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DYNEX CAPITAL INC
Form 10-Q/A
October 07, 2002

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q/A

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

FOR THE QUARTER ENDED MARCH 31, 2002

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

COMMISSION FILE NUMBER 1-9819

DYNEX CAPITAL, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

VIRGINIA
(State or other jurisdiction of
incorporation or organization)

52-1549373
(I.R.S. Employer
Identification No.)

4551 COX ROAD, SUITE 300, GLEN ALLEN, VIRGINIA
(Address of principal executive offices)

23060
(Zip Code)

(804) 217-5800
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety days.

YES NO

On April 30, 2002, the registrant had 10,873,853 shares of common stock of \$.01 value outstanding, which is the registrant's only class of common stock.

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DYNEX CAPITAL, INC.
FORM 10-Q

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THIS FILING OF FORM 10-Q/A REFLECTS RESTATEMENT OF THE FINANCIAL STATEMENTS AS DISCUSSED IN NOTE 12 TO THE CONSOLIDATED FINANCIAL STATEMENTS.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DYNEX CAPITAL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS, UNAUDITED

(amounts in thousands except share data)

	March 31, 2002	Decemb 2
	-----	-----
	(As restated, see Note 12)	
ASSETS		
Investments:		
Collateral for collateralized bonds	\$ 2,310,625	\$ 2,47
Other investments	61,780	6
Securities	6,190	
Loans	7,428	

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	-----	-----
	2,386,023	2,54
Cash	4,466	
Cash -- restricted	12,550	
Other assets	8,117	
	-----	-----
	\$ 2,411,156	\$ 2,56
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Non-recourse debt - collateralized bonds	\$ 2,118,044	\$ 2,26
Recourse debt	46,975	5
	-----	-----
	2,165,019	2,32
Accrued interest payable	771	
Accrued expenses and other liabilities	1,477	
	-----	-----
	2,167,267	2,32
	-----	-----
Commitments and contingencies (Note 10)	--	
SHAREHOLDERS' EQUITY		
Preferred stock, par value \$.01 per share, 50,000,000 shares authorized:		
9.75% Cumulative Convertible Series A,		
992,038 and 992,038 issued and outstanding, respectively		
(\$29,903 and \$29,322 aggregate liquidation preference, respectively)	22,658	2
9.55% Cumulative Convertible Series B,		
1,378,807 and 1,378,807 issued and outstanding, respectively		
(\$42,084 and \$41,443 aggregate liquidation preference, respectively)	32,275	3
9.73% Cumulative Convertible Series C,		
1,383,532 and 1,383,532 issued and outstanding, respectively		
(\$51,865 and \$51,101 aggregate liquidation preference, respectively)	39,655	3
Common stock, par value \$.01 per share,		
100,000,000 shares authorized,		
10,873,853 issued and outstanding	109	
Additional paid-in capital	364,740	36
Accumulated other comprehensive loss	(13,527)	(1
Accumulated deficit	(202,021)	(20
	-----	-----
	243,889	24
	-----	-----
	\$ 2,411,156	\$ 2,56
	=====	=====

See notes to unaudited condensed consolidated financial statements.

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DYNEX CAPITAL, INC.
CONDENSED CONSOLIDATED STATEMENTS
OF OPERATIONS, UNAUDITED
(amounts in thousands except share data)

Three Months Ended
March 31,

2002

2001

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	(As restated, see Note 12)	(As restated, see Note 12)
Interest income:		
Collateral for collateralized bonds	\$ 42,714	\$ 61,114
Securities	122	309
Other investments	10	1,928
Loans	94	153
	-----	-----
	42,940	63,504
	-----	-----
Interest and related expense:		
Non-recourse debt	31,966	50,125
Recourse debt	1,030	2,587
Other	444	363
	-----	-----
	33,440	53,075
	-----	-----
Net interest margin before provision for losses	9,500	10,429
Provision for losses	(5,643)	(4,806)
	-----	-----
Net interest margin	3,857	5,623
Net (loss) gain on sales, write-downs, impairment charges, and litigation	(2,055)	5,304
Other income	196	295
	-----	-----
	1,998	11,222
	-----	-----
General and administrative expenses	(1,894)	(1,844)
	-----	-----
Income before extraordinary item	104	9,378
Extraordinary item - gain on extinguishment of debt	377	2,271
	-----	-----
Net income	481	11,649
Preferred stock charges	(2,396)	(3,228)
	-----	-----
Net (loss) income applicable to common shareholders	\$ (1,915)	\$ 8,421
	=====	=====
(Loss) income per common share before extraordinary item:		
Basic and diluted	\$ (0.21)	\$ 0.54
	=====	=====
Net (loss) income per common share:		
Basic and diluted	\$ (0.18)	\$ 0.74
	=====	=====
Weighted average number of common shares outstanding		
Basic and diluted	10,873,853	11,446,200

See notes to unaudited condensed consolidated financial statements.

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DYNEX CAPITAL, INC.
 CONDENSED CONSOLIDATED STATEMENTS
 OF CASH FLOWS, UNAUDITED
 (amounts in thousands)

	Three Ma
	----- 2002 ----- (As restated, see Note 12) -----
Operating activities:	
Net income	\$ 481
Adjustments to reconcile net income to net cash provided (used) by operating activities:	
Provision for losses	5,643
Net (gain) loss on sales, write-downs, impairment charges and litigation	2,055
Extraordinary item - net gain on extinguishment of debt	(377)
Payment (made) received from litigation settlement, net of legal fees	(863)
Amortization and depreciation	4,181
Decrease in accrued interest receivable	2
Change in accrued interest payable	(519)
Net change in restricted cash	(8,216)
Net change in accrued interest, other assets and other liabilities	(2,839)

Net cash (used) provided by operating activities	(452)

Investing activities:	
Principal payments on collateral	151,283
Net (increase) decrease in funds held by trustee	(152)
Net decrease in loans held for sale or securitization	1,621
Purchase of other investments	(38)
Payments received on other investments	2,602
Proceeds from sales of other investments	-
Payments received on securities	393
Proceeds from sale of loan production operations	-
Capital expenditures	(2)

Net cash provided by investing activities	155,707

Financing activities:	
Principal payments on bonds	(147,090)
Repayment of senior notes	(10,828)

Net cash used for financing activities	(157,918)

Net (decrease) increase in cash	(2,663)
Cash at beginning of period	7,129

Cash at end of period	\$ 4,466
	=====
Cash paid for interest	\$ 34,968
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See notes to unaudited condensed consolidated financial statements.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS DYNEX CAPITAL, INC.

March 31, 2002

(amounts in thousands except share data)

NOTE 1--BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. The condensed consolidated financial statements include the accounts of Dynex Capital, Inc. and its qualified REIT subsidiaries and taxable REIT subsidiary ("Dynex" or the "Company"). All significant inter-company balances and transactions have been eliminated in consolidation of Dynex.

In the opinion of management, all material adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation of the condensed consolidated financial statements have been included. The Condensed Consolidated Balance Sheet at March 31, 2002, the Condensed Consolidated Statements of Operations for the three months ended March 31, 2002 and 2001, the Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2002 and 2001 and related notes to consolidated financial statements are unaudited. Operating results for the three months ended March 31, 2002 are not necessarily indicative of the results that may be expected for the year ending December 31, 2002. For further information, refer to the audited consolidated financial statements and footnotes included in the Company's Form 10-K/A for the year ended December 31, 2001.

Certain reclassifications have been made to the financial statements for 2001 to conform to presentation for 2002.

Cash - Restricted. At March 31, 2002 and December 31, 2001, respectively, \$12,550 and \$4,334 of cash was held in trust to cover losses on securities not otherwise covered by insurance or was held in trust as collateral for the payment of principal on the Senior Notes. As a result of an amendment to the indenture governing the Company's senior notes due July 2002 (the "Senior Notes") entered into in March 2001 and a settlement agreement entered into in October 2001 with ACA Financial Guaranty Corporation (ACA), the Company's ability to make distributions on its capital stock and to reinvest cash flow from its investment portfolio and other assets are materially restricted (the amendment to the indenture and the settlement agreement, collectively the "Senior Note Agreements"). Until the Senior Notes are defeased or fully repaid, the Senior Note Agreements effectively restrict the Company from making any new distributions on its capital stock, or from making any new investments, except to call securities previously issued by the Company. In addition, as a result of the Senior Note Agreements, the Company has pledged substantially all its assets (including the stock of its material subsidiaries) to the indenture trustee and deposits cash in excess of a working capital balance of \$3,000 into a restricted account.

NOTE 2 - USE OF ESTIMATES

Fair Value. The Company uses estimates in establishing fair value for its financial instruments. Estimates of fair value for financial instruments may be

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based on market prices provided by certain dealers. Estimates of fair value for certain other financial instruments are determined by calculating the present value of the projected cash flows of the instruments using appropriate discount rates, prepayment rates and credit loss assumptions. Collateral for collateralized bonds make up a significant portion of the Company's investments. The estimate of fair value for collateral for collateralized bonds is determined by calculating the present value of the projected cash flows of the instruments, using discount rates, prepayment rate assumptions and credit loss assumptions established by management. The discount rate used in the determination of fair value of the collateral for collateralized bonds was 16% at March 31, 2002 and December 31, 2001. Prepayment rate assumptions at March 31, 2002, and December

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31, 2001, were generally at a "constant prepayment rate," or CPR ranging from 35%-60% for both 2002 and 2001, respectively, for collateral for collateralized bonds consisting of single-family mortgage loans and securities, and a CPR equivalent ranging from 9%-10% for both 2002 and 2001, respectively for collateral for collateralized bonds consisting of manufactured housing loans and securities collateral. Commercial mortgage loan collateral was generally assumed to repay in accordance with their contractual terms. CPR assumptions for each year are based in part on the actual prepayment rates experienced for the prior six-month period and in part on management's estimate of future prepayment activity. The loss assumptions utilized vary for each series of collateral for collateralized bonds, depending on the collateral pledged. The cash flows for the collateral for collateralized bonds were projected to the estimated date that the security could be called and retired by the Company if there is economic value to the Company in calling and retiring the security. Such call date is typically triggered on the earlier of a specified date or when the remaining collateral balance equals 35% of the original balance (the "Call Date"). The Company estimates anticipated market prices of the underlying collateral at the Call Date.

As discussed in Note 6, the Company estimated the fair value of certain other investments as the present value of expected future cash flows, less costs to service such investments, discounted at a rate of 12%.

Estimates of fair value for other financial instruments are based primarily on management's judgment. Since the fair value of Dynex's financial instruments is based on estimates, actual gains and losses recognized may differ from those estimates recorded in the consolidated financial statements.

NOTE 3--NET INCOME PER COMMON SHARE

Net income per common share is presented on both a basic net income per common share and diluted net income per common share basis. Diluted net income per common share assumes the conversion of the convertible preferred stock into common stock, using the if-converted method, and stock appreciation rights to the extent that there are rights outstanding, using the treasury stock method, but only if these items are dilutive. As a result of the two-for-one split in May 1997 and the one-for-four reverse split in July 2000 of Dynex's common stock, the preferred stock is convertible into one share of common stock for two shares of preferred stock.

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The following table reconciles the numerator and denominator for both the basic and diluted net income per common share for the three months ended March 31, 2002 and 2001.

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	Three Months Ended March 31		
	2002		
	Income (loss)	Weighted-Average Number of Shares	Income (loss)
Income before extraordinary item	\$ 104		\$ 9,
Extraordinary item - net gain on extinguishment of debt	377		2,
Net income	481		11,
Preferred stock charges	(2,396)		(3,
Net (loss) income applicable to common shareholders	\$ (1,915)	10,873,853	\$ 8,
Effect of dividends and additional shares of Series A, Series B, and Series C preferred stock	-	-	
Diluted	\$ (1,915)	10,873,853	\$ 8,
(Loss) income per share before extraordinary item:			
Basic EPS		\$ (0.21)	
Diluted EPS		\$ (0.21)	
Net (loss) income per share:			
Basic EPS		\$ (0.18)	
Diluted EPS		\$ (0.18)	
Dividends and potentially dilutive common shares assuming conversion of preferred stock:			
Series A	\$ 580	496,019	\$ 1,
Series B	806	689,404	1,
Series C	1,010	691,766	1,
	\$ 2,396	1,877,189	\$ 3,

NOTE 4 -- COLLATERAL FOR COLLATERALIZED BONDS

The following table summarizes the components of collateral for collateralized

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bonds as of March 31, 2002 and December 31, 2001:

	March 31, 2002	December 31, 2001
Loans, at amortized cost	\$ 1,913,182	\$ 2,027,619
Debt securities, at fair value	419,892	467,038
	2,333,074	2,494,657
Reserve for loan losses	(22,449)	(21,454)
	\$ 2,310,625	\$ 2,473,203

The following table summarizes the amortized cost basis, gross unrealized gains and losses and estimated fair value of debt securities pledged as collateral for collateralized bonds as of March 31, 2002 and December 31, 2001 :

	March 31, 2002	December 31, 2001
Debt securities, at amortized cost	\$ 416,794	\$ 463,666
Gross unrealized gains	3,098	3,372
Gross unrealized losses	-	-
Estimated fair value	\$ 419,892	\$ 467,038

The components of collateral for collateralized bonds at March 31, 2002 and December 31, 2001 are as follows:

	March 31, 2002	December 31, 2001
Collateral, net of allowance	\$ 2,271,229	\$ 2,429,968
Funds held by trustees	542	391
Accrued interest receivable	15,294	16,594
Unamortized premiums and discounts, net	20,462	22,878
Unrealized gain, net	3,098	3,372
	\$ 2,310,625	\$ 2,473,203

Collateral for collateralized bonds. Collateral for collateralized bonds consists primarily of loans and securities backed by adjustable-rate and fixed-rate mortgage loans secured by first liens on single family housing, fixed-rate loans on multifamily and commercial properties and manufactured housing installment loans secured by either a UCC filing or a motor vehicle title. All collateral for collateralized bonds is pledged to secure repayment of the related collateralized bonds. All principal and interest (less servicing-related fees) on the collateral is remitted to a trustee and is available for payment on the collateralized bonds.

NOTE 5 -- SECURITIES

The following table summarizes Dynex's amortized cost basis and fair value of

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investments classified as available-for-sale, as of March 31, 2002 and December 31, 2001:

	March 31, 2002	December 31, 2001
Securities:		
Adjustable-rate mortgage securities	\$ 600	\$ 600
Fixed-rate mortgage securities	575	351
Derivative and residual securities	4,688	4,358
	5,863	5,309
Allowance for losses	(55)	(55)
	5,808	5,254
Amortized cost, net	2,273	2,134
Gross unrealized gains	(1,891)	(1,880)
Gross unrealized losses	\$ 6,190	\$ 5,508

Securities. Adjustable-rate mortgage ("ARM") securities consist of mortgage certificates secured by ARM loans. Fixed-rate mortgage securities consist of mortgage certificates secured by mortgage loans that have a fixed rate of interest for at least one year from the balance sheet date. Derivative securities are classes of collateralized bonds, mortgage pass-through certificates or mortgage certificates that pay to the holder substantially all interest (i.e., an interest-only security), or substantially all principal (i.e., a principal-only security). Residual interests represent the right to receive the excess of (i) the cash flow from the collateral pledged to secure related mortgage-backed securities, together with any reinvestment income thereon, over (ii) the amount required for principal and interest payments on the mortgage-backed securities or repurchase arrangements, together with any related administrative expenses.

NOTE 6 -- OTHER INVESTMENTS

The following table summarizes the Company's investment in delinquent property tax receivables and real estate owned as of March 31, 2002 and December 31, 2001:

	March 31, 2002	December 31, 2001
Amortized cost basis of receivables, before discount	\$ 72,465	\$ 75,800
Discount recorded as adjustment to other comprehensive loss	(17,007)	(18,450)
Amortized cost basis of receivables, net	55,458	57,350
Real estate owned	6,091	5,920
Other	231	270
	\$ 61,780	\$ 63,540

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Other investments at March 31, 2002 and December 31, 2001 consist primarily of delinquent property tax receivables and related real estate owned. Delinquent property tax receivables have been classified as non-accrual, and all cash collections on such receivables is used to amortize the principal balance of the Company's investment. During the three months ended March 31, 2002, the Company collected \$4.0 million. The Company also amortized \$1.4 million of discount on the carrying value of the delinquent property tax receivables as a reduction to accumulated other comprehensive loss.

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NOTE 7 -- RECOURSE DEBT

The following table summarizes Dynex's recourse debt outstanding at March 31, 2002 and December 31, 2001:

	March 31, 2002	December 31, 2001
7.875% Senior Notes	\$ 46,830	\$ 57,969
Capital lease obligations	178	244
Capital costs	(33)	(79)
	\$ 46,975	\$ 58,134

As of March 31, 2002 and December 31, 2001, Dynex had \$46,830 and \$57,969, respectively, outstanding of its Senior Notes. On March 30, 2001, the Company entered into an amendment to the related indenture governing the Senior Notes whereby the Company pledged to the Trustee of the Senior Notes substantially all of the Company's unencumbered assets in its investment portfolio and the stock of its subsidiaries. In consideration of this pledge, the indenture was further amended to provide for the release of the Company from certain covenant restrictions in the indenture, and specifically provided for the Company's ability to make distributions on its capital stock in an amount not to exceed the sum of (i) \$26,000, (ii) the cash proceeds of any "permitted subordinated indebtedness", (iii) the cash proceeds of the issuance of any "qualified capital stock", and (iv) any distributions required in order for the Company to maintain its REIT status. In addition, the Company entered into a Purchase Agreement with holders of 50.1% of the Senior Notes which requires the Company to purchase, and such holders to sell, their respective Senior Notes at various discounts prior to maturity based on a computation of the Company's available cash. During the quarter ended March 31, 2002, the Company completed the purchase of all amounts required pursuant to the Purchase Agreement and fulfilled all its obligations thereunder. In addition, the Company has purchased Senior Notes in the open market from time-to-time. In April 2002, the Company purchased an additional \$550 of Senior Notes, and as of April 30, 2002, the remaining principal amount of the Senior Notes outstanding is \$46,280.

NOTE 8 -- RECENT ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 addresses the initial recognition and measurement of intangible assets acquired outside of a business combination and the accounting for goodwill and other intangible assets subsequent to their acquisition. SFAS No. 142 provides that intangible assets with finite useful lives be amortized and that goodwill and intangible assets with indefinite lives will not be

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amortized, but will rather be tested at least annually for impairment. As the Company has no goodwill or intangible assets that it is amortizing, the adoption of SFAS No. 142 did not have any effect on the financial position, results of operations or cash flows of the Company.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. SFAS No. 143 is effective for fiscal years beginning after June 15, 2002. The Company does not believe the adoption of SFAS No. 143 will have a significant impact on the financial position, results of operations or cash flows of the Company.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets" which supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of" and the accounting and reporting provisions of Accounting Principles Board (APB) Opinion No. 30, "Reporting the Results of Operations - Reporting and Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions (APB 30)" for the disposal of a segment of business. This statement is effective for fiscal years beginning after December 15, 2001. SFAS No. 144 retains many of the provisions of SFAS No. 121, but

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addresses certain implementation issues associated with that Statement. The adoption of SFAS No. 144 did not have a significant impact on the financial position, results of operations or cash flows of the Company.

In April 2002, the FASB issued SFAS No. 145, "Recission of FASB Statements No. 4, 44 and 64, Amendment of SFAS No. 13 and Technical Corrections". Effective January 1, 2003, SFAS No. 145 requires gains and losses from the extinguishment or repurchase of debt to be classified as extraordinary items only if they meet the criteria for such classification in APB 30. Until January 1, 2003, gains and losses from the extinguishment or repurchase of debt must be classified as extraordinary items, as Dynex has done. After January 1, 2003, any gain or loss resulting from the extinguishment or repurchase of debt classified as an extraordinary item in a prior period that does not meet the criteria for such classification under APB Opinion 30 must be reclassified. The Company is in the process of evaluating SFAS No. 145 but believes it will not have a significant impact on the financial position, results of operations or cash flows of the Company.

NOTE 9 -- PREFERRED STOCK

As of March 31, 2002 and December 31, 2001, the total liquidation preference on the Preferred Stock was \$123,852 and \$121,867, respectively, and the total amount of dividends in arrears on Preferred Stock were \$25,167 and \$22,771, respectively. Individually, the amount of dividends in arrears on the Series A, the Series B and the Series C were \$6,094 (\$6.14 per Series A share), \$8,469 (\$6.14 per Series B share) and \$10,604 (\$7.66 per Series C share), respectively at March 31, 2002 and \$5,513 (\$5.56 per Series A share), \$7,663 (\$5.56 per Series B share) and \$9,595 (\$6.94 per Series C share), respectively at December 31, 2001.

NOTE 10 -- COMMITMENTS AND CONTINGENCIES

GLS Capital, Inc. ("GLS"), a subsidiary of the Company, together with the County of Allegheny, Pennsylvania ("Allegheny County"), were defendants in a lawsuit in

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the Commonwealth Court of Pennsylvania (the "Commonwealth Court") wherein the plaintiffs challenged the right of Allegheny County and GLS to collect certain interest, costs and expenses related to delinquent property tax receivables in Allegheny County. This lawsuit was related to the purchase by GLS of delinquent property tax receivables from Allegheny County in 1997, 1998, and 1999 for approximately \$58,258. On July 5, 2001, the Commonwealth Court ruling addressed, among other things, (i) the right of the Company to charge to the delinquent taxpayer a rate of interest of 12% versus 10% on the collection of its delinquent property tax receivables, (ii) the charging of attorney's fees to the delinquent taxpayer for the collection of such tax receivables, and (iii) the charging to the delinquent taxpayer of certain other fees and costs. The Commonwealth Court remanded for further consideration to the Court of Common Pleas items (i) and (iii), and ruled that neither Allegheny County nor GLS had the right to charge attorney's fees to the delinquent taxpayer related to the collection of such tax receivables, reversing the Court of Common Pleas decision. The Pennsylvania Supreme Court has accepted the Application for Extraordinary Jurisdiction filed by Allegheny County and GLS. No damages have been claimed in the action; however, the decision may impact the ultimate amount recoverable on the delinquent property tax receivables, including attorney fees incurred in the collection process. To date, GLS has incurred attorneys fees of approximately \$2,000 related to foreclosures on such delinquent property tax receivables, approximately \$1,000 of which have been reimbursed to GLS by the taxpayer or through liquidation of the underlying real property.

The Company is also subject to other lawsuits or claims which have arisen in the ordinary course of its business, some of which seek damages in amounts which could be material to the financial statements. Although no assurance can be given with respect to the ultimate outcome of any such litigation or claim, the

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Company believes the resolution of such lawsuits or claims will not have a material effect on the Company's consolidated balance sheet, but could materially affect consolidated results of operations in a given year.

NOTE 11 -- RELATED PARTY TRANSACTIONS

The Company has made a loan to Thomas H. Potts, president of the Company, as evidenced by a demand promissory note (the "Potts Note"). Mr. Potts directly owns 399,502 shares of common stock of the Company, all of which have been pledged as collateral to secure the Potts Note. Interest is charged on the Potts Note at the applicable short-term monthly applicable federal rate (commonly known as the AFR Rate) as published by the Internal Revenue Service. As of March 31, 2002 and December 31, 2001, the outstanding balance of the Potts Note was \$262 and \$369, respectively, and interest was current.

NOTE 12 - RESTATEMENT OF FINANCIAL STATEMENTS

Subsequent to the issuance of its financial statements for the quarter ended March 31, 2002, the Company determined that certain of the assets previously reported as debt securities subject to the requirements of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities" were, in fact, collateralized borrowings, where the collateral being pledged as securities were loans that should have been accounted for under the requirements of SFAS No. 5, "Accounting for Contingencies" or SFAS No. 114, "Accounting by Creditors for Impairment of a Loan." As a result, the accompanying condensed consolidated financial statements as of March 31, 2002, and for the three month periods ended March 31, 2002 and 2001, have been restated from the amounts previously reported to correct the accounting for these investments.

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A summary of the significant effects of the restatement is as follows:

(amounts in thousands)	As of March 31, 2002	
	(As Previously Reported)	(As Restated)
Collateral for collateralized bonds	\$ 2,248,716	\$ 2,310,625
Total investments	2,324,114	2,386,023
Total assets	2,349,247	2,411,156
Accumulated other comprehensive loss	(75,437)	(13,527)
Total Shareholders' Equity	181,980	243,889

	For the Three Months Ended March 31, 2002		2001	
	(As Previously Reported)	(As Restated)	(As Previously Reported)	(As Restated)
Provision for losses	\$ (7,604)	\$ (5,643)	\$ (6,589)	\$ (4,806)
Net interest margin	1,895	3,857	3,837	5,623
Impairment charges	(94)	(2,055)	7,087	5,304

The restatement did not have any effect on income before extraordinary items or net income.

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

As discussed in Note 12 to the condensed consolidated financial statements included in Item 1, the Company has restated its financial statements for the three month periods ended March 31, 2002 and 2001. The following management discussion and analysis takes into account the effects of the restatement.

The Company is a financial services company, which invests in a portfolio of securities and investments backed principally by single family mortgage loans, commercial mortgage loans, manufactured housing installment loans and delinquent property tax receivables. These loans were funded primarily by the Company's loan production operations or purchased in bulk in the market. Historically, the Company's loan production operations have included single-family mortgage lending, which was sold in 1996, commercial mortgage lending and manufactured housing lending. Through its specialty finance business, the Company also has provided for the purchase and leaseback of single family model homes to builders and the purchase and management of delinquent property tax receivables. Loans funded through the Company's production operations have generally been pooled and pledged (i.e. securitized) as collateral for non-recourse bonds ("collateralized bonds"), which provided long-term financing for such loans while limiting credit, interest rate and liquidity risk. The Company has elected to be treated as a real estate investment trust ("REIT") for federal income tax purposes under the Internal Revenue Code of 1986, as amended, and, as such, must distribute substantially all of its taxable income to shareholders. Provided that the Company meets all of the prescribed Internal Revenue Code requirements

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for a REIT, the Company will generally not be subject to federal income tax.

The Company owns the right to call adjustable-rate and fixed-rate mortgage pass-through securities previously issued and sold by the Company once the outstanding balance of such securities reaches a call trigger, generally either 10% or less of the original amount issued or a specified date. At March 31, 2002, the aggregate callable balance of such securities at the time of the projected call is approximately \$228 million, relating to 20 securities. The Company may or may not elect to call one or more of these securities when eligible to call. During the first four months of 2002, the Company initiated the call of twelve securities with a balance of \$143 million. All securities acquired pursuant to such calls were included in a securitization completed by the Company in April 2002. The Company may call additional securities in the future.

On April 25, 2002, the Company completed the issuance of \$605 million of collateralized bonds. These bonds were collateralized by single-family loans aggregating \$602 million, \$447 million of which were loans already owned by the Company and \$155 million of which represented new loans from the purchase of mortgage backed securities from third parties pursuant to certain call rights owned by the Company. The transaction will be accounted for as a financing; thus the loans and associated bonds will be included in the Company's second quarter 2002 consolidated balance sheet as assets and liabilities of the Company. Cash proceeds from the securitization, net of related costs, was approximately \$22 million. The Company will use the proceeds from the securitization toward repayment of the Senior Notes due July 15, 2002. Approximately \$11 million of foreclosure loans and real estate owned were not included in the transaction and will be retained by the Company.

Separately, the Company announced that the financial advisor it engaged to assist in evaluating the feasibility of the Company forming or acquiring a depository institution has recommended that the Company pursue the acquisition of an existing thrift institution. The financial advisor recommended initially targeting a thrift institution with assets of \$200 million to \$300 million located in Virginia or neighboring areas. The advisor recommended that the Company would then acquire similar-sized institutions over the next three to five years in order to reach \$1 billion in assets over that time frame. As a result of this recommendation, the Company plans to continue its evaluation of a depository institution business plan. While the Company plans to continue its evaluation, there are no definitive plans at this time for the Company to acquire a thrift.

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FINANCIAL CONDITION (amounts in thousands)

	March 31, 2002	December 31, 2001
Investments:		
Collateral for collateralized bonds	\$ 2,310,625	\$ 2,473,203
Securities	6,190	5,508
Other investments	61,780	63,553
Loans	7,428	7,315
Non-recourse debt - collateralized bonds	2,118,044	2,264,213
Recourse debt	46,975	58,134
Shareholders' equity	243,889	242,110

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COLLATERAL FOR COLLATERALIZED BONDS

Collateral for collateralized bonds consists primarily of loans and securities backed by adjustable-rate and fixed-rate mortgage loans secured by first liens on single family housing, fixed-rate loans secured by first liens on multifamily and commercial properties, and manufactured housing installment loans secured by either a UCC filing or a motor vehicle title. As of March 31, 2002, the Company had 23 series of collateralized bonds outstanding. The collateral for collateralized bonds decreased to \$2.31 billion at March 31, 2002 compared to \$2.47 billion at December 31, 2001. This decrease of \$0.16 billion is primarily the result of \$151.3 million in paydowns on the collateral.

Below is a summary as of March 31, 2002, by each series where the fair value exceeds \$0.5 million of the Company's net investment in collateralized bond securities. The Company master services the majority of its collateralized bond securities. Monthly payment reports for those securities master-serviced by the Company may be found on the Company's website at www.dynexcapital.com.

(amounts in thousands)

Collateralized Bond Series (1)	Collateral Type	Principal balance of collateral pledged	Principal balance of collateralized bonds outstanding to third parties	Principal Balance Net Investment
MERIT Series 11A	Single-family loans; manufactured housing loans	\$ 409,988	\$ 363,042	\$ 46,9
MERIT Series 12-1	Manufactured housing loans	276,742	247,535	29,2
MERIT Series 12-2	Single-family loans	331,540	311,178	20,3
MERIT Series 13	Manufactured housing loans	335,463	293,202	42,2
MERIT Series 14-1	Single-family loans	136,855	135,936	9
MERIT Series 14-2	Single-family loans	2,643	-	2,6
MCA One Series 1	Commercial mortgage loans	86,187	81,444	4,7
CCA One Series 2	Commercial mortgage loans	298,791	276,688	22,1
CCA One Series 3	Commercial mortgage loans	413,399	368,111	45,2
		\$ 2,291,608	\$ 2,077,136	\$ 214,4

(1) MERIT stands for MERIT Securities Corporation; MCA stands for Multifamily Capital Access One, Inc. (now known as Commercial Capital Access One, Inc.); and CCA stands for Commercial Capital Access One, Inc. Each such entity is a wholly owned limited purpose subsidiary of the Company.

The following table summarizes the fair value of the Company's net investment in collateralized bond securities, the various assumptions made in estimating value, the unrealized gain (loss) on the Company's net investment and the cash flow received from such net investment during the first quarter of 2002.

Fair Value Assumptions

Collateralized Bond Series	Weighted-average prepayment speeds	Losses	Projected cash flow termination date	Fair value of net investment (1)
MERIT Series 11A	40%-60% CPR on SF loans; 10% CPR on MH loans	3.5% annually on MH loans	Anticipated final maturity in 2025	\$ 4
MERIT Series 12-1	9% CPR	2.8% annually on MH Loans	Anticipated final maturity in 2027	
MERIT Series 12-2	35% CPR	0.55% annually	Anticipated call date in 2002 (3)	3
MERIT Series 13	10% CPR	4.0% annually	Anticipated final maturity in 2026	
MERIT Series 14-1	35% CPR	0.2% annually	Anticipated call date in 2002 (3)	
MERIT Series 14-2	50% CPR	10.0% annually	Anticipated call date in 2002 (3)	
MCA One Series 1	(4)	Losses of \$2,096 in 2004, \$1,500 in 2006 and \$1,000 in 2008	Anticipated final maturity in 2018	
CCA One Series 2	(5)	0.60% annually beginning in 2003	Anticipated call date in 2012	
CCA One Series 3	(5)	0.60% annually beginning in 2004	Anticipated call date in 2009	2
				\$ 13

(1) Calculated as the net present value of expected future cash flows, discounted at 16%. Expected cash flows were based on the level of interest rates as of March 31, 2002, and incorporates the resetting of the interest rates on the adjustable rate assets to a level consistent with the respective index level as of March 31, 2002. Increases or decreases in interest rates and index levels from March 31, 2002 would impact the calculation of fair value, as would differences in actual prepayment speeds and credit losses versus the assumptions set forth above.

(2) Cash flows received by the Company during the year, equal to the excess of the cash flows received on the collateral pledged, over the cash flow requirements of the collateralized bond security

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- (3) These series were called in April 2002
- (4) Computed at 0% CPR through June 2008, then 20% CPR thereafter
- (5) Computed at 0% CPR until the respective call date

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The following table compares the fair value of these investments at various discount rates, but otherwise using the same assumptions as set forth for the two immediately preceding tables:

Fair Value of Net Investment				

Collateralized Bond Series	12%	16%	20%	25%
MERIT Series 11A	\$ 53,985	\$ 48,105	\$ 43,411	\$ 38,733
MERIT Series 12-1	3,492	3,371	3,213	3,000
MERIT Series 12-2	35,081	34,966	34,851	34,709
MERIT Series 13	3,831	3,712	3,557	3,346
MERIT Series 14-1	7,422	7,397	7,373	7,343
MERIT Series 14-2	2,626	2,617	2,609	2,598
MCA One Series 1	2,044	1,711	1,455	1,214
CCA One Series 2	9,653	8,005	6,781	5,659
CCA One Series 3	25,396	20,755	17,134	13,687
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	\$143,530	\$130,639	\$120,384	\$110,289
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Securities. Securities consist primarily of adjustable-rate and fixed-rate mortgage-backed securities. Securities also include derivative and residual securities. Securities increased during the three months ended March 31, 2002 by \$0.7 million to \$6.2 million at March 31, 2002 from \$5.5 million at December 31, 2001 due primarily to the call of a fixed-rate mortgage-backed security, previously sold by the Company to a third party.

Other investments. Other investments at March 31, 2002 consist primarily of delinquent property tax receivables. Other investments decreased from \$63.6 million at December 31, 2001 to \$61.8 million at March 31, 2002. This decrease is primarily the result of pay-downs of delinquent property tax receivables which totaled \$4.0 million during the quarter, partially offset by the amortization of discounts recorded to accumulated other comprehensive loss.

Loans. Loans increased from \$7.3 million at December 31, 2001 to \$7.4 million at March 31, 2002 as the result of the repurchase of certain single-family loans from one of the Company's collateralized securities for inclusion in the securitization the Company completed in April 2002. This increase was partially offset by paydowns on loans during the first three months of 2002.

Non-recourse debt. Collateralized bonds issued by the Company are recourse only to the assets pledged as collateral, and are otherwise non-recourse to the Company. Collateralized bonds decreased from \$2.3 billion at December 31, 2001 to \$2.1 billion at March 31, 2002. This decrease was primarily a result of principal payments received on the associated collateral pledged which were used to pay down the collateralized bonds in accordance with the respective indentures.

Recourse debt. Recourse debt decreased to \$47.0 million at March 31, 2002 from \$58.1 million at December 31, 2001. This decrease was due to \$11.1 million of purchases on the Senior Notes due July 2002.

Shareholders' equity. Shareholders' equity increased to \$243.9 million at March 31, 2002 from \$242.1 million at December 31, 2001. This increase was a combined

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result of a \$1.3 million decrease in the net unrealized loss on investments available-for-sale from \$14.8 million at December 31, 2001 to \$13.5 million at March 31, 2002 and net income of \$0.5 million during the three months ended March 31, 2002.

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RESULTS OF OPERATIONS

(amounts in thousands except per share information)	Three Months Ended March 31,	
	2002	2001
Net interest margin	\$ 3,857	\$ 5,623
Net (loss) gain on sales, write-downs, impairment charges and litigation	(2,055)	5,304
Trading gains	-	238
General and administrative expenses	1,894	1,844
Extraordinary item -gain on extinguishment of debt	377	2,271
Net income	481	11,649
Basic and diluted (loss) income per common share before extraordinary gain	\$ (0.21)	\$ 0.54
Basic and diluted net (loss) income per common share	\$ (0.18)	\$ 0.74

Three Months Ended March 31, 2002 Compared to Three Months Ended March 31, 2001. The decrease in net income and net income per common share during the three months ended March 31, 2002 as compared to the same period in 2001 is primarily the result of several positive non-recurring items in 2001, including the favorable settlement of litigation, and an extraordinary gain related to the early extinguishment of \$11.7 million of the Company's Senior Notes.

Net interest margin for the three months ended March 31, 2002 decreased to \$3.9 million from \$5.6 million for the same period for 2001. This decrease was primarily the result of an increase in provision for losses to \$5.6 million during the three months ended March 31, 2002 compared to \$4.8 million during the three months ended March 31, 2001. This increase in provision for losses was a result of increasing the reserve for losses on various manufactured housing loan pools pledged as collateral for collateralized bonds where the Company has retained credit risk. In addition, average interest-earning assets declined from \$3.2 billion for the three months ended March 31, 2001 to \$2.5 billion for the three months ended March 31, 2002. These decreases were partially offset by an increase in the net interest spread from 0.88% for the three months ended March 31, 2001 to 1.21% for the three months ended March 31, 2002. Further, accrual of interest on the Company's investment in delinquent property tax receivables was discontinued in 2002.

Net gain on sales, write-downs, impairment charges and litigation declined by \$7.4 million, from a gain of \$5.3 million during the three months ended March 31, 2001, to a loss of \$2.1 million during the three months ended March 31, 2002. During the three months ended March 31, 2001, the Company favorably

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resolved litigation for \$7.1 million, net of legal expenses.

The following table summarizes the average balances of interest-earning assets and their average effective yields, along with the average interest-bearing liabilities and the related average effective interest rates, for each of the periods presented.

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AVERAGE BALANCES AND EFFECTIVE INTEREST RATES

	Three Months Ended March 31,		
	2002		2001
	Average Balance	Effective Rate	Average Balance
Interest-earning assets: (1)			
Collateral for collateralized bonds (2)	\$ 2,365,993	7.22%	\$ 3,075,898
Securities	5,340	9.16%	11,878
Other investments	78,119	(0.12)%	36,131
Loans	2,967	11.79%	6,314
Cash	7,280	2.0%	37,780
	\$ 2,459,699	6.98%	\$ 3,168,001
Interest-bearing liabilities:			
Non-recourse debt (3)	\$ 2,192,492	5.72%	\$ 2,781,292
Recourse debt secured by collateralized bonds retained	-	-%	31,265
	2,192,492	5.72%	2,812,557
Other recourse debt - secured	50,589	8.13%	99,038
	\$ 2,243,081	5.78%	\$ 2,911,595
Net interest spread on all investments (3)		1.21%	
Net yield on average interest-earning assets (3)		1.71%	

(1) Average balances exclude adjustments made in accordance with Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities" to record available-for-sale securities at fair value.

(2) Average balances exclude funds held by trustees of \$534 and \$437 for the three months ended March 31, 2002 and 2001, respectively.

(3) Effective rates are calculated excluding non-interest related collateralized bond expenses and provision for credit losses. If included, the net yield on average interest-earning assets would be 0.63% and 0.74%

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for the three months ended March 31, 2002 and 2001, respectively.

The net interest spread increased 0.33%, to 1.21% for the three months ended March 31, 2002 from 0.88% for the same period in 2001. The net interest spread for the three months ended March 31, 2002 also improved relative to the same period in 2001, to 1.71% from 1.46%. The improvement in the Company's net interest spread can be attributed to a decline in the cost of interest-bearing liabilities from the respective 2001 period, which have declined as a result in the decline of One-Month LIBOR due to the reduction in short-term interest rates by the Federal Reserve. This was partially offset by the discontinuance of accrual of interest on the Company's investment in delinquent property tax receivables in 2001. The majority of the Company's variable-rate interest-bearing liabilities are priced relative to One-Month LIBOR. Interest-bearing liability costs declined 1.38% for the three month period ended March 31, 2002, compared to the same period in 2001. For the three month period ended March 31, 2002, there has been a lesser decline in the effective interest-earning yield on the collateral for collateralized bonds due to the 'reset' lag and 'floors' (the loans generally adjust or 'reset' every six or twelve months and are generally limited to maximum adjustments upwards or downwards of 1% each six months) on the approximate \$576 million in single-family ARM loans that comprise a portion of the collateral for collateralized bonds. The Company would expect its net interest spread on its interest-earning assets for the balance of 2002 to decrease as rates on adjustable collateral loans continue to adjust downward while rates on collateralized bonds remain flat or begin to adjust upward. The average One-Month LIBOR rate declined to 1.85% for the three-month period ended March 31, 2002 from 5.51% for the three-month period ended March 31, 2001.

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From March 31, 2001 to March 31, 2002, average interest-earning assets declined \$708 million, or approximately 22%. A large portion of such reduction relates to paydowns on the Company's adjustable-rate single-family mortgage loans. The Company's portfolio as of March 31, 2002 consists of \$576.1 million of adjustable rate assets and \$1.7 billion of fixed-rate assets. The Company currently finances approximately \$186.7 million of the fixed-rate assets with non-recourse LIBOR based floating-rate liabilities. Assuming short-term interest rates stay at or about current levels, the single-family ARM loans should continue to reset downwards in rate (subject to the floors) which will have the impact of reducing net interest spread in future periods.

Interest Income and Interest-Earning Assets. At March 31, 2002, \$1.7 billion of the investment portfolio consists of loans which pay a fixed-rate of interest. Also at March 31, 2002, approximately \$576.1 million of the investment portfolio is comprised of loans or securities that have coupon rates which adjust over time (subject to certain periodic and lifetime limitations) in conjunction with changes in short-term interest rates. Approximately 70% of the ARM loans underlying the ARM securities and collateral for collateralized bonds are indexed to and reset based upon the level of six-month LIBOR; approximately 17% of the ARM loans are indexed to and reset based upon the level of the one-year Constant Maturity Treasury (CMT) index. The following table presents a breakdown, by principal balance, of the Company's collateral for collateralized bonds and ARM and fixed mortgage securities by type of underlying loan. This table excludes derivative and residual securities, other investments and loans held for sale.

INVESTMENT PORTFOLIO COMPOSITION (1) (\$ in millions)

Other Indices

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	LIBOR Based ARM Loans	CMT Based ARM Loans	Based ARM Loans	Fixed-Rate Loans	Total
2000, Quarter 1	\$ 976.7	\$ 362.6	\$ 117.4	\$ 2,029.4	\$ 3,486.1
2000, Quarter 2	902.5	375.8	110.8	1,998.2	3,387.3
2000, Quarter 3	830.1	348.9	103.2	1,960.8	3,243.0
2000, Quarter 4	758.6	309.9	97.4	1,926.3	3,092.2
2001, Quarter 1	688.4	271.6	91.3	1,892.8	2,944.1
2001, Quarter 2	604.4	224.0	81.3	1,852.7	2,762.4
2001, Quarter 3	527.4	173.2	78.2	1,802.4	2,581.2
2001, Quarter 4	472.4	144.6	73.6	1,765.8	2,456.4
2002, Quarter 1	410.2	100.2	65.7	1,725.1	2,301.2

(1) Includes only the principal amount of collateral for collateralized bonds, ARM securities and fixed-rate mortgage securities.

The average asset yield is reduced for the amortization of premiums, net of discounts on the investment portfolio. As indicated in the table below, net premium on the collateral for collateralized bonds, ARM securities, fixed-rate mortgage securities at March 31, 2002 was \$20.0 million, or approximately 0.89% of the aggregate balance of collateral for collateralized bonds, ARM securities and fixed-rate securities. The \$20.0 million net premium consists of gross collateral premiums of \$45.2 million, less gross collateral discounts of \$25.2 million. Of the \$45.2 million in gross premiums on collateral, \$31.9 million relates to the premium on multifamily and commercial mortgage loans with a principal balance of \$799.5 million at March 31, 2002, and that have average initial prepayment lockouts or yield maintenance for at least ten years. Such prepayment lockouts and yield maintenance provisions generally extend to at least 2008. Net premium on such multifamily and commercial loans is \$25.9 million. Amortization expense as a percentage of principal paydowns has increased to 1.59% for the three months ended March 31, 2002 from 1.43% for the same period in 2001. The principal prepayment rate for the Company (indicated in the table below as "CPR Annualized Rate") was approximately 26% for the three months ended March 31, 2002. CPR or "constant prepayment rate" is a measure of the annual prepayment rate on a pool of loans.

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PREMIUM BASIS AND AMORTIZATION
(\$ in millions)

	Net Premium	Amortization Expense	CPR Annualized Rate	Principal Paydowns	Amortization Expense as a % of Principal Paydowns
2000, Quarter 1	\$ 36.2	\$ 2.0	18%	\$ 122.6	1.64%
2000, Quarter 2	34.1	2.1	18%	131.6	1.56%
2000, Quarter 3	32.0	2.1	18%	134.1	1.59%
2000, Quarter 4	30.1	1.9	20%	134.7	1.41%
2001, Quarter 1	28.0	2.0	23%	142.6	1.43%
2001, Quarter 2	25.7	2.3	28%	174.6	1.31%
2001, Quarter 3	23.7	2.1	28%	162.9	1.30%
2001, Quarter 4	22.4	1.8	24%	122.0	1.46%
2002, Quarter 1	20.0	2.4	26%	150.9	1.59%

Credit Exposures. The Company invests in collateralized bonds or pass-through securitization structures. Generally these securitization structures use over-collateralization, subordination, third-party guarantees, reserve funds,

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bond insurance, mortgage pool insurance or any combination of the foregoing as a form of credit enhancement. The Company generally has retained a limited portion of the direct credit risk in these securities. In most instances, the Company retained the "first-loss" credit risk on pools of loans that it has securitized.

The following table summarizes the aggregate principal amount of collateral for collateralized bonds and ARM and fixed-rate mortgage pass-through securities outstanding; the direct credit exposure retained by the Company (represented by the amount of over-collateralization pledged and subordinated securities owned by the Company), net of the credit reserves and discounts maintained by the Company for such exposure; and the actual credit losses incurred for each year. For 2001, the table includes any subordinated security retained by the Company, whereas in prior years the table included only subordinated securities rated below "BBB" by one of the nationally recognized rating agencies.

The table excludes other forms of credit enhancement from which the Company benefits, and based upon the performance of the underlying loans, may provide additional protection against losses as discussed above in Investment Portfolio Risks. This table also excludes any risks related to representations and warranties made on single-family loans funded by the Company and securitized in mortgage pass-through securities generally funded prior to 1995. This table also excludes any credit exposure on loans and other investments.

The Company has settled a dispute with the counterparty to the \$30.3 million in reimbursement guarantees. Such guarantees are payable when cumulative loss trigger levels are reached on certain of the Company's single-family mortgage loan securitizations. The Company was paid \$0.75 million in settlement of \$2.4 million in claims which had been carried on the Company's books at \$1.1 million. As part of the settlement, certain trigger levels were reset and the reasons that a loss in the future would be a 'non-qualifying' loss were significantly narrowed. As of March 31, 2002, \$122 million of loans were subject to such reimbursement guarantees.

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CREDIT RESERVES AND ACTUAL CREDIT LOSSES (\$ in millions)

	OUTSTANDING LOAN PRINCIPAL BALANCE	CREDIT EXPOSURE, NET OF CREDIT RESERVES	ACTUAL CREDIT LOSSES	CREDIT EXPOSURE, NET OF CREDIT RESERVES TO OUTSTANDING LOAN BALANCE
2000, Quarter 1	\$ 3,679.6	\$ 166.3	\$ 4.8	4.52%
2000, Quarter 2	3,677.3	195.5	5.4	5.32%
2000, Quarter 3	3,503.1	172.7	6.8	4.93%
2000, Quarter 4	3,245.3	186.6	9.6	5.75%
2001, Quarter 1	3,137.0	142.0	8.1	4.53%
2001, Quarter 2	2,948.0	135.8	8.2	4.61%
2001, Quarter 3	2,771.2	130.4	9.2	4.71%
2001, Quarter 4	2,588.4	153.5	7.1	5.93%
2002, Quarter 1	2,423.0	141.8	6.0	5.85%

The following table summarizes single family mortgage loan, manufactured housing loan and commercial mortgage loan delinquencies as a percentage of the outstanding collateral balance for those securities in which Dynex has retained a portion of the direct credit risk. The delinquencies as a percentage of the outstanding collateral balance have increased to 1.96% at March 31, 2002 from 1.75% at March 31, 2001. The Company monitors and evaluates its exposure to credit losses and has established reserves based upon anticipated losses,

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general economic conditions and trends in the investment portfolio. As of March 31, 2002, management believes the credit reserves are sufficient to cover anticipated losses that may occur as a result of current delinquencies presented in the table below.

DELINQUENCY STATISTICS (1)

	60 TO 90 DAYS DELINQUENT	90 DAYS AND OVER DELINQUENT (2)	TOTAL
2000, Quarter 1	0.26%	1.46%	1.72%
2000, Quarter 2	0.34%	1.52%	1.86%
2000, Quarter 3	0.35%	1.61%	1.96%
2000, Quarter 4	0.37%	1.59%	1.96%
2001, Quarter 1	0.20%	1.55%	1.75%
2001, Quarter 2	0.29%	1.45%	1.74%
2001, Quarter 3	0.33%	1.42%	1.75%
2001, Quarter 4	0.28%	1.50%	1.78%
2002, Quarter 1	0.29%	1.67%	1.96%

(1) Excludes other investments and loans held for sale or securitization.

(2) Includes foreclosures, repossessions and REO.

Recent Accounting Pronouncements. In June 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 addresses the initial recognition and measurement of intangible assets acquired outside of a business combination and the accounting for goodwill and other intangible assets subsequent to their acquisition. SFAS No. 142 provides that intangible assets with finite useful lives be amortized and that goodwill and intangible assets with indefinite lives will not be amortized, but will rather be tested at least annually for impairment. As the Company has no goodwill or intangible assets which it is amortizing, the adoption of SFAS No. 142 did not have any effect on the financial position, results of operations or cash flows of the Company.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 addresses financial accounting and reporting for

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obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. SFAS No. 143 is effective for fiscal years beginning after June 15, 2002. The Company does not believe the adoption of SFAS No. 143 will have a significant impact on the financial position, results of operations or cash flows of the Company.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets" which supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" and the accounting and reporting provisions of Accounting Principles Board (APB) Opinion No. 30, "Reporting the Results of Operations - Reporting and Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions (APB 30)" for the disposal of a segment of a business. This statement is effective for fiscal years beginning after December 15, 2001. SFAS No. 144 retains many of the provisions of SFAS No. 121, but addresses certain implementation issues associated with that Statement. The adoption of SFAS No. 144 did not have a significant impact on the financial position, results of operations or cash flows of the Company.

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In April 2002, the FASB issued SFAS No. 145, "Recission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13 and Technical Corrections". Effective January 1, 2003, SFAS No. 145 requires gains and losses from the extinguishment or repurchase of debt to be classified as extraordinary items only if they meet the criteria for such classification in APB 30. Until January 1, 2003, gains and losses from the extinguishment or repurchase of debt must be classified as extraordinary items, as Dynex has done. After January 1, 2003, any gain or loss resulting from the extinguishment or repurchase of debt classified as an extraordinary item in a prior period that does not meet the criteria for such classification under APB Opinion No. 30 must be reclassified. The Company is in the process of evaluating SFAS No. 145 but believes it will not have a significant impact on the financial position, results of operations or cash flows of the Company.

LIQUIDITY AND CAPITAL RESOURCES

The Company has historically financed its operations from a variety of sources. These sources have included cash flow generated from the investment portfolio, including net interest income and principal payments and prepayments, common stock offerings through the dividend reinvestment plan, short-term warehouse lines of credit with commercial and investment banks, repurchase agreements and the capital markets via the asset-backed securities market (which provides long-term non-recourse funding of the investment portfolio via the issuance of collateralized bonds). Historically, cash flow generated from the investment portfolio has satisfied its working capital needs, and the Company has had sufficient access to capital to fund its loan production operations, on both a short-term (prior to securitization, and recourse) and long-term (after securitization, and non-recourse) basis. However, market conditions since October 1998 have substantially reduced the Company's access to capital. The Company has been unable to access short-term warehouse lines of credit, and, with the exception for the resecuritization of seasoned loans in its investment portfolio, has been unable to efficiently access the asset-backed securities market to meet its long-term funding needs. Largely as a result of its inability to access additional capital, the Company sold its manufactured housing and model home purchase/leaseback operations in 1999, and ceased issuing new commitments in its commercial lending operations. Since 1999, the Company has focused on substantially reducing its recourse debt and minimizing its capital requirements. The Company has made substantial progress in both areas since 1999, and based upon its available cash, the expected investment portfolio cash flows, and the proceeds from the resecuritization of assets completed in April 2002, the Company anticipates that it will repay all of its recourse debt obligations in accordance with their respective terms. Such repayment is expected in July 2002. At such time, the Company expects that it would again have access to short-term credit lines.

Non-recourse Debt. Dynex, through limited-purpose finance subsidiaries, has issued non-recourse debt in the form of collateralized bonds to fund the majority of its investment portfolio. The obligations under the collateralized bonds are payable solely from the collateral for collateralized bonds and are otherwise non-recourse to Dynex. Collateral for collateralized bonds is not subject to margin calls. The maturity of each class of collateralized bonds is

directly affected by the rate of principal prepayments on the related collateral. Each series is also subject to redemption according to specific terms of the respective indentures, generally on the earlier of a specified date or when the remaining balance of the bonds equals 35% or less of the original principal balance of the bonds. At March 31, 2002, Dynex had \$2.1 billion of

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collateralized bonds outstanding.

Recourse Debt. As of March 31, 2002, the Company has \$46.8 million outstanding of its senior notes issued in July 1997 and due July 15, 2002 (the "Senior Notes"). On March 30, 2001, the Company entered into an amendment to the related indenture governing the Senior Notes (the "Supplemental Indenture") whereby the Company pledged to the Trustee of the Senior Notes substantially all of the Company's unencumbered assets and the stock of its material subsidiaries. In consideration of this pledge, the indenture was further amended to provide for the release of the Company from certain covenant restrictions in the indenture, and specifically provided for the Company's ability to make distributions on its capital stock in an amount not to exceed the sum of (a) \$26 million, (b) the cash proceeds of any "permitted subordinated indebtedness", (c) the cash proceeds of the issuance of any "qualified capital stock", and (d) any distributions required in order for the Company to maintain its REIT status. Pursuant to its settlement with ACA (see Item 1 below), the Company is not permitted to make any further distributions on its capital stock pursuant to clause (a) above. In addition, the Company entered into a Purchase Agreement with holders of 50.1% of the Senior Notes which required the Company to purchase, and such holders to sell, their respective Senior Notes at various discounts based on a computation of the Company's available cash. The discounts provided for under the Purchase Agreement are as follows: by April 15, 2001, 10%; by July 15, 2001, 8%; by October 15, 2001, 6%; by January 15, 2002, 4%; by March 1, 2002, 2%; thereafter until maturity, 0%. Through March 31, 2002, the Company has retired \$50,420 of Senior Notes for \$46,297 in cash under the Purchase Agreement, and the Company had no further obligations under such Purchase Agreement. In April, 2002, an additional \$550 of Senior Notes were purchased in the open market at a discount of 0.4%.

The Company's ability to incur additional indebtedness has been substantially limited by the Supplemental Indenture. The only remaining recourse debt of the Company is the Senior Notes. Based on available cash, the proceeds of the securitization completed in April 2002, and a pro-forma analysis of cash flows from its investment portfolio, the Company anticipates that the Senior Notes will be repaid in accordance with their contractual terms, although no complete assurance can be given of such repayment.

On April 25, 2002, the Company completed a securitization where it issued \$605 million of collateralized bonds. These bonds were collateralized by single-family loans aggregating \$602 million, \$447 million of which were loans already owned by the Company and \$155 million of which represented new loans from the purchase of mortgage backed securities from third parties pursuant to certain call rights owned by the Company. The transaction will be accounted for as a financing; thus the loans and associated bonds will be included in the Company's second quarter 2002 consolidated balance sheet as assets and liabilities of the Company.

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TABLE 1
NON-GAAP NET BALANCE SHEET (1)
(\$ IN THOUSANDS)

	MARCH 31, 2002

ASSETS	
Investments:	
Collateral for collateralized bonds	\$ 2,310,625
Less: Collateralized bonds issued	(2,118,260)

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Net investment in collateralized bonds	192,365
Securities	6,190
Other investments	61,780
Loans held for sale	7,428

	267,763
Cash, including restricted	17,016
Accrued interest receivable	251
Other assets	8,082

Total Assets	\$ 293,112
	=====
LIABILITIES AND SHAREHOLDERS' EQUITY	
Liabilities:	
Notes payable	46,975
Accrued interest payable	771
Other liabilities	1,477

Total Liabilities	49,223

Shareholders' Equity:	
Preferred stock, par value \$.01 per share	94,588
Common stock, par value \$.01 per share,	109
Additional paid-in capital	364,740
Accumulated other comprehensive loss	(13,527)
Accumulated deficit	(202,021)

Total Shareholders' Equity	243,889

Total Liabilities and Shareholders' Equity	\$ 293,112
	=====

- (1) This presents the balance sheet where the collateralized bonds are "netted" against the collateral for collateralized bonds. This presentation does not comply with generally accepted accounting principles applicable to the Company's transactions. Management has included this table to illustrate the Company's net investment in the collateralized bonds, which represents its economic interest in the collateralized bond securities.

FORWARD-LOOKING STATEMENTS

Certain written statements in this Form 10-Q made by the Company, that are not historical fact constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such forward-looking statements may involve factors that could cause the actual results of the Company to differ materially from historical results or from any results expressed or implied by such forward-looking statements. The Company cautions the public not to place undue reliance on forward-looking statements, which may be based on assumptions and anticipated events that do not materialize. The Company does not undertake, and the Securities Litigation Reform Act specifically relieves the Company from, any obligation to update any forward-looking statements.

Factors that may cause actual results to differ from historical results or from

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any results expressed or implied by forward-looking statements include the following:

Economic Conditions. The Company is affected by general economic conditions. The risk of defaults and credit losses could increase during an economic slowdown or recession. This could have an adverse effect on the Company's financial performance and the performance on the Company's securitized loan pools.

Capital Resources. The Company will rely on available cash and cash flow from its investment portfolio to fund its operations to repay the remaining outstanding Senior Notes due July 15, 2002. The Company may be unable to repay such notes when due in the event of a material decline in cash flow in May or June 2002. Cash flows from our portfolio are subject to fluctuation due to changes in interest rates, repayment rates and default rates and related losses.

Interest Rate Fluctuations. The Company's income depends on its ability to earn greater interest on its investments than the interest cost to finance these investments. Interest rates in the markets served by the Company generally rise or fall with interest rates as a whole. A majority of the loans currently pledged as collateral for collateralized bonds by the Company are fixed-rate. The Company currently finances these fixed-rate assets through non-recourse debt, approximately \$186.7 million of which is variable rate. In addition, a significant amount of the investments held by the Company is adjustable-rate collateral for collateralized bonds. These investments are financed through non-recourse long-term collateralized bonds. The net interest spread for these investments could decrease materially during a period of rapidly rising short-term interest rates, since the investments generally have interest rates which reset on a delayed basis and have periodic interest rate caps, whereas the related borrowing have no delayed resets or such interest rate caps.

Defaults. Defaults by borrowers on loans retained by the Company may have an adverse impact on the Company's financial performance, if actual credit losses differ materially from estimates made by the Company. The allowance for losses is calculated on the basis of historical experience and management's best estimates. Actual default rates or loss severity may differ from the Company's estimate as a result of economic conditions. In particular, the default rate and loss severity on the Company's portfolio of manufactured housing loans has been higher than initially estimated. Actual defaults on ARM loans may increase during a rising interest rate environment. The Company believes that its reserves are adequate for such risks on loans that were delinquent as of March 31, 2002.

Third-party Servicers. Third-party servicers service the majority of the Company's investment portfolio. To the extent that these servicers are financially impaired, the performance of the Company's investment portfolio may deteriorate, and defaults and credit losses may be greater than estimated.

Prepayments. Prepayments by borrowers on loans securitized by the Company may have an adverse impact on the Company's financial performance. Prepayments are expected to increase during a declining interest rate or flat yield curve environment. The Company's exposure to rapid prepayments is primarily (i) the faster amortization of premium on the investments and, to the extent applicable, amortization of bond discount, and (ii) the replacement of investments in its portfolio with lower yield securities.

Depository Institution Strategy. The Company intends to explore the formation or acquisition of a depository institution. However, the pursuit of this strategy is subject to the outcome of the Company's investigation. No business plan has been prepared for such strategy. Therefore, any forward-looking statement made

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in the report is subject to the outcome of a variety of factors that are unknown at this time.

Competition. The financial services industry is a highly competitive market. Increased competition in the market has adversely affected the Company, and may continue to do so.

Regulatory Changes. The Company's businesses as of March 31, 2002 are not subject to any material federal or state regulation or licensing requirements. However, changes in existing laws and regulations or in the interpretation thereof, or the introduction of new laws and regulations, could adversely affect the Company and the performance of the Company's securitized loan pools or its ability to collect on its delinquent property tax receivables.

Risks and Uncertainties. See Note 1 to the Company's audited financial statements for the year ended December 31, 2001.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk generally represents the risk of loss that may result from the potential change in the value of a financial instrument due to fluctuations in interest and foreign exchange rates and in equity and commodity prices. Market risk is inherent to both derivative and non-derivative financial instruments, and accordingly, the scope of the Company's market risk management extends beyond derivatives to include all market risk sensitive financial instruments. As a financial services company, net interest margin comprises the primary component of the Company's earnings. Additionally, cash flow from the investment portfolio represents the primary component of the Company's incoming cash flow. The Company is subject to risk resulting from interest rate fluctuations to the extent that there is a gap between the amount of the Company's interest-earning assets and the amount of interest-bearing liabilities that are prepaid, mature or re-price within specified periods. The Company's strategy has been to mitigate interest rate risk through the creation of a diversified investment portfolio of high quality assets that, in the aggregate, preserves the Company's capital base while generating stable income and cash flow in a variety of interest rate and prepayment environments.

The Company monitors the aggregate cash flow, projected net yield and market value of its investment portfolio under various interest rate and prepayment assumptions. While certain investments may perform poorly in an increasing or decreasing interest rate environment, other investments may perform well, and others may not be impacted at all.

The Company focuses on the sensitivity of its cash flow, and measures such sensitivity to changes in interest rates. Changes in interest rates are defined as instantaneous, parallel, and sustained interest rate movements in 100 basis point increments. The Company estimates its net interest margin cash flow for the next twenty-four months assuming no changes in interest rates from those at period end. Once the base case has been estimated, cash flows are projected for each of the defined interest rate scenarios. Those scenario results are then compared against the base case to determine the estimated change to cash flow.

The following table summarizes the Company's net interest margin cash flow sensitivity analysis as of March 31, 2002. This analysis represents management's estimate of the percentage change in net interest margin cash flow given a parallel shift in interest rates, as discussed above. Other investments are excluded from this analysis because they are not interest rate sensitive. The "Base" case represents the interest rate environment as it existed as of March 31, 2002. At March 31, 2002, one-month LIBOR was 2.33% and six-month LIBOR was 1.88%. The analysis is heavily dependent upon the assumptions used in the model. The effect of changes in future interest rates, the shape of the yield curve or

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the mix of assets and liabilities may cause actual results to differ significantly from the modeled results. In addition, certain financial instruments provide a degree of "optionality." The most significant option

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affecting the Company's portfolio is the borrowers' option to prepay the loans. The model applies prepayment rate assumptions representing management's estimate of prepayment activity on a projected basis for each collateral pool in the investment portfolio. The model applies the same prepayment rate assumptions for all five cases indicated below. The extent to which borrowers utilize the ability to exercise their option may cause actual results to significantly differ from the analysis. Furthermore, the projected results assume no additions or subtractions to the Company's portfolio, and no change to the Company's liability structure. Historically, there have been significant changes in the Company's assets and liabilities, and there are likely to be such changes in the future.

BASIS POINT INCREASE (DECREASE) IN INTEREST RATES	% CHANGE IN NET INTEREST MARGIN CASH FLOW FROM BASE CASE
+200	(5.1)%
+100	(2.6)%
Base	
-100	2.6%
-200	5.1%

Approximately \$576 million of the Company's investment portfolio as of March 31, 2002 is comprised of loans or securities that have coupon rates which adjust over time (subject to certain periodic and lifetime limitations) in conjunction with changes in short-term interest rates. Approximately 70% and 17% of the ARM loans underlying the Company's ARM securities and collateral for collateralized bonds are indexed to and reset based upon the level of six-month LIBOR and one-year CMT, respectively.

Generally, during a period of rising short-term interest rates, the Company's net interest spread earned on its investment portfolio will decrease. The decrease of the net interest spread results from (i) the lag in resets of the ARM loans underlying the ARM securities and collateral for collateralized bonds relative to the rate resets on the associated borrowings and (ii) rate resets on the ARM loans which are generally limited to 1% every six months or 2% every twelve months and subject to lifetime caps, while the associated borrowings have no such limitation. As short-term interest rates stabilize and the ARM loans reset, the net interest margin may be restored to its former level as the yields on the ARM loans adjust to market conditions. Conversely, net interest margin may increase following a fall in short-term interest rates. This increase may be temporary as the yields on the ARM loans adjust to the new market conditions after a lag period. In each case, however, the Company expects that the increase or decrease in the net interest spread due to changes in the short-term interest rates to be temporary. The net interest spread may also be increased or decreased by the proceeds or costs of interest rate swap, cap or floor agreements, to the extent that the Company has entered into such agreements.

The remaining portion of the Company's investment portfolio as of March 31, 2002, approximately \$1.73 billion, is comprised of loans or securities that have coupon rates that are fixed. The Company has substantially limited its interest rate risk on such investments through (i) the issuance of fixed-rate collateralized bonds which approximated \$1.3 billion as of March 31, 2002, and

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(ii) equity, which was \$243.9 million. Overall, the Company's interest rate risk is primarily related both to the rate of change in short term interest rates, and to the level of short-term interest rates.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

GLS Capital, Inc. ("GLS"), a subsidiary of the Company, together with the County of Allegheny, Pennsylvania ("Allegheny County"), were defendants in a lawsuit in the Commonwealth Court of Pennsylvania (the "Commonwealth Court") wherein the plaintiffs challenged the right of Allegheny County and GLS to collect certain

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interest, costs and expenses related to delinquent property tax receivables in Allegheny County. This lawsuit was related to the purchase by GLS of delinquent property tax receivables from Allegheny County in 1997, 1998, and 1999 for approximately \$58.3 million. In July 2001, the Commonwealth Court ruling addressed, among other things, (i) the right of the Company to charge to the delinquent taxpayer a rate of interest of 12% versus 10% on the collection of its delinquent property tax receivables, (ii) the charging of attorney's fees to the delinquent taxpayer for the collection of such tax receivables, and (iii) the charging to the delinquent taxpayer of certain other fees and costs. The Commonwealth Court remanded for further consideration to the Court of Common Pleas items (i) and (iii), and ruled that neither Allegheny County nor GLS had the right to charge attorney's fees to the delinquent taxpayer related to the collection of such tax receivables, reversing the Court of Common Pleas decision. The Pennsylvania Supreme Court has accepted the Application for Extraordinary Jurisdiction filed by Allegheny County and GLS. No damages have been claimed in the action; however, the decision may impact the ultimate amount recoverable on the delinquent property tax receivables, including attorney fees incurred in the collection process. To date, GLS has incurred attorneys fees of approximately \$2.0 million related to foreclosures on such delinquent property tax receivables, approximately \$1.0 million of which have been reimbursed to GLS by the taxpayer or through liquidation of the underlying real property.

The Company is also subject to other lawsuits or claims which have arisen in the ordinary course of its business, some of which seek damages in amounts which could be material to the financial statements. Although no assurance can be given with respect to the ultimate outcome of any such litigation or claim, the Company believes the resolution of such lawsuits or claims will not have a material effect on the Company's consolidated balance sheet, but could materially affect consolidated results of operations in a given year.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

Not applicable

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

See Note 9 to accompanying condensed consolidated financial statements in Part I Item 1.

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

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Not applicable

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

Exhibit 10.10 Terms of Employment between Dynex Capital, Inc. and Mr. Stephen J. Benedetti dated March 18, 2002.

(b) Reports on Form 8-K None.

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SIGNATURES

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

DYNEX CAPITAL, INC.

By: /s/ Stephen J. Benedetti

Stephen J. Benedetti
Executive Vice President
(Principal Executive Officer)

Dated: October 7, 2002

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