

RNS Euro. Eq Tranche Inc EET Preliminary Results  
Oct 13 2006 13:00

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European Equity Tranche Income Ltd.  
13 October 2006

#### EUROPEAN EQUITY TRANCHE INCOME LIMITED

#### PRELIMINARY ANNOUNCEMENT OF ANNUAL RESULTS

The directors announce the statement of results for the period from incorporation on 17 March 2006 to 30 June 2006 as follows:-

#### ABOUT THE COMPANY

European Equity Tranche Income Limited (`the Company`) was incorporated in Guernsey as a closed-ended investment company on 17 March 2006 and issued its prospectus for the raising of capital on 6 April 2006 (the "Prospectus"). The Company commenced business on 26 April 2006 ("Admission") when 100,000,000 Ordinary shares of no par value ("Shares") were allotted to applicants pursuant to the initial offering of Shares at an issue price of 1 each. The Company does not have a fixed life. Shareholders will have the opportunity to review the future of the Company after an initial period of seven years following Admission and every second year thereafter.

#### INVESTMENT OBJECTIVE AND POLICY

The Company`s investment objective is to deliver stable returns to shareholders in the form of quarterly dividends and to preserve capital.

It intends to achieve this by investment in non-investment grade and equity tranche (or "first loss") positions of residential mortgage-backed securities ("RMBS") and, to a limited extent, other asset-backed securities ("ABS") in Europe. The directors intend that, once fully invested no less than 75 per cent of investments are made in RMBS and up to 25 per cent in other ABS.

#### CHAIRMAN`S STATEMENT FOR THE PERIOD FROM INCORPORATION TO 30 JUNE 2006

I am pleased to present the first annual report and accounts for European Equity Tranche Income Limited ("EET"). EET is a Guernsey incorporated investment company listed on the AIM London Stock Exchange. The Company successfully completed its initial public offering in April, raising 100 million at a price of 1 per share. The initial net asset value was 97.7 million after the Company incurred flotation costs of 2.3 million. For the period ended 30 June 2006 the Company has reported a net profit of 375,216 and earnings per ordinary share of 0.0061. The market capitalisation as at 30 June was 98 million. The Company had invested 55 million at June 30 and held 42.6 million in cash.

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## Strategy

The Company's investment objective is to preserve capital and to provide stable returns to shareholders by distributing dividends on a quarterly basis. It intends to achieve this by investing in the equity tranches and/or lowly rated securities of residential mortgage backed securities (RMBS) and, to a limited extent, in similar corporate asset backed securities (ABS) in Europe. In due course the Company is authorised to increase the leverage of the fund by using debt financing. The Company targets a yield (excluding leverage) between 10% and 13% on its investments. The Investment Manager, Ocean Capital Associates LLP, has started to build an attractive and well diversified portfolio of subordinated tranches of RMBS across Continental Europe.

## Investments to Date

The Company successfully invested 55% of its IPO proceeds by the end of June 2006 and continues to invest in Continental Europe. As at the time of writing, the Company has invested close to 70 million and has a pipeline of potential investments. Our prospectus enunciated an objective of being fully invested within 12 months of the IPO. However, given current market conditions we expect to be fully invested earlier than this, possibly by 31 December 2006. The asset pools underlying the investments held by the Company consist of residential mortgages granted primarily to prime borrowers in Continental Europe. The portfolio includes both non rated and rated (below investment grade) investments.

## Portfolio Diversification

As at year end the Company's investment portfolio was diversified geographically, with investments in Italy, The Netherlands, Portugal and France. Once fully invested the portfolio will consist of a minimum of 75% of RMBS. We will also consider investing in other European asset backed securities which have strong granularity characteristics and attractive yields.

## Outlook

The Company is well positioned to deliver stable value to our shareholders. The market for equity tranches in Europe remains a niche in the overall credit market, albeit with good growth prospects which will be helped by the implementation of the Basel II framework in January 2007. EET has developed a network of relationships with blue chip banks and issuers across Europe. We are confident in the Company's ability to capitalise on the development of that niche. Once fully invested the Company has an unlimited power to borrow. However your directors will be using this power cautiously and in any case will not borrow an amount in excess of 240% of net assets.

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The market we operate in is highly specialised, but we believe the expertise provided by our fund managers Ocean Capital, combined with careful oversight by your board, offers the opportunity for excellent returns. Your board has regular and active conversations with our managers and although we are at an early stage we are optimistic that the goals we have set are achievable.

#### Annual General Meeting

Our first Annual General Meeting will be held at the registered offices of the Company on 16 November 2006. The Notice of the Annual General Meeting is set out at the end of the annual report and a form of proxy accompanies the annual report.

Robin Monro-Davis  
Chairman

#### INVESTMENT MANAGER`S REPORT FOR THE PERIOD FROM INCORPORATION TO 30 JUNE 2006

##### Overview

EET closed its first accounting period on 30 June 2006, 9 weeks after 26 April 2006, its first day of listing.

The Company intends to achieve its investment objective by investing in both non-investment grade and equity tranches of residential mortgage backed securities (RMBS) and, to a limited extent, in the equity tranches of corporate asset backed securities (ABS) in Continental Europe and the UK. Types of ABS the Company may invest in will include securities which are backed by collateral, such as trade receivables and leases where the underlying obligors are individuals or corporations, as well, potentially, as loans, whole business loans, aircraft loans, auto loans, credit card loans, auto leases, CBOs/CLOs(1) and reinsurance. The equity tranches of the securities will, in most cases, be rated below investment grade or unrated and will, in many cases, represent the residual income typically retained by the Originator of a securitisation transaction as the `equity tranche` or `first loss position`.

The Company`s strategy is to buy and hold its investments to maturity and it does not factor in trading opportunities when assessing the potential returns of an investment. The Company`s portfolio as at 30 June 2006 is comprised entirely of residual income positions and subordinated tranches of Continental European RMBS, valued at approximately 55 million at acquisition cost.

##### Investment Performance and Portfolio Characteristics

At the year end the Company`s portfolio comprised 6 individual investments

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consisting of residual income positions or subordinated tranches of RMBS in Continental Europe. The underlying asset pools are comprised of prime mortgages originated by established local banks in Italy, the Netherlands, France and Portugal. As all investments are Euro denominated, the fund currently has no forex exposures.

The Investment Manager has reviewed a number of other investment opportunities backed by mortgage pools in Continental Europe and the UK, as well as by SME loans. It has chosen not to enter into these transactions as the risk reward profile has not matched our investment criteria. The Company's investment portfolio has performed in line with initial expectations and the fair values and effective yields attributed to each investment at the time they were acquired have not been adjusted since acquisition.

#### Financing Strategy

At 30 June 2006, the Company had approximately 43 million in cash, which represented the remaining cash from funds raised in the IPO as well as payments received on its investments. As at 30 June 2006, the Company's indebtedness was nil.

Once the cash has been invested, the Company intends to leverage its portfolio to increase its investment capacity and enhance returns to shareholders. The Company's Board has limited the leverage to 240 per cent. of shareholders' equity but it is unlikely that future indebtedness, if any, would reach this limit.

#### Market Outlook

Primary RMBS issuance in Continental Europe and the UK represented a total volume of approximately 105 billion in the first half of 2006(2), compared with an issuance volume of approximately 170bn for the whole of 2005. UK issuance continued to be strong over the period, making up approximately 45% of the total, supported by growing issuance by non-conforming and sub-prime lenders. The main issuing countries in Continental Europe were the Netherlands, Spain and Italy. At this point, our view is that total issuance volume of RMBS for the whole of 2006 should equal or exceed the volume for 2005.

While we are not aware of any publicly available statistics, we believe the value of RMBS deeply subordinated tranches sold in Continental Europe and the UK will have substantially increased in 2006. Supply has come from a broadening base of Continental European issuers as well as UK non-conforming mortgage lenders. Residual income positions from securitisations of UK non-conforming mortgages represented, in our assessment, approximately half of the total market during the first half of 2006.

The sale of residual income positions of securitisation structures by issuing

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banks or lenders has gained momentum over the past years, largely driven by new regulatory capital treatment and accounting regulations. The Basel II regulatory framework changes the regulatory capital treatment for banks and provides a strong economic incentive to focus on the capital management of the residual income positions, which historically, they retained. Basel II comes into force in January 2007 for most European countries. In addition, the convergence of international accounting standards following the introduction of IFRS in 2005, requires, in most cases, the transfer or sale of the equity tranche of securitisations in order to achieve off-balance sheet treatment.

Ocean Capital continues to believe that the market for residual income positions of RMBS as well as of other asset classes, should experience sustained growth in the foreseeable future.

#### Investment Focus

The Company focuses on investment opportunities in residual income positions of RMBS in Continental Europe and the UK. At present the Company is focussing its main attention in Continental Europe where the outlook for housing and the level of consumer indebtedness is less uncertain. In addition, most RMBS transactions issued in these countries are backed by "prime" mortgage borrowers.

As previously mentioned, there is a significant deal flow consisting of UK mortgage lenders financing non-conforming and sub-prime borrowers. The Company has evaluated several opportunities in that segment but to date has not invested in any such positions. This choice reflects, among other factors, our view of a deteriorating credit outlook in the UK, particularly among non-conforming and sub-prime borrowers, and uncertainty on the valuation trend of non-prime properties. This could translate into higher volatility in cash flows and returns on residual income positions over the coming years, despite the overall strong current performance of such instruments.

Once fully invested the Company's portfolio will consist of no less than 75% RMBS.

#### Investment Process

Ocean Capital sources investment opportunities on behalf of the Company through a variety of channels, including Ocean Capital's direct relationships with commercial and investment banks. In addition, Ocean Capital's securitisation expertise allows us, on behalf of the Company, to source direct purchases of granular asset portfolios. We believe that the Company's existing asset sourcing capability and its efforts to broaden it across Europe will enable it to continue to secure residual income positions at attractive levels for the foreseeable future.

Prior to making any investment, Ocean Capital conducts an extensive analysis of

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the potential investment centred on a number of aspects pertaining to the economic environment of that particular jurisdiction, the quality of the originating lender and of the servicer, the performance of previous comparable transactions and the expected risk and reward profile of the asset. Once the decision to further evaluate a particular investment is made, Ocean Capital conducts extensive due diligence and financial modelling with a view to refining its assumptions and establishing the appropriate valuation level.

We thank the Board for its continued confidence in our ability to source investments for the Company and to manage the Company`s investment portfolio.

- (1) Collaterised Bond Obligations / Collaterised Loan Obligations  
 (2) Figures are based on The International Securitisation Report of July 2006

Ocean Capital Associates LLP  
 Investment Manager

INCOME STATEMENT  
 for the period from incorporation to 30 June 2006

17 Mar 2006  
 to 30 Jun 2006

Operating income	778,122
Operating expenses	(402,906)
	-----
Net profit for the period	375,216
	=====
Basic and diluted earnings per share for the period	0.0061
Proforma basic and diluted earnings per share for the period	0.0037

In arriving at the results for the financial period, all amounts above relate to continuing operations.

BALANCE SHEET  
 as at 30 June 2006

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## ASSETS

Non-current assets		
Investments designated at fair value through the income statement		55,104,283
Current assets		
Trade and other receivables	608,025	
Cash at bank	42,663,014	
	-----	
		43,271,039
		-----
Total assets		98,375,322
		=====

## EQUITY AND LIABILITIES

Equity		
Issued capital	-	
Share premium	50,000,000	
Retained earnings	48,051,553	
	-----	
		98,051,553
		-----
Current liabilities		
Trade and other payables		323,769
		-----
Total equity and liabilities		98,375,322
		=====

STATEMENT OF CHANGES IN SHAREHOLDERS` EQUITY  
 for the period from incorporation to 30 June 2006

Balance at beginning of the period		-
Formation expenses		(2,323,663)
Profit for the period		375,216
		-----
Total recognised income and expenses for the period		(1,948,447)

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Share premium on issue of shares	100,000,000
	-----
Balance at 30 June 2006	98,051,553
	=====

#### CASH FLOW STATEMENT

for the period from incorporation to 30 June 2006

17 Mar 2006  
 to 30 Jun 2006

#### Cash flows from operating activities

Profit for the period	375,216
Increase in accrued expenses	323,769
(Increase) in prepayments and accrued income	(608,025)
Purchase of non-current assets	(55,104,283)
	-----

Net cash flow from operating activities	(55,013,323)
	-----

#### Cash flows from financing activities

Proceeds of issue of ordinary shares	100,000,000
Costs related to the issuance of ordinary shares	(2,323,663)
	-----

Net cash flow from financing activities	97,676,337
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Cash and cash equivalents at the beginning of the period	-
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Net increase in cash and cash equivalents	42,663,014
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Cash and cash equivalents at the end of the period	42,663,014
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For further information contact:

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Anson Fund Managers Limited  
Company Secretary

Tel: Guernsey 01481 722260

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END OF ANNOUNCEMENT

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