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EUROPEAN EQUITY TRANCHE INCOME

ANNUAL REPORT  
JUNE 2006



# Report & Financial Statements

for the period ended 30 June 2006

## **European Equity Tranche Income Limited**



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## 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.

The Company's Investment Manager is Ocean Capital Associates LLP, a United Kingdom based investment management partnership authorised and regulated by the Financial Services Authority of the United Kingdom.

## 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.

## INVESTMENT PERFORMANCE

As at 30 June 2006, the net asset value of a share was €0.9805.

## DIRECTORS

### European Equity Tranche Income Limited Directors

The Company has six directors. They are responsible for the implementation of the Company's investment policy and on going management.

#### **Robin Monro-Davies (Chairman) (British)**

Mr Monro-Davies, aged 65, has worked in the City for over 25 years and is a director of HSBC Bank plc and AXA UK plc. He was co-managing director of Fox-Pitt, Kelton Limited from 1976 and 1992 and chief executive of Fitch Ratings Limited from 1992 to 2002. He is currently also a director of Assured Guaranty Limited (Bermuda), AXA Asia Pacific Holdings and Mergermarket Limited as well as North American Banks Fund Limited. Mr Monro-Davies is resident in England.

#### **Leslie Goodman (British)**

Mr Goodman, aged 60, has worked in the City for over 30 years and is chairman of Viatel Holdings Bermuda Limited. He qualified as a solicitor and subsequently became a director of Hill Samuel and of BZW. He was chief executive of ACE Global Markets Limited from 1994 to 1998 and Jardine Lloyds Advisers Limited from 1991 to 1994. Mr Goodman is resident in England.

#### **John Le Prevost (British)**

Mr Le Prevost, aged 54, is the Chairman of Anson Fund Managers Limited and of Anson Registrars Limited and has over 34 years experience in investments during which time he was managing director of County NatWest Investment Management in Guernsey and Royal Bank of Canada's mutual fund company in Guernsey. He is currently a director of several investment companies including The Close Man Hedge Fund Limited, Guaranteed Investment Products I PCC Limited, Harewood Structured Investment PCC Limited and Thai Prime Fund Limited. Mr Le Prevost is resident in Guernsey.

#### **Françoise Henry (French)**

Françoise Henry aged 65 is currently Chief Investment Officer of Alternative Leader S.A. Ms Henry was previously the Head of alternative investment strategy for Europe at Goldman Sachs Asset Management and Head of Proprietary trading at Credit Agricole. Ms. Henry is resident in France.

#### **Tanguy Boulet (French)**

Tanguy Boulet aged 43 is a co-founder of the Investment Manager, Ocean Capital Associates LLP. He was the Head of Debt products origination for French corporations and Head of French Real Estate Investment Banking at Lehman Brothers from 2000 to 2004, Head of Debt products origination, French Corporates at Merrill Lynch from 1996 to 2000 and Head of French Derivative linked and structured assets marketing at Merrill Lynch from 1992 to 1996. Mr Boulet is resident in France.

#### **Juan de Dios Sanchez-Roselly Moreno (Spanish)**

Mr de Dios Sanchez-Roselly Moreno, aged 38, is currently the Chief Investment Officer at Santander Asset Management. He was previously at Ahorro Corporación and Arthur Andersen. Mr Sanchez-Roselly Moreno is resident in Spain.

## ADMINISTRATOR AND SECRETARY

Anson Fund Managers Limited ("Anson") is a Guernsey incorporated privately owned company and provides administration and secretarial services to the Company pursuant to an Administration Agreement. In such capacity, the administrator is responsible for the general secretarial functions required by The Companies (Guernsey) Law, 1994, as amended, and for ensuring that the Company complies with its continuing obligations as a company having its shares listed on the Channel Islands Stock Exchange and admitted to trading on AIM. The administrator is also responsible for the Company's general administrative functions such as the calculation of the net asset value of shares and the maintenance of its accounting records. Anson provides such services to a number of investment schemes and companies.

## REPORT OF THE DIRECTORS

### The directors present their report and financial statements for the period from incorporation to 30 June 2006.

#### Principal Activity

European Equity Tranche Income Limited is a closed-ended investment company incorporated in Guernsey on 17 March 2006. On 26 April 2006 the shares were admitted to trading on AIM and admitted to listing and trading on the Channel Islands Stock Exchange.

Pursuant to the Company's admission document the Company offered its shares for issue by means of a placing and on 26 April 2006 raised €100 million by the issue of 100,000,000 shares of €nil each at a price of €1 each.

#### Investment Objective and Investment Policy

The investment objective and policy of the Company is as stated on page 3.

#### Dividends and Dividend Policy

The Company's dividend policy is to pay quarterly dividends subject to having profits or distributable reserves available for that purpose.

Net profit for the period and amounts transferred from share premium is classed as distributable profit.

The Company will not be paying a dividend for the initial financial period ending 30 June 2006.

The Company intends to pay quarterly dividends in respect of periods ending 31 March, 30 June, 30 September and 31 December. The directors anticipate that the first such quarterly dividend be paid for the quarter ending 30 September 2006.

#### Financing Strategy

The Company intends to use borrowings with the objective of enhancing returns to shareholders once substantially all of the net proceeds of the initial issue of shares have been invested, subject to the discretion of the board. Whilst the Company has an unlimited power to borrow, the directors intend to limit borrowing to an amount equal to 240 per cent of the Company's net assets.

#### Shareholder Information

The net asset value per share will be calculated by the administrator, based on information supplied by the investment manager, and announced on a quarterly basis on a regulatory information service and simultaneously announced on the Channel Islands Stock Exchange, generally within fifteen business days after the quarter-end.

The shares are listed on the Channel Islands Stock Exchange and have been admitted to trading on AIM. Shares may be dealt in directly through a stockbroker or professional adviser acting on an investor's behalf. The buying and selling of shares may be settled through CREST.

The Company's register of shareholders is maintained by Anson Registrars Limited in Guernsey and they can be contacted on (44) 01481 711301.

#### Results

The results for the period are set out in the Income Statement on page 13. The directors do not propose declaring a dividend for the period.

#### Directors

The directors' details are given on pages 4. John Le Prevost and Tanguy Boulet were appointed on 17 March 2006 and the remaining Directors appointed on 20 March 2006. Directors' interests in shares are as follows:

| Director                            | Shares  | Percentage of issued share capital |
|-------------------------------------|---------|------------------------------------|
| Robin Monro-Davies                  | 500,000 | 0.5                                |
| Leslie Goodman                      | 20,000  | 0.02                               |
| Tanguy Boulet                       | 30,000  | 0.03                               |
| Juan de Dios Sanchez-Roselly Moreno | 3,000   | 0.003                              |

Mr Tanguy Boulet has an indirect interest in 200,000 (0.20%) shares.

### Directors Remuneration

The directors are entitled to receive fees for their services as directors, such sums not to exceed £200,000 per annum in aggregate. Currently the Chairman receives the sum of £25,000 p.a. and the remaining directors receive the sum of £15,000 p.a. with the exception of Tanguy Boulet who has waived his fee. During the period to 30 June 2006 the Chairman received the sum of £4,520 and the remaining directors received the sum of £2,712 with the exception of Tanguy Boulet who has waived his fee.

### Related Party Transactions

Anson Fund Managers Limited is the Company's administrator and secretary and Anson Registrars Limited is the Company's registrar, transfer agent and paying agent. John R Le Prevost is a director and controller of Anson Fund Managers Limited and of Anson Registrars Limited. €13,601 was paid by the Company to these related parties in the period. €5,763 is due to these related parties at 30 June 2006. In addition, €8,750 was paid for services provided in respect of the launch of the Company.

Tanguy Boulet is a partner in the investment manager, Ocean Capital Associates LLP. €220,276 was payable by the Company to the investment manager in the period and is due to the investment manager at 30 June 2006. In addition, Ocean Capital Associates LLP was reimbursed €26,614 in respect of expenses incurred during the launch of the Company.

During the period €10 million of investments were purchased by the Company from companies of which a partner of the investment manager, Dr Shamil Chandaria, is a director.

### Statement of Directors' Responsibilities

The directors are required to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the Company as at the end of the financial period and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and

- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements have been properly prepared in accordance with The Companies (Guernsey) Law, 1994, as amended. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

### Corporate Governance

As a closed-ended investment company incorporated in Guernsey and listed on the Channel Islands Stock Exchange and admitted to trading on AIM, the Company is not required to comply with the requirements of the Combined Code issued by the UK Listing Authority. The Board has however put in place a framework for corporate governance which it believes is suitable for an investment company of its kind, taking into consideration the Channel Island Stock Exchange Listing Rules and the AIM Rules for Companies.

Furthermore the Company intends, where practicable for a company of its size and nature, to comply with the principles of the Combined Code.

The board plans to meet at least four times a year and between these formal meetings there is regular contact with the secretary and investment manager. The directors are kept fully informed of investment and financial controls and other matters that are relevant to the business of the Company and should be brought to their attention. The directors also have access, where necessary in the furtherance of their duties, to professional advice at the expense of the Company.

The board has a breadth of experience relevant to the Company, and the directors believe that any changes to the board's composition can be managed without undue disruption. With any new director appointment to the board, consideration will be given as to whether an induction process is appropriate.

### **Audit Committee**

An audit committee has been established consisting of all non-executive directors of the board excluding the Chairman, Tanguy Boulet and John Le Prevost. The function of the audit committee is to ensure that the Company maintains high standards of integrity, financial reporting and internal controls. The audit committee examines the effectiveness of the Company's internal control systems, the annual and interim reports and financial statements, the auditors' remuneration and engagement, as well as the auditors' independence and any non-audit services provided by them. The audit committee receives information from the administrator and secretary and from the external auditors as to the objectivity of their audit and their independence.

### **Management Committee**

A management committee has been established consisting of all members of the board excluding Tanguy Boulet and John Le Prevost. The function of the management committee is:

(a) to ensure that the Company's contracts of engagement with the investment manager, administrator, and other service providers are operating satisfactorily so as to ensure the safe and accurate management and administration of the Company's affairs and business and are competitive and reasonable for the shareholders and to make appropriate recommendations to the board; and

(b) to ensure that the Company complies to the best of its ability with applicable laws and regulations and adheres to the tenet of generally accepted codes of conduct.

In addition the chairmanship of the above two committees and each director's performance will be reviewed annually by the chairman and the performance of the chairman will be assessed by the remaining directors.

### **Internal Controls**

The board is responsible for the Company's system of internal control and for reviewing its effectiveness. The board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company. This process has been in place for the period under review and up to the date of approval of this annual report and financial

statements, and is reviewed by the board.

The board has reviewed the effectiveness of the system of internal control. In particular, it has reviewed and updated the process for identifying and evaluating the significant risks affecting the Company and the policies by which these risks are managed.

The internal control systems are designed to meet the Company's particular needs and the risks to which it is exposed. Accordingly, the internal control systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and by their nature can only provide reasonable and not absolute assurance against misstatement and loss.

The Company does not have an internal audit department. All the Company's management and administration functions are delegated to independent third parties and it is therefore felt there is no need for the Company to have an internal audit facility. However, this matter is reviewed periodically.

### **Going Concern**

The directors are satisfied that it is appropriate to continue to adopt the going concern basis in preparing the financial statements as the directors consider that the Company has adequate resources to continue in operational existence for the foreseeable future.

### **By order of the Board**

Robin Monro-Davies  
Chairman

Leslie Goodman  
Director

## CHAIRMAN'S STATEMENT

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.

### 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.

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-Davies, Chairman**  
11 October 2006

## REPORT OF THE INVESTMENT MANAGER

### 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<sup>1</sup> 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 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<sup>2</sup>, 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 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,

<sup>1</sup> Collateralised Bond Obligations/Collateralised Loans Obligations

<sup>2</sup> Figures are based on The International Securitisation Report of July 2006

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 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.

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF EUROPEAN EQUITY TRANCHE INCOME LIMITED

We have audited the financial statements of European Equity Tranche Income Limited for the period ended 30 June 2006 which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement, the Statement of Changes in Shareholders' Equity and related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with Section 64 of The Companies (Guernsey) Law 1994, as amended. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

## Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities the Company's directors are responsible for the preparation of the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted for use in European Union.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements, which have been prepared in accordance with International Financial Reporting Standards, give a true and fair view and are properly prepared in accordance with The Companies (Guernsey) Law 1994, as amended. We also report to you if, in our opinion, the Report of the Directors is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the Company is not disclosed.

We read other information contained in the annual report, and consider whether it is consistent with the

financial statements. This other information comprises the Chairman's Statement and the Report of the Investment Manager. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

## Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

## Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRS as adopted for use in the European Union, of the state of the Company's affairs as at 30 June 2006 and of its profit for the period then ended;
- the financial statements have been properly prepared in accordance with The Companies (Guernsey) Law 1994, as amended; and
- the information given in the Directors' Report is consistent with the financial statements.

Mazars LLP  
Chartered Accountants  
and Registered Auditors  
London, UK

Chandlers Limited  
Chartered Accountants  
Guernsey  
Channel Islands

Date: 13 October 2006

**INCOME STATEMENT**

for the period from incorporation to 30 June 2006

|  | <b>Notes</b> | <b>17 Mar 2006<br/>to 30 Jun 2006</b> |
|--|--------------|---------------------------------------|
|  |              | €                                     |
| Operating income   | 2            | 778,122                               |
| Operating expenses   | 3            | (402,906)                             |
| Net profit for the period                                    |              | <u>375,216</u>                        |
| Basic and diluted earnings per share for the period          | 7            | 0.0061                                |
| Proforma basic and diluted earnings per share for the period | 7            | 0.0037                                |

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

The notes on pages 16 to 22 form an integral part of these financial statements.

**BALANCE SHEET**

as at 30 June 2006

|   | Notes | €                 | €                        |
|---|-------|-------------------|--------------------------|
| <b>ASSETS</b>   |       |                   |                          |
| <b>Non-current assets</b>   |       |                   |                          |
| Investments designated at fair value through the income statement | 8     |                   | 55,104,283               |
| <b>Current assets</b>   |       |                   |                          |
| Trade and other receivables                                       | 9     | 608,025           |                          |
| Cash at bank  | 10    | <u>42,663,014</u> |                          |
|   |       |                   | 43,271,039               |
| <b>Total assets</b>   |       |                   | <u><u>98,375,322</u></u> |
| <b>EQUITY AND LIABILITIES</b>                                     |       |                   |                          |
| <b>Equity</b>   |       |                   |                          |
| Issued capital  | 11    | -                 |                          |
| Share premium   | 12    | 50,000,000        |                          |
| Retained earnings   | 12    | <u>48,051,553</u> |                          |
|   |       |                   | 98,051,553               |
| <b>Current liabilities</b>  |       |                   |                          |
| Trade and other payables  | 13    |                   | 323,769                  |
| <b>Total equity and liabilities</b>                               |       |                   | <u><u>98,375,322</u></u> |

The financial statements were approved by the Board of directors on 11 October 2006 and are signed on its behalf by:

Robin Monro-Davies  
Director

Leslie Goodman  
Director

The notes on pages 16 to 22 form an integral part of these financial statements.

**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               | <u>(55,104,283)</u> |

**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 | <u>(2,323,663)</u> |

**Net cash flow from financing activities** 97,676,337**Cash and cash equivalents at the beginning of the period**

-

Net increase in cash and cash equivalents 42,663,014**Cash and cash equivalents at the end of the period**42,663,014**STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**

for the period from incorporation to 30 June 2006

**Notes**

€

**Balance at the beginning of the period**

-

|                       |                |
|-----------------------|----------------|
| Formation expenses    | (2,323,663)    |
| Profit for the period | <u>375,216</u> |

**Total recognised income and expenses for the period** (1,948,447)Share premium on issue of shares 11 100,000,000**Balance at 30 June 2006**98,051,553

The notes on pages 16 to 22 form an integral part of these financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

as at 30 June 2006

## I ACCOUNTING POLICIES

### (a) Basis of Preparation

The financial statements of European Equity Tranche Income Limited, a closed-ended investment company in Guernsey, Channel Islands have been prepared in conformity with International Financial Reporting Standards issued by the International Accounting Standards Board, as adopted by the European Union, and the Interpretations of International Financial Reporting Standards issued by the Standing Interpretations Committee of the International Accounting Standards Board and applicable requirements of Guernsey Law.

The financial statements have been prepared on an historical cost basis except for the measurement at fair value of investments designated at fair value through the income statement. The accounting policies have been applied consistently by the Company in the accounting period which is from incorporation on 17 March 2006 to 30 June 2006. The financial statements have been prepared in its functional currency, Euro, as this reflects the Company's primary activity of investing in Euro financial instruments. The Company has not implemented IFRS 7 "Financial Instruments: Disclosures", as this standard is only effective for accounting periods beginning on or after 1 January 2007. The standard is expected to have a negligible effect on the Company's financial statements when adopted.

The preparation of financial statements in conformity with IFRS requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### (b) Foreign currencies

Transactions in foreign currencies are translated into euros, which is deemed to be the functional currency, at the rates of exchange ruling on the date on which the transactions occur. At the balance sheet date, foreign currency monetary items are translated into euros at the foreign exchange rate ruling at the balance sheet date. Foreign exchange differences arising on translation are recognised in the income statement in the period in which they arise. At the balance sheet

date, non-monetary items which are carried at fair value denominated in foreign currency are reported using the exchange rates that existed at the date when the fair values were determined.

### (c) Interest income

Interest income is accounted for on an accruals basis on cash and cash equivalents. Premiums and discounts associated with the purchase of financial assets are amortised or accreted into interest income over the projected lives of the investments using the effective interest method as defined under IAS 39 "Financial Instruments: Recognition and Measurement". The Company's policy for estimating prepayment speeds for calculating the effective yield is to evaluate historical performance, market consensus indicators and current market conditions.

### (d) Formation expenses

Formation expenses are deducted from share premium.

### (e) Fair Value of Financial instruments

Under IAS 39, the Company's investments are measured initially at cost, which is the fair value of whatever was paid to acquire them. Associated transaction costs are written off to the income statement. All purchases and sales of investments are recognised using trade date accounting. After initial recognition the Company's investments are measured at fair value through the income statement. The Company's investments are designated to this category at inception.

Investments are fair valued using quoted market prices, independent appraisals, discounted cash flow analysis or other appropriate valuation models at the balance sheet date by the investment manager. The investment manager uses financial pricing models that reflect numerous factors including the investment manager's assessment of the nature of the investment and the collateral, security position, risk profile, historical default rates and the originator and servicer. Each of these factors involves subjective judgements and forward-looking determinations by the investment manager.

### (f) Cash and cash equivalents

Cash and cash equivalents are carried at cost. Cash

and cash equivalents are defined as cash and deposits at bank.

**(g) Trade and other receivables and payables**

Trade and other receivables and payables are carried at cost.

**(h) Taxation**

The Company has been granted exemption under the Income Tax (Exempt Bodies) (Guernsey) Ordinance, 1989 from Guernsey Income Tax, and is charged an annual fee of £600.

**(i) Earnings per share**

The Company calculates both basic and diluted earnings per share in accordance with IAS 33 'Earnings per share'. Under IAS 33 basic earnings per share is computed using the weighted average number of shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of shares outstanding during the period plus the dilutive effect of any instruments outstanding during the period.

**(j) Segmental reporting**

In the opinion of the directors the Company has only one business segment.

| <b>2 OPERATING INCOME</b>                          | <b>17 Mar 2006<br/>to 30 Jun 2006</b> |
|--|---------------------------------------|
|  | €                                     |
| Interest on investments in asset backed securities | 479,266                               |
| Interest from cash and cash equivalents            | <u>298,856</u>                        |
|  | <u><u>778,122</u></u>                 |

| <b>3 OPERATING EXPENSES</b>      | <b>17 Mar 2006<br/>to 30 Jun 2006</b> |
|----------------------------------|---------------------------------------|
|                                  | €                                     |
| Investment managers fees         | 220,276                               |
| Directors' remuneration          | 22,388                                |
| Directors expenses               | 518                                   |
| Directors and Officers insurance | 5,274                                 |
| Audit fees                       | 50,226                                |
| Investment transaction costs     | 42,475                                |
| Administration fees              | 10,672                                |
| Registration fees                | 2,929                                 |
| Other operating expenses         | <u>48,148</u>                         |
|                                  | <u><u>402,906</u></u>                 |

In addition, one of the joint auditors, Mazars, was paid £35,000 as Reporting Accountants during the AIM listing.

## 4 INVESTMENT MANAGERS FEES

### Management Fee

Under the terms of the Investment Management Agreement, a management fee is payable to the Investment Manager at an annual rate of 1.25 per cent of the lower of (i) the Net Asset Value of the Company immediately following Admission and (ii) the Net Asset Value of the Company on 31 March, 30 June, 30 September and 31 December (before deduction of accruals in respect of the management fee for the current period and any performance fee) (excluding current period income).

The management fee accrues daily and is payable quarterly in arrears.

### Performance Fee

Under the terms of the Investment Management Agreement, the Investment Manager is entitled to receive a performance related fee in respect of each performance period which will be paid quarterly in arrears.

A performance period will comprise each successive quarter, except the first such period shall be the period from Admission to 30 June 2006

The performance fee for each performance period will be an amount equal to 20 per cent of the amount by which the Company's net income (as calculated for these purposes) after tax for the relevant period, before payment of any performance fee, exceeds an amount equal to a simple interest rate of two per cent per quarter (the "quarterly hurdle") multiplied by the weighted average number of Ordinary Shares outstanding during the relevant period multiplied by the weighted average offer price of such Ordinary Shares, subject to the Net Asset Value of an Ordinary Share at the end of the relevant performance period being no less than the Net Asset Value of an Ordinary Share immediately following Admission.

The sum of quarterly performance fees based on the quarterly hurdle payable to the Investment Manager for any full financial period will be capped at that amount which would be payable based on 20 per cent of the amount by which the Company's net income after tax for the relevant period (before payment of any performance fees) exceeds an amount equal to an annualised simple interest rate of 8 per

cent (the annual hurdle) multiplied by the weighted average number of Ordinary Shares outstanding during the relevant full financial period multiplied by the weighted average offer price of such Ordinary Shares.

Where the sum of quarterly performance fees paid for any financial period based on the quarterly hurdle exceeds that amount which would have been payable based on the annual hurdle, the Investment Manager shall repay to the Company any such excess.

The performance fee, if any, will be calculated on behalf of the Company by the Administrator.

Where there is a difference between the Company's net income for the relevant performance period as shown in the Company's quarterly management accounts compared to the Company's audited annual accounts, the net income for the relevant performance period as reflected in the audited accounts shall prevail. Any excess performance fee paid or any additional performance fee due in respect of any performance period attributable to any such difference will be repaid by or paid to the Investment Manager, as the case may be.

## 5 STAFF COSTS

The Company has no employees other than the directors. Directors' expenses totalled €518 in the period.

## 6 DIRECTORS' REMUNERATION

Unless otherwise decided by the Company by ordinary resolution, the Company shall pay to the directors (but not alternate directors) for their services as directors out of the funds of the Company by way of fees such sums as the board decides (not exceeding £200,000 per annum in aggregate or such larger amount as the Company may by ordinary resolution decide). The aggregate fees will be divided among the directors in such proportions as the board decides or, if no decision is made, equally. Directors remuneration totalled €22,388 in the period.

## 7 EARNINGS PER SHARE

The earnings per share is based on the net profit for the period of €375,216 and on 61,904,761 shares, being the weighted average number of shares in issue

during the period. There were no dilutive instruments in issue in the period.

Proforma basic and diluted earnings per share is based on the same net profit and 100,000,000 shares in issue i.e. the number of shares is not adjusted for the prelisting period when the Company did not trade.

| <b>8 INVESTMENTS DESIGNATED AS FAIR VALUE THROUGH THE INCOME STATEMENT</b> | <b>30 Jun 2006</b> |
|--|--------------------|
|  | €                  |
| Investments  |                    |
| Additions - Cost   | 55,343,773         |
| Capital repayments   | <u>(239,490)</u>   |
|  | <u>55,104,283</u>  |

The weighted average floating interest rate on these investments in the period was 10.5%.

Although investments in residual income positions have been treated as floating rate investments in the schedule above, income derived from these investments is based on their expected internal rate of return (IRR) over their estimated life. These IRR reflect a number of collateral performance and other assumptions, which may be adjusted over time.

| <b>9 TRADE AND OTHER RECEIVABLES</b> | <b>30 Jun 2006</b> |
|--------------------------------------|--------------------|
|                                      | €                  |
| Prepayments                          | 27,071             |
| Accrued interest - Investments       | 488,548            |
| Accrued interest - Cash              | <u>92,406</u>      |
|                                      | <u>608,025</u>     |

| <b>10 CASH AT BANK</b> | €                 |
|------------------------|-------------------|
| Bank balances          | 2,442,256         |
| Call deposits          | <u>40,220,758</u> |
|                        | <u>42,663,014</u> |

The weighted average floating interest rate on call deposits was 2.54%. Call deposits are due on demand.

| <b>I I SHARE CAPITAL</b>                                    |                         |                          | <b>30 Jun 2006</b>                       |
|---|-------------------------|--------------------------|--|
|   |                         |                          | €  |
|   |                         |                          | <b>Authorised, issued and fully paid</b> |
| 100,000,000 ordinary shares of no par value                 |                         |                          | -  |
| <b>The issues of Ordinary Shares took place as follows:</b> |                         |                          |  |
| <b>Date of issue</b>  | <b>Number of shares</b> | <b>Price per share €</b> | <b>Amount received</b>                   |
| 17 March 2006   | 2                       | 1                        | 2  |
| 26 April 2006   | <u>99,999,998</u>       | 1                        | <u>99,999,998</u>                        |
|   | <u>100,000,000</u>      |                          | <u>100,000,000</u>                       |

As the Company will have only one class of shares, the holders of its shares will under general law be entitled to participate in any surplus assets in a winding-up in proportion to their shareholdings.

The Company has passed a special resolution reducing the amount standing to the credit of the share premium account to €50,000,000, and that the surplus created form a distributable reserve. In accordance with The Companies (Guernsey) Law, 1994 (as amended) (the "Companies Law"), the Directors applied to the Royal Court of Guernsey for an order confirming such reduction of the share premium account following admission. The distributable reserve created on cancellation is available as distributable profits to be used for all purposes permitted by the Companies Law, including the buy back of Ordinary Shares and the payment of dividends.

| <b>I2 RESERVES</b>                 |                      |                          |                    |
|------------------------------------|----------------------|--------------------------|--------------------|
|                                    | <b>Share premium</b> | <b>Retained earnings</b> | <b>Total</b>       |
|                                    | €                    | €                        | <b>30 Jun 2006</b> |
|                                    |                      |                          | €                  |
| Issue of capital                   | 100,000,000          | -                        | 100,000,000        |
| Formation expenses                 | (2,323,663)          |                          | (2,323,663)        |
| Net profit for the period          | -                    | 375,216                  | 375,216            |
|                                    | <u>97,676,337</u>    | 375,216                  | <u>98,051,553</u>  |
| Transfer to distributable reserves | (47,676,337)         | 47,676,337               | -                  |
|                                    | <u>50,000,000</u>    | 48,051,553               | <u>98,051,553</u>  |

| <b>13 TRADE AND OTHER PAYABLES</b> | <b>30 Jun 2006</b> |
|------------------------------------|--------------------|
|                                    | €                  |
| Accrued investment managers fees   | 220,276            |
| Accrued audit fees                 | 50,226             |
| Accrued administration fees        | 5,022              |
| Accrued registration fees          | 741                |
| Other accrued expenses             | 35,279             |
| Accrued transaction costs          | 12,225             |
|                                    | <hr/>              |
|                                    | 323,769            |
|                                    | <hr/> <hr/>        |

## 14 FINANCIAL INSTRUMENTS

The Company's main financial instruments comprise:

- (a) Cash and cash equivalents that arise directly from the Company's operations; and
- (b) Non-investment grade and equity tranches of RMBS in Europe.

## 15 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The most important types of risks to which the Company is exposed are market price risk, credit risk, liquidity risk, interest rate risk, residual interest risk and currency risk. Save where the Company purchases synthetic securities to gain exposure to an underlying cash asset or assets, derivative transactions will only be used for the purposes of hedging risks or for efficient portfolio management. The Company will not enter into derivative transactions for speculative purposes.

### (a) Market Price Risk

The Company's exposure to market risk is comprised mainly of movements in the value of its investments and, to the extent that the Company utilises leverage, changes in interest rates that either increase its cost of borrowing or decrease any interest income. Several of the Company's investments will be floating rate or backed by floating rate assets and, as such, will be valued based on a market credit spread over a benchmark (such as EURIBOR). Increases in the credit spreads above such benchmarks may affect the Company's net equity or net income directly through their impact on unrealised gains or losses on investments within the portfolio, and therefore the Company's ability to make gains on such investments, or indirectly through their impact on the Company's

ability to borrow and access capital.

Details of the Company's Investment Objective and Policy are given on page 3.

### (b) Credit Risk

Credit risk refers to each individual borrower's ability to make the required interest and principal payments on the scheduled due dates. The Company seeks to mitigate credit risk by actively monitoring its portfolio of investments and the underlying credit quality of its holdings. The Company seeks to minimise credit risk further by ensuring its investment portfolio is diversified by geography, originator, servicer and issuer. The Company does not intend to undertake any credit hedging activities other than from time to time entering into transactions to hedge its credit exposure in relation to individual investments.

### (c) Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in realising assets or otherwise raising funds to meet financial commitments. The market for subordinated asset-backed securities, including residual income positions, is illiquid. Accordingly, many of the Company's investments are illiquid. In addition, investments that the Company purchases in privately negotiated (also called "over the counter" or "OTC") transactions may not be registered under relevant securities laws or otherwise may not be freely tradable, resulting in restrictions on their transfer, sale, pledge or other disposition except in a transaction that is exempt from the registration requirements of, or is otherwise in accordance with, those laws. As a result of this illiquidity, the Company's ability to vary its portfolio in a timely

fashion and to receive a fair price in response to changes in economic and other conditions may be limited.

Furthermore, where the Company acquires investments for which there is not a readily available market, the Company's ability to deal in any such investment or obtain reliable information about the value of such investment or risks to which such investment is exposed may be limited.

All the Company's financial assets, other than cash, have a remaining maturity of over 5 years.

#### **(d) Interest Rate Risk**

Changes in interest rates can affect, among other things, the Company's ability to acquire loans and investments, the value of its investments and the Company's ability to realise gains from the settlement of such assets.

#### **(e) Residual Interest Risk**

The majority of the Company's investments consist of interests in and/or economic exposures to limited recourse securities that are subordinated in right of payment and ranked junior to other securities that are secured by or represent ownership in the same pool of assets. In the event of default by an issuer in relation to such investments, holders of the issuer's more senior securities are entitled to payments in priority to the Company. Some of the Company's investments also have structural features that divert payments of interest and/or principal to more senior classes of securities secured by or representing ownership in the same pool of assets when the delinquency or loss experience of the pool exceeds certain levels. This may lead to interruptions in the income stream that the Company anticipates receiving from its investment portfolio, which may lead to the Company having less income to distribute to shareholders.

Although holders of asset-backed securities generally have the benefit of first ranking security (or other priority rights) over any collateral, control of the timing and manner of the disposal of such collateral upon a default typically will devolve to the holders of the senior class of securities outstanding. There can be no assurance that the proceeds of any such sale of collateral will be adequate to repay in full the Company's investments.

#### **(f) Currency Risk**

The Company's accounts will be denominated in euros while investments may be made and realised in both euros and sterling. Changes in rates of exchange may have an adverse effect on the value, price or income of the investments. A change in foreign currency exchange rates may adversely impact returns on the Company's non-euro-denominated investments.

The Company will seek to reduce the currency risk by financing investments in the same currency as the relevant investment where commercially practical or enter into hedging transactions for whole or part of the currency exposure. The investment manager may elect, however, to have the Company bear a level of currency risk that could otherwise be hedged where it considers that bearing such risks is acceptable.

At the balance sheet date the Company has no material financial assets or liabilities not denominated in euros.

## **16 RELATED PARTY TRANSACTIONS**

Anson Fund Managers Limited is the Company's administrator and secretary and Anson Registrars Limited is the Company's registrar, transfer agent and paying agent. John R Le Prevost is a director and controller of Anson Fund Managers Limited and of Anson Registrars Limited. €13,601 of fees were incurred by the Company with these related parties in the period, of which €5,763 was due to these related parties as at 30 June 2006. In addition, €8,750 was paid for services provided in respect of the launch of the Company.

Tanguy Boulet is a partner in the investment manager, Ocean Capital Associates LLP. €220,276 in fees was incurred by the Company with the investment manager in the period, of which €220,276 was due to the investment manager as at 30 June 2006. In addition, Ocean Capital Associates LLP was reimbursed €26,614 in respect of expenses incurred during the launch of the Company.

The Directors were reimbursed the sum of €1,361 for expenses incurred during the launch of the Company.

During the period €10 million of investments were purchased by the Company from a company of which a partner in the investment manager, Dr Shamil Chandaria, is a director.

## SHAREHOLDER INFORMATION

The Company announces the estimated net asset value per share on a quarterly basis.

Shares are listed on the Channel Islands Stock Exchange and traded through AIM. Shares may be dealt directly through a stockbroker or professional adviser acting on an investor's behalf. The buying and selling of shares may be settled through CREST.

The Company's register of shareholders is maintained by Anson Registrars Limited in Guernsey and they can be contacted on (44) 01481 711301.

## DIRECTORS AND SERVICE PROVIDERS

European Equity Tranche Income Limited, Registered in Guernsey No. 44552

### Directors

Anthony Robin Dominic Monro-Davies (*Chairman*)  
Leslie David Goodman  
John Reginald Le Prevost  
Francoise Adeline Henry  
Tanguy Patrice Marie Dominique Boulet  
Juan de Dios Sanchez-Roselly Moreno

### Registered Office of the Company

Anson House  
St George's Place  
St George's Esplanade  
St Peter Port  
Guernsey  
GY1 2BE  
Telephone +44 (0)1481 722260

### Administrator and Company Secretary

Anson Fund Managers Limited  
PO Box 405  
Anson House  
St George's Place  
St George's Esplanade  
St Peter Port  
Guernsey  
GY1 3GF

### Investment Manager

Ocean Capital Associates LLP  
47 Curzon Street  
London  
England  
W1J 7UJ

### Nominated Adviser and Broker

Arbuthnot Securities Limited  
Arbuthnot House  
29 Ropemaker Street  
London  
England  
EC2Y 9ARL

### Joint Auditors

Mazars LLP  
24 Bevis Marks  
London  
England  
EC3A 7NR

Chandlers Limited  
PO Box 313  
Anson Court  
La Route des Camps  
St Martins  
Guernsey  
GY1 3TF

**Sponsor to CISX Listing**

Ogier Corporate Finance Limited  
Whiteley Chambers  
Don Street  
St Helier  
Jersey  
JE4 9WG

**Principal Bankers**

Royal Bank of Scotland International Limited  
Guernsey Branch  
PO Box 62  
Royal Bank Place  
I Glatigny Esplanade  
St Peter Port  
Guernsey  
GY1 4BQ

**Registrar, Transfer Agent, Paying Agent and Receiving Agent**

Anson Registrars Limited  
PO Box 426  
Anson House  
St Georges Esplanade  
St Peter Port  
Guernsey  
GY1 3WX

**UK Transfer Agent and Paying Agent**

Anson Administration (UK) Limited  
Enterprise House  
Ocean Village  
Southampton  
Hampshire  
England  
SO14 3XB

**Custodian**

RBSI Trustee Services (Guernsey) Limited  
PO Box 62  
Royal Bank Place  
I Glatigny Esplanade  
St Peter Port  
Guernsey  
GY1 4BQ

# NOTICE OF ANNUAL GENERAL MEETING

European Equity Tranche Income Limited. Registered in Guernsey No. 44552

## Notice of Annual General Meeting

NOTICE IS HEREBY GIVEN that the ANNUAL GENERAL MEETING of the voting Members of European Equity Tranche Income Limited (the "Company") will be held at Anson House, St George's Place, St Georges Esplanade, St Peter Port, Guernsey, Channel Islands GY1 2BE on 16 November 2006 at 10.00 a.m., for the following purposes:

### Ordinary Business:

1. To receive the Report of the Directors and the audited financial statements for the period from incorporation to 30 June 2006.
2. To reappoint the joint auditors Mazars LLP and Chandlers Limited to hold office from the conclusion of this meeting until the conclusion of the next Annual General Meeting and to authorise the Board to agree their remuneration as Auditors to the Company.
3. To re-elect Mr John R Le Prevost as a director.
4. To re-elect Mr Tanguy Boulet as a director.
5. To approve the Company's investing strategy (in accordance with the AIM Rules and the requirements of the CISX) as follows:

"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."

6. To authorise the Directors until the next Annual General Meeting of the Company at their discretion to buy back up to 14.99% of all Shares currently in issue.

### BY ORDER OF THE BOARD

Anson Fund Managers Limited  
Company Secretary

11 October 2006

### Registered Office:

Anson House, St George's Place,  
St Georges Esplanade,  
St Peter Port,  
Guernsey,  
Channel Islands.

#### Notes:

- Ordinary Resolutions: These resolutions require a simple majority of the votes cast by those Shareholders voting in person or by proxy at the Annual General Meeting to be passed.
- A member entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and vote instead of him or her. A proxy need not be a member of the Company. Completion and return of the form of proxy will not preclude members from attending or voting at the meeting, if they so wish.
- To be valid the Form of Proxy, together with the power of attorney or other authority, if any, under which it is executed (or a notarially certified copy of such power of authority) must be deposited with the Company's agent, for this purpose being, Anson Registrars Limited, PO Box 426, Anson House, St George's Place, St Georges Esplanade, St Peter Port, Guernsey, C.I. GY1 3WX, not less than 48 hours before the time for holding the meeting. A Form of Proxy is enclosed with this Notice.
- None of the Directors has a contract of service with the Company

## FORM OF PROXY

European Equity Tranche Income Limited. Registered in Guernsey No. 44552

**FOR USE BY HOLDERS OF ORDINARY SHARES AT THE ANNUAL GENERAL MEETING OF EUROPEAN EQUITY TRANCHE INCOME LIMITED (THE "COMPANY") CONVENED FOR 16 NOVEMBER 2006 AND AT ANY ADJOURNMENT THEREOF:**

I/WE ..... (Block Letters)

OF ..... (Block Letters)

being [a] member[s] of the above named Company in respect of \*.....Shares, hereby appoint the Chairman of the Meeting \*\*or ..... as my/our proxy to vote for me/us on my/our behalf, as directed below on the Ordinary Resolutions to be proposed at the Annual General Meeting of the Company to be held at Anson House, St George's Place, St Georges Esplanade, St Peter Port, Guernsey at 10.00 a.m. on 16 November 2006, and at any adjournment thereof.

Notes: \*If no number is inserted voting will be applied to your total holding. \*\*If it is desired to appoint as proxy any person other than the Chairman of the Meeting, his/her name and address should be inserted in the relevant place and reference to the Chairman of the meeting deleted and the alternation initialled.

I/WE direct the proxy to vote on the Resolutions as follows:

| <b>ORDINARY RESOLUTIONS:</b>   | <b>FOR</b> | <b>AGAINST</b> |
|--|------------|----------------|
| <b>1.</b> To receive the Report of the Directors and the audited financial statements for the period from incorporation to 30 June 2006.   |            |                |
| <b>2.</b> To reappoint the joint auditors Mazars LLP and Chandlers LLP to hold office from the conclusion of this meeting until the conclusion of the next Annual General Meeting and to authorise the Board to agree their remuneration as Auditors to the Company.   |            |                |
| <b>3.</b> To re-elect Mr John R Le Prevost as a director.  |            |                |
| <b>4.</b> To re-elect Mr Tanguy Boulet as a director.  |            |                |
| <b>5.</b> To approve the Company's investment strategy (in accordance with the AIM Rules and the requirements of the CISX).<br>"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." |            |                |
| <b>6.</b> To authorise the Directors until the next Annual General Meeting of the Company at their discretion to buy back up to 14.99% of all Shares currently in issue.   |            |                |

Please indicate with an X in the appropriate space how you wish your vote to be cast. On receipt of the form duly executed and in the absence of a specific direction, your proxy will vote or abstain as he or she thinks fit on the resolutions.

Signed:

Dated:

Notes:

1. If the shareholder is a Corporation, this form must be executed under its common seal or under the hand of its duly authorised officer or attorney.
2. In the case of joint members, the vote of the senior who tenders a vote, whether in person, or by proxy, will be accepted to the exclusion of the votes of the other joint holders. For this purpose, seniority is determined by the order in which the names stand in the Register of Members in respect of the joint holding.
3. Any alterations to this proxy should be initialled by the person who signs it.

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