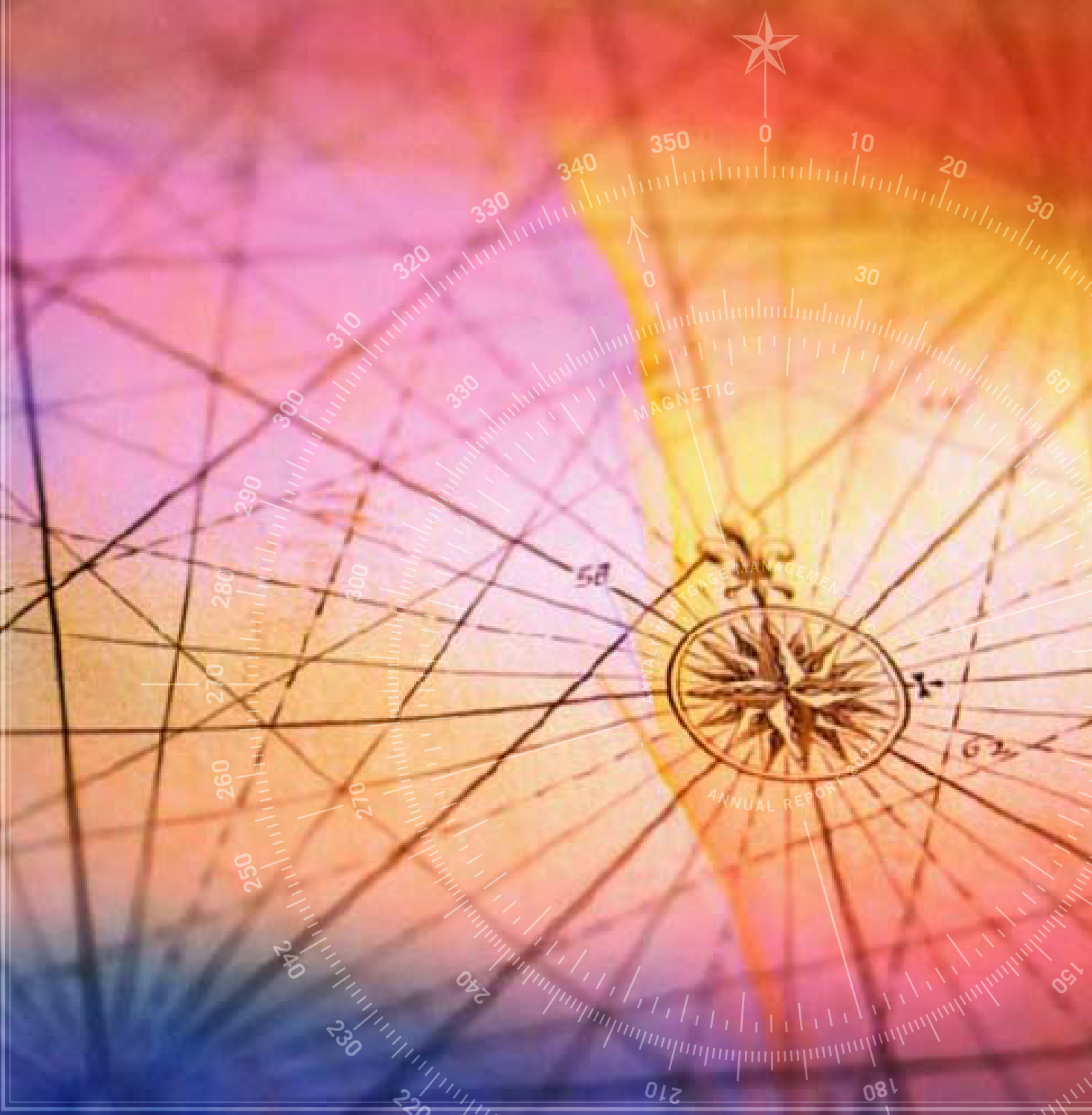


ANNALY MORTGAGE MANAGEMENT, INC.
ANNUAL REPORT 2004





ANNUAL REPORT 2004

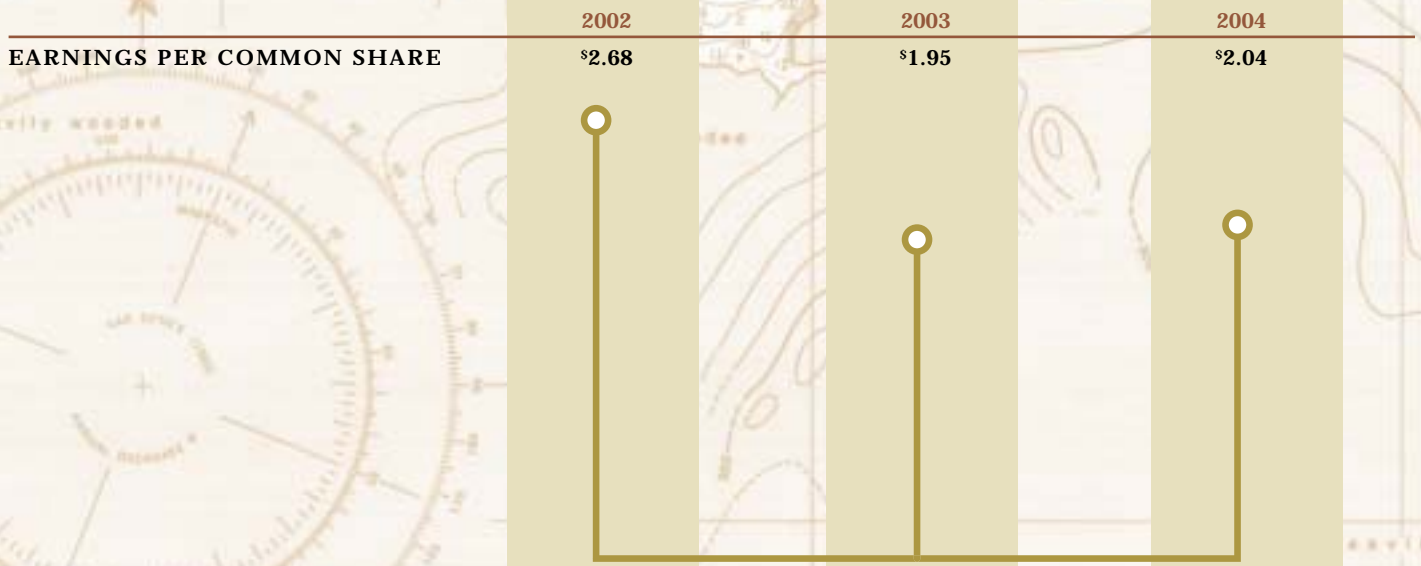
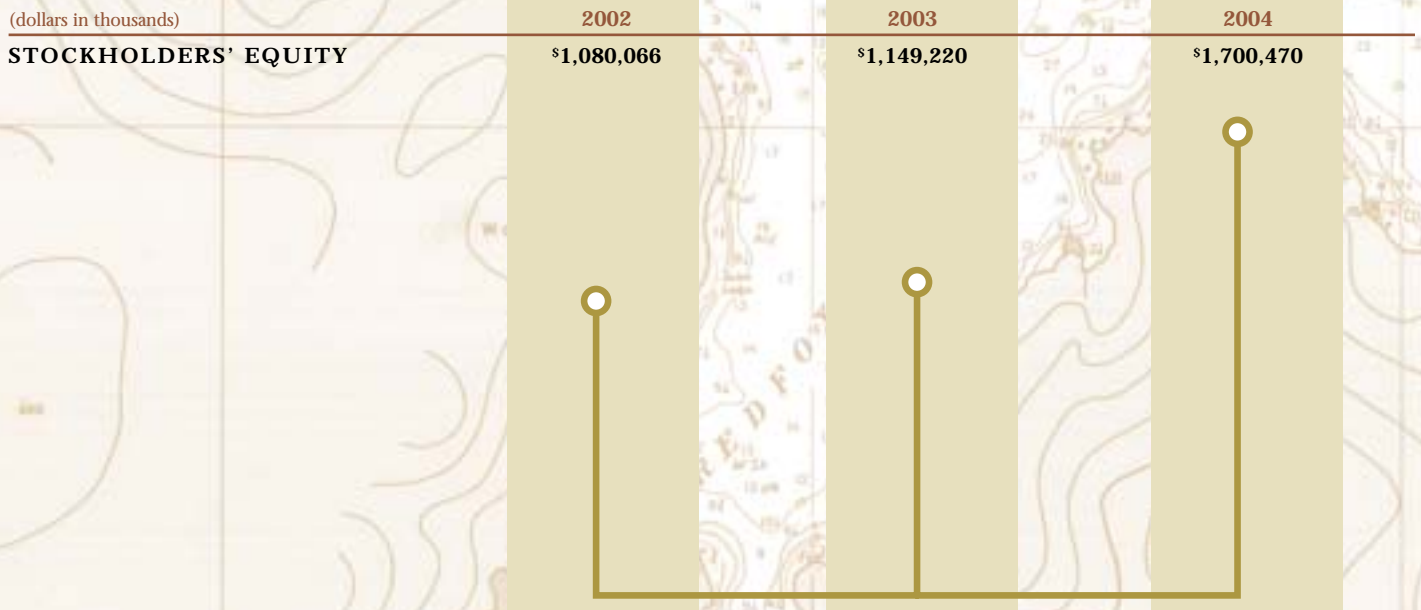
Our family crest and its motto “Prodesse non Nocere” are the trademarks of the Company. The description figuratively means ‘Proceed without fear.’ That symbolizes the confidence we try to instill in our investors. It is reinforced by years of reliable, consistent investment performance.

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The year 2004 demonstrated Annaly's ability to generate compelling returns for shareholders. It also demonstrated our ability to navigate the company through changing times. During the year, Annaly acquired Fixed Income Discount Advisory Company, a registered investment advisor, to take the next step towards becoming an asset management company. The addition of the fee income stream from FIDAC will complement our proven model of investing in liquid, high quality assets and accessing the capital markets through sequential, accretive stock offerings. Our objective is to protect shareholders' capital while providing an attractive dividend yield.

(dollars in thousands)



> Annaly Mortgage Management, Inc. manages assets on behalf of institutional and individual investors worldwide through Annaly and through the funds managed by its wholly-owned registered investment advisor, FIDAC. The Company's principal business objective is to generate net income for distribution to investors from the spread between the interest income on its mortgage-backed securities and the cost of borrowing to finance their acquisition and from dividends the Company receives from FIDAC. We have elected to be taxed as a real estate investment trust (or REIT) under the Internal Revenue Code and are therefore required to pay out at least 90% of our earnings to our shareholders in order to avoid taxation at the corporate level. We commenced operations on February 18, 1997.

All of the mortgage-backed securities we own are issued by an agency of the United States government and carry an actual or implied AAA rating. Mortgage-backed securities are ownership interests in mortgage loans made by financial institutions (savings and loans, commercial banks and mortgage bankers). When an institution has made enough loans it will "pool" or package them together and sell them to

mortgage investors like Annaly. The institution will collect the principal and interest payments made by the homeowners and forward them to the mortgage investor. We structure our portfolio with a combination of adjustable-, floating-, and fixed-rate mortgage-backed securities so that it can perform well through a wide range of interest rate environments.

We employ leverage to enhance our returns. To date, our debt has consisted entirely of borrowings collateralized by a pledge of our mortgage-backed securities. On our balance sheet, these borrowings appear as Repurchase Agreements. Our leverage, measured as a ratio of debt-to-equity, typically is managed in a band of 8:1 to 12:1.

FIDAC is a registered investment advisor which manages, assists in managing or supervises investment funds for a wide array of clients around the world on a discretionary basis. FIDAC is a fee-based asset management business with a global distribution reach.

Jennifer S. Karve
Executive Vice President &
Portfolio Manager

Wellington J. Denahan-Norris
Vice Chairman &
Chief Investment Officer

Michael A. J. Farrell
Chairman,
President & CEO

Kathryn F. Fagan
Chief Financial Officer
& Treasurer



> Annaly's team is experienced in Wall Street trading, management and operations, with a specialization in investing in mortgage-backed securities on a leveraged basis. Senior management founded FIDAC in July 1994 and Annaly Mortgage Management in November 1996. Since our IPO in October 1997, Annaly has raised almost \$1.5 billion in subsequent offerings, making Annaly one of the largest mortgage REITs. Annaly has consistently generated annual double-digit returns for its shareholders. Our success and future growth prospects are based on the proven ability of our strong and seasoned management team to deliver excellent results in volatile markets.

We are self-advised and self-managed. Management incentives are tied to book value and earnings, and we have no performance fees for management. Our low general and administrative expense ratio keeps our operating costs low and adds to shareholder return.

Jeremy Diamond



Rose-Marie Lyght



Kristopher Konrad



Ron Kazel



James Fortescue



Annaly

Team

Dear Fellow Shareholders,

Navigation is the theme of Annaly's 2004 annual report and this letter. For those of you who have been Annaly shareholders for years, you have heard me speak about the changing environment around us and our quest to navigate through it. In June 2003, the 10-year US Treasury note yield dropped to almost 3%, a generational low point. In our earnings call of that quarter, I described it as a "Lewis and Clark" environment; that is, we were entering uncharted territory which no business model, risk analysis tool or living money manager had predicted or experienced. Many economists and analysts believed that at the end of 2003 and throughout 2004 we were headed for much higher interest rates. We begged to differ, citing the 3% level as a harbinger of a prolonged period of nominally low interest rates. This is what has come to pass. We have been locked in an era of great complacency about risk and range-bound trading levels for the equity and debt markets. As I write this letter today, I believe that this era is now coming to an end. I believe we are entering a period of the reawakening of risk assessment. The price of this reassessment will be high, its lesson invaluable, its duration long and, therefore, its threat to value incalculable. Unlike the past two years, however, we have "seen this picture before" as a management team.

As most of you know from our regular quarterly conference calls, we at Annaly do not pretend to have a crystal ball. Today, however, I thought I would take a moment to review the times we live in and take a peek down the road to see what I think is going to happen.

For many years now investors have banked their risk-taking on the theory that there was a "Greenspan put" in the markets. This meant that if things really got out of hand, the Federal Reserve would ride to the rescue and inject liquidity and vigor back into the markets. These days are over. As the Japanese and the European Central Banks have learned over the past 15 years, there are times when monetary policy by itself can be ineffective. This is because a central bank's main constituents, commercial banks, have financially disintermediated risk away from their own balance sheets and into the hands of investors who are not under the clear jurisdiction of the central bank. The result is that the private sector has been repricing risk premiums because they control the underwriting standards, and these standards are looser than those of regulated banks.

Just as Long Term Capital Management created its problems without detection because it was not directly under the Fed's jurisdiction, there are now hundreds, if not thousands, of diverse pools of capital operating with inadequate supervision. Some are regulated investments, some are hedge funds, some are concentrated in hard assets, and some are simply levered into an overpriced house. I now believe that the combination of rising short-term rates and poor underwriting standards is setting up these pools of capital for what will look like a 'slow motion car wreck.' As credit conditions deteriorate, the market will correct itself, but the process is painful. Some may call me alarmist, but the daisy chain of credit 'car wrecks' seems to be a lot closer today than it was yesterday.

MICHAEL A. J. FARRELL



Listening to Congress argue over the federal budget deficit is a lot like watching a table full of people in a restaurant arguing with the maitre d' over the check he has just presented. The question at the table is the same one that our government is asking: "Who is going to pay for all of these things we ordered?" The unfortunate answer is—the taxpayers. Most people I talk to as I travel across the nation understand that every dime that the Federal tax cuts gave us since 2001 has been taken back, and then some, by our local municipalities and states. In effect, there really was no tax cut, merely a shift in tax liability. The residual growth effect from the cut, changes in dividend laws and extra low interest rates are now fading. During this couple of years, money has been enlisted in the pursuit of extra yield as the demographic surge of baby boomers began to shed risk in the equity markets and seek safer cash flows. From where I sit, as a global money manager, let me assure you that America is not alone in this regard. There has been and will continue to be, I think, a global thirst for yield. As the chairman of a company that I have often described as a 'yield manufacturer,' our product line is robust and ready to go. Our generation is faced with a looming series of deficits which will not be cured by 2% to 4% GDP growth alone. Real reform is necessary to protect the equity that we all have in America, from real estate to securities. The cost of this 'dinner check' for our nation will be slow growth at best and relatively low inflation-adjusted rates of return.

As I said earlier, we have no crystal ball at Annaly. But, like all business people, we constantly review the environment for our businesses and make adjustments. From Annaly's perspective we believe we are preparing ourselves for this investment climate change. We strategically deployed our portfolio of mortgage-backed securities into a defensive configuration. We acquired FIDAC, our investment manager, to help spread our expenses across a wider asset base. We continue to expand our asset management business to meet our objectives of controlling expenses, developing diverse growth elements under our strong core earnings and cementing our management team for the long run via deep equity ties to the firm. Last year's results are very telling of this constant self-review and improvement. In 2004, against the background of rising funding rates, a declining dollar and questions about the application of accounting guidelines by Fannie Mae and Freddie Mac, Annaly created a 16.04% return on average equity, increased earnings over the prior year, held expenses constant as a percentage of assets, grew our equity base and improved our book value from the prior year, issued two accretive preferred deals, grew assets under management at FIDAC and expanded distribution in foreign markets.

To paraphrase an old saying, "It is amazing what a small group of committed people can accomplish." That small group consists of the very same people I say "Good morning" to every morning. We continue to adapt to and navigate through the very dynamic investment environment in which we all live.

Prodesse non Nocere.



“Real reform is necessary to protect the equity that we all have in America...”



FIDAC

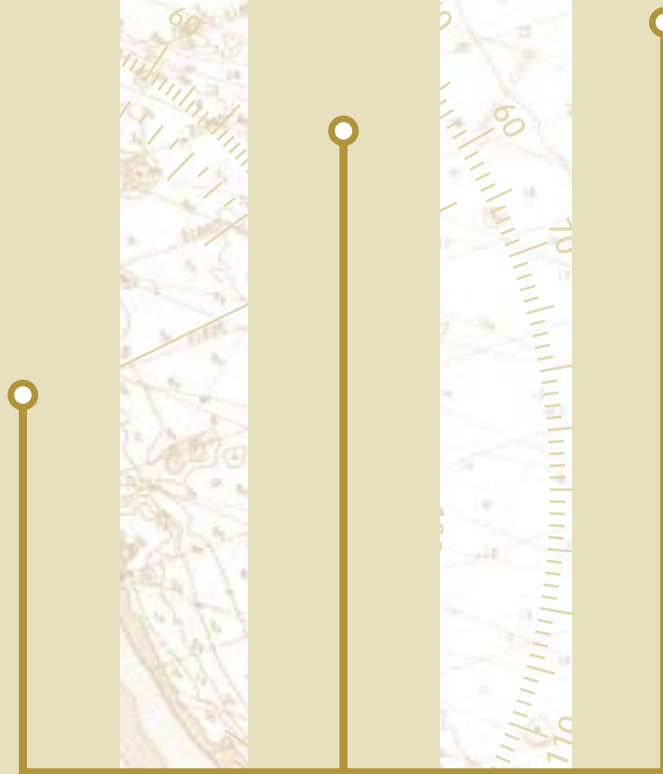
When Annaly acquired FIDAC in June 2004, it began the transition from pure mortgage REIT to asset management company. The FIDAC acquisition had an immediate positive impact for Annaly shareholders, blending fee income with Annaly's spread income and increasing assets under management. FIDAC generated over \$3.7 million and \$4.6 million in net fee income in the third and fourth quarter, respectively. At December 31, 2004, FIDAC managed, advised or sub-advised approximately \$16 billion in gross assets through numerous off-shore and on-shore public and private investment funds distributed globally as well as separate accounts for high net worth individuals, municipal funds and school endowments.

Formed in 1994, FIDAC is an asset management firm and one of the leading fixed income management companies in the United States. FIDAC's team of investment professionals, trained in-house and expert at all phases of the investment process, has built a successful long-term track record through some of the most challenging fixed income markets in memory. By prudently executing its strategy of applying leverage to liquid, high-quality, short-duration assets, and by not taking performance bonuses in any of its investment vehicles, FIDAC has consistently produced superior risk-adjusted returns.

(dollars in millions)

GROSS ASSETS UNDER MANAGEMENT

	2002	2003	2004
Gross Assets Under Management	\$8,000	\$13,600	\$15,900



The team managing Annaly fulfills the same roles at FIDAC. FIDAC earns management fees for executing the same general strategy as Annaly Mortgage Management. The strategy of the investment products managed by FIDAC is to provide net interest income for distribution to investors from the spread between the interest income earned from portfolios of residential mortgage-backed securities and the cost of repurchase agreements entered into to finance their acquisition, while seeking to limit exposure to interest rate risk and credit risk. Since the majority of the assets in FIDAC-managed portfolios are created and guaranteed by a U.S. Agency and further secured by the relevant mortgaged property of the homeowners, FIDAC believes that there is minimal credit risk in its portfolios.

FIDAC's strategy is differentiated from those of other fixed income and mortgage investment managers by the liquidity of the assets it purchases, its ability to leverage these assets, the transparency of the business model and the management compensation structure. Acquiring the most basic and liquid mortgage-backed securities is intended to give investors the desired element of clear and accurate valuation. The focus of the business model—to capture the spread between the yield on these assets and the cost to finance their acquisition, without introducing credit or other business risks—enables investors to more easily evaluate management performance. The management fees payable to FIDAC are not linked to investment performance, but rather they are linked to assets under

management. FIDAC believes that this remuneration philosophy increases the returns to investors and encourages a focus on long-term goals.

Distribution partners in the U.S. and around the world market the investment vehicles managed by FIDAC. This distribution system and the track record of FIDAC will serve as a platform for growth into new investment products and strategies. The long-term growth of FIDAC will enable Annaly shareholders to benefit from a growing stream of dividend income we receive from FIDAC.

THE FIDAC GLOBAL DISTRIBUTION NETWORK



(dollars in thousands, except for per share data)

	For the Year Ended December 31, 2004 (Consolidated)	For the Year Ended December 31, 2003	For the Year Ended December 31, 2002	For the Year Ended December 31, 2001	For the Year Ended December 31, 2000
STATEMENT OF OPERATIONS DATA:					
Interest income	\$532,328	\$337,433	\$404,165	\$263,058	\$109,750
Interest expense	270,116	182,004	191,758	168,055	92,902
Net interest income	\$262,212	\$155,429	\$212,407	\$95,003	\$16,848
Investment advisory and service fees	12,512	—	—	—	—
Gain on sale of mortgage-backed securities	5,215	40,907	21,063	4,586	2,025
Distribution fees	(2,860)	—	—	—	—
General and administrative expenses (G&A expense)	(24,029)	(16,233)	(13,963)	(7,311)	(2,286)
Income before taxes	253,050	180,103	219,507	92,278	16,587
Income taxes	4,458	—	—	—	—
Net income	248,592	180,103	219,507	92,278	16,587
Dividend on preferred stock	7,745	—	—	—	—
Net income available to common shareholders	\$240,847	\$180,103	\$219,507	\$92,278	\$16,587
Basic net income per average common share	\$2.04	\$1.95	\$2.68	\$2.23	\$1.18
Diluted net income per average common share	\$2.03	\$1.94	\$2.67	\$2.21	\$1.15
Dividends declared per common share	\$1.98	\$1.95	\$2.67	\$1.75	\$1.15
Dividends declared per preferred share	\$1.45	—	—	—	—

BALANCE SHEET DATA:

	December 31, 2004 (Consolidated)	December 31, 2003	December 31, 2002	December 31, 2001	December 31, 2000
Mortgage-Backed Securities, at fair value	\$19,038,386	\$11,956,512	\$11,551,857	\$7,575,379	\$1,978,219
Agency Debentures, at fair value	390,509	978,167	—	—	—
Total assets	19,560,299	12,990,286	11,659,084	7,717,314	2,035,029
Repurchase agreements	16,707,879	11,012,903	10,163,174	6,367,710	1,628,359
Total liabilities	17,859,829	11,841,066	10,579,018	7,049,957	1,899,386
Total stockholders' equity	1,700,470	1,149,220	1,080,066	667,357	135,642
Number of common shares outstanding	121,263,000	96,074,096	84,569,206	59,826,975	14,522,978

OTHER DATA:

	For the Year Ended December 31, 2004 (Consolidated)	For the Year Ended December 31, 2003	For the Year Ended December 31, 2002	For the Year Ended December 31, 2001	For the Year Ended December 31, 2000
Average total assets	\$17,293,174	\$12,975,039	\$10,486,423	\$5,082,852	\$1,652,459
Average investment securities	16,399,184	12,007,333	9,575,365	4,682,778	1,564,228
Average borrowings	15,483,118	11,549,368	9,128,933	4,388,900	1,449,999
Average equity	1,550,076	1,122,633	978,107	437,376	117,727
Yield on average interest earning assets	3.25%	2.81%	4.22%	5.62%	7.02%
Cost of funds on average interest bearing liabilities	1.74%	1.58%	2.10%	3.83%	6.41%
Interest rate spread	1.51%	1.23%	2.12%	1.79%	0.61%

FINANCIAL RATIOS:

Net interest margin (net interest income/average total assets)	1.52%	1.20%	2.03%	1.87%	1.02%
G&A expense as a percentage of average total assets	0.14%	0.13%	0.13%	0.14%	0.14%
G&A expense as a percentage of average equity	1.55%	1.45%	1.43%	1.67%	1.94%
Return on average total assets	1.44%	1.39%	2.09%	1.82%	1.00%
Return on average equity	16.04%	16.04%	22.44%	21.10%	14.09%

OVERVIEW

Annaly manages assets on behalf of institutional and individual investors worldwide through Annaly and through the funds managed by its wholly-owned registered investment advisor, FIDAC. The Company's principal business objective is to generate net income for distribution to investors from the spread between the interest income on its mortgage-backed securities and the cost of borrowing to finance their acquisition and from dividends it receives from FIDAC.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements contained in this annual report, and certain statements contained in our future filings with the Securities and Exchange Commission (the "SEC" or the "Commission"), in our press releases or in our other public or shareholder communications may not be based on historical facts and are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements, which are based on various assumptions (some of which are beyond our control), may be identified by reference to a future period or periods or by the use of forward-looking terminology, such as "may," "will," "believe," "expect," "anticipate," "continue," or similar terms or variations on those terms or the negative of those terms. Actual results could differ materially from those set forth in forward-looking statements due to a variety of factors, including, but not limited to, changes in interest rates, changes in yield curve, changes in prepayment rates, the availability of mortgage-backed securities for purchase, the availability of financing and, if available, the terms of any financing, and risks associated with the investment advisory business of FIDAC, including the removal by FIDAC's clients of assets FIDAC manages, FIDAC's regulatory requirements and competition in the investment advisory business. For a discussion of the risks and uncertainties which could cause actual results to differ from those contained in the forward-looking statements, please see the information under the caption "Risk Factors" described in our Form 10-K. We do not undertake, and specifically disclaim any obligation, to publicly release the result of any revisions which may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

OVERVIEW

Annaly manages assets on behalf of institutional and individual investors worldwide through Annaly and through the funds managed by its wholly-owned registered investment advisor, FIDAC. The Company's principal business objective is to generate net income for distribution to investors from the spread between the interest income on its mortgage-backed securities and the cost of borrowing to finance their acquisition and from dividends it receives from FIDAC.

We are primarily engaged in the business of investing, on a leveraged basis, in mortgage pass-through certificates, collateralized mortgage obligations and other mortgage-backed securities representing interests in or obligations backed by pools of mortgage loans (collectively, "Mortgage-Backed Securities"). We also invest in Federal Home Loan Bank ("FHLB"), Federal Home Loan Mortgage Corporation ("FHLMC"), and Federal National Mortgage Association ("FNMA") debentures. The Mortgage-Backed Securities and agency debentures are collectively referred to herein as "Investment Securities."

Under our capital investment policy, at least 75% of our total assets must be comprised of high-quality mortgage-backed securities and short-term investments. High quality securities means securities that (1) are rated within one of the two highest rating categories by at least one of the nationally recognized rating agencies, (2) are unrated but are guaranteed by the United States government or an agency of the United States government,

or (3) are unrated but we determine them to be of comparable quality to rated high-quality mortgage-backed securities.

The remainder of our assets, comprising not more than 25% of our total assets, may consist of other qualified REIT real estate assets which are unrated or rated less than high quality, but which are at least "investment grade" (rated "BBB" or better by Standard & Poor's Corporation ("S&P") or the equivalent by another nationally recognized rating agency) or, if not rated, we determine them to be of comparable credit quality to an investment which is rated "BBB" or better.

We may acquire mortgage-backed securities backed by single-family residential mortgage loans as well as securities backed by loans on multi-family, commercial or other real estate-related properties. To date, all of the mortgage-backed securities that we have acquired have been backed by single-family residential mortgage loans.

We have elected to be taxed as a REIT for federal income tax purposes. Pursuant to the current federal tax regulations, one of the requirements of maintaining its status as a REIT is that we must distribute at least 90% of our REIT taxable income (determined without regard to the deduction for dividends paid and by excluding any net capital gain) to our stockholders, subject to certain adjustments.

The results of our operations are affected by various factors, many of which are beyond our control. Our results of operations primarily depend on, among other things, the level of our net interest income, the market value of our assets and the supply of and demand for such assets. Our net interest income, which reflects the amortization of purchase premiums, varies primarily as a result of changes in interest rates, borrowing costs and prepayment speeds, the behavior of which involves various risks and uncertainties. Prepayment speeds, as reflected by the Constant Prepayment Rate, or CPR, and interest rates vary according to the type of investment, conditions in financial markets, competition and other factors, none of which can be predicted with any certainty. In general, as prepayment speeds on our Mortgage-Backed Securities portfolio increase, related purchase premium amortization increases, thereby reducing the net yield on such assets. The CPR on our Mortgage Backed Securities portfolio averaged 29% and 42% for the years ended December 31, 2004 and 2003, respectively. Since changes in interest rates may significantly affect our activities, our operating results depend, in large part, upon our ability to effectively manage interest rate risks and prepayment risks while maintaining our status as a REIT.

The following table presents the CPR experienced on our Mortgage-Backed Securities portfolio, on an annualized basis, for the quarterly periods presented.

QUARTER ENDED	CPR
December 31, 2004	27%
September 30, 2004	25%
June 30, 2004	33%
March 31, 2004	31%
December 31, 2003	42%

We believe that the CPR in future periods will depend, in part, on changes in and the level of market interest rates across the yield curve, with higher CPRs expected during periods of declining interest rates and lower CPRs expected during periods of rising interest rates.

We have extended contractual maturities on borrowings, such that our weighted average contractual maturity on our repurchase agreements was 211 days at December 31, 2004, as compared to 203 days at December 31, 2003.

The table below provides quarterly information regarding our average balances, interest income, interest expense, yield on assets, cost of funds and net interest income for the quarterly periods presented.

(ratios for the quarters have been annualized, dollars in thousands)	Average Investment Securities Held ⁽¹⁾	Total Interest Income	Yield on Average Interest Earning Assets	Average Balance of Repurchase Agreements	Total Interest Expense	Average Cost of Funds	Net Interest Income
Quarter Ended December 31, 2004	\$17,932,449	\$156,783	3.50%	\$16,896,216	\$93,992	2.23%	\$62,791
Quarter Ended September 30, 2004	\$16,562,971	\$138,970	3.36%	\$15,568,691	\$70,173	1.80%	\$68,797
Quarter Ended June 30, 2004	\$16,649,072	\$122,234	2.94%	\$15,880,353	\$55,648	1.40%	\$66,586
Quarter Ended March 31, 2004	\$14,452,245	\$114,341	3.16%	\$13,587,211	\$50,303	1.48%	\$64,038

⁽¹⁾ Does not reflect unrealized gains/(losses).

We continue to explore alternative business strategies, alternative investments and other strategic initiatives to complement our core business strategy of investing, on a leveraged basis, in high quality Investment Securities. No assurance, however, can be provided that any such strategic initiative will or will not be implemented in the future.

CRITICAL ACCOUNTING POLICIES

Management's discussion and analysis of financial condition and results of operations is based on the amounts reported in our financial statements. These financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. In preparing the financial statements, management is required to make various judgments, estimates and assumptions that affect the reported amounts. Changes in these estimates and assumptions could have a material effect on our financial statements. The following is a summary of our policies most affected by management's judgments, estimates and assumptions. These policies have not changed during 2004.

Market valuation of Investment Securities: All assets classified as available-for-sale are reported at fair value, based on market prices. Although we generally intend to hold most of our Investment Securities until maturity, we may, from time to time, sell any of our Investment Securities as part our overall management of our portfolio. Accordingly, we are required to classify all of our Investment Securities as available-for-sale. Our policy is to obtain market values from at least three independent sources and record the market value of the securities based on the average of the three. Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. The investments with unrealized losses are not considered other-than-temporarily impaired since the Company has the ability and intent to hold the investments for a period of time, to maturity if necessary, sufficient for a forecasted market price recovery up to or beyond the cost of the investments. Unrealized losses on Investment Securities 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 Investment Securities is adjusted. There were no such adjustments for the years ended December 31, 2004, 2003 or 2002. If in the future, management determines an impairment to be other-than temporary we may need to realize a loss that would have an impact on future income.

Interest income: Interest income is accrued based on the outstanding principal amount of the outstanding principal amount of the Investment Securities and their contractual terms. Premiums and discounts associated with the purchase of the Investment Securities are amortized or accreted into interest income over the projected lives of the securities using the interest

method. Our policy for estimating prepayment speeds for calculating the effective yield is to evaluate historical performance, Wall Street consensus prepayment speeds, and current market conditions. If our estimate of prepayments is incorrect, we may be required to make an adjustment to the amortization or accretion of premiums and discounts that would have an impact on future income.

Repurchase Agreements: We finance the acquisition of our Investment Securities through the use of repurchase agreements. Repurchase agreements are treated as collateralized financing transactions and are carried at their contractual amounts, including accrued interest, as specified in the respective agreements. Accrued interest is recorded as a separate line item on the statements of financial condition.

Income Taxes: We have elected to be taxed as a Real Estate Investment Trust ("REIT") and intend to comply with the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), with respect thereto. Accordingly, the Company will not be subjected to federal income tax to the extent of its distributions to shareholders and as long as certain asset, income and stock ownership tests are met. The Company and FIDAC have made a joint election to treat FIDAC as a taxable REIT subsidiary. As such, FIDAC will be taxable as a domestic C corporation and subject to federal and state and local income taxes based upon its taxable income.

RESULTS OF OPERATIONS

Net Income Summary

For the year ended December 31, 2004, our net income was \$248.6 million or \$2.04 basic earnings per average share available for common shareholders, as compared to \$180.1 million or \$1.95 basic earnings per average share for the year ended December 31, 2003. For the year ended December 31, 2002, our net income was \$219.5 million, or \$2.68 basic earnings per average share available for common shareholders. Net income per average share increased by \$0.09 and total net income increased \$68.5 million for the year ended December 31, 2004, when compared to the year ended December 31, 2003. We attribute the increase in total net income for the year ended December 31, 2004 over the year ended December 31, 2003 as being due to the increased asset base and the interest rate spread. The increased asset base was the result of deploying additional capital of approximately \$581.0 million from December 31, 2003 to December 31, 2004 into our strategy. Also, the addition of \$12.5 million advisory fee income from FIDAC for seven months of the year aided the increased revenue of the combined companies. The interest rate spread increased from 1.23% to 1.51%. The total amortization for the year ended December 31, 2004 was \$179.6 million and for the year ended December 31, 2003 was \$216.6 million. For the year ended December 31, 2004, gain on sale of Mortgage-Backed Securities was \$5.2 million, as compared to \$40.9 million for the year ended December 31, 2003. Even with the substantial decline in gain on sale of Mortgage-Backed Securities, the increase in spread income resulted in an increase in earnings per share year over year.

Net income per average share decreased by \$0.73 and total net income decreased \$39.4 million for the year ended December 31, 2003, when compared to the year ended December 31, 2002. The reason for the decline in net income was due to the interest rate spread decreasing to 1.23% in 2003 from 2.12% for the prior year. The primary reason for the decline in interest rate spread is the amortization of premium paid on the mortgage-backed securities. The total amortization for the year ended December 31, 2003 was \$216.6 million and for the year ended December 31, 2002 was \$106.2 million. The trend of record prepayment levels began to decline in the fourth quarter of the year 2003. This was evidenced by the amortization for

the fourth quarter of \$38.4 million, in comparison to the third quarter of 2003 of \$72.0 million.

Dividends per share for the year ended December 31, 2004 were \$1.98 per share, or \$245.6 million in total. Dividends per share for the year ended December 31, 2003 were \$1.95 per share, or \$179.3 million in total. Dividends per share for the year ended December 31, 2002 were \$2.67 per share, or \$223.6 million in total. Our return on average equity was 16.04% for the year ended December 31, 2004, 16.04% for the year ended December 31, 2003, and 22.44% for the year ended December 31, 2002.

The table below presents the net income summary for the years ended December 31, 2004, 2003, 2002, 2001, and 2000.

NET INCOME SUMMARY

(dollars in the thousands, except for per share data)	Year Ended December 31, 2004	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001	Year Ended December 31, 2000
Interest income	\$532,328	\$337,433	\$404,165	\$263,058	\$109,750
Interest expense	270,116	182,004	191,758	168,055	92,902
Net interest income	\$262,212	\$155,429	\$212,407	\$95,003	\$16,848
Investment advisory and service fees	12,512	—	—	—	—
Gain on sale of mortgage-backed securities	5,215	40,907	21,063	4,586	2,025
Distribution fees	(2,860)	—	—	—	—
General and administrative expenses	(24,029)	(16,233)	(13,963)	(7,311)	(2,286)
Income before income taxes	253,050	180,103	219,507	92,278	16,587
Income taxes	4,458	—	—	—	—
Net income	248,592	180,103	219,507	92,278	16,587
Dividend on preferred stock	7,745	—	—	—	—
Net income available to common shareholders	\$240,847	\$180,103	\$219,507	\$92,278	\$16,587
Weighted average number of basic common shares outstanding	118,223,330	92,215,352	82,044,141	41,439,631	14,089,436
Weighted average number of diluted common shares outstanding	118,459,145	93,031,253	82,282,883	41,857,498	14,377,459
Basic net income per share available to common shareholders	\$2.04	\$1.95	\$2.68	\$2.23	\$1.18
Diluted net income per share available to common shareholders	\$2.03	\$1.94	\$2.67	\$2.21	\$1.15
Average total assets	\$17,293,174	\$12,975,039	\$10,486,423	\$5,082,852	\$1,652,459
Average equity	1,550,076	1,122,633	978,107	437,376	117,727
Return on average total assets	1.44%	1.39%	2.09%	1.82%	1.00%
Return on average equity	16.04%	16.04%	22.44%	21.10%	14.09%

Interest Income and Average Earning Asset Yield

We had average earning assets of \$16.4 billion for the year ended December 31, 2004. We had average earning assets of \$12.0 billion for the year ended December 31, 2003. We had average earning assets of \$9.6 billion for the year ended December 31, 2002. Our primary source of income is interest income. A portion of our income was generated by gains on the sales of our Mortgage-Backed Securities of \$5.2 million, \$40.9 million, and \$21.1 million for the years ended December 31, 2004, 2003 and 2002, respectively. Our interest income was \$532.3 million for the year ended December 31, 2004, \$337.4 million for the year ended December 31, 2003, and \$404.2 million for the year ended December 31, 2002. The yield on average investment securities was 3.25%, 2.81%, and 4.22% for the same respective periods. Our average earning asset balance increased by \$4.4 billion for the year ended December 31, 2004 in comparison to the prior year. The increase was the direct result of the increased asset base and the increase in the interest rate yields. The weighted average coupon rate at December 31, 2004 was 4.53%, as compared to 4.36%

at December 31, 2003. The prepayment speeds decreased to 29% CPR for the year ended December 31, 2004, from 42% CPR for the year ended December 31, 2003. The increase in coupon, in conjunction with lower prepayment speeds, resulted in an increase in yield of 44 basis points for the year 2004, when compared to 2003. The declining yield of 2.81% for the year ended December 31, 2003, as compared to the yield of 4.22% for the year ended December 31, 2002 were the direct result of increased amortization on our assets due to the rise in prepayments speeds to 42% CPR for the year ended December 31, 2003, from 33% CPR for the year ended December 31, 2002, especially in the third quarter of 2003. The homeowners' prepayment option makes the average term, yield and performance of a mortgage-backed security uncertain because of the uncertainty in timing the return of principal. In general, prepayments decrease the total yield on a bond purchased at a premium, because over the life of the bond that premium has to be amortized. The faster prepayments, the shorter the life of the security, which results in increased amortization.

The table below shows our average balance of cash equivalents and Investment Securities, the yields we earned on each type of earning assets, our yield on average earning assets and our interest income for the years ended December 31, 2004, 2003, 2002, 2001, and 2000, and the four quarters in 2004.

AVERAGE EARNING ASSET YIELD

(ratios for the four quarters in 2004 are annualized, dollars in thousands)	Average Investment Securities	Yield on Average Investment Securities	Average Constant Prepayment Rate	Interest Income
For the Year Ended December 31, 2004	\$16,399,184	3.25%	29%	\$532,328
For the Year Ended December 31, 2003	\$12,007,333	2.81%	42%	\$337,433
For the Year Ended December 31, 2002	\$9,575,365	4.22%	33%	\$404,165
For the Year Ended December 31, 2001	\$4,682,778	5.62%	27%	\$263,058
For the Year Ended December 31, 2000	\$1,564,228	7.02%	11%	\$109,750
For the Quarter Ended December 31, 2004	\$17,932,449	3.50%	27%	\$156,783
For the Quarter Ended September 30, 2004	\$16,562,971	3.36%	25%	\$138,970
For the Quarter Ended June 30, 2004	\$16,649,072	2.94%	33%	\$122,234
For the Quarter Ended March 31, 2004	\$14,452,245	3.16%	31%	\$114,341

The Constant Prepayment Rate decreased to 29% for the year ended December 31, 2004, as compared to 42% for the year ended December 31, 2003 and 33% for the year ended December 31, 2002. The total amortization for the year ended December 31, 2004, 2003, and 2002 was \$179.6 million, \$216.6 million, and \$106.2 million, respectively. For the first, second, third, and fourth quarters of 2004, amortization was \$41.5 million, \$56.1 million, \$39.7 million, and \$42.3 million, respectively. The second quarter experienced the highest level of prepayments and the third and fourth quarters were materially unchanged, providing evidence that the trend of higher prepayments is continuing.

Interest Expense and the Cost of Funds

We anticipate that our largest expense will be the cost of borrowed funds. We had average borrowed funds of \$15.5 billion and total interest expense of \$270.1 million for the year ended December 31, 2004. We had average borrowed funds of \$11.5 billion and total interest expense of \$182.0 million for the year ended December 31, 2003. We had average borrowed funds of \$9.1 billion and total interest expense of \$191.8 million for the year ended December 31, 2002. Our average cost of funds was 1.74% for the year ended December 31, 2004 and 1.58% for the year ended December 31, 2003 and 2.10% for the year December 31, 2002. The cost of funds rate increased by

16 basis points and the average borrowed funds increased by \$4.0 billion for the year ended December 31, 2004 when compared to the year ended December 31, 2003. Interest expense for the year increased by \$88.1 million; due to the substantial increase in the average repurchase balance and the increase in the cost of funds rate. The increase in the average repurchase balance was the result of our implementing our leveraged strategy after the completion of the equity offerings in the first quarter 2004, in addition to equity acquired through the equity shelf program, the direct purchase and dividend reinvestment plan, and options exercised. The cost of funds rate decreased by 52 basis points and the average borrowed funds increased by \$2.4 billion for the year ended December 31, 2003, when compared to the year ended December 31, 2002. Interest expense for the year ended December 31, 2003 declined \$9.8 million over the previous year, even with the increase in the average borrowed funds for the year. Since a substantial portion of our repurchase agreements are short term, changes in market rates are directly reflected in our interest expense. Our average cost of funds was 0.24% above average one-month LIBOR and 0.06% below average six-month LIBOR for the year ended December 31, 2004. Our average cost of funds was 0.37% above average one-month LIBOR and 0.35% above average six-month LIBOR for the year ended December 31, 2003.

The table below shows our average borrowed funds and average cost of funds as compared to average one-month and average six-month LIBOR for the years ended December 31, 2004, 2003, 2002, 2001, and 2000 and the four quarters in 2004.

AVERAGE COST OF FUNDS

(Ratios for the four quarters in 2004 have been annualized, dollars in thousands)	Average Borrowed Funds	Interest Expense	Average Cost of Funds	Average One-Month LIBOR	Average Six-Month LIBOR	Average One-Month LIBOR Relative to Average Six-Month LIBOR	Average Cost of Funds Relative to Average One-Month LIBOR	Average Cost of Funds Relative to Average Six-Month LIBOR
For the Year Ended December 31 2004	\$15,483,118	\$270,116	1.74%	1.50%	1.80%	(0.30%)	0.24%	(0.06%)
For the Year Ended December 31, 2003	\$11,549,368	\$182,004	1.58%	1.21%	1.23%	(0.02%)	0.37%	0.35%
For the Year Ended December 31, 2002	\$9,128,933	\$191,758	2.10%	1.77%	1.88%	(0.11%)	0.33%	0.22%
For the Year Ended December 31, 2001	\$4,388,900	\$168,055	3.83%	3.88%	3.73%	0.15%	(0.05%)	0.10%
For the Year Ended December 31, 2000	\$1,449,999	\$92,902	6.41%	6.41%	6.66%	(0.25%)	—	(0.25%)
For the Quarter Ended December 31, 2004	\$16,896,216	\$93,992	2.23%	2.14%	2.48%	(0.34%)	0.09%	(0.25%)
For the Quarter Ended September 30, 2004	\$15,568,691	\$70,173	1.80%	1.59%	1.97%	(0.38%)	0.21%	(0.17%)
For the Quarter Ended June 30, 2004	\$15,880,353	\$55,648	1.40%	1.15%	1.54%	(0.39%)	0.25%	(0.14%)
For the Quarter Ended March 31, 2004	\$13,587,211	\$50,303	1.48%	1.10%	1.18%	(0.08%)	0.38%	0.30%

Net Interest Income

Our net interest income which equals interest income less interest expense, totaled \$262.2 million for the year ended December 31, 2004, \$155.4 for the year ended December 31, 2003 and \$212.4 million for the year ended December 31, 2002. Our net interest income increased because of the increase in our assets that resulted from the common stock and preferred stock offerings during 2004 as well as the increase in our spread income. Our net interest spread, which equals the yield on our average assets for the period less the average cost of funds for the period, was 1.51% for the year ended

December 31, 2004 as compared to 1.23% for the year ended December 31, 2003. This 28 basis point increase was a result of the increase of the weighted average coupon at December 31, 2004 of 4.53% from 4.36% at December 31, 2003, and the improvement in CPR discussed above. The increase in yield was only partially offset by the 16 basis point increase in the cost of funds. Our net interest income decreased \$57.0 million for the year ended December 31, 2003 over the prior year. This was the direct result of the CPR, which increased from 33% in 2002 in the prior year to 42% in 2003.

The table below shows our interest income by earning asset type, average earning assets by type, total interest income, interest expense, average repurchase agreements, average cost of funds, and net interest income for the years ended December 31, 2004, 2003, 2002, 2001, and 2000 and the four quarters in 2004.

NET INTEREST INCOME

(Ratios for the four quarters in 2004 have been annualized, dollars in thousands)	Average Investment Securities Held	Total Interest Income	Yield Average Interest Earning Assets	Average Balance of Repurchase Agreements	Interest Expense	Average Cost of Funds	Net Interest Income	Net Interest Rate Spread
For the Year Ended December 31, 2004	\$16,399,184	\$532,328	3.25%	\$15,483,118	\$270,116	1.74%	\$262,212	1.51%
For the Year Ended December 31, 2003	\$12,007,333	\$337,433	2.81%	\$11,549,368	\$182,004	1.58%	\$155,429	1.23%
For the Year Ended December 31, 2002	\$9,575,365	\$404,165	4.22%	\$9,128,933	\$191,758	2.10%	\$212,407	2.12%
For the Year Ended December 31, 2001	\$4,682,778	\$263,058	5.62%	\$4,388,900	\$168,055	3.83%	\$95,003	1.79%
For the Year Ended December 31, 2000	\$1,564,228	\$109,750	7.02%	\$1,449,999	\$92,902	6.41%	\$16,848	0.61%
For the Quarter Ended December 31, 2004	\$17,932,449	\$156,783	3.50%	\$16,896,216	\$93,992	2.23%	\$62,791	1.27%
For the Quarter Ended September 30, 2004	\$16,562,971	\$138,970	3.36%	\$15,568,691	\$70,173	1.80%	\$68,797	1.56%
For the Quarter Ended June 30, 2004	\$16,649,072	\$122,234	2.94%	\$15,880,353	\$55,648	1.40%	\$66,586	1.54%
For the Quarter Ended March 31, 2004	\$14,452,245	\$114,341	3.16%	\$13,587,211	\$70,173	1.48%	\$64,038	1.68%

Investment Advisory and Service Fees

FIDAC is a registered investment advisor that generally receives annual net investment advisory fees of approximately 10 to 15 basis points of the gross assets it manages, assists in managing or supervises. At December 31, 2004, FIDAC had under management approximately \$1.9 billion in net assets and \$15.9 billion in gross assets, compared to \$1.5 billion in net assets and \$13.6 billion in gross assets at December 31, 2003. Investment advisory and service fees for the year ended December 31, 2004 totaled \$9.7 million, net of fees paid to third parties pursuant to distribution service agreements for facilitating and promoting distribution of shares of FIDAC's clients. FIDAC's net advisory fees were included in the consolidated statements post the merger dated June 4, 2004.

Gains and Losses on Sales of Mortgage-Backed Securities

For the year ended December 31, 2004, we sold Mortgage-Backed Securities with an aggregate historical amortized cost of \$591.7 million for an aggregate gain of \$5.2 million. For the year ended December 31, 2003, we sold Mortgage-Backed Securities with an aggregate historical amortized cost of \$2.8 billion for an aggregate gain of \$40.9 million. For the year ended December 31, 2002, we sold Mortgage-Backed Securities with an aggregate historical amortized cost of \$2.0 billion for an aggregate gain of \$21.1 million. The gain on sale of assets for the year ended December 31, 2004 declined by \$35.7 million. During the year ended December 31, 2003 the amount of sale was higher than historically, with a bulk of the liquidations in the second quarter. Due to declining rates, fixed rate securities had significantly appreciated and it was determined by the Company's management to take advantage of

the appreciation. The gain on sale of assets for the year ended December 31, 2003 increased by \$19.8 million over the prior year. The difference between the sale price and the historical amortized cost of our Mortgage-Backed Securities is a realized gain and increases income accordingly. We do not expect to sell assets on a frequent basis, but may from time to time sell existing assets to move into new assets, which our management believes might have higher risk-adjusted returns, or to manage our balance sheet as part of our asset/liability management strategy. There have been insignificant losses from the sale of securities during the periods.

General and Administrative Expenses

General and administrative ("G&A") expenses were \$24.0 million for the year ended December 31, 2004, \$16.2 million for the year ended December 31, 2003, and \$14.0 million for the year ended December 31, 2002. G&A expenses as a percentage of average total assets was 0.14%, 0.13%, and 0.13%, for the years ended December 31, 2004, 2003, and 2002, respectively. The increase in G&A expenses of \$7.8 million for the year December 31, 2004, was primarily the result of increased salaries, directors and officers insurance and additional costs related to the FIDAC merger. Staff increased from 20 at the end of 2003 to 30 at the end of 2004. G&A expense has increased proportionately with our increased capital base and the growth in staff from 15 at the end of 2002 to 20 at the end of 2003. Salaries and bonuses for the years ended December 31, 2004, 2003, 2002, and 2001 were \$17.2 million, \$11.5 million, \$10.8 million, and \$4.7 million. Even with the increased asset base, G&A expense as a percentage of average assets has not increased significantly.

The table below shows our total G&A expenses as compared to average total assets and average equity for the years ended December 31, 2004, 2003, 2002, 2001, and 2000, and the four quarters in 2004.

G&A EXPENSES AND OPERATING EXPENSE RATIOS

(Ratios for the four quarters in 2004 have been annualized, dollars in thousands)	Total G&A Expenses	Total G&A Expenses/ Average Assets	Total G&A Expenses/ Average Equity
For the Year Ended December 31, 2004	\$24,029	0.14%	1.55%
For the Year Ended December 31, 2003	\$16,233	0.13%	1.45%
For the Year Ended December 31, 2002	\$13,963	0.13%	1.43%
For the Year Ended December 31, 2001	\$7,311	0.14%	1.67%
For the Year Ended December 31, 2000	\$2,286	0.14%	1.94%
For the Quarter Ended December 31, 2004	\$6,862	0.14%	1.63%
For the Quarter Ended September 30, 2004	\$6,159	0.14%	1.53%
For the Quarter Ended June 30, 2004	\$5,643	0.13%	1.39%
For the Quarter Ended March 31, 2004	\$5,790	0.15%	1.63%

Net Income and Return on Average Equity

Our net income was \$248.6 million for the year ended December 31, 2004, \$180.1 million for the year ended December 31, 2003, and \$219.5 million for the year ended December 31, 2002. Our return on average equity was 16.04% for the year ended December 31, 2004, 16.04% for the year ended December 31, 2003, and 22.44% for the year ended December 31, 2002. We attribute the increase in total net income for the year ended December 31, 2004 over the year ended December 31, 2003 due to the increased asset base and the interest rate spread. The increased asset base was the result of

deploying additional capital of approximately \$581.0 million from December 31, 2003 to December 31, 2004 into our strategy. To a lesser extent, the seven months of advisory fee income from FIDAC aided in the income growth.

Even though total net income increased, the return on average equity remained unchanged at 16.04%. Net income decreased by \$39.4 million in the year 2003 over the previous year, due to the declining interest rate spread. In addition to spread income, we were able to take advantage of appreciation in asset value in 2003, 2002, and 2001.

The table below shows our net interest income, net investment advisory and service fees, gain on sale of mortgage-backed securities, G&A expenses, and income taxes each as a percentage of average equity, and the return on average equity for the years ended December 31, 2004, 2003, 2002, 2001, and 2000, and for the four quarters in 2004.

COMPONENTS OF RETURN ON AVERAGE EQUITY

(Ratios for the four quarters in 2004 have been annualized)	Net Interest Income/ Average Equity	Net Investment Advisory and Service Fees/ Average Equity	Gain on Sale of Mortgage-Backed Securities/ Average Equity	G&A Expenses/ Average Equity	Income Taxes/ Average Equity	Return on Average Equity
For the Year Ended December 31, 2004	16.92%	0.62%	0.34%	1.55%	0.29%	16.04%
For the Year Ended December 31, 2003	13.85%	—	3.64%	1.45%	—	16.04%
For the Year Ended December 31, 2002	21.72%	—	2.15%	1.43%	—	22.44%
For the Year Ended December 31, 2001	21.72%	—	1.05%	1.67%	—	21.10%
For the Year Ended December 31, 2000	14.31%	—	1.72%	1.94%	—	14.09%
For the Quarter Ended December 31, 2004	14.95%	1.10%	0.27%	1.63%	0.57%	14.12%
For the Quarter Ended September 30, 2004	17.13%	0.94%	0.34%	1.53%	0.29%	16.59%
For the Quarter Ended June 30, 2004	16.44%	0.31%	0.52%	1.39%	0.12%	15.76%
For the Quarter Ended March 31, 2004	18.05%	—	0.17%	1.63%	—	16.59%

FINANCIAL CONDITION

Investment Securities

All of our Mortgage-Backed Securities at December 31, 2004, 2003, and 2002 were adjustable-rate or fixed-rate Mortgage-Backed Securities backed by single-family mortgage loans. All of the mortgage assets underlying these Mortgage-Backed Securities were secured with a first lien position on the underlying single-family properties. All our Mortgage-Backed Securities were FHLMC, FNMA or GNMA mortgage pass-through certificates or CMOs, which carry an implied "AAA" rating. We mark-to-market all of our earning assets to fair value.

All of our Agency Debentures are callable and carry an implied "AAA" rating. We mark-to-market all of our Agency Debentures to fair value.

We accrete discount balances as an increase in interest income over the life of discount investment securities and we amortize premium balances as a decrease in interest income over the life of premium investment securities. At December 31, 2004, 2003, and 2002 we had on our balance sheet a total of \$1.1 million, 1.5 million and \$664,000, respectively, of unamortized discount (which is the difference between the remaining principal value and current historical amortized cost of our Investment Securities acquired at a

price below principal value) and a total of \$427.0 million, \$301.3 million and \$274.6 million respectively, of unamortized premium (which is the difference between the remaining principal value and the current historical amortized cost of our investment securities acquired at a price above principal value).

We received mortgage principal repayments of \$6.5 billion for the year ended December 31, 2004, \$8.3 billion for the year ended December 31, 2003, and \$4.7 billion for the year ended December 31, 2002. The overall prepayment speed for the year ended December 31, 2004, 2003, and 2002 was 29%, 42%, and 33% respectively. During the year ended December 31, 2004, the CPR declined to 29%, from 42%, due to a decline in refinancing activity. During the year ended December 31, 2003, the annual prepayment speed was the

highest in our history at 42%. The result was record returns of principal for the year, relative to the asset size. Given our current portfolio composition, if mortgage principal prepayment rates were to increase over the life of our Mortgage-Backed Securities, all other factors being equal, our net interest income would decrease during the life of these mortgage-backed securities as we would be required to amortize our net premium balance into income over a shorter time period. Similarly, if mortgage principal prepayment rates were to decrease over the life of our Mortgage-Backed Securities, all other factors being equal, our net interest income would increase during the life of these Mortgage-Backed Securities as we would amortize our net premium balance over a longer time period.

The table below summarizes our Investment Securities at December 31, 2004, 2003, 2002, 2001, and 2000, and September 30, 2004, June 30, 2004, and March 31, 2004.

INVESTMENT SECURITIES

(dollars in thousands)	Principal Amount	Net Premium	Amortized Cost	Amortized Cost/Principal Amount	Estimated Fair Value	Estimated Fair Value/Principal Amount	Weighted Average Yield
At December 31, 2004	\$19,123,902	\$425,792	\$19,549,694	102.23%	\$19,428,895	101.59%	3.43%
At December 31, 2003	\$12,682,130	\$299,810	\$12,981,940	102.36%	\$12,934,679	101.99%	2.96%
At December 31, 2002	\$11,202,384	\$273,963	\$11,476,347	102.45%	\$11,551,857	103.12%	3.25%
At December 31, 2001	\$7,399,941	\$137,269	\$7,537,210	101.86%	\$7,575,379	102.37%	4.41%
At December 31, 2000	\$1,967,967	\$23,296	\$1,991,263	101.18%	\$1,978,219	100.52%	7.09%
At September 30, 2004	\$17,893,902	\$409,115	\$18,303,017	102.29%	\$18,211,030	101.77%	3.36%
At June 30, 2004	\$16,914,635	\$384,648	\$17,299,283	102.27%	\$17,121,795	101.22%	3.04%
At March 31, 2004	\$17,662,596	\$412,563	\$18,075,159	102.34%	\$18,079,598	102.36%	2.72%

The tables below set forth certain characteristics of our Investment Securities. The index level for adjustable-rate Investment Securities is the weighted average rate of the various short-term interest rate indices, which determines the coupon rate.

ADJUSTABLE-RATE INVESTMENT SECURITY CHARACTERISTICS

(dollars in thousands)	Principal Amount	Weighted Average Coupon Rate	Weighted Average Index Level	Weighted Average Net Margin	Weighted Average Term to Next Adjustment	Weighted Average Lifetime Cap	Weighted Average Asset Yield	Principal Amount at Period End as % of Total Investment Securities
At December 31, 2004	\$13,544,872	4.23%	2.45%	1.78%	24 months	10.12%	3.24%	70.83%
At December 31, 2003	\$9,294,934	3.85%	2.25%	1.60%	23 months	9.86%	2.47%	73.29%
At December 31, 2002	\$7,007,062	4.10%	2.51%	1.59%	11 months	10.37%	2.33%	62.55%
At December 31, 2001	\$5,793,250	5.90%	3.95%	1.95%	24 months	11.49%	3.87%	78.29%
At December 31, 2000	\$1,454,356	7.61%	5.76%	1.85%	15 months	11.47%	7.24%	73.90%
At September 30, 2004	\$12,645,118	4.12%	2.34%	1.78%	25 months	10.12%	3.06%	70.67%
At June 30, 2004	\$11,806,171	3.95%	2.19%	1.76%	29 months	10.07%	2.73%	69.80%
At March 31, 2004	\$13,059,967	3.90%	2.20%	1.70%	30 months	9.77%	2.91%	73.94%

FIXED-RATE INVESTMENT SECURITY CHARACTERISTICS

(dollars in thousands)	Principal Amount	Weighted Average Coupon Rate	Weighted Average Asset Yield	Principal Amount at Period End as % of Total Investment Securities
At December 31, 2004	\$5,579,030	5.24%	3.89%	29.17%
At December 31, 2003	\$3,387,196	5.77%	4.29%	26.71%
At December 31, 2002	\$4,195,322	6.76%	4.78%	37.45%
At December 31, 2001	\$1,606,691	6.92%	6.33%	21.71%
At December 31, 2000	\$513,611	6.62%	6.68%	26.10%
At September 30, 2004	\$5,248,784	5.19%	4.08%	29.33%
At June 30, 2004	\$5,108,464	5.15%	3.77%	30.20%
At March 31, 2004	\$4,602,629	5.53%	3.41%	26.06%

At December 31, 2004 and 2003, we held Investment Securities with coupons linked to various indices. The following tables detail the portfolio characteristics by index.

ADJUSTABLE-RATE INVESTMENT SECURITIES BY INDEX—DECEMBER 31, 2004

	One-Month LIBOR	Six-Month LIBOR	Twelve-Month LIBOR	Six-Month Auction Average	Twelve-Month Moving Average	11th District Cost of Funds	National Financial Average Mortgage Rate	Six-Month CD Rate	1-Year Treasury Index	2-Year Treasury Index	3-Year Treasury Index	5-Year Treasury Index	Monthly Federal Cost of Funds Index
Weighted Average Term to Next Adjustment	1 mo.	27 mo.	34 mo.	2 mo.	1 mo.	0 mo.	5 mo.	3 mo.	25 mo.	10 mo.	17 mo.	31 mo.	0 mo.
Weighted Average Annual Period Cap	8.01%	1.07%	2.18%	1.00%	0.17%	0.82%	2.00%	1.00%	1.86%	2.00%	2.00%	2.00%	2.00%
Weighted Average Lifetime Cap at December 31, 2004	8.88%	9.86%	10.08%	13.03%	10.65%	12.13%	10.58%	11.66%	10.31%	11.92%	12.96%	12.59%	13.39%
Investment Principal Value as Percentage of Investment Securities at December 31, 2004	8.67%	2.50%	22.96%	0.01%	0.22%	0.98%	0.01%	0.05%	34.31%	0.01%	0.25%	0.07%	0.79%

ADJUSTABLE-RATE INVESTMENT SECURITIES BY INDEX—DECEMBER 31, 2003

	One-Month LIBOR	Six-Month LIBOR	Twelve-Month LIBOR	Six-Month Auction Average	Twelve-Month Moving Average	11th District Cost of Funds	National Financial Average Mortgage Rate	Six-Month CD Rate	1-Year Treasury Index	2-Year Treasury Index	3-Year Treasury Index	5-Year Treasury Index	Monthly Federal Cost of Funds Index
Weighted Average Term to Next Adjustment	1mo.	25 mo.	34 mo.	2 mo.	1 mo.	1 mo.	175 mo.	2 mo.	23 mo.	15 mo.	16 mo.	26 mo.	1 mo.
Weighted Average Annual Period Cap	None	2.14%	2.09%	1.00%	0.14%	None	2.00%	1.00%	1.88%	2.00%	2.00%	2.00%	None
Weighted Average Lifetime Cap at December 31, 2003	8.88%	9.88%	10.12%	13.04%	10.70%	12.42%	6.76%	11.62%	10.05%	11.92%	12.89%	12.63%	13.40%
Investment Principal Value as Percentage of Investment Securities at December 31, 2003	17.26%	1.73%	12.00%	0.01%	0.53%	2.13%	2.21%	0.09%	35.10%	0.01%	0.44%	0.17%	1.61%

Borrowings

To date, our debt has consisted entirely of borrowings collateralized by a pledge of our Investment Securities. These borrowings appear on our balance sheet as repurchase agreements. At December 31, 2004, we had established uncommitted borrowing facilities in this market with 32 lenders in amounts which we believe are in excess of our needs. All of our Investment Securities are currently accepted as collateral for these borrowings. However, we limit our borrowings, and thus our potential asset growth, in order to maintain unused borrowing capacity and thus increase the liquidity and strength of our balance sheet.

For the year ended December 31, 2004, the term to maturity of our borrowings ranged from one day to three years, with a weighted average original term to maturity of 211 days at December 31, 2004. For the year ended December 31, 2003, the term to maturity of our borrowings ranged from one day to three years, with a weighted average original term to maturity of 203 days at December 31, 2003. For the year ended December 31, 2002, the term to maturity of our borrowings ranged from one day to three years, with a weighted average original term to maturity of 166 days at December 31, 2002.

At December 31, 2004, the weighted average cost of funds for all of our borrowings was 2.46% and the weighted average term to next rate adjustment was 111 days. At December 31, 2003, the weighted average cost of funds for all of our borrowings was 1.51% and the weighted average term to next rate adjustment was 90 days. At December 31, 2002, the weighted average cost of funds for all of our borrowings was 1.72% and the weighted average term to next rate adjustment was 124 days.

Liquidity

Liquidity, which is our ability to turn non-cash assets into cash, allows us to purchase additional investment securities and to pledge additional assets to secure existing borrowings should the value of our pledged assets decline. Potential immediate sources of liquidity for us include cash balances and unused borrowing capacity. Unused borrowing capacity will vary over time as the market value of our investment securities varies. Our balance sheet also generates liquidity on an on-going basis through mortgage principal repayments and net earnings held prior to payment as dividends. Should our needs ever exceed these on-going sources of liquidity plus the immediate sources of liquidity discussed above, we believe that in most circumstances our investment securities could be sold to raise cash. The maintenance of liquidity is one of the goals of our capital investment policy. Under this policy, we limit asset growth in order to preserve unused borrowing capacity for liquidity management purposes.

Borrowings under our repurchase agreements increased by \$5.7 million to \$16.7 billion at December 31, 2004, from \$11.0 billion at December 31, 2003. This increase in leverage was facilitated by the increase in our equity capital as a result of the issuance of common stock primarily through public offerings during 2004.

We anticipate that, upon repayment of each borrowing under a repurchase agreement, we will use the collateral immediately for borrowing under a new repurchase agreement. We have not at the present time entered into any commitment agreements under which the lender would be required to enter into new repurchase agreements during a specified period of time, nor do we presently plan to have liquidity facilities with commercial banks.

Under our repurchase agreements, we may be required to pledge additional assets to our repurchase agreement counterparties (i.e., lenders) in the event the estimated fair value of the existing pledged collateral under such agreements declines and such lenders demand additional collateral (a "margin call"), which may take the form of additional securities or cash. Specifically, margin calls result from a decline in the value of the Mortgage-Backed Securities securing our repurchase agreements, prepayments on the mortgages securing such Mortgage-Backed Securities and to changes in the estimated fair value of such Mortgage-Backed Securities generally due to principal reduction of such

Mortgage-Backed Securities from scheduled amortization and resulting from changes in market interest rates and other market factors. Through December 31, 2004, we did not have any margin calls on our repurchase agreements that we were not able to satisfy with either cash or additional pledged collateral. However, should prepayment speeds on the mortgages underlying our Mortgage-Backed Securities and/or market interest rates suddenly increase, margin calls on our repurchase agreements could result, causing an adverse change in our liquidity position.

The following table summarizes the effect on our liquidity and cash flows from contractual obligations for repurchase agreements and the non-cancelable office lease at December 31, 2004.

(dollars in thousands)	Within One Year	One to Three Years	Three to Five Years	More than Five Years	Total
Repurchase Agreements	\$14,957,879	\$1,750,000	—	—	\$16,707,879
Long-term operating lease obligations	500	1,062	1,064	—	2,626
Employment contracts	8,432	—	—	—	8,432
Total	\$14,966,811	\$1,751,062	\$1,064	—	\$16,718,937

Stockholders' Equity

During the year ended December 31, 2004, we declared dividends to common shareholders totaling \$237.9 million or \$1.98 per share, of which \$60.6 million was paid on January 27, 2005. During the year ended December 31, 2004, we declared and paid dividends to preferred shareholders totaling \$7.7 million or \$1.45 per share. On January 21, 2004, the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$363.6 million in an offering of 20,700,000 shares of common stock. On March 31, 2004, the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$102.9 million through an offering of 4,250,000 shares of 7.875% Series A Cumulative Redeemable Preferred Stock, which settled on April 5, 2004. On October 14, 2004, the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$74.5 million through an offering of 3,162,500 shares of 7.875% Series A Cumulative Redeemable Preferred Stock, which settled on October 19, 2004.

During the year ended December 31, 2004, 2,103,525 shares of the Company's common stock were issued through the Equity Shelf Program, totaling net proceeds of \$37.5 million. During the year ended December 31, 2004, options were exercised under the long-term compensation plan at \$856,000. Also, 127,020 common shares were sold through the dividend reinvestment and direct purchase program for \$2.3 million during the year ended December 31, 2004.

The FIDAC acquisition was completed on June 4, 2004. We issued 2,201,080 common shares to the shareholders of FIDAC, based on the December 31,

2003 closing price of \$18.40. We continue to operate as a self-managed and self-advised real estate investment trust, with FIDAC operating as our wholly-owned taxable REIT subsidiary.

FIDAC's shareholders may also receive additional shares of our common stock as an earn-out in 2005 and 2006 worth up to \$49,500,000 if FIDAC meets specific performance goals under the merger agreement. We cannot calculate how many shares we will issue under the earn-out provisions since that will vary depending upon whether and the extent to which FIDAC achieves specific performance goals. Even if FIDAC achieves specific performance goals for a fiscal year, the number of additional shares to be issued to the FIDAC shareholders will vary depending on our average share price for the first 20 trading days of the following fiscal year.

With our "available-for-sale" accounting treatment, unrealized fluctuations in market values of assets do not impact our GAAP or taxable income but rather are reflected on our balance sheet by changing the carrying value of the asset and stockholders' equity under "Accumulated Other Comprehensive Income (Loss)." By accounting for our assets in this manner, we hope to provide useful information to stockholders and creditors and to preserve flexibility to sell assets in the future without having to change accounting methods.

As a result of this mark-to-market accounting treatment, our book value and book value per share are likely to fluctuate far more than if we used historical amortized cost accounting. As a result, comparisons with companies that use historical cost accounting for some or all of their balance sheet may not be meaningful.

The table below shows unrealized gains and losses on the Investment Securities in our portfolio.

UNREALIZED GAINS AND LOSSES

(dollars in thousands)	2004	2003	2002	2001	2000
Unrealized Gain	\$23,021	\$24,886	\$90,507	\$53,935	\$3,020
Unrealized Loss	(143,821)	(72,147)	(14,996)	(15,766)	(16,064)
Net Unrealized Gain (Loss)	(\$120,800)	(\$47,261)	\$75,511	\$38,169	(\$13,044)
Net Unrealized Gain (Loss) as % of Investment Securities Principal Amount	(0.63%)	(0.37%)	0.67%	0.52%	(0.66%)
Net Unrealized Gain (Loss) as % of Investment Securities Amortized Cost	(0.62%)	(0.37%)	0.67%	0.51%	(0.66%)

Unrealized changes in the estimated net market value of Investment Securities have one direct effect on our potential earnings and dividends: positive mark-to-market changes increase our equity base and allow us to increase our borrowing capacity while negative changes tend to limit borrowing capacity under our capital investment policy. A very large negative change in the net market value of our Investment Securities might impair our liquidity position, requiring us to sell assets with the likely result of realized losses upon sale. The net unrealized gains (loss) on available for sale securities was (\$120.8) million, or (0.62%) of the amortized cost of our Investment Securities as of December 31, 2004, (\$47.3) million, or (0.37%) of the amortized cost of our Investment Securities as of December 31, 2003 and \$75.5 million, or 0.67% of the amortized cost of our Investment Securities as of December 31, 2002. Mortgage-Backed Securities with a carrying value of \$2.2 billion were in a continuous unrealized loss position over 12 months at December 31, 2004 in the amount of \$34.1 million. Mortgage-Backed Securities with a carrying value of \$13.1 billion were in a continuous unrealized loss position for less than 12 months at December 31, 2004 in the amount of \$105.3 million. Mortgage-Backed Securities with a carrying value of \$809.0 million were in a continuous unrealized loss position over 12 months at December 31, 2003 in the amount of \$8.2 million. Mortgage-Backed Securities with a carrying value of \$6.7 billion were in a continuous unrealized loss position

for less than 12 months at December 31, 2003 in the amount of \$52.2 million. The agency debentures with a carrying value of \$390.5 million were in a continuous unrealized loss position over 12 months at December 31, 2004 in the amount of \$4.5 million. The debentures with a carrying value of \$978.2 million were in a continuous unrealized loss position for less than 12 months at December 31, 2003 in the amount of \$11.8 million. The Company's agency debentures are adjustable rate and fixed rate with a weighted average lifetime cap of 3.71% at December 31, 2004 and 5.80% at December 31, 2003. The reason for the decline in value of these securities is solely due to increases in interest rates. All of the Mortgage-Backed Securities are "AAA" rated or carry an implied "AAA" rating. These investments are not considered other-than-temporarily impaired since the Company has the ability and intent to hold the investments for a period of time, to maturity, if necessary, sufficient for a forecasted market price recovery up to or beyond the cost of the investments. Also, the Company is guaranteed payment on the par value of the securities.

Issuances of common stock, the level of earnings as compared to dividends declared, and other factors influence our historical cost equity capital base. The reported equity capital base is influenced by these factors plus changes in the "Net Unrealized Gains (Losses) on Assets Available for Sale" account.

The table below shows our equity capital base as reported and on a historical amortized cost basis at December 31, 2004, 2003, 2002, 2001, and 2000, and September 30, 2004, June 30, 2004 and March 31, 2004.

STOCKHOLDERS' EQUITY

(dollars in thousands, except per share data)	7.875% Series A Cumulative Redeemable Preferred stock: 7,412,500 shares	Historical Amortized Cost Equity Base	Net Unrealized Gains (Losses) on Assets Available for Sale	Reported Equity Base (Book Value)	Historical Amortized Cost Equity Per Share	Reported Equity (Book Value) Per Share
At December 31, 2004	\$177,077	\$1,821,270	(\$120,800)	\$1,700,470	\$13.56	\$12.56
At December 31, 2003	-	\$1,196,481	(\$47,261)	\$1,149,220	\$12.45	\$11.96
At December 31, 2002	-	\$1,004,555	\$75,511	\$1,080,066	\$11.88	\$12.77
At December 31, 2001	-	\$629,188	\$38,169	\$667,357	\$10.52	\$11.15
At December 31, 2000	-	\$148,686	(\$13,044)	\$135,642	\$10.24	\$9.34
At September 30, 2004	\$102,708	\$1,648,869	(\$91,987)	\$1,556,882	\$13.60	\$12.84
At June 30, 2004	\$102,708	\$1,627,292	(\$177,489)	\$1,449,803	\$13.54	\$12.07
At March 31, 2004	\$102,870	\$1,581,218	\$4,500	\$1,585,718	\$13.42	\$13.45

Leverage

Our debt-to-equity ratio at December 31, 2004, 2003, and 2002 was 9.8:1, 9.6:1, and 9.4:1, respectively. We generally expect to maintain a ratio of debt-to-equity of between 8:1 and 12:1, although the ratio may vary from this range from time to time based upon various factors, including our management's opinion of the level of risk of our assets and liabilities, our liquidity position, our level of unused borrowing capacity and over-collateralization levels required by lenders when we pledge assets to secure borrowings.

Our target debt-to-equity ratio is determined under our capital investment policy. Should our actual debt-to-equity ratio increase above the target level due to asset acquisition or market value fluctuations in assets, we will cease to acquire new assets. Our management will, at that time, present a plan to our board of directors to bring us back to our target debt-to-equity ratio; in many circumstances, this would be accomplished over time by the monthly reduction of the balance of our Mortgage-Backed Securities through principal repayments.

Asset/Liability Management and Effect of Changes in Interest Rates

We continually review our asset/liability management strategy with respect to interest rate risk, mortgage prepayment risk, credit risk and the related issues of capital adequacy and liquidity. Our goal is to provide attractive risk-adjusted stockholder returns while maintaining what we believe is a strong balance sheet.

We seek to manage the extent to which our net income changes as a function of changes in interest rates by matching adjustable-rate assets with variable-rate borrowings. In addition, although we have not done so to date, we may seek to mitigate the potential impact on net income of periodic and lifetime coupon adjustment restrictions in our portfolio of Investment Securities by entering into interest rate agreements such as interest rate caps and interest rate swaps.

Changes in interest rates may also affect the rate of mortgage principal prepayments and, as a result, prepayments on mortgage-backed securities. We will seek to mitigate the effect of changes in the mortgage principal repayment rate by balancing assets we purchase at a premium with assets we purchase at a discount. To date, the aggregate premium exceeds the aggregate discount on our Mortgage-Backed Securities. As a result, prepayments, which result in the expensing of unamortized premium, will reduce our net income compared to what net income would be absent such prepayments.

Off-Balance Sheet Arrangements

We do not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Further, we have not guaranteed any obligations of unconsolidated entities nor do we have any commitment or intent to provide

additional funding to any such entities. As such, we are not materially exposed to any market, credit, liquidity or financing risk that could arise if we had engaged in such relationships.

Inflation

Virtually all of our assets and liabilities are financial in nature. As a result, interest rates and other factors drive our performance far more than does inflation. Changes in interest rates do not necessarily correlate with inflation rates or changes in inflation rates. Our financial statements are prepared in accordance with GAAP and our dividends based upon our net income as calculated for tax purposes; in each case, our activities and balance sheet are measured with reference to historical cost or fair market value without considering inflation.

Other Matters

We calculate that our qualified REIT assets, as defined in the Internal Revenue Code, are 100% of our total assets at December 31, 2004 and 2003 as compared to the Internal Revenue Code requirement that at least 75% of our total assets be qualified REIT assets. We also calculate that 93.3% and 93.7%, respectively, of our revenue qualifies for the 75% source of income test, and 100% of our revenue qualifies for the 95% source of income test, under the REIT rules for the years ended December 31, 2004 and 2003. We also met all REIT requirements regarding the ownership of our common stock and the distribution of our net income. Therefore, as of December 31, 2004 and 2003, we believe that we qualified as a REIT under the Internal Revenue Code.

We at all times intend to conduct our business so as not to become regulated as an investment company under the Investment Company Act of 1940, as amended (the "Investment Company Act"). If we were to become regulated as an investment company, then our use of leverage would be substantially reduced. The Investment Company Act exempts entities that are "primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate" (qualifying interests). Under current interpretation of the staff of the SEC, in order to qualify for this exemption, we must maintain at least 55% of our assets directly in qualifying interests. In addition, unless certain mortgage securities represent all the certificates issued with respect to an underlying pool of mortgages, the mortgage-backed securities may be treated as securities separate from the underlying mortgage loans and, thus, may not be considered qualifying interests for purposes of the 55% requirement. We calculate that as of December 31, 2004 and 2003, we were in compliance with this requirement.

Other Information

The Company has included as exhibits to its annual report on Form 10-K for fiscal year ended 2004 certificates of the Company's Chief Executive Officer and Chief Financial Officer certifying the quality of the Company's public disclosure controls, and the Company has submitted to the New York Stock Exchange a certificate of the Company's Chief Executive Officer certifying that he is not aware of any violation by the Company of New York Stock Exchange corporate governance listing standards.

MANAGEMENT REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Dated: March 7, 2005

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

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. As a result, even systems determined to be effective can provide only reasonable assurance regarding the preparation and presentation of financial statements. Moreover, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2004. In making this assessment, the Company's management used criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on its assessment, the Company's management believes that, as of December 31, 2004, the Company's internal control over financial reporting was effective based on those criteria.

**TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF
ANNALY MORTGAGE MANAGEMENT, INC.**

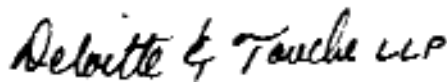
We have audited the accompanying statements of financial condition of Annaly Mortgage Management, Inc. (the "Company") as of December 31, 2004 and 2003, and the related statements of operations and comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2004. We also have audited management's assessment, included in the Management Report On Internal Control Over Financial Reporting included on page 19 of this Annual Report, that the Company maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on these financial statements, an opinion on management's assessment, and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Furthermore, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.



New York, New York
March 7, 2005

STATEMENTS OF FINANCIAL CONDITION
DECEMBER 31, 2004 AND 2003
ASSETS

(dollars in thousands, except for share data)	December 31, 2004 (Consolidated)	December 31, 2003
Cash and cash equivalents	\$5,853	\$247
Mortgage-Backed Securities, at fair value	19,038,386	11,956,512
Agency debentures, at fair value	390,509	978,167
Receivable for Mortgage-Backed Securities sold	1,025	—
Accrued interest receivable	81,557	53,743
Receivable for advisory and service fees	2,359	—
Intangible for customer relationships	15,613	—
Goodwill	23,122	—
Other assets	1,875	1,617
Total assets	\$19,560,299	\$12,990,286

LIABILITIES AND STOCKHOLDERS' EQUITY**Liabilities:**

Repurchase agreements	\$16,707,879	\$11,012,903
Payable for Mortgage-Backed Securities purchased	1,044,683	761,115
Accrued interest payable	35,721	14,989
Dividends payable	60,632	45,155
Other liabilities	2,819	4,017
Accounts payable	8,095	2,887
Total liabilities	17,859,829	11,841,066

Stockholders' Equity:

7.875% Series A Cumulative Redeemable Preferred Stock: 8,000,000 authorized 7,412,500 shares issued and outstanding	177,077	—
Common stock: par value \$.01 per share; 500,000,000 authorized, 121,263,000 and 96,074,096 shares issued and outstanding, respectively	1,213	961
Additional paid-in capital	1,638,635	1,194,159
Accumulated other comprehensive loss	(120,800)	(47,261)
Retained earnings	4,345	1,361
Total stockholders' equity	1,700,470	1,149,220
Total liabilities and stockholders' equity	\$19,560,299	\$12,990,286

See notes to financial statements.

STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
Years Ended December 31, 2004, 2003 and 2002

(dollars in thousands, except per share amounts)	For the Year Ended December 31, 2004 (Consolidated)	For the Year Ended December 31, 2003	For the Year Ended December 31, 2002
Interest income	\$532,328	\$337,433	\$404,165
Interest expense	270,116	182,004	191,758
Net interest income	262,212	155,429	212,407
Other income:			
Investment advisory and service fees	12,512	—	—
Gain on sale of mortgage-backed securities	5,215	40,907	21,063
Total other income	17,727	40,907	21,063
Expenses:			
Distribution fees	2,860	—	—
General and administrative expenses	24,029	16,233	13,963
Total expenses	26,889	16,233	13,963
Income before income taxes	253,050	180,103	219,507
Income taxes	4,458	—	—
Net income	248,592	180,103	219,507
Dividend on preferred stock	7,745	—	—
Net income available to common shareholders	\$240,847	\$180,103	\$219,507
Net income per share available to common shareholders:			
Basic	\$2.04	\$1.95	\$2.68
Diluted	\$2.03	\$1.94	\$2.67
Weighted average number of common shares outstanding:			
Basic	118,223,330	92,215,352	82,044,141
Diluted	118,459,145	93,031,253	82,282,883
Net income	\$248,592	\$180,103	\$219,507
Comprehensive income (loss):			
Unrealized gain (loss) on available—for sale securities	(68,324)	(81,865)	58,405
Less: reclassification adjustment for net gains (losses) included in net income	(5,215)	(40,907)	(21,063)
Other comprehensive income (loss)	(73,539)	(122,772)	37,342
Comprehensive income	\$175,053	\$57,331	\$256,849

See notes to financial statements.

STATEMENTS OF STOCKHOLDER'S EQUITY
Years Ended December 31, 2004 (Consolidated), 2003 and 2002

(dollars in thousands, except per share data)	Preferred Stock	Common Stock Par Value	Additional Paid-In Capital	Other Accumulated Comprehensive Income (Loss)	Retained Earnings	Total
Balance, December 31, 2001		\$598	\$623,986	\$38,169	\$4,604	\$667,357
Net Income					219,507	
Other comprehensive income:						
Unrealized net gain on securities, net of reclassification adjustment				37,342		
Comprehensive income						256,849
Exercise of stock options		1	1,089			1,090
Shares exchanged upon exercise of stock options			(76)			(76)
Net proceeds from direct purchase and dividend reinvestment		2	3,007			3,009
Net proceeds from equity shelf program		15	28,088			28,103
Net proceeds from follow-on offering		230	347,106			347,336
Common dividends declared, \$2.67 per share					(223,602)	(223,602)
Balance, December 31, 2002		\$846	\$1,003,200	\$75,511	\$509	\$1,080,066
Net Income					180,103	
Other comprehensive loss:						
Unrealized net loss on securities, net of reclassification adjustment				(122,772)		
Comprehensive income						57,331
Exercise of stock options		1	913			914
Net proceeds from direct purchase and dividend reinvestment		2	4,199			4,201
Net proceeds from follow-on offering		93	151,222			151,315
Net proceeds from equity shelf program offering		19	34,625			34,644
Common dividends declared, \$1.95 per share					(179,251)	(179,251)
Balance, December 31, 2003		\$961	\$1,194,159	(\$47,261)	\$1,361	\$1,149,220
Net Income					248,592	
Other comprehensive loss:						
Unrealized net loss on securities, net of reclassification adjustment				(73,539)		
Comprehensive income						175,053
Exercise of stock options		1	855			856
Net proceeds from direct purchase and dividend reinvestment		1	2,285			2,286
Net proceeds from follow-on offering		207	363,385			363,592
Common shares issued in FIDAC transaction		22	40,478			40,500
Net proceeds from preferred offering	\$177,077					177,077
Net proceeds from equity shelf program		21	37,473			37,494
Preferred dividends declared, \$1.45 per share					(7,745)	(7,745)
Common dividends declared, \$1.98 per share					(237,863)	(237,863)
Balance, December 31, 2004	\$177,077	\$1,213	\$1,638,635	(\$120,800)	\$4,345	\$1,700,470

See notes to financial statements.

STATEMENTS OF CASH FLOWS
Years Ended December 31, 2004, 2003 and 2002

(dollars in thousands)	For the Year Ended December 31, 2004 (Consolidated)	For the Year Ended December 31, 2003	For the Year Ended December 31, 2002
Cash flows from operating activities:			
Net income	\$248,592	\$180,103	\$219,507
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization of premiums and discounts, net	179,602	216,570	106,198
Amortization of intangibles	130	—	—
Gain on sale of Mortgage-Backed Securities	(5,215)	(40,907)	(21,063)
Stock option expense	317	121	240
Market value adjustment on long-term repurchase agreement	(1,133)	1,607	1,204
Decrease (increase) in accrued interest receivable, net of interest purchased on securities	(27,964)	(2,833)	(2,903)
Decrease (increase) in other assets	(1,749)	(776)	(641)
Decrease (increase) in advisory and service fees receivable	(795)	—	—
Increase (decrease) in accrued interest payable	20,732	55	(1,109)
Increase in accounts payable	4,400	979	673
Net cash provided by operating activities	416,917	354,919	302,106
Cash flows from investing activities:			
Purchase of Mortgage-Backed Securities	(14,147,323)	(11,404,133)	(11,079,561)
Purchase of Agency debentures	(250,000)	(1,735,940)	—
Proceeds from sale of Mortgage-Backed Securities	596,962	2,899,267	2,076,800
Proceeds from called agency debentures	845,000	746,000	—
Principal payments of Mortgage-Backed Securities	6,495,911	8,290,724	4,728,666
Cash from FIDAC acquisition	2,526	—	—
Net cash used in investing activities	(6,456,924)	(1,204,082)	(4,274,095)
Cash flows from financing activities:			
Net proceeds from repurchase agreements	152,739,827	117,066,588	87,463,924
Principal payments on repurchase agreements	(147,045,071)	(116,217,261)	(83,668,862)
Proceeds from exercise of stock options	539	792	774
Proceeds from direct purchase and dividend reinvestment	2,286	4,201	3,010
Net proceeds from follow-on offerings	363,592	151,315	347,336
Proceeds from preferred offering	177,077	—	—
Net proceeds from equity shelf program	37,494	34,644	28,103
Dividends paid	(230,131)	(191,595)	(201,999)
Net cash provided by financing activities	6,045,613	848,684	3,972,286
Net increase (decrease) in cash and cash equivalents	5,606	(479)	297
Cash and cash equivalents, beginning of year	247	726	429
Cash and cash equivalents, end of year	\$5,853	\$247	\$726
Supplemental disclosure of cash flow information: Interest paid	\$249,384	\$181,949	\$190,650
Noncash financing activities:			
Net change in unrealized loss on available-for-sale securities net of reclassification adjustment	(\$73,539)	(\$122,772)	\$37,342
Dividends declared, not yet paid	\$60,632	\$45,155	\$57,499
Noncash investing and financing activities:			
Noncash acquisition of FIDAC	\$40,500		

See notes to financial statements.

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Annaly Mortgage Management, Inc. (the "Company") was incorporated in Maryland on November 25, 1996. The Company commenced its operations of purchasing and managing an investment portfolio of mortgage-backed securities on February 18, 1997, upon receipt of the net proceeds from the private placement of equity capital. An initial public offering was completed on October 14, 1997. The Company acquired Fixed Income Discount Advisory Company ("FIDAC") on June 4, 2004 (See Note 2). FIDAC is a registered investment advisor and is a taxable REIT subsidiary of the Company.

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

Basis of Presentation – The consolidated financial statements as of and for the year ended December 31, 2004 include the accounts of the Company and FIDAC. All material intercompany balances have been eliminated. Certain reclassifications have been made to prior year financial statements, where appropriate, to conform to the current year presentation.

Cash and Cash Equivalents – Cash and cash equivalents include cash on hand and money market funds.

Mortgage-Backed Securities and Agency Debentures – The Company invests primarily in mortgage pass-through certificates, collateralized mortgage obligations and other mortgage-backed securities representing interests in or obligations backed by pools of mortgage loans (collectively, "Mortgage-Backed Securities"). The Company also invests in Federal Home Loan Bank ("FHLB"), Federal Home Loan Mortgage Corporation ("FHLMC"), and Federal National Mortgage Association ("FNMA") debentures. The Mortgage-Backed Securities and agency debentures are collectively referred to herein as "Investment Securities."

Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities," requires the Company to classify its Investment Securities as either trading investments, available-for-sale investments or held-to-maturity investments. Although the Company generally intends to hold most of its Investment Securities until maturity, it may, from time to time, sell any of its Investment Securities as part of its overall management of its portfolio. Accordingly, SFAS No. 115 requires the Company to classify all of its Investment Securities as available-for-sale. All assets classified as available-for-sale are reported at estimated fair value, based on market prices provided by certain dealers who make markets in these financial instruments, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Unrealized losses on Investment Securities 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 Investment Securities is adjusted. There were no such adjustments for the year ended December 31, 2004, 2003, or 2002.

SFAS No. 107, *Disclosure About Fair Value of Financial Instruments*, requires disclosure of the fair value of financial instruments for which it is practicable to estimate that value. The fair value of mortgage-backed securities and agency debentures available-for-sale and futures contracts is equal to their carrying value presented in the balance sheet. The fair value of cash and cash equivalents, accrued interest receivable, receivable for mortgage-backed securities sold, receivable for advisory fees, repurchase agreements, and payable for mortgage-backed securities purchased, dividends payable, accounts payable, and accrued interest payable, generally approximates cost as of December 31, 2004, due to the short-term nature of these securities.

Interest income is accrued based on the outstanding principal amount of the Investment Securities and their contractual terms. Premiums and discounts associated with the purchase of the Investment Securities are amortized or accreted into interest income over the projected lives of the securities using the interest method. The Company's policy for estimating prepayment speeds for calculating the effective yield is to evaluate historical performance, street consensus prepayment speeds, and current market conditions.

Investment Securities transactions are recorded on the trade date. Purchases of newly issued securities are recorded when all significant uncertainties regarding the characteristics of the securities are removed, generally shortly before settlement date. Realized gains and losses on sale of Investment Securities are determined on the specific identification basis.

Credit Risk – At December 31, 2004 and December 31, 2003, the Company has limited its exposure to credit losses on its portfolio of Investment Securities by only purchasing securities issued by FHLMC, FNMA, Government National Mortgage Association ("GNMA"), or FHLB. The payment of principal and interest on the FHLMC and FNMA Mortgage-Backed Securities are guaranteed by those respective agencies and the payment of principal and interest on the GNMA Mortgage-Backed Securities is backed by the full-faith-and-credit of the U.S. government. At December 31, 2004 and December 31, 2003 all of the Company's Investment Securities have an actual or implied "AAA" rating.

Repurchase Agreements – The Company finances the acquisition of its Investment Securities through the use of repurchase agreements. Repurchase agreements are treated as collateralized financing transactions and are carried at their contractual amounts, including accrued interest, as specified in the respective agreements. Accrued interest payable is recorded as a separate line item on the statement of financial condition.

Income Taxes – The Company has elected to be taxed as a Real Estate Investment Trust ("REIT") and intends to comply with the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), with respect thereto. Accordingly, the Company will not be subjected to federal income tax to the extent of its distributions to shareholders and as long as certain asset, income and stock ownership tests are met. The Company and FIDAC have made a joint election to treat FIDAC as a taxable REIT subsidiary. As such, FIDAC will be taxable as a domestic C corporation and subject to federal and state and local income taxes based upon its taxable income.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Intangible assets – The Company's acquisition of FIDAC is accounted for using the purchase method. Under the purchase method, net assets and results of operations of acquired companies are included in the consolidated financial statements from the date of acquisition. In addition, the cost of FIDAC must be allocated to the assets acquired, including identifiable intangible assets, and the liabilities assumed based on their estimated fair values at the date of acquisition. The excess of cost over the fair value of the net assets acquired is recognized as goodwill.

Recent Accounting Pronouncements – In March 2004, the Emerging Issues Task Force, or EITF, reached a consensus on Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments. This Issue provides clarification with respect to the meaning of other-than-temporary impairment and its application to investments classified as either available-for-sale or held-to-maturity under SFAS No. 115, and investments accounted for under the cost method or the equity method. Certain provisions of this Issue have been deferred to a later date. This Issue is not expected to have a significant impact on the Company's financial statements when adopted.

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123, (Revised 2004) – Share-Based Payment (“SFAS No. 123R”). SFAS 123R, which replaces SFAS No. 123, requires the Company to measure and recognize in the financial statements the compensation cost relating to share-based payment transactions. The compensation cost should be reassured based on the fair value of the equity instruments issued. SFAS No. 123R is effective as of the first interim or annual reporting period that begins after June 15, 2005. The adoption of SFAS No. 123R is not expected to have a significant impact on the Company's financial statements when adopted as of July 1, 2005.

2. FIXED INCOME DISCOUNT ADVISORY COMPANY

On December 31, 2003, the Company entered into a merger agreement with FIDAC. At the annual meeting of the Company's shareholders held on May 27, 2004, shareholders voted to approve the merger. The merger closed before the opening of business on June 4, 2004. The merger was accounted for using the purchase method of accounting in accordance with SFAS No. 141. Accordingly, the consolidated balance sheet as of December 31, 2004 includes the effects of the merger and the Company's application of the purchase method of accounting. Additionally, the consolidated statements of operations and of cash flows for the respective periods ended December 31, 2004 include the results of the Company and FIDAC for the period from June 4, 2004 to December 31, 2004.

Upon completion of the merger and pursuant to the merger agreement, FDC Merger Sub, (“Merger Sub”), the Company's wholly owned subsidiary created solely for the purpose of effectuating the merger, merged with and into FIDAC. As a result of the merger, Merger Sub ceased to exist, and FIDAC is the surviving corporation and operates as the Company's wholly owned taxable REIT subsidiary. At the time of the merger, each FIDAC shareholder received approximately 2,935 shares of the Company's common stock for each share of FIDAC stock the shareholder owned and has the right to receive additional shares of the Company's common stock in the future, based on FIDAC achieving specific performance goals. FIDAC's shareholders may also receive additional shares of our common stock as an earn-out in 2005 and 2006 worth up to \$49,500,000 if FIDAC meets specific performance goals under the merger agreement. We cannot calculate how many shares we will issue under the earn-out provisions since that will vary depending upon whether and the extent to which FIDAC achieves specific performance goals. Even if FIDAC achieves specific performance goals for a fiscal year, the number of additional shares to be issued to the FIDAC shareholders will vary depending on our average share price for the first 20 trading days of the following fiscal year.

The value of the shares of the Company's common stock issued to the FIDAC shareholders immediately upon the consummation of the acquisition was fixed at \$40,500,000 based upon the closing price of the Company's common stock on December 31, 2003, and was paid on June 4, 2004 by delivering 2,201,080 shares of the Company's common stock.

The total amount of goodwill represents the purchase price in excess of the fair value of the net assets acquired. Under SFAS No. 142, “Goodwill and Other Intangible Assets,” goodwill is not amortized, but tested at least annually for impairment. Customer relationships are deemed by the Company to have an indefinite life based on a lack of attrition history and management's expectation of continued service to FIDAC clients and, accordingly, are not being amortized. Instead, they are required to be tested at least annually for impairment. FIDAC trademark and non-compete agreements are considered intangible assets subject to amortization over their estimated life of three years and one year, respectively. For the year ended December 31, 2004, amortization expense related to these intangibles was \$130,000. A deferred tax liability of \$104,000 arising from the temporary difference between the book and tax basis relating to these amortizable intangible is included in “Other liabilities” in the Statement of Financial Condition as of December 31, 2004.

A summary of the fair values of the net assets acquired is as follows:

	(dollars in thousands)
Cash and cash equivalents	\$2,526
Receivable for advisory fees and services	1,564
Other assets	591
Customer relationships	15,613
FIDAC trademark	250
Non-compete agreements	140
Goodwill	22,905
Accounts payable	(748)
Total fair value of net assets, including acquisition cost	\$42,841

3. MORTGAGE-BACKED SECURITIES

The following tables pertain to the Company's Mortgage-Backed Securities classified as available-for-sale as of December 31, 2004 and 2003, which are carried at their fair value:

(dollars in thousands)	Federal Home Loan Mortgage Corporation	Federal National Mortgage Association	Government National Mortgage Association	Total Mortgage-Backed Securities
DECEMBER 31, 2004				
Mortgage-Backed Securities, gross	\$6,063,131	\$12,061,462	\$604,310	\$18,728,903
Unamortized discount	(171)	(843)	(109)	(1,123)
Unamortized premium	130,211	288,217	8,528	426,956
Amortized cost	6,193,171	12,348,836	612,729	19,154,736
Gross unrealized gains	11,534	9,905	1,582	23,021
Gross unrealized losses	(39,429)	(97,890)	(2,052)	(139,371)
Estimated fair value	\$6,165,276	\$12,260,851	\$612,259	\$19,038,386
(dollars in thousands)				
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
Adjustable rate	\$13,833,122	\$20,713	(\$93,796)	\$13,760,039
Fixed rate	5,321,614	2,308	(45,575)	5,278,347
Total	\$19,154,736	\$23,021	(\$139,371)	\$19,038,386

(dollars in thousands)	Federal Home Loan Mortgage Corporation	Federal National Mortgage Association	Government National Mortgage Association	Total Mortgage-Backed Securities
DECEMBER 31, 2003				
Mortgage-Backed Securities, gross	\$3,763,364	\$7,509,544	\$419,223	\$11,692,130
Unamortized discount	(198)	(1,034)	(209)	(1,441)
Unamortized premium	87,726	206,580	7,005	301,311
Amortized cost	3,850,892	7,715,090	426,019	11,992,000
Gross unrealized gains	8,301	16,133	452	24,886
Gross unrealized losses	(18,114)	(39,984)	(2,277)	(60,374)
Estimated fair value	\$3,841,079	\$7,691,239	\$424,194	\$11,956,512
(dollars in thousands)				
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
Adjustable rate	\$8,565,873	\$13,118	(\$35,490)	\$8,543,501
Fixed rate	3,426,127	11,768	(24,884)	3,413,011
Total	\$11,992,000	\$24,886	(\$60,374)	\$11,956,512

Actual maturities of mortgage-backed securities are generally shorter than stated contractual maturities. Actual maturities of the Company's mortgage-backed securities are affected by the contractual lives of the underlying mortgages, periodic payments of principal, and prepayments of principal.

The following table summarizes the Company's mortgage-backed securities on December 31, 2004 and 2003 according to their estimated weighted-average life classifications:

(dollars in thousands)	December 31, 2004 Fair Value	December 31, 2003 Amortized Cost	Fair Value	Amortized Cost
Weighted-Average Life				
Less than one year	\$357,135	\$359,433	\$743,137	\$744,571
Greater than one year and less than five years	14,623,143	14,705,212	8,240,101	8,254,989
Greater than or equal to five years	4,058,108	4,090,091	2,973,274	2,992,440
Total	\$19,038,386	\$19,154,736	\$11,956,512	\$11,992,000

The weighted-average lives of the mortgage-backed securities at December 31, 2004 and 2003 in the table above are based upon data provided through subscription-based financial information services, assuming constant principal prepayment rates to the reset date of each security. The prepayment model considers current yield, forward yield, steepness of the yield curve, current mortgage rates, mortgage rate of the outstanding loans, loan age, margin and volatility.

Mortgage-Backed Securities with a carrying value of \$2.2 billion were in a continuous unrealized loss position over 12 months at December 31, 2004 in the amount of \$34.1 million. Mortgage-Backed Securities with a carrying value of \$13.1 billion were in a continuous unrealized loss position for less than 12 months at December 31, 2004 in the amount of \$105.3 million. Mortgage-Backed Securities with a carrying value of \$809.0 million were in a continuous unrealized loss position over 12 months at December 31, 2003 in the amount of \$8.2 million. Mortgage-Backed Securities with a

carrying value of \$6.7 billion were in a continuous unrealized loss position for less than 12 months at December 31, 2003 in the amount of \$52.2 million. The reason for the decline in value of these securities is solely due to increases in interest rates. All of the Mortgage-Backed Securities are "AAA" rated or carry an implied "AAA" rating. These investments are not considered other-than-temporarily impaired since the Company has the ability and intent to hold the investments for a period of time, to maturity, if necessary, sufficient for a forecasted market price recovery up to or beyond the cost of the investments. Also, the Company is guaranteed payment on the par value of the securities.

4. AGENCY DEBENTURES

At December 31, 2004, the Company owned callable agency debentures totaling \$395.0 million par value and a total unamortized discount of \$40,000. FHLMC, FNMA, and FHLB are the issuers of the debentures. All of the Company's agency debentures are classified as available-for-sale. All agency debentures had carrying values of \$390.5 million and \$978.2 million at December 31, 2004 and December 31, 2003, respectively. The agency debentures with a carrying value of \$390.5 million were in a continuous unrealized loss position over 12 months at December 31, 2004 in the amount of \$4.5 million. All debentures with a carrying value of \$978.2 million were in a continuous unrealized loss position for less than 12 months at December 31, 2003 in the amount of \$11.8 million. The Company's agency debentures are adjustable rate and fixed rate with a weighted average lifetime cap of 3.71% at December 31, 2004 and 5.80% at December 31, 2003. All of the agency debentures carry an implied "AAA" rating. These investments are not considered other-than-temporarily impaired since the Company has the ability and intent to hold the investments for a period of time, to maturity, if necessary, sufficient for a forecasted market price recovery up to or beyond the cost of the investments. Also, the Company is guaranteed payment on the par value of the agency debentures.

5. REPURCHASE AGREEMENTS

The Company had outstanding \$16.7 billion and \$11.0 billion of repurchase agreements with weighted average borrowing rates of 2.46% and 1.51%, and weighted average remaining maturities of 111 days and 90 days as of December 31, 2004 and December 31, 2003, respectively. Investment Securities pledged as collateral under these repurchase agreements had an estimated fair value of \$17.4 billion at December 31, 2004.

At December 31, 2004 and December 31, 2003, the repurchase agreements had the following remaining maturities:

(dollars in thousands)	December 31, 2004	December 31, 2003
Within 30 days	\$13,059,810	\$8,589,184
30 to 59 days	1,598,069	709,552
60 to 89 days	—	—
90 to 119 days	—	—
Over 120 days	2,050,000	1,714,167
Total	\$16,707,879	\$11,012,903

6. OTHER LIABILITIES

In 2001, the Company entered into a repurchase agreement maturing in July 2004, at which time the repurchase agreement gave the buyer the right to extend, in whole or in part, in three-month increments up to July 2006. In October 2004, the buyer extended the repurchase agreement, in whole, for the next three months, with the right to further extend in January, 2005, which the buyer did extend. The repurchase agreement has a principal amount of \$100,000,000, included in repurchase agreements on the statement of financial condition. The Company accounts for the extension option as a separate interest rate floor liability carried at fair value. The initial fair value of \$1.2 million allocated to the extension option resulted in a similar discount on the repurchase agreement borrowings that is being amortized over the initial term of three years using the effective yield method. At December 31, 2004 and December 31, 2003, the fair value of this interest rate floor was \$2.7 million and \$4.0 million, respectively, and is included in other liabilities in the Statement of Financial Condition.

7. PREFERRED STOCK AND COMMON STOCK

During the year ended December 31, 2004, the Company declared dividends to common shareholders totaling \$237.9 million or \$1.98 per share, of which \$60.6 million were paid on January 27, 2005. During the year ended December 31, 2004, the Company declared and paid dividends to preferred shareholders totaling \$7.7 million or \$1.45 per share. On January 21, 2004, the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$363.6 million in an offering of 20,700,000 shares of common stock. On March 31, 2004, the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$102.9 million through an offering of 4,250,000 shares of 7.875% Series A Cumulative Redeemable Preferred Stock, which settled on April 5, 2004. On October 14, 2004, the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$74.5 million through an offering of 3,162,500 shares of 7.875% Series A Cumulative Redeemable Preferred Stock, which settled on October 19, 2004. During the twelve months ended December 31, 2004, 2,103,525 shares of the Company's common stock were issued through the Equity Shelf Program, totaling net proceeds of \$37.5 million. During the year ended December 31, 2004, 57,000 options were exercised under the long-term compensation plan at \$856,000. Also, 127,020 common shares were sold through the dividend reinvestment and direct purchase program for \$2.3 million during the year ended December 31, 2004.

On April 1, 2003 the Company entered into an underwriting agreement pursuant to which the Company raised net proceeds of approximately \$151.3 million in equity in an offering of 9,300,700 shares of common stock. During the year ended December 31, 2003, 1,879,600 shares were issued through the Equity Shelf Program, totaling net proceeds of \$34.6 million. During the year ended December 31, 2003, 92,697 options were exercised under the long-term compensation plan at \$914,000. Also, 231,893 shares were purchased in the dividend reinvestment and direct purchase program at \$4.2 million.

During the year ended December 31, 2002, the Company completed an offering of common stock in the first quarter issuing 23,000,000 shares, with aggregate net proceeds of approximately \$347.3 million. Through the Equity Shelf Program, the Company raised \$28.1 million in net proceeds and issued 1,484,100 shares. During the year ended December 31, 2002, 97,095 options were exercised at \$1.1 million. Total shares exchanged upon exercise of the stock options were 4,444 at a value of \$76,000. Also, 165,480 shares were purchased in dividend reinvestment and share purchase plan, totaling \$3.0 million.

8. EARNINGS PER SHARE (EPS)

For the year ended December 31, 2004, the reconciliation is as follows:

(Amounts in thousands, except per share amounts)	Income (Numerator)	Weighted Average Shares (Denominator)	Per-Share Amount
Net income available to common shareholders	\$240,847		
Basic earnings per common share	\$240,847	118,223	\$2.04
Effect of dilutive securities: Dilutive stock options		236	
Diluted earnings per common share	\$240,847	118,459	\$2.03

Options to purchase 12,500 shares of common stock were outstanding and considered anti-dilutive as their exercise price exceeded the average stock price for the year ended December 31, 2004.

For the year ended December 31, 2003, the reconciliation is as follows:

(Amounts in thousands, except per share amounts)	Income (Numerator)	Weighted Average Shares (Denominator)	Per-Share Amount
Net income	\$180,103		
Basic earnings per share	\$180,103	92,215	\$1.95
Effect of dilutive securities: Dilutive stock options		816	
Diluted earnings per share	\$180,103	93,031	\$1.94

Options to purchase 12,500 shares of common stock were outstanding and considered anti-dilutive as their exercise price exceeded the average stock price for the year ended December 31, 2003.

For the year ended December 31, 2002, the reconciliation is as follows:

(Amounts in thousands, except per share amounts)	Income (Numerator)	Weighted Average Shares (Denominator)	Per-Share Amount
Net income	\$219,507		
Basic earnings per share	219,507	82,044	\$2.68
Effect of dilutive securities: Dilutive stock options		239	
Diluted earnings per share	\$219,507	82,283	\$2.67

Options to purchase 6,250 shares of common stock were outstanding and considered anti-dilutive as their exercise price exceeded the average stock price for the year ended December 31, 2002.

9. LONG-TERM STOCK INCENTIVE PLAN

The Company has adopted a long term stock incentive plan for executive officers, key employees and non employee directors (the "Incentive Plan"). The Incentive Plan authorizes the Compensation Committee of the board of directors to grant awards, including non-qualified options as well as incentive stock options as defined under Section 422 of the Code. The Incentive Plan authorizes the granting of options or other awards for an aggregate of the greater of 500,000 shares or 9.5% of the diluted outstanding shares of the Company's common stock.

The following table sets forth activity relating to the Company's stock options awards:

	2004		2003		2002	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Options outstanding at the beginning of period	1,063,259	\$14.28	512,706	\$8.59	635,826	\$8.48
Granted	639,750	17.39	643,450	18.00	6,250	20.35
Exercised	(57,288)	9.40	(92,697)	8.54	(97,095)	8.75
Expired	—	—	(200)	17.97	(32,275)	8.28
Options outstanding at the end of period	1,645,721	\$15.66	1,063,259	\$14.28	512,706	\$8.59

The following table summarizes information about stock options outstanding at December 31, 2004:

Range of Exercise Prices	Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)
\$7.94 – \$19.99	1,633,221	\$15.62	7.95
\$20.00 – \$29.99	12,500	20.53	2.98
	1,645,721	\$15.66	7.91

The Company accounts for the incentive plan under the intrinsic value method in accordance with APB Opinion No. 25, Accounting for Stock Issued to Employees, and related Interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation:

(dollars in thousands, except per share data)	For the year ended December 31, 2004	For the year ended December 31, 2003	For the year ended December 31, 2002
Net income available to common shareholders, as reported	\$240,847	\$180,103	\$219,507
Deduct: Total stock-based employee compensation expense determined under fair value based method	(149)	(48)	(33)
Pro-forma net income available to common shareholders	\$240,698	\$180,055	\$219,474
Net income per share available to common shareholders, as reported			
Basic	\$2.04	\$1.95	\$2.68
Diluted	\$2.03	\$1.94	\$2.67
Pro-forma net income per share available to common shareholders			
Basic	\$2.03	\$1.95	\$2.68
Diluted	\$2.03	\$1.94	\$2.67

10. INCOME TAXES

Annaly has elected to be taxed as a Real Estate Investment Trust status under the Internal Revenue Code. In connection with the Company's merger with FIDAC effective June 4, 2004, FIDAC elected taxable REIT subsidiary status under the Internal Revenue Code. As a REIT, the Company is not subject to Federal income tax on earnings distributed to its shareholders. Most states recognize REIT status as well. The Company has decided to distribute the majority of its income and retain a portion of the permanent difference between book and taxable income arising from Internal Revenue Code Section 162(m) pertaining to employee remuneration.

During the year ended December 31, 2004, the Company recorded \$4.5 million of income tax expense for income attributable to taxable REIT subsidiary and the portion of earnings retained based on Code Section 162(m) limitations. The Company's effective tax rate was 45% for the year ended December 31, 2004. Such rate differed from the federal statutory rate as a result of state and local taxes and permanent difference pertaining to employee remuneration as discussed above. During the years ended December 31, 2003 and 2002, 100% of the taxable income of the Company was distributed and as a result, the Company was not subject to income taxes.

11. LEASE COMMITMENTS

The Company has a noncancelable lease for office space, which commenced in May 2002 and expires in December 2009.

The Company's aggregate future minimum lease payments are as follows:

	Total per Year (dollars in thousands)
2005	500
2006	530
2007	532
2008	532
2009	532
Total remaining lease payments	\$2,626

12. INTEREST RATE RISK

The primary market risk to the Company is interest rate risk. Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond the Company's control. Changes in the general level of interest rates can affect net interest income, which is the difference between the interest income earned on interest-earning assets and the interest expense incurred in connection with the interest-bearing liabilities, by affecting the spread between the interest-earning assets and interest-bearing liabilities. Changes in the level of interest rates also can affect the value of the Investment Securities and the Company's ability to realize gains from the sale of these assets. A decline in the value of the Investment Securities pledged as collateral for borrowings under repurchase agreements could result in the counterparties demanding additional collateral pledges or liquidation of some of the existing collateral to reduce borrowing levels.

The Company seeks 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 borrowings. In addition, although the Company has not done so to date, the Company may seek to mitigate the potential impact on net income of periodic and lifetime coupon adjustment restrictions in the portfolio of Investment Securities by entering into interest rate agreements such as interest rate caps and interest rate swaps.

Changes in interest rates may also have an effect on the rate of mortgage principal prepayments and, as a result, prepayments on Mortgage-Backed Securities. The Company will seek to mitigate the effect of changes in the mortgage principal repayment rate by balancing assets purchased at a premium with assets purchased at a discount. To date, the aggregate premium exceeds the aggregate discount on the Mortgage-Backed Securities. As a result, prepayments, which result in the expensing of unamortized premium, will reduce net income compared to what net income would be absent such prepayments.

13. SUMMARIZED QUARTERLY RESULTS (Unaudited)

The following is a presentation of the quarterly results of operations for the year ended December 31, 2004.

(dollars in thousands, except per share data)	March 31, 2004	June 30, 2004	September 30, 2004	December 31, 2004
Interest income	\$114,341	\$122,234	\$138,970	\$156,783
Interest expense	50,303	55,648	70,173	93,992
Net interest income	64,038	66,586	68,797	62,791
Investment advisory and service fees	—	1,260	4,811	6,143
Gain on sale of Mortgage-Backed Securities	595	2,126	1,350	1,144
Distribution fees	—	(298)	(1,024)	(1,538)
General and administrative expenses	(5,790)	(5,643)	(6,159)	(6,862)
Income before income taxes	\$58,843	\$64,031	\$67,775	\$61,678
Income taxes	—	494	1,155	2,384
Net income	\$58,843	\$63,537	\$66,620	\$59,294
Dividends on preferred stock		1,998	2,082	3,665
Net income available to commons shareholders	\$58,843	\$61,837	\$64,538	\$55,629
Weighted average number of basic common shares outstanding	112,506,206	118,276,509	120,802,814	121,246,246
Weighted average number of diluted common shares outstanding	112,804,001	118,469,756	120,994,191	121,514,941
Net income per share available to common shareholders:				
Basic	\$0.52	\$0.52	\$0.53	\$0.46
Diluted	\$0.52	\$0.52	\$0.53	\$0.46

The following is a presentation of the quarterly results of operations for the year ended December 31, 2003.

(dollars in thousands, except per share data)	March 31, 2003	June 30, 2003	September 30, 2003	December 31, 2003
Interest income	\$87,500	\$93,892	\$66,855	\$89,186
Interest expense	44,048	51,770	43,922	42,264
Net interest income	43,452	42,122	22,933	46,922
Gain on sale of Mortgage-Backed Securities	11,020	20,231	9,656	—
General and administrative expenses	(3,697)	(4,201)	(4,110)	(4,225)
Net income	\$50,775	\$58,152	\$28,479	\$42,697
Weighted average number of basic common shares outstanding	84,606,786	93,384,128	94,685,685	96,027,468
Weighted average number of diluted common shares outstanding	84,837,390	93,588,024	95,500,486	96,232,899
Net income per share available to common shareholders:				
Basic	\$0.60	\$0.62	\$0.30	\$0.44
Diluted	\$0.60	\$0.62	\$0.30	\$0.44

The following is a presentation of the quarterly results of operations for the year ended December 31, 2002.

(dollars in thousands, except per share data)	March 31, 2002	June 30, 2002	September 30, 2002	December 31, 2002
Interest income from investment securities	\$92,900	\$109,423	\$109,201	\$92,641
Interest expense on repurchase agreements	40,012	47,860	54,012	49,874
Net interest income	52,888	61,563	55,189	42,767
Gain on sale of Mortgage-Backed Securities	3,410	1,343	4,747	11,563
General and administrative expenses	(3,255)	(3,536)	(3,268)	(3,904)
Net income	\$53,043	\$59,370	\$56,668	\$50,426
Weighted average number of basic common shares outstanding	76,709,836	82,910,206	83,668,422	84,525,171
Weighted average number of diluted common shares outstanding	77,017,431	83,186,865	83,939,870	84,766,747
Net income per share available to common shareholders:				
Basic	\$0.69	\$0.72	\$0.68	\$0.60
Diluted	\$0.69	\$0.71	\$0.68	\$0.60

The following table sets forth, for the periods indicated, the high, low, and closing sales prices per share of our common stock as reported on the New York Stock Exchange composite tape and the cash dividends declared per share of our common stock and our preferred stock.

STOCK PRICES	HIGH	LOW	CLOSE
First Quarter ended March 31, 2004	\$21.22	\$18.15	\$18.02
Second Quarter ended June 30, 2004	\$19.63	\$15.94	\$16.09
Third Quarter ended September 30, 2004	\$18.44	\$15.95	\$16.71
Fourth Quarter ended December 31, 2004	\$20.53	\$16.33	\$19.62
First Quarter ended March 31, 2003	\$19.55	\$16.54	\$17.47
Second Quarter ended June 30, 2003	\$20.80	\$17.43	\$19.91
Third Quarter ended September 30, 2003	\$21.10	\$16.13	\$16.42
Fourth Quarter ended December 31, 2003	\$19.00	\$15.65	\$18.40

COMMON DIVIDENDS DECLARED PER SHARE

First Quarter ended March 31, 2004	\$0.50
Second Quarter ended June 30, 2004	\$0.48
Third Quarter ended September 30, 2004	\$0.50
Fourth Quarter ended December 31, 2004	\$0.50
First Quarter ended March 31, 2003	\$0.60
Second Quarter ended June 30, 2003	\$0.60
Third Quarter ended September 30, 2003	\$0.28
Fourth Quarter ended December 31, 2003	\$0.47

We intend to pay quarterly dividends and to distribute to our stockholders all or substantially all of our taxable income in each year (subject to certain adjustments). This will enable us to qualify for the tax benefits accorded to a REIT under the Code. We have not established a minimum dividend payment level and our ability to pay dividends may be adversely affected for the reasons described under the caption "Risk Factors" in our 2004 Form 10-K. All distributions will be made at the discretion of our board of directors and will depend on our earnings, our financial condition, maintenance of our REIT status and such other factors as our board of directors may deem relevant from time to time.

CORPORATE OFFICERS**Michael A. J. Farrell**

*Chairman of the Board,
President &
Chief Executive Officer*

Wellington J. Denahan-Norris

*Vice Chairman &
Chief Investment Officer*

Kathryn F. Fagan

*Chief Financial Officer &
Treasurer*

Jennifer S. Karve

*Executive Vice President &
Portfolio Manager*

James P. Fortescue

Senior Vice President

Kristopher R. Konrad

Senior Vice President

Rose-Marie Lyght

Senior Vice President

Jeremy Diamond

Executive Vice President

Ronald D. Kazel

Executive Vice President

Nicholas Singh

*Executive Vice President,
General Counsel,
Secretary &
Chief Compliance Officer*

BOARD OF DIRECTORS**Michael A. J. Farrell**

*Chairman of the Board,
President &
Chief Executive Officer*

Wellington J. Denahan-Norris

*Vice Chairman &
Chief Investment Officer*

Kevin P. Brady

*Founder &
Chief Executive Officer
TaxStream*

Spencer I. Browne

*Principal
Strategic Asset
Management, LLC*

*Former President &
Chief Executive Officer
Asset Investors
Corporation*

Jonathan D. Green

*President &
Chief Executive Officer
Rockefeller Group
International, Inc.*

John A. Lambiase

*Former Managing Director
Salomon Brothers, Inc.*

E. Wayne Nordberg

*Senior Director
Ingalls & Synder, LLC*

Donnell A. Segalas

*Pinnacle Asset
Management, L.P.*

CORPORATE HEADQUARTERS**Annaly Mortgage Management, Inc.**

1211 Avenue of the Americas, Suite 2902
New York, New York 10036

LEGAL COUNSEL**McKee Nelson LLP**

1919 M. Street, NW
Suite 800
Washington, D.C. 20036

AUDITORS**Deloitte & Touche LLP**

Two World Financial Center
New York, New York 10281-1434

STOCK TRANSFER AGENT

Shareholder inquiries concerning dividend payments, lost certificates, change of address:

Mellon Investors Services, LLC

P.O. Box 3315
South Hackensack, New Jersey
07606-1163
www.mellon-investor.com

STOCK EXCHANGE LISTING

The common stock is listed on the New York Stock Exchange (symbol: NLY).

The preferred stock is listed on the New York Stock Exchange (symbol: NLY-A).

ANNUAL MEETING

The Annual Meeting of Stockholders will be held Thursday, May 26, 2005 at 9:30 am at:

New York Marriott Marquis

1535 Broadway
New York, New York 10036

SHAREHOLDER COMMUNICATIONS

Copies of the Company's Annual Report and 2004 Form 10-K may be obtained by writing the Secretary, by calling the investor relations hot line at 888-8ANNALY, or by visiting our website www.annaly.com.

ANNALY MORTGAGE MANAGEMENT, INC.

ANNUAL REPORT 2004

ANNALY MORTGAGE MANAGEMENT, INC.
1211 Avenue of the Americas, Suite 2902
New York, New York 10036

1.888.8ANNALY
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