million. There is a risk that the counter-parties to the interest rate agreements will not be able to perform to the terms of these contracts. If this were to happen, the Company's total accounting exposure would be limited to its historical amortized cost basis in these assets, although the true economic opportunity cost to the Company could be higher. Each of the twelve counter-parties to the Company's interest rate agreements had a credit rating of at least "A" as of March 31, 1997.

BORROWINGS

At March 31, 1997, the Company's debt consisted of collateralized borrowing arrangements of various types (reverse repurchase agreements, notes payable, revolving lines of credit). All such borrowings were short-term and their market value approximated the historical cost and carrying value of $2.37 billion. To date, the Company has borrowed from fifteen different collateralized lenders. The Company's ability to roll over such borrowings when they mature depends on the market value, liquidity and credit quality of its assets, the soundness of the Company's balance sheet as a whole, the state of the collateralized lending market, and other factors. See "Note 5. Short-Term Borrowings" in the Notes to Consolidated Financial Statements for additional

information. The Company has established uncommitted borrowing facilities in this market in amounts in excess of its current requirements.

On average, the Company believes that its average total borrowing capacity has been 94% to 97% of the market value of its mortgage assets. The Company, however, has limited its borrowings, and thus its potential asset growth, in order to maintain unused borrowing capacity and thus increase the liquidity and strength of its balance sheet.

The term-to-maturity of the Company's borrowings have ranged from one day to one year. For some borrowings, the cost of funds adjusts to a market level on a monthly basis during the term of the borrowing, so the term-to-next-rate-adjustment may be shorter than the term-to-maturity. At March 31, 1997, the weighted average term-to-maturity was 79 days and the weighted average term-to-next-rate-adjustment was 43 days; at December 31, 1996, the average term-to-maturity was 98 days and the average term-to-next-rate-adjustment was 55 days. The Company adjusts the maturities and other terms of its borrowings over time based on the interest rate characteristics of its balance sheet, the degree to which interest rate risk has been reduced through the use of interest rate agreements and other factors. Since late 1996, the Company has been reducing the term-to-next-rate adjustment of its liabilities while increasing its interest rate agreement hedging activities.

TABLE 23
BORROWING SUMMARY

END OF PERIOD	MARKET VALUE OF PLEDGABLE MORTGAGE ASSETS	ESTIMATED BORROWING CAPACITY AS A % OF PLEDGABLE ASSETS	ESTIMATED BORROWING CAPACITY	TOTAL BORROWINGS	AVERAGE TERM TO MATURITY	AVERAGE TERM TO RATE ADJUSTMENT	RATE ON BORROWINGS OUTSTANDING AT PERIOD-END
			(DOLLARS IN THOUSANDS)				
Fiscal 1994	$ 117,447	95.6%	$ 112,283	$ 100,376	112 days	70 days	5.80%
1995, Quarter 1	141,860	94.3%	133,719	121,998	97 days	27 days	6.25%
1995, Quarter 2	175,242	95.4%	167,192	155,881	64 days	28 days	6.23%
1995, Quarter 3	298,785	94.5%	282,442	228,826	38 days	31 days	5.95%
1995, Quarter 4	432,244	94.6%	409,014	370,316	74 days	26 days	6.01%
1996, Quarter 1	565,159	95.2%	537,874	508,721	48 days	19 days	5.62%
1996, Quarter 2	1,007,480	95.9%	965,795	896,214	72 days	72 days	5.70%
1996, Quarter 3	1,375,870	96.2%	1,324,220	1,225,094	102 days	71 days	5.78%
1996, Quarter 4	2,153,427	96.5%	2,077,098	1,953,103	98 days	55 days	5.83%
1997, Quarter 1	2,604,240	96.5%	2,513,840	2,373,279	79 days	43 days	5.82%

STOCKHOLDERS' EQUITY

From December 31, 1996 to March 31, 1997, the Company's equity base (exclusive of the mark-to-market valuation account) grew from $214.4 million to $245.5 million. This growth was the result of the Company's January 1997 common stock offering ($29.2 million), proceeds from the issuance of common stock upon the exercise of warrants ($2.1 million) and common stock sold pursuant to the Company's Dividend Reinvestment Plan ($0.5 million). Stockholders' equity was decreased by $0.7 million in the first quarter as dividend distributions (which are based on taxable income, see "Results of Operations - Taxable Income") exceeded GAAP income.

Book value, or equity, per share (including common and preferred, excluding the valuation account) increased by 6% from $17.87 to $19.03 from December 31, 1996 to March 31, 1997. See Table 24.

For balance sheet purposes, the Company carries some of its mortgage assets and interest rate agreements on its balance sheet at their estimated bid-side liquidation market value. As a result, the Company's equity base and book value per share may fluctuate due to market conditions and other factors. Reported GAAP net unrealized gain or loss includes both mark-downs on some assets taken immediately upon acquisition (as liquidation values

are generally estimated to be lower than acquisition prices) and the effect of

subsequent market value fluctuations on a portion of the Company's assets. This valuation account also includes balance sheet accounting entries being made over time as a result of a re-classification of certain assets. The GAAP account does not include the effect of market value changes of "held-to-maturity" assets or of liabilities.

TABLE 24
STOCKHOLDERS' EQUITY
(GAAP REPORTING BASIS)

<TABLE>
<CAPTION>

END OF PERIOD	VALUATION ACCOUNT FOR MORTGAGE ASSETS	VALUATION ACCOUNT FOR INTEREST RATE AGREEMENTS	TOTAL VALUATION ACCOUNT	TOTAL VALUATION ACCOUNT AS % OF TOTAL ASSETS	HISTORICAL AMORTIZED COST EQUITY BASE	GAAP REPORTED EQUITY BASE INCLUDING VALUATION ACCOUNT	HISTORICAL AMORTIZED COST EQUITY PER COMMON AND PREFERRED SHARE	GAAP REPORTED EQUITY PER SHARE
	(DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ (2,657)	$ 101	$(2,556)	(2.1%)	$ 22,837	$ 20,280	$12.18	$10.82
1995, Quarter 1	86	(635)	(549)	(0.4%)	22,901	22,352	12.22	11.93
1995, Quarter 2	886	(1,200)	(314)	(0.2%)	22,847	22,533	12.19	12.02
1995, Quarter 3	34	(1,585)	(1,551)	(0.5%)	74,024	72,473	13.42	13.14
1995, Quarter 4	(3,502)	(1,974)	(5,476)	(1.2%)	73,766	68,290	13.37	12.38
1996, Quarter 1	(3,763)	(1,302)	(5,065)	(0.9%)	73,211	68,146	13.26	12.34
1996, Quarter 2	(3,068)	(1,485)	(4,553)	(0.4%)	128,847	124,295	15.12	14.59
1996, Quarter 3	353	(2,413)	(2,060)	(0.1%)	165,578	163,517	16.43	16.23
1996, Quarter 4	139	(3,599)	(3,460)	(0.2%)	214,465	211,005	17.87	17.58
1997, Quarter 1	2,225	(2,107)	118	0.0%	245,544	245,662	19.03	19.04

</TABLE>

The table below presents the Company's estimated mark-to-market value of its entire balance sheet. As such it represents an estimate of the theoretical liquidation value of the Company if all assets and liabilities could be disposed of at their current market values. The Company expects that these values will fluctuate significantly over time, and that such fluctuations may or may not imply changes in the Company's credit worthiness or its potential to generate earnings and dividends in the future.

TABLE 25
STOCKHOLDERS' EQUITY
(ESTIMATED FULL MARK-TO-MARKET BASIS)

<TABLE>
<CAPTION>

END OF PERIOD	HISTORICAL AMORTIZED COST EQUITY PER COMMON AND PREFERRED SHARE	CHANGES FROM HISTORICAL AMORTIZED COST BASIS				TOTAL MARK-TO-MARKET EQUITY	MARK-TO-MARKET EQUITY PER COMMON AND PREFERRED SHARE
		MORTGAGE ASSETS	INTEREST RATE AGREEMENTS	BORROWINGS	OTHER ASSETS/ LIABILITIES		
	(DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)						
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$12.18	$(2,381)	$ 101	$ 0	$(244)	$ 20,036	$10.69
1995, Quarter 1	12.22	86	(635)	0	(210)	22,142	11.81
1995, Quarter 2	12.19	886	(1,200)	0	(157)	22,376	11.94
1995, Quarter 3	13.42	34	(1,584)	0	(177)	72,296	13.11
1995, Quarter 4	13.37	(3,502)	(1,974)	0	(151)	68,139	12.35
1996, Quarter 1	13.26	(3,764)	(1,302)	0	(26)	68,119	12.34
1996, Quarter 2	15.12	(3,068)	(1,484)	0	65	124,360	14.60
1996, Quarter 3	16.43	353	(2,414)	0	35	163,552	16.23
1996, Quarter 4	17.87	139	(3,598)	0	236	211,241	17.60
1997, Quarter 1	19.03	1,750	(2,106)	0	410	245,598	19.03

</TABLE>

LIQUIDITY

A financial institution has ample liquidity when it is able, without seriously disrupting its operations, to meet the demands made upon it for cash payments with its cash reserves, operating cash flow, borrowing capacity, proceeds from asset sales, or other sources of cash. Liquidity allows the Company to purchase

additional mortgage assets and allows the Company to pledge additional assets to secure existing borrowings should the value of pledged assets decline. Potential immediate sources of liquidity for the Company include cash balances and unused borrowing capacity. Unused borrowing capacity is defined as estimated borrowing capacity (as shown above in Table 23) less total borrowings and is based on the market value of the Company's assets and market conditions in the collateralized lending markets at period-end. Unused borrowing capacity will vary over time as the market value of the Company's mortgage assets and market conditions fluctuate and due to other factors. Potential immediate sources of liquidity totaled $135 million at December 31, 1996 and $154 million at March 31, 1997. The maintenance of liquidity is one of the goals of the Company's risk-adjusted capital policy; under this policy, asset growth is limited in order to preserve unused borrowing capacity for liquidity management purposes.

The Company's balance sheet generates liquidity on an on-going basis through mortgage principal repayments and net earnings held prior to payment as dividends. The Company's operations through March 31, 1997 have been cash flow positive. Should the Company's needs ever exceed these on-going sources of liquidity plus the immediate sources of liquidity discussed above, management believes that the Company's mortgage assets and interest rate agreements could be sold in most circumstances to raise cash (although such sales could cause realized losses). The table below shows the potential immediate sources of liquidity available to the Company.

TABLE 26
SOURCES OF LIQUIDITY

<TABLE>
<CAPTION>

	CASH BALANCE	ESTIMATED UNUSED BORROWING CAPACITY	POTENTIAL IMMEDIATE SOURCES OF LIQUIDITY (CASH + EST. UNUSED BORROWING CAPACITY)	MORTGAGE PRINCIPAL REPAYMENTS	NET INCOME BEFORE PREFERRED DIVIDENDS	ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH (SEE STATEMENT OF CASH FLOWS IN FINANCIAL STATEMENTS)	NET CASH PROVIDED BY OPERATING ACTIVITIES
				(DOLLARS IN THOUSANDS)			
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 1,027	$ 11,907	$ 12,934	$ 1,244	$ 382	$ (501)	$ (119)
1995, Quarter 1	953	11,721	12,674	2,673	401	(191)	211
1995, Quarter 2	1,620	11,311	12,931	2,934	450	(870)	(420)
1995, Quarter 3	1,150	53,616	54,766	8,319	994	(393)	601
1995, Quarter 4	4,825	38,698	43,523	24,898	1,310	(68)	1,242
1996, Quarter 1	9,705	29,153	38,858	32,814	1,954	127	2,081
1996, Quarter 2	10,407	69,581	79,988	53,058	2,500	320	2,820
1996, Quarter 3	14,599	99,126	113,725	76,942	3,387	5,553	8,940
1996, Quarter 4	11,068	123,995	135,063	95,610	4,844	1,790	6,634
1997, Quarter 1	12,985	140,561	153,546	173,362	7,211	3,735	10,946

</TABLE>

CAPITAL ADEQUACY/RISK-ADJUSTED CAPITAL POLICY

The Company's target equity-to-assets ratio was 9.97% at December 31, 1996 and 10.09% at March 31, 1997 (These ratios are based on the Company's estimated market values of the assets.) The Company's target equity-to-assets ratio varies over time as a function of the Company's liquidity position, the maturity of the Company's borrowings, the level of unused borrowing capacity, the level of interest rates as compared to the periodic and life caps in the Company's assets, the over-collateralization levels required by the Company's lenders and the market value of the assets. The Company has sought to maintain an equity-to-assets ratio of 7% to 10% for assets funded with short-term borrowings which have low credit risk, relatively low interest rate risk, good liquidity, and low lender over-collateralization requirements. For less liquid assets with credit risk that are funded with short-term borrowings, the Company has sought to maintain an equity-to-assets ratio of 40% to 100%. For assets funded to maturity with long-term borrowings, the Company anticipates it would seek to maintain an equity-to-assets ratio of 5% or less in most circumstances. The Company's per-asset capital requirements have not changed significantly since the founding of the Company; the decline in target equity-to-assets ratio during 1996 was a function of a change in asset mix. The increase in the target ratio in the first quarter of 1997 was primarily due to the increase in market interest rates late in the quarter. These target levels of equity capitalization are higher than that of many banks, savings and loans, Federal government mortgage agencies, insurance companies, and REITs that act as mortgage portfolio lenders.

The target equity-to-assets ratio is determined through a Board-level process determined by the Company's Risk-Adjusted Capital Policy. Since the factors on

which the guidelines and the actual capital levels of the Company are based do fluctuate, the Company expects that its actual capital levels will fall below its capital guidelines from time to time. For instance, if short-term interest rates rose sharply, for assets funded with short-term borrowings the Company's actual capital levels would decline at the same time that its capital requirements would rise. When the capital guidelines exceed the actual available capital, management will cease the acquisition of new mortgage assets and will make plans to bring the Company's capital levels back into compliance with its guidelines over time.

In certain limited circumstances and in limited amounts, the Company may, prior to a planned equity offering, acquire or commit to acquire assets in excess of the levels proscribed by its Risk-Adjusted Capital levels. For example, the Company ended the first quarter of 1997 with assets of $213 million in excess of what could have been supported by its capital base in the absence of this special provision. The Company's capital ratios were brought back within its standard Risk-Adjusted Capital guidelines through the Company's April 1997 common

stock offering. In a similar manner, the Company owned excess assets at the end of the fourth quarter of 1996 in anticipation of its January 1997 common stock offering.

The Company attempts to hold what it believes to be a reasonable amount of capital given the risks in its balance sheet; target capital levels could rise or fall over time. If the Company continues to move towards a lower- risk balance sheet (through acquiring higher-quality more-liquid mortgage assets, acquiring mortgages with no periodic caps, replacing short-term debt with long-term debt, or other such means), the Company would seek to lower its target equity-to-assets ratio in what it believes to be an appropriate manner.

In the past, the Company has operated with significantly fewer assets than would have been allowed under its Risk-Adjusted Capital system. As shown in Table 10, the average equity-to-assets ratio has exceeded the target equity-to-assets ratio; that is, the Company's balance sheet capacity has been under-utilized. Average balance sheet capacity utilization was 88% in the first quarter of 1996, with an average equity-to-assets ratio of 14.5% as compared to an average target equity-to-assets ratio of 12.8%. Average balance sheet capacity utilization was 98% during the first quarter of 1997, with an average balance sheet capacity utilization of 10.3% as compared to an average target equity-to-assets ratio of 10.1%. The Company's rate of asset growth has made it difficult for the Company to achieve optimum capital efficiency. In the past, the Company has raised equity in advance of seeking to acquire new mortgages. As evidenced by the improvement in the capacity utilization from the first quarter of 1996 to the first quarter of 1997, the Company has succeeded in increasing its capital efficiency through the use of its equity shelf registration and through committing to acquire some assets in advance of planned equity offerings as described above.

The table below shows the Company's actual and target equity-to-assets ratios and the Company's actual asset size as compared to its full potential asset size given its equity capital base and the guidelines of the Company's Risk-Adjusted Capital Policy.

TABLE 27
EXCESS CAPITAL AND ASSET GROWTH POTENTIAL AT END OF QUARTER

<TABLE>
<CAPTION>

END OF PERIOD	ACTUAL "RISK-BASED" CAPITAL	TARGET EQUITY TO ASSETS RATIO	ACTUAL END OF PERIOD EQUITY TO ASSETS RATIO	EXCESS CAPITAL	POTENTIAL ASSET SIZE WITH SAME ASSET MIX	ACTUAL ASSET SIZE	ASSET GROWTH POTENTIAL WITH SAME ASSET MIX
			(DOLLARS IN THOUSANDS)				
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	$ 20,280	10.84%	16.69%	$ 6,716	$ 187,048	$ 121,528	$ 65,520
1995, Quarter 1	22,352	12.41%	15.37%	3,970	180,173	145,440	34,733
1995, Quarter 2	22,533	12.95%	12.57%	(1,069)	173,989	179,321	(5,332)
1995, Quarter 3	72,473	13.08%	23.89%	32,155	554,183	303,394	250,789
1995, Quarter 4	68,290	12.59%	15.47%	12,028	542,431	441,557	100,874
1996, Quarter 1	68,146	11.72%	11.72%	26	581,540	581,313	227
1996, Quarter 2	124,295	10.77%	12.09%	13,566	1,154,303	1,028,330	125,973
1996, Quarter 3	163,517	10.32%	11.65%	18,664	1,584,315	1,403,478	180,837
1996, Quarter 4	211,005	9.97%	9.66%	(6,798)	2,116,028	2,184,197	(68,169)
1997, Quarter 1	245,188	10.09%	9.28%	(21,504)	2,429,511	2,642,590	(213,079)

</TABLE>

CLASS B PREFERRED STOCK

In August 1996, the Company issued 1,006,250 shares of Class B Preferred Stock; these shares trade on the Nasdaq National Market under the symbol RWTIP. As of March 31, 1997, there were 999,638 such shares outstanding; 6,612 shares of Preferred Stock were converted into Common Shares in the first quarter of 1997. The liquidation preference of each share of Class B Preferred is $31.00 plus any accrued dividends. Preferred holders receive a quarterly dividend equal to the greater of $0.755 or the common stock dividend. Each share of Class B Preferred is convertible at any time at the option of the holder thereof into one share of common

stock (subject to possible future adjustment in certain circumstances); the Company has the right to force this conversion on or after October 1, 1999 providing that the market price of the common stock for a period of time prior to such redemption exceeds the conversion price (initially equal to the issue price of $31.00). The Company also has the right to call the Preferred for $31.00 per share plus any accrued dividends in cash starting October 1, 1999. See "Note 7. Class B 9.74% Cumulative Convertible Preferred Stock" in the Notes to Consolidated Financial Statements for additional information.

WARRANTS

At March 31, 1997, the Company had 272,304 warrants outstanding; at December 31, 1996 the Company had 412,894 warrants outstanding. In the first quarter of 1997, 140,590 warrants were exercised generating additional equity proceeds to the Company of $2.1 million. The remaining warrants trade on the Nasdaq National Market under the symbol RWTIW. Each warrant gives the holder the right until December 31, 1997 to buy 1.000667 shares of common stock at a price per share of $15.00. See "Note 8. Stock Purchase Warrants" in the Notes to Consolidated Financial Statements for additional information. If the Company's common stock continues to trade at a price above $15.00 per share, the remaining warrants are likely to be exercised on or prior to December 31, 1997. If all these warrants are exercised, the Company will receive additional new equity capital of approximately $4.1 million.

ASSET/LIABILITY MANAGEMENT AND EFFECT OF CHANGES IN INTEREST RATES

Management continually reviews the Company's asset/liability strategy with respect to interest rate risk, mortgage principal repayment risk, credit risk and the related issues of capital adequacy and liquidity. The Company seeks attractive risk-adjusted shareholder returns while seeking to maintain a strong balance sheet and long-term pattern of net income which grows over time relative to its competitors in the banking and savings and loan industries.

Changes in interest rates, mortgage principal repayment rates, and other factors are likely, however, to cause short-term volatility in the Company's reported EPS results; the Company generally does not seek to hedge away or otherwise significantly reduce this potential short-term earnings volatility.

The Company has sought to manage the extent to which net income changes as a function of changes in interest rates by matching adjustable-rate assets with variable-rate liabilities and by hedging through the use of interest rate agreements to mitigate the potential impact on net income of periodic and lifetime caps (coupon adjustment restrictions) in the assets. Should the Company acquire other types of mortgages (including fixed rate mortgages) in the future, the Company anticipates it will seek to reduce interest rate risks through funding with appropriately matched debt, through hedging, or other means. In general, the Company does not seek to anticipate future changes in interest rates. The Company seeks to prepare itself for a variety of possible future interest rate environments.

A primary goal of the Company's asset/liability strategy is to preserve liquidity by preserving the market value of its mortgage assets and interest rate agreements and thus preserving, in most conditions, the Company's ability to maintain its level of borrowings. Through March 31, 1997, all of the Company's borrowings were secured by the market value of its mortgage assets. In seeking to preserve liquidity and the Company's ability to roll over short-term borrowings, the Company allocates what it believes to be a sufficient amount of capital to each mortgage asset which serves to act as a cushion preserving the Company's ability to secure borrowings despite potential market value fluctuations of its mortgage assets. The Company has also undertaken a hedging program utilizing interest rate agreements. In the event of an increase in short-term and/or long-term interest rates, the market value of the Company's mortgage assets would likely fall, particularly in the short-term. The Company anticipates that, in such an event, the market value of its interest rate agreements would likely rise and partially offset decreases in mortgage values. Management believes that the combined effect of the Company's equity allocations and its hedging program are likely to preserve liquidity for the Company in most

interest rate environments. See "Asset/Liability Management and Effect of Changes in Interest Rates -- Equity Duration"

below. The market value of the Company's mortgage assets can also fluctuate as a function of changes in supply and demand, market volatility, and other factors which may be difficult or impossible to hedge.

Changes in interest rates also may have an effect on the rate of mortgage principal repayment; the Company has sought in the past to mitigate the economic effect of changes in the mortgage principal repayment rate by balancing assets purchased at a premium with assets purchased at a discount. The Company has not been able to achieve such balancing in 1996 and in the first quarter of 1997, however, as virtually all mortgage assets which were available for acquisition from the secondary mortgage market and which were otherwise attractive to the Company were priced at a premium. As a result, the Company has significantly increased its net unamortized premium balance relative to the size of its balance sheet. Potential short-term earnings volatility with respect to changes in mortgage principal repayment rates has increased as a result. At March 31, 1997, the Company estimates that its quarterly EPS in the short-term would be decreased by approximately $0.01 for each one percentage point increase in the Company's rate of mortgage principal repayment, all other factors being equal; EPS would increase in a similar manner should principal repayment rates slow.

Although the net effects on earnings of changes in interest rates, mortgage prepayment rates, and other factors cannot be determined in advance, management believes, given the balance sheet as of March 31, 1997, that some of the following effects may occur in an environment of rising short-interest rates: (i) earnings on that portion of the balance sheet funded with equity may rise over time as the coupons on adjustable rate mortgages adjust upwards, (ii) earnings on that portion of the balance sheet funded with borrowings (spread lending) may be initially reduced as borrowing costs rise more quickly than the coupons on adjustable rate mortgages, although most or all of the spread might be restored over time as the mortgage coupons fully adjust to the rate change, (iii) earnings may benefit from net hedge income or reduced net hedge expense from interest rate agreements, (iv) premium amortization expenses may be reduced if the rate of mortgage principal repayment diminishes. All other factors being equal, the net effect of an increase in short-term interest rates may be an initial drop in earnings followed by increased earnings after a lag period. The length of any such lag period would likely be determined by the speed and extent of the change in interest rates. Management believes that most of these effects would likely be reversed in an environment of falling short-term interest rates. All other factors being equal, therefore, the net effect of falling short-term interest rates, given the balance sheet as of March 31, 1997, could be an initial increase in earnings followed by decreased earnings after a lag period.

The Company's change in its mix of assets throughout 1996 and in the first quarter of 1997 increased the Company's basis risk between LIBOR interest rates and U.S. Treasury bill interest rates. The majority of the Company's assets at March 31, 1997 had coupons which changed as a function of U.S. Treasury bill rates while all the Company's borrowings had a cost of funds which tends to change in conjunction with changes in LIBOR rates. The Company believes its interest rate agreements mitigate to some degree the extent to which a reduced spread for the Company would result from LIBOR rates rising relative to U.S. Treasury interest rates. See "Note 3. Interest Rate Agreements" in the Notes to Consolidated Financial Statements for additional information.

Should the Company continue its funding strategy in effect at March 31, 1997, the Company's short-term earnings will also fluctuate to some extent with changes in the relationship between six and twelve month interest rates (off of which the coupons on Company's mortgage assets adjust) and one to six month interest rates (on which the Company's cost of funds is based). All other factors being equal, a flatter yield curve in the short end of the yield curve (when six and twelve month rates are low relative to one to six month rates) may have a negative effect on the Company's spread earnings.

In general, the Company's goal is to stabilize spread lending income over longer periods of time and allow income from equity-funded lending to rise as short-term interest rates rise and fall as short-term interest rates fall. If the Company were to achieve this goal, the Company's return on average equity, earnings and dividends would, over longer periods of time, rise as short-term interest rates rise, fall as short-term interest rates fall, and thus maintain a constant or widening spread to the level of short-term interest rates.

Should long-term interest rates rise while short-term interest rates remain stable, management expects, based on the Company's balance sheet as of March 31,

1997, that mortgage principal repayment rates may slow (thus benefiting earnings) but the market value of the Company's assets, net of hedges, would likely fall (thus potentially reducing the amount of assets the Company could carry on its balance sheet.)

INTEREST RATE SENSITIVITY GAP BEFORE HEDGING

The table below shows the Company's cumulative interest rate sensitivity gap, or maturity gap, for periods of one month to five years as a percentage of total assets. The interest rate sensitivity gap is a tool used by financial institutions, such as banks and savings and loans, to analyze the possible effects of interest rate changes on net income over time. The gap measures the amount of assets that mature or have a coupon adjustment in a particular period as compared to the amount of liabilities similarly adjusting during that time. A negative gap implies that rising interest rates will lead to lower earnings, while a positive gap implies that rising interest rates will lead to higher earnings. Lower interest rates would have the opposite effect. In each case, these effects are limited to the particular time period for which the gap is calculated.

As applied to the Company, this gap analysis ignores the effect of the Company's hedging activities (interest rate agreements), the effect of the periodic and lifetime caps in the Company's assets, the effects of "lookbacks" whereby coupon rates on Company assets are set based on interest rates one to three months prior to the start of accrual of a new coupon rate, the effect of changes in mortgage principal repayment rates and other factors. Nevertheless, the gap analysis can provide some useful information on the Company's interest rate risk profile.

The Company's three-month cumulative gap as a percentage of total assets was negative 34% at March 31, 1997. This suggests that the initial impact on the Company's earnings of rising interest rates would be negative. Falling interest rates would have the opposite effect. The Company had a cumulative twelve-month gap of positive 7% at March 31, 1997. This implies that the impact on net interest income of increasing interest rates may be positive after several quarters even though the initial impact could have been negative. Falling interest rates would likely have the opposite effect.

Although the Company's balance sheet does have these underlying characteristics, since a variety of factors (such as interest rate agreements) have not been taken into account in the gap analysis, it is not possible to assess, solely on this basis, what the actual impact of such interest rate changes on the Company's net income would be, especially over shorter time periods.

The Company has a positive interest rate sensitivity gap for periods of one year or longer even though most assets and liabilities adjust within one year because the Company has more earning assets than interest-bearing liabilities (i.e., a portion of the Company's earning assets are funded with equity).

TABLE 28
INTEREST RATE SENSITIVITY GAP EXCLUDING INTEREST RATE AGREEMENTS

<TABLE>
<CAPTION>

END OF PERIOD	CUMULATIVE 3-MONTH GAP AS A % OF TOTAL ASSETS	CUMULATIVE 6-MONTH GAP AS A % OF TOTAL ASSETS	CUMULATIVE 9-MONTH GAP AS A % OF TOTAL ASSETS	CUMULATIVE ONE YEAR GAP AS A % OF TOTAL ASSETS	CUMULATIVE THREE YEAR GAP AS A % OF TOTAL ASSETS	CUMULATIVE FIVE YEAR GAP AS A % OF TOTAL ASSETS
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Fiscal 1994	5%	15%	15%	15%	15%	15%
1995, Quarter 1	(27%)	14%	14%	14%	14%	14%
1995, Quarter 2	(33%)	11%	12%	12%	12%	12%
1995, Quarter 3	(19%)	18%	20%	23%	23%	23%
1995, Quarter 4	(26%)	9%	12%	15%	15%	15%
1996, Quarter 1	(34%)	4%	8%	11%	11%	11%
1996, Quarter 2	(3%)	(2%)	5%	12%	12%	12%
1996, Quarter 3	(9%)	(4%)	3%	12%	12%	12%
1996, Quarter 4	(28%)	(12%)	(1%)	10%	10%	10%
1997, Quarter 1	(34%)	(17%)	(4%)	7%	9%	9%

</TABLE>

INTEREST RATE AGREEMENTS

The Company's interest rate agreements materially alter the interest rate risk profile suggested by the interest rate sensitivity gap analysis. See "Results of Operations -- Cost of Borrowed Funds and Hedging and the Interest Rate Spread" above and "Note 3. Interest Rate Agreements" of the Notes to Consolidated

Financial Statements for further detail and information.

The interest rate agreements are designed to produce income for the Company as short-term interest rates rise to partially offset possible losses of net interest income from the spread lending portion of the Company's balance sheet. These agreements can be thought of as serving to limit potential increases in the costs of the Company's borrowings or, alternatively, as serving to remove some of the periodic and lifetime caps imbedded in the Company's assets. These agreements also serve to remove some of the short-term risk arising from funding assets that have fixed coupon adjustments for six to twelve months with liabilities that are fixed, on average as of March 31, 1997, for a three month shorter period of time. In addition, the interest rate agreements are designed to appreciate in market value in most circumstances in which short-term and/or long-term interest rates rise sharply, thereby partially offsetting likely concurrent declines in the market value of the Company's mortgage assets.

INTEREST RATE FUTURES AND OPTIONS

The Company has used interest rate futures and may use listed options on interest rate futures as part of its on-going interest rate risk management process. These instruments are in some ways similar to the interest rate agreements; the Company uses them in a similar manner and for hedging purposes only. The Company currently limits the aggregate amount of funds that the Company will deposit as original margin on futures plus premiums on listed options to less than 1% of the Company's total assets, after taking into account unrealized gains and unrealized losses on any such contracts. The Company currently limits its use of futures and listed options so that its profits from such instruments will be limited to 5% or less of the Company's gross taxable income on an annual basis. The Company had no positions in futures or options on futures at December 31, 1996 or March 31, 1997.

EQUITY DURATION

The Company uses "equity duration" to measure the stability of the market value of its assets with respect to the size of its equity base as interest rates fluctuate. Equity duration is a theoretical calculation of the projected percentage change in the reported equity base of the Company that would occur if short-term and long-term

interest rates moved up or down by 1% overnight. The Company's goal is to maintain an equity duration of less than 15%. In practice, the Company believes it has maintained an equity duration of less than 10%. Should interest rates increase by more than 1%, the Company believes its equity duration would increase from its current levels.

INFLATION

Virtually all of the Company's assets and liabilities are financial in nature. As a result, interest rates and other factors drive the Company's performance far more than does inflation. Changes in interest rates do not necessarily correlate with inflation rates or changes in inflation rates. The Company's Consolidated Financial Statements are prepared in accordance with Generally Accepted Accounting Principals and the Company's dividends are determined by the Company's net income as calculated for tax purposes; in each case, the Company's activities and balance sheet are measured with reference to historical cost or fair market value without considering inflation.

SEASONAL EFFECTS

There are three factors that management has identified which may have seasonal effects on the Company's earnings. First, management believes that in many years there may be more mortgage assets for sale by motivated sellers in the fourth quarter of the year than at any other time. If this is true, in many years the Company could grow at a faster rate in the fourth quarter than at other times of the year. This would generally benefit earnings in the first quarter of the following year. Secondly, mortgage principal repayment rates have a seasonal pattern of slowing in the winter and accelerating in the summer. Since the Company's premium amortization expenses are based on the Company's actual monthly principal repayment experience, overall earnings may be higher, all other things being equal, in the winter months. Finally, there is a mismatch in the day-count method that is used each month to determine the Company's interest income from mortgages and its interest expense from short-term borrowings. As a result, given the characteristics of the Company's balance sheet as of March 31, 1997 and assuming all other factors are equal, net interest income should tend to be higher in quarters, such as the first and second quarters of the year, that have fewer days.

PART II   OTHER INFORMATION

Item 1. Legal Proceedings

At March 31, 1997, 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

None

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 11.1 to Part I - Computation of Earnings Per Share for the three months ended March 31, 1997.

Exhibit 27 - Financial Data Schedule.

(b) Reports
Form 8-K filed on January 7, 1997 containing the Company's Amended and Restated Bylaws, amended December 13, 1996.

SIGNATURES

Pursuant to the requirements of the Securities 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 9, 1997   By: /s/ Douglas B. Hansen

Douglas B. Hansen
President and Chief Financial Officer
(authorized officer of registrant)

Dated: May 9, 1997   By: /s/ Vickie L. Rath

Vickie L. Rath
Vice President, Treasurer and Controller
(principal accounting officer)

REDWOOD TRUST, INC.
INDEX TO EXHIBIT

Exhibit Number		Sequentially Numbered Page
11.1	Computation of Earnings per Share.................	53
27	Financial Data Schedule...........................	54

EXHIBIT 11.1

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

	Three Months Ended March 31, 1997	Three Months Ended March 31, 1996
PRIMARY:		
Average common shares outstanding	11,605,171	5,521,376
Net effect of dilutive stock options outstanding during the period -- based on the treasury stock method	253,274	164,227
Net effect of dilutive stock warrants outstanding during the period -- based on the treasury stock method	258,422	443,984
Total	12,116,867	6,129,587
Net Income	$ 6,456,238	$1,954,190
Per Share Amount	$ 0.53	$ 0.32
FULLY DILUTED:		
Average common shares outstanding	11,605,171	5,521,376
Net effect of dilutive stock options outstanding during the period -- based on the treasury stock method	265,566	164,548
Net effect of dilutive stock warrants outstanding during the period -- based on the treasury stock method	263,005	446,724
Total	12,133,742	6,132,648
Net Income	$ 6,456,238	$1,954,190
Per Share Amount	$ 0.53	$ 0.32

<TABLE> <S> <C>

<ARTICLE> 5
<LEGEND>
THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM MARCH 31, 1997 QUARTERLY REPORT ON FORM 10-Q.
</LEGEND>
<MULTIPLIER> 1,000

<S>	<C>
<PERIOD-TYPE>	3-MOS
<FISCAL-YEAR-END>	DEC-31-1997
<PERIOD-START>	JAN-01-1997
<PERIOD-END>	MAR-31-1997
<CASH>	12,985
<SECURITIES>	2,610,487
<RECEIVABLES>	19,251
<ALLOWANCES>	0
<INVENTORY>	0
<CURRENT-ASSETS>	2,643,064
<PP&E>	0
<DEPRECIATION>	0
<TOTAL-ASSETS>	2,643,064
<CURRENT-LIABILITIES>	2,397,402
<BONDS>	0
<PREFERRED-MANDATORY>	0
<PREFERRED>	29,383
<COMMON>	219,580
<OTHER-SE>	(3,301)
<TOTAL-LIABILITY-AND-EQUITY>	2,643,064
<SALES>	0
<TOTAL-REVENUES>	38,568
<CGS>	0
<TOTAL-COSTS>	0
<OTHER-EXPENSES>	1,762
<LOSS-PROVISION>	695
<INTEREST-EXPENSE>	28,900
<INCOME-PRETAX>	7,211
<INCOME-TAX>	0
<INCOME-CONTINUING>	0
<DISCONTINUED>	0
<EXTRAORDINARY>	0
<CHANGES>	0
<NET-INCOME>	7,211
<EPS-PRIMARY>	0.53
<EPS-DILUTED>	0.53

</TABLE>