

HOLLY
MORTGAGE
TRUST

1998 ANNUAL REPORT

TO OUR SHAREHOLDERS:

Holly Mortgage Trust ("Holly") began operating on January 2, 1998 with an initial investment of \$600,000 by First Commonwealth Mortgage Trust (FCM). This investment was equally divided between 300,000 shares of Holly stock having a stated value of One Dollar (\$1.00) per share and a five-year \$300,000 land development loan. On January 15, 1998 FCM paid a dividend to their shareholders of one share of Holly stock for every four shares of FCM stock owned.

This dividend resulted in 241,868 shares of Holly being distributed to the shareholders of FCM. The remaining 58,132 shares are held as an investment by FCM. Concurrently, Holly issued two sets of warrants to its new shareholders. Each shareholder received five warrants maturing on December 31, 1998 and another five warrants maturing on December 31, 1999 for each share of stock owned. Each warrant could be exercised for one share of Holly stock at a price of \$1.00 per share.

During 1998, 459,254 warrants were exercised and converted into shares of Holly stock. These conversions included 71,151 warrants maturing in December 1999. The exercise of more of the 1999 warrants will support Holly's program to maximize leverage. Holly's strategy is to invest on a leveraged basis in loans that generate higher yields because they are secured by junior mortgages of unimproved or development property. Holly limits loans to an amount management deems it could recover if for some unforeseen reason Holly had to foreclose on the collateral.

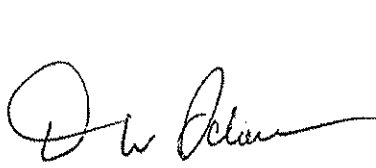
In its first year Holly initiated \$1,636,000 of loans. These investments included a number of second mortgages on homes in Northern California, a work/live conversion in Emeryville, California and a real estate development in Florida. The first two loans were purchased as participations from a California REIT to which Holly has recourse in case of default. In addition, as part of the second loan Holly received options to purchase shares in the REIT at any time over the next five years.

The \$300,000 land development loan initially contributed by FCM provided for an accrual of interest at 13% p.a. until maturity in 2000. Holly has elected to pay taxes on a cash basis, therefore the REIT was not required to distribute any earnings for 1998 and management decided it was more prudent to retain the earnings to continue to expand its portfolio.

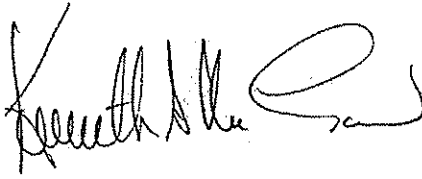
On December 31, 1998 Holly acquired all of the stock of A.R. Goldrick Company, Inc., the General Partner of Wilco Building Partners, LTD., (Wilco) in exchange for 75,000 shares of Holly stock. Wilco owns a twenty-two story office building in Midland, Texas. Holly assumed management of the building on April 1, 1999. Management believes its resources, expertise and contacts will enable Holly to improve the results of operations of the Wilco building.

The audited financial statements for the year ended December 31, 1998 as presented by Mann Frankfort Stein & Lipp, Certified Public Accountants, appear at the end of this report.

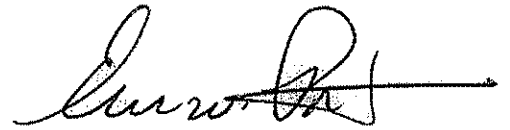
Net income was \$30,521 or \$0.10 per share. This represents a ten percent (10%) return on the \$1.00 stated value of a share of Holly stock. The calculation of per share earnings is adjusted to reflect the time shares were outstanding. Because 1998 was the first year of operations there are no comparative figures for 1997.



Robert W. Scharar
Chairman of the Board



Kenneth A. McGaw
President & Chief
Executive Officer



Eric W. Porter
Vice President &
Chief Operating Officer

**HOLLY MORTGAGE TRUST
AND WHOLLY-OWNED SUBSIDIARY**

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1998

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1998

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**MANN
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Report of Independent Auditors

Board of Trustees
Holly Mortgage Trust and Subsidiary

We have audited the consolidated balance sheet of Holly Mortgage Trust and wholly-owned subsidiary (the "Trust") as of December 31, 1998, and the related consolidated statements of income, shareholders' equity, and cash flows for the period from inception (January 2, 1998) to December 31, 1998. These consolidated financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principals used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Holly Mortgage Trust and wholly-owned subsidiary at December 31, 1998, and the results of its operations and its cash flows for the initial period then ended, in conformity with generally accepted accounting principles.

Our audit was conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The information in the accompanying Schedules I and II is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information has been subjected to the audit procedures applied to the audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

Mann Frankfort Stein & Lipp, P.C.

Houston, Texas
April 30, 1999

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
CONSOLIDATED BALANCE SHEET
DECEMBER 31, 1998

ASSETS	
Cash	\$ 464,896
Mortgage notes receivable	1,569,032
Accrued interest receivable	113,906
Goodwill	74,999
Investment in partnership	<u>1</u>
TOTAL ASSETS	<u>\$ 2,222,834</u>
LIABILITIES AND SHAREHOLDERS' EQUITY	
LIABILITIES	
Accrued expenses	\$ 115,356
Long-term debt - affiliate	642,702
Long-term debt	<u>600,001</u>
TOTAL LIABILITIES	1,358,059
SHAREHOLDERS' EQUITY	
Shares of beneficial interest, no par value, unlimited shares authorized, 834,254 issued and outstanding	834,254
Retained earnings	<u>30,521</u>
TOTAL SHAREHOLDERS' EQUITY	<u>864,775</u>
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u>\$ 2,222,834</u>

See accompanying notes to financial statements.

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
CONSOLIDATED STATEMENT OF INCOME
PERIOD FROM INCEPTION (JANUARY 2, 1998) TO DECEMBER 31, 1998

REVENUES	
Interest income	\$ 127,725
COSTS AND EXPENSES	
General and administrative	21,628
Interest expense	<u>75,576</u>
NET INCOME	<u>\$ 30,521</u>
NET INCOME PER SHARE, basic and fully dilutive	<u>\$.10</u>
WEIGHTED AVERAGE SHARES OUTSTANDING	<u>317,299</u>

See accompanying notes to financial statements.

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
PERIOD FROM INCEPTION (JANUARY 2, 1998) TO DECEMBER 31, 1998

	Shares of Beneficial Interest		Retained Earnings	Total Shareholders' Equity
	Number	Amount		
Initial issuance of shares	300,000	\$ 300,000	\$ -	\$ 300,000
Issuance of shares through exercised warrants	459,254	459,254	-	459,254
Issuance of shares for acquisition of Goldrick	75,000	75,000	-	75,000
Net income	<u>-</u>	<u>-</u>	<u>30,521</u>	<u>30,521</u>
Balance at December 31, 1998	<u>834,254</u>	<u>\$ 834,254</u>	<u>\$ 30,521</u>	<u>\$ 864,775</u>

See accompanying notes to financial statements.

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
CONSOLIDATED STATEMENT OF CASH FLOWS
PERIOD FROM INCEPTION (JANUARY 2, 1998) TO DECEMBER 31, 1998

CASH FLOWS FROM OPERATING ACTIVITIES

Net income	\$ 30,521
Adjustments to reconcile net income to net cash used in operating activities:	
Change in assets and liabilities, net of effects of acquisition:	
Accrued interest receivable	(79,310)
Accounts payable and other liabilities	<u>14,234</u>
NET CASH USED IN OPERATING ACTIVITIES	<u>(34,555)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Mortgage notes originated	(1,902,702)
Mortgage note participations sold	700,000
Principal collected on mortgage notes receivable	155,670
Effect of acquisition of Goldrick	<u>101,122</u>
NET CASH USED IN INVESTING ACTIVITIES	<u>(945,910)</u>

CASH FLOWS FROM FINANCING ACTIVITIES

Proceeds from long-term debt - affiliate	602,702
Payments on long-term debt - affiliate	(260,000)
Proceeds from long-term debt	600,001
Proceeds from issuance of shares	<u>502,658</u>
NET CASH PROVIDED BY IN FINANCING ACTIVITIES	<u>1,445,361</u>

INCREASE IN CASH AND CASH EQUIVALENTS 464,896

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR -

CASH AND CASH EQUIVALENTS AT END OF YEAR \$ 464,896

SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest \$ 75,576

NONCASH ACTIVITY

Contribution of mortgage note receivable for \$522,000 and accrued interest of \$34,596 less debt of \$300,000 for issuance of shares \$ 256,596

Purchase of subsidiary allocated to goodwill and investment in partnership \$ 75,000

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1998

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES

The accompanying consolidated financial statements include the accounts of Holly Mortgage Trust ("Holly") and AR Goldrick Company, Inc. ("Goldrick"), its wholly-owned subsidiary (collectively referred to as the "Trust"). All significant accounts and transactions have been eliminated upon consolidation. Holly was organized as a Massachusetts business trust on January 2, 1998 and Goldrick was acquired through a stock purchase (see Note B). The Trust is engaged primarily in the business of investing in second mortgages and equity participation mortgages. FCA Corporation ("FCA"), whose principal stockholder is a trustee and a shareholder of the Trust, is the Trust's compensated manager and advisor.

Cash Equivalents: The Trust considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Mortgage Notes Receivable: Mortgage notes receivable are carried at unpaid principal balance since generally it is management's intention to hold mortgage notes to maturity. Commitment and origination fees collected from prospective borrowers are deferred and recognized as income using a method approximating the interest method over the life of those loans.

A loan is considered impaired when it is probable that the scheduled principal or interest will not be collected when due. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or collateral fair value, if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment loss is recognized through a valuation allowance and a corresponding charge to operations.

Allowance for Losses: The allowance for losses is based on management's estimate of the amount required to maintain an allowance adequate to reflect the risks inherent in the loan portfolio after giving consideration to existing economic conditions, loss experience in relation to outstanding loans, changes in the loan portfolio, borrowers' performance in reducing loan principal, adequacy of loan collateral, and other relevant factors.

Interest Income: Interest income on loans is accrued based upon the principal amount outstanding.

If a loan is placed on nonaccrual status, interest previously recognized but uncollected is reversed and charged against current income. Subsequent interest collected on such a loan is credited to principal if, in the opinion of management, collectibility of principal is doubtful; otherwise, the interest collected is recognized as revenue.

Concentration of Credit Risk: The Trust's primary business activity is investing in loans collateralized by mortgages on real estate projects. These loans are principally collateralized by real estate in Florida and California.

The Trust maintains cash balances in a bank which at times, exceeds federal insured limits. The Trust monitors the financial condition of the bank and has experienced no losses associated with this account.

Net Income per Share: Net income per share is calculated by dividing net income by the weighted average number of shares of beneficial interest outstanding during the year. Earnings per share, both basic and fully dilutive, are the same.

Management Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1998

NOTE B - BUSINESS COMBINATION

On December 31, 1998, Holly acquired 100% of the outstanding stock of Goldrick, in which Holly issued 75,000 shares of beneficial interest in exchange for 1,000 shares of Goldrick's common stock. The acquisition has been accounted for as a purchase transaction and, accordingly, the fair value of the consideration was allocated to Goldrick's assets and liabilities based on the estimated fair values as of the acquisition date. The excess value over the value of the net assets acquired was \$74,999 and has been recorded as goodwill to be amortized on the straight-line basis over 10 years.

NOTE C - MORTGAGE NOTES RECEIVABLE AND COMMITMENTS

Notes receivable from funding mortgage loans are principally collateralized by second mortgage loans on commercial or residential property and are due at various dates, with the latest maturity due in 2003. Notes receivable bear interest at rates ranging from 9.5% to 14%.

NOTE D - FEDERAL INCOME TAXES

The Trust operates in such a manner to qualify as a "real estate investment trust" under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended, and the Treasury Regulations promulgated thereunder. Under those sections, the Trust will not be taxed on that portion of its qualifying income distributed to shareholders so long as at least 95% of the Trust's otherwise taxable income is distributed to shareholders each year and other requirements of a qualified real estate investment trust are met. The Trust satisfied the income distribution requirement for the year ended December 31, 1998. Management believes that all other requirements of a qualified real estate investment trust have been met.

NOTE E - LONG-TERM DEBT-AFFILIATES

Long-term debt-affiliates consisted of the following at December 31, 1998:

Note payable to an affiliate, secured by assets, bearing interest at 9.8%, interest payments due quarterly, principal and any accrued interest due December 1999.	\$ 402,702
Note payable to an affiliate, secured by assets, bearing interest at 11%, principal and accrued interest due in five annual payments maturing December 2003.	<u>240,000</u>
	<u>\$ 642,702</u>

Interest expense paid to affiliates totaled approximately \$61,500 for the period ended December 31, 1998.

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 DECEMBER 31, 1998

NOTE F - LONG-TERM DEBT

Long-term debt consisted of the following at December 31, 1998:

Line of credit with a bank, secured by assets, bearing interest at 9.80%, interest payments due monthly, principal and any accrued interest due March 2000.	\$ 500,001
Line of credit with a bank, secured by assets, bearing interest at 9.75%, interest payments due monthly, principal and any accrued interest due April 2000.	<u>100,000</u>
	<u>\$ 600,001</u>

The following are future maturities of long-term debt for both bank and affiliated debt at December 31, 1998:

1999	\$ 462,702
2000	660,001
2001	60,000
2002	<u>60,000</u>
	<u>\$1,242,703</u>

NOTE G - ADVISORY AGREEMENT AND RELATED PARTY TRANSACTIONS

The Trust is managed and advised by FCA, whose principal shareholder is a trustee and shareholder of the Trust. The advisory fee was waived for the year ended December 31, 1998. The fee is based on 1% of the book value of the assets of the Trust at the end of each fiscal year.

During the year, the Trust sold a participation in a mortgage note receivable to an affiliated real estate investment trust for \$700,000. The mortgage note matures December 1999. Subsequent to December 31, 1998, the affiliate sold their participating amount to another affiliated business trust.

NOTE H - WARRANTS

On January 2, 1998, the Trust issued 2,418,690 warrants to its shareholders, 50% exercisable during 1998 and the remaining half exercisable through 1999. Each shareholder is entitled to purchase one share of beneficial interest at \$1 per share. The warrants were granted to the shareholders on the basis of 5 warrants for each share owned by the shareholder. During 1998, 459,254 warrants were exercised, 388,103 which were due to expire during 1998 and 71,151 which are due to expire during 1999. At December 31, 1998, 821,242 warrants expired and 1,138,194 warrants were outstanding and exercisable during 1999.

NOTE I - MAJOR LOANS

During the year, the Trust derived approximately 95% of its interest income from two mortgage notes. These notes comprised approximately 62% of the mortgage notes receivable, net of participation at December 31, 1998.

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
SCHEDULE I - CONSOLIDATING BALANCE SHEET
DECEMBER 31, 1998

	Holly Mortgage Trust	AR Goldrick Company, Inc.	Elimination Entries	Consolidated Total
ASSETS				
Cash	\$ 363,774	\$ 101,122	\$ -	\$ 464,896
Mortgage notes receivable	1,569,032	-	-	1,569,032
Accrued interest receivable	113,906	-	-	113,906
Goodwill	-	74,999	-	74,999
Investments	<u>75,000</u>	<u>1</u>	<u>(75,000)</u>	<u>1</u>
TOTAL ASSETS	<u><u>\$ 2,121,712</u></u>	<u><u>\$ 176,122</u></u>	<u><u>\$ (75,000)</u></u>	<u><u>\$ 2,222,834</u></u>
 LIABILITIES AND SHAREHOLDERS' EQUITY				
LIABILITIES				
Accrued expenses	\$ 14,234	\$ 101,122	\$ -	\$ 115,356
Long-term debt – affiliate	642,702	-	-	642,702
Long-term debt	<u>600,001</u>	<u>-</u>	<u>-</u>	<u>600,001</u>
TOTAL LIABILITIES	<u>1,256,937</u>	<u>101,122</u>	<u>-</u>	<u>1,358,059</u>
 SHAREHOLDERS' EQUITY				
Shares of beneficial interest/capital	834,254	75,000	(75,000)	834,254
Retained earnings	<u>30,521</u>	<u>-</u>	<u>-</u>	<u>30,521</u>
TOTAL SHAREHOLDERS' EQUITY	<u>864,775</u>	<u>75,000</u>	<u>(75,000)</u>	<u>864,775</u>
 TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	 <u><u>\$ 2,121,712</u></u>	 <u><u>\$ 176,122</u></u>	 <u><u>\$ (75,000)</u></u>	 <u><u>\$ 2,222,834</u></u>

HOLLY MORTGAGE TRUST AND WHOLLY-OWNED SUBSIDIARY
 SCHEDULE II - CONSOLIDATING STATEMENT OF INCOME
 PERIOD FROM INCEPTION(JANUARY 2, 1998) TO DECEMBER 31, 1998

	<u>Holly Mortgage Trust</u>	<u>AR Goldrick Company, Inc.</u>	<u>Elimination Entries</u>	<u>Consolidated Total</u>
REVENUES				
Interest income	\$ 127,725	\$ -	\$ -	\$ 127,725
COSTS AND EXPENSES				
General and administrative	21,628	-	-	21,628
Interest expense	<u>75,576</u>	<u>-</u>	<u>-</u>	<u>75,576</u>
NET INCOME	<u>\$ 30,521</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 30,521</u>

See Report of Independent Auditors.

TRUSTEES

George M. Beatty, Jr.
President, Chamber of Commerce Division
Greater Houston Partnership

William C. Brooks
Financial Consultant

Josef C. Hermans
Hotel Consultant

Robert W. Scharar
President, FCA Corp

EXECUTIVE OFFICERS

Robert W. Scharar
Chairman

Kenneth A. McGaw
President and
Chief Executive Officer

Eric W. Porter
Vice President and
Chief Operating Officer

Robert P. Messer, Jr.
Vice President and Secretary

Juliann E. Barkley
Treasurer

William B. Le Vay
Assistant Secretary

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