EUROCASTLE INVESTMENT LIMITED

2006 ANNUAL REPORT

'06

COMPANY OVERVIEW

EUROCASTLE INVESTMENT LIMITED OWNS AND INVESTS PRIMARILY IN GERMAN COMMERCIAL PROPERTY. THE COMPANY IS EURO DENOMINATED AND CURRENTLY LISTED ON EURONEXT AMSTERDAM UNDER THE SYMBOL "ECT." EUROCASTLE'S OBJECTIVE IS TO BUILD LONG-TERM VALUE FOR ITS SHAREHOLDERS AND TO PAY OUT STABLE AND GROWING DIVIDENDS. EUROCASTLE IS MANAGED BY AN AFFILIATE OF FORTRESS INVESTMENT GROUP LLC.

Contents

Financial and Operational Highlights 1
Letter to Our Shareholders 2
Who We Are 4
Our Strategy 5
Our Competitive Strengths 6
Business Review 9
Investment Property—Data 11
Financing 18
Financial Review 19
Report of the Directors 26
Independent Auditors' Report 29
Consolidated Income Statement 30
Consolidated Balance Sheet 31
Consolidated Statement of Cash Flows 32
Consolidated Statement of Changes in Equity . . . 33
Notes to Consolidated Financial Statements 34
Corporate Information . . . . IBC

FINANCIAL AND OPERATIONAL HIGHLIGHTS

Funds From Operations [1]
up 137% to €74.7 million
(2005: €31.6 million)

137%

[1] *See definition on page 21.*

Dividend Per Share
up 16% from €0.37 in Q4 '05 to
€0.43 in Q4 '06

16%

Net Profit After Tax
of €143.8 million
(2005: €39.7 million)

€143.8 million

Total Assets
up 149% to €5.7 billion
(2005: €2.3 billion)

149%

German Property Portfolio
grew to €3.3 billion
(2005: €0.5 billion)

€3.3 billion

Key Highlights;

- Acquired €2.8 billion of German commercial properties
- Agreed to acquire €2.2 billion of German commercial properties (completed by end of February 2007)
- Signed nearly 200 new leases for approximately 45,600 square meters
- Raised €1.2 billion of new equity capital

LETTER TO OUR SHAREHOLDERS

2006 was a year of dramatic and exciting growth for Eurocastle. Our German commercial property portfolio increased by €2.8 billion to €3.3 billion. Including year-end agreements to acquire a further €2.2 billion of German commercial properties which we completed in February 2007, the portfolio now stands at €5.5 billion. We raised our 4th quarter dividend by 16% compared to the fourth quarter 2005, more than doubled our capital base, and expanded our board of directors. Compared to 2005, our Funds from Operations (FFO) increased 137%, operating profit before taxation increased 252% and net asset value doubled to €24.73 per share.

Our €5.5 billion German commercial property portfolio consists of 617 properties, with approximately 2.5 million square meters of lettable space. Today, we are one of the largest owners of German commercial real estate among listed property investment companies. Our size and presence in all major office markets in Germany give us a competitive advantage in identifying new acquisition opportunities, particularly in the major metropolitan markets. The German commercial property market continues to be active and with this competitive advantage we are confident that the portfolio will continue to grow in 2007.

Our objective is to build long-term value by delivering stable and growing dividends through a combination of accretive acquisitions and organic growth. Our dividend policy is to pay out substantially all of our FFO in the form of quarterly dividends. We believe this provides the greatest level of transparency to our shareholders, as well as imposing terrific investment discipline with respect to new investments.

Given our rapid growth and commitment to strong corporate governance, we felt that the business would benefit from a broader range of experience and expertise at the board level. During the year we were very pleased to welcome Dr. Udo Scheffel, Dr. Simon Thornton and Mr. Randal Nardone, increasing the board from three to six directors.

We think the best is yet to come—the recovery of the German commercial property market has begun. Greater demand from tenants for office space has translated into increased portfolio occupancy. Along with rising market rents, these were the two main drivers of organic growth in the portfolio during 2006. With our strong asset management team we are well positioned to capitalize on the recovering commercial property market and expect to see further growth in our FFO through increased occupancy and rental growth.

By every measure, 2006 was a tremendous year and we are in great shape for 2007. With a solid investment portfolio of high quality real estate and excellent prospects for new investments, we believe that our disciplined business model and focus on long-term profitability will continue to attract investor interest and set us apart in the years to come.

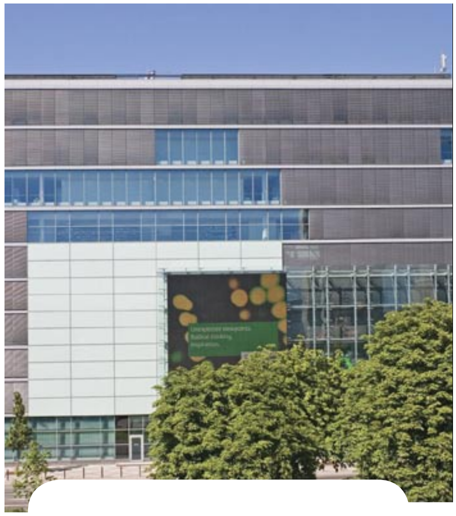
We are very excited about the future at Eurocastle and we look forward to 2007 as another year of significant growth.

Wesley R. Edens

Chairman

OPPORTUNITY

WHO WE ARE: EUROCASTLE INVESTMENT LIMITED is incorporated in Guernsey and its core business is the acquisition, ownership and management of high quality German commercial properties. Following the acquisition of a €2.1 billion commercial property portfolio (Mars) at the end of February 2007, Eurocastle's German commercial property portfolio now totals €5.5 billion and consists of 617 properties with approximately 2.5 million square meters of lettable space. In addition, Eurocastle invests in real estate related debt which is complementary to its core business. The Company has a tax efficient structure with no taxation at the holding company level and no withholding on its dividend distributions to shareholders. Eurocastle's shares currently trade on Eurolist by Euronext Amsterdam and are expected to list on the Frankfurt Stock Exchange in 2007.



20%

ORGANIC GROWTH + ACCRETIVE GROWTH = ANNUAL GROWTH

OUR STRATEGY

EUROCASTLE'S OBJECTIVE IS TO BUILD LONG-TERM VALUE FOR ITS SHAREHOLDERS. OUR INTENTION IS TO INCREASE FUNDS FROM OPERATIONS THROUGH A COMBINATION OF ORGANIC AND ACCRETIVE GROWTH AND TO PAY OUT SUBSTANTIALLY ALL OF THIS IN THE FORM OF QUARTERLY DIVIDENDS. OUR STRATEGY FOR ACHIEVING THIS OBJECTIVE IS AS FOLLOWS:

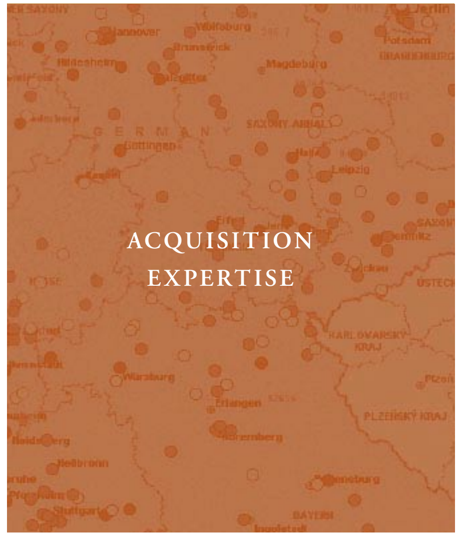
Increasing Returns from Current Commercial Property Portfolio

We will seek to continue increasing returns from our portfolio through active asset management. Increasing portfolio occupancy will not only generate additional rental income but also reduce Eurocastle's net operating expenses. With an average occupancy of approximately 87% across the portfolio, there continues to be significant potential for organic growth. Our dedicated asset management advisory team in Germany closely monitors the properties, proactively seeking out new tenants. In 2006, we signed nearly 200 new leases for approximately 45,600 square meters. We believe that further organic growth can be achieved through increases in market rents, as well as from indexation of existing leases.

Growing Our Commercial Property Portfolio in Germany

We will seek to continue taking advantage of the trend of banks, open-ended funds and corporates selling their commercial property by targeting larger portfolio acquisitions, as well as smaller-sized transactions in Germany. We intend to pursue acquisitions which we perceive to be earnings accretive, and our acquisition strategy will focus on German commercial property with stable income and the potential to provide earnings upside through active asset management. Since December 2004, we have acquired approximately €5.5 billion (including €2.2 billion completed in February 2007) of commercial property in Germany. We use a combination of debt and equity to finance our acquisitions and we currently target leverage levels of approximately 75% of the gross asset value, although we may choose to utilize higher or lower leverage levels where appropriate. In addition, we will seek to take advantage of opportunities to invest in the real estate debt business but expect that it will represent a decreasing proportion of the Group's total assets and net income.

IN-DEPTH MARKET KNOWLEDGE



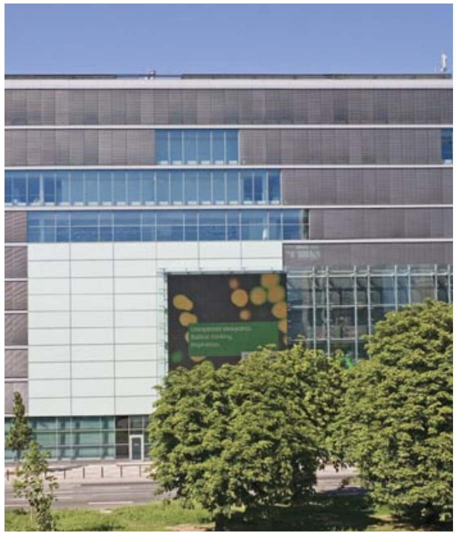
OUR COMPETITIVE STRENGTHS

THE COMBINATION OF OUR SIZE, NATIONWIDE PRESENCE AND REPUTATION MAKES US A LEADING PLAYER IN THE GERMAN COMMERCIAL PROPERTY MARKET AND POSITIONS US WELL TO ACHIEVE OUR OBJECTIVES. OUR STRENGTHS INCLUDE:

In-Depth Market Knowledge

Our significant presence in the major German office markets gives us a competitive advantage over smaller, less diversified investors. Our active asset management gives us insight into local market conditions and activity throughout Germany which enables us to identify, evaluate and acquire both smaller and more frequent off-market deals as well as large and complex portfolios.

STRONG
MANAGEMENT
TEAM



ACCESS TO
CAPITAL RESOURCES

Acquisition Expertise

Our local Investment Manager's presence in Germany gives us strong local sourcing and execution capabilities. Having acquired over 600 commercial property assets, our experience encompasses large, small and complex transactions. We are a respected trade buyer in Germany and our acquisition experience positions us well to continue to make successful and accretive acquisitions.

Strong Management Team

The principals and employees of our Investment Manager, an affiliate of Fortress Investment Group LLC, and its subsidiaries in Germany have significant experience in sourcing, pricing, financing and overseeing the management of real estate assets worldwide and in particular in Germany. Our Investment Manager employs over 50 real estate professionals in Germany who have comprehensive industry expertise and enable us to add significant value to our investments and facilitate the selection of only those investments that meet our return and quality criteria.

Access to Capital Resources

We have benefited from our Investment Manager's financing expertise and experience. Fortress Investment Group LLC has extensive access to debt and equity markets, which enabled Eurocastle to raise additional debt financing of €2.1 billion and new equity capital of €1.2 billion during 2006.

Expansion

BUSINESS REVIEW

€5.5 BILLION PORTFOLIO[1]

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617 PROPERTIES

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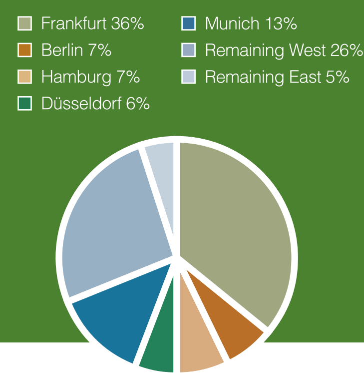
2.5 MILLION M² LEASEABLE SPACE

PROPERTY PORTFOLIO BREAKDOWN BY USE[1]

PROPERTY PORTFOLIO BREAKDOWN BY LOCATION[1]

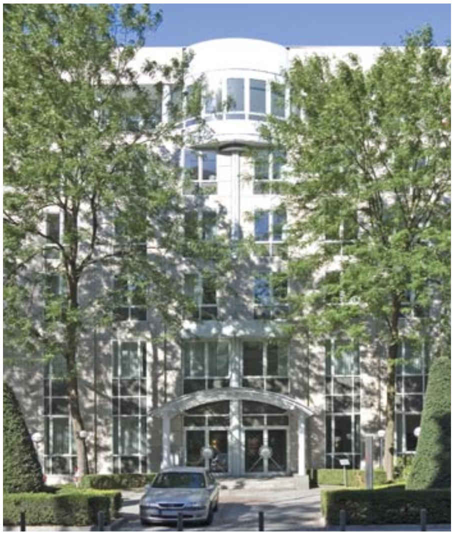


[1]*Includes Mars acquisition completed in February 2007.*

In 2006, Eurocastle grew its real estate investment portfolio by €2.8 billion from €0.7 billion to €3.5 billion, acquiring high quality office and retail property portfolios throughout Germany and transforming itself into a company that primarily owns German commercial properties. The Company continues to see opportunities to acquire high quality office and retail properties, particularly in the major metropolitan markets in Germany.

In December 2006, Eurocastle entered into an agreement to acquire a €2.1 billion property portfolio (Mars) comprising of 56 German commercial real estate assets from an open-ended fund. Following the completion of this portfolio acquisition at the end of February 2007, Eurocastle's German commercial real estate investment portfolio totals €5.5 billion and consist of 617 properties and approximately 2.5 million square meters of lettable space. The Mars transaction will be accounted for in the year ending 31 December 2007.

The Company's dedicated asset management team was highly productive in 2006, signing 186 new leases during the year for approximately 45,600 square meters. The new leases contributed to an increase in occupancy of the portfolio during the year from 81.3% to 87.5%. During the year Eurocastle successfully integrated the portfolio acquired from Dresdner Bank and occupancy has already increased from 80.7% at acquisition to over 83.6% as at 31 December 2006. The year-end occupancy target for the Deutsche Bank portfolio of 80% was exceeded and by the end of 2006 stood at more than 81%.



€5.5 BILLION PORTFOLIO OF GERMAN REAL ESTATE INVESTMENTS[1]

[1]Includes Mars acquisition completed in February 2007.

Real Estate Investment Portfolio

As at 31 December 2006, Eurocastle owned an approximate €3.5 billion portfolio of property investments, comprising investment properties of €3.3 billion (including unrealised fair value gains of €78 million as at 31 December 2006) and real estate fund units of €148 million (including cumulative unrealised fair value gains of €2.9 million as at 31 December 2006).

Overview Real Estate Investment Portfolio*

In €'000, except for percentages	As of 31 December 2006	As of 31 December 2005
Investment properties at fair value**	3,308,872	463,540
Real estate fund units	148,077	189,591
Total investment in real estate investments	3,456,949	653,131
Weighted average NOI*** yield on cost	5.90%	7.69%
Weighted average liability cost	4.41%	4.84%
Weighted average net spread	1.49%	2.85%

Investment property portfolios defined on page 37.
**The investment value above includes the €25.8 million (2005: €2.95 million) relating to finance leases on head lease. This balance has not been included in the property valuations shown in the following table headed Investment Property—Valuation Data.*
***Net Operating Income (NOI) represents gross rental income less net service charge expenses and property operating expenses.*

The following tables show the split of real estate property investments by portfolio name, use, and geographical location as at 31 December 2006.

At the year end the investment property portfolio comprised 561 properties with approximately 1.6 million square meters of lettable space. The portfolio had total occupancy of 87.5% and stable cash flows with weighted average remaining lease term of 7.1 years.

INVESTMENT PROPERTY—RENTAL DATA

By Portfolio

Portfolio	Lettable (sqm)	Occupancy %	Passing Rent* €'million Annual	Passing Rent* %	Passing Rent* € per sqm/ month
Drive	841,682	83.6%	112.0	57%	13.25
Bridge	192,498	94.4%	30.1	15%	13.82
Wave	294,486	81.3%	26.4	13%	9.20
Turret	139,999	99.7%	14.9	7%	8.90
Truss	81,165	99.6%	8.4	4%	8.65
Belfry	55,784	99.8%	5.5	3%	8.20
Bastion	25,928	100.0%	2.7	1%	8.70
Total Portfolio	**1,631,542**	**87.5%**	**200.0**	**100%**	**11.68**

By Use

Use	Lettable (sqm)	Occupancy %	Passing Rent €'million Annual	Passing Rent %	Passing Rent € per sqm/ month
Office	901,990	83.5%	113.3	57%	12.54
Retail	327,313	97.7%	39.6	20%	10.31
Bank Hall	145,741	95.1%	26.2	13%	15.76
Other	256,498	84.2%	20.9	10%	8.08
Total Portfolio	**1,631,542**	**87.5%**	**200.0**	**100%**	**11.68**

By Location

Location	Lettable (sqm)	Occupancy %	Passing Rent €'million Annual	Passing Rent %	Passing Rent € per sqm/ month
Frankfurt	330,154	92.2%	63.1	32%	17.28
Berlin	74,931	86.4%	12.2	6%	15.75
Hamburg	55,536	97.3%	10.4	5%	16.11
Düsseldorf	49,390	91.8%	9.0	5%	16.62
Munich	42,239	98.5%	8.0	4%	16.09
Subtotal—Top 5 Markets	552,250	92.4%	102.7	52%	16.81
Remaining West	770,805	89.0%	75.4	38%	9.13
Remaining East	308,487	74.9%	21.9	10%	7.92
Total Portfolio	**1,631,542**	**87.5%**	**200.0**	**100%**	**11.68**

**Passing rent is defined as the annual gross rental income at the period end, excluding the net effects of straightlining for lease incentives.*

INVESTMENT PROPERTY—LEASE EXPIRY DATA

By Use

Use	Average Lease Term	Passing Rent on Expiring Leases (€'million) Yr 1	Yr 2–3	Yr 4–6	Yr 7–10	Yr 10+
Office	7.0	3.1	14.8	40.6	16.0	38.9
Retail	7.7	1.2	4.8	6.7	16.1	10.8
Bank Hall	6.6	—	3.4	9.8	8.7	4.3
Other	6.6	2.3	3.3	5.7	3.6	6.0
Total Portfolio	**7.1**	**6.6**	**26.3**	**62.8**	**44.4**	**60.0**

By Location

Location	Average Lease Term	Passing Rent on Expiring Leases (€'million) Yr 1	Yr 2–3	Yr 4–6	Yr 7–10	Yr 10+
Frankfurt	7.4	1.1	4.0	25.5	3.1	29.5
Berlin	4.9	0.9	3.3	3.2	4.5	0.3
Hamburg	9.1	0.4	3.0	0.8	0.2	6.0
Düsseldorf	11.4	0.6	0.2	1.3	0.2	6.8
Munich	7.2	0.1	0.1	5.0	0.6	2.2
Subtotal—Top 5 Markets	**7.6**	**3.1**	**10.6**	**35.8**	**8.6**	**44.8**
Remaining West	6.8	2.1	9.1	22.3	28.3	13.4
Remaining East	5.4	1.4	6.6	4.7	7.5	1.8
Total Portfolio	**7.1**	**6.6**	**26.3**	**62.8**	**44.4**	**60.0**

INVESTMENT PROPERTY—VALUATION DATA

Markets	Properties	Lettable Space (sqm)	Property Valuation (€m)*	Property Cost (€m)	% of Portfolio	Gross Rental Income (€m)	Net Operating Income (€m)	Net Operating Income yield on cost (%)
Top 5 Markets								
Frankfurt	39	330,154	1,107	1,079	34%	63.9	58.1	5.4%
Berlin	9	74,931	218	214	7%	12.4	11.3	5.3%
Hamburg	11	55,536	211	200	6%	11.1	9.8	4.9%
Düsseldorf	4	49,390	188	174	5%	9.2	8.3	4.8%
Munich	8	42,239	165	159	5%	8.2	7.2	4.6%
Subtotal—Top 5 Markets	**71**	**552,250**	**1,889**	**1,826**	**57%**	**104.8**	**94.7**	**5.2%**
Remaining West	370	770,805	1,106	1,098	34%	75.7	67.1	6.1%
Remaining East	120	308,487	288	279	9%	21.9	19.4	7.0%
Total Portfolio	**561**	**1,631,542**	**3,283**	**3,203**	**100%**	**202.4**	**181.2**	**5.7%**

**The above valuation does not include €25.8 million relating to head leases.*

Acquisitions

In 2006, Eurocastle added approximately €3 billion of commercial real estate in Germany to its portfolio, and entered into an agreement to acquire a further €2.2 billion which has been completed by the end of February 2007. The 2006 additions include the acquisition of a €2 billion German property portfolio from Dresdner Bank via the acquisition of Dresdner Grund-Fonds in February 2006. The Company also added to its retail portfolios and acquired 91 properties for an aggregate all-in purchase price of €266 million with an average lease term of 8.4 years and average occupancy of 99.8%. The properties are leased primarily to national German retailers, mainly comprising grocery, discounter or supermarket formats and had an initial NOI yield of 6.8%. In the fourth quarter of 2006, Eurocastle acquired a portfolio of six office properties for an all-in purchase price of approximately €502 million from DB Real Estate Investment GmbH. The properties are located in Berlin, Frankfurt, Düsseldorf, Wiesbaden, Eschborn and Sulzbach. The purchase price reflects an initial NOI yield of approximately 5.6%. The properties have an average age of less than ten years and approximately 192,500 square meters. The portfolio has stable cash flows with an average lease term of seven years and over 80% of annual revenue contributed by major corporate tenants. The main tenants include Deutsche Bahn, Arcor AG & Co. KG, CSC Ploenkzke AG, Clariant GmbH and Daimler Chrysler AG. The acquisition fits Eurocastle's focus on high quality commercial office property let to creditworthy tenants with an opportunity for significant value creation through active management. In the short period of time since acquisition, occupancy has increased from 93% to over 94%.

On 14 December 2006, Eurocastle signed a definitive agreement with DB Real Estate to acquire 56 properties from the open-ended fund DB Grundbesitz Invest, comprising substantially all of its German commercial real estate assets, for an all-in purchase price of approximately €2.1 billion. The properties, totaling approximately 840,000 square meters of lettable space, consist primarily of high quality class A office space and approximately 88% of rent is derived from assets located in or around the five major German markets of Frankfurt, Munich, Berlin, Hamburg and Düsseldorf. Over 83% of the portfolio, referred to as Mars, is currently occupied, with an average remaining lease term of approximately 5 years. The initial annual passing rent amounts to €119.6 million and includes a rental guarantee of €19.9 million per annum on approximately 91,000 square meters of currently vacant space. The rental guarantee will be paid until the space is let, subject to a maximum total payment of €40 million (including service charge income) or three years. The occupancy and lease expiry information in the tables below reflect the benefit of the guarantee. The initial NOI yield on the portfolio is approximately 5.3%. The transaction had closed at the end of February 2007, and will be accounted for in the year ending 31 December 2007.

The information set out below shows the key property and segmental information relating to the Mars portfolio.

INVESTMENT PROPERTY—MARS RENTAL DATA

By Use

Use	Lettable (sqm)	Occupancy %	Passing Rent €'million Annual	Passing Rent %	Passing Rent € per sqm/month
Office	548,611	85.9%	78.2	65%	13.83
Retail	82,488	78.4%	13.8	12%	17.78
Other	208,539	81.0%	27.6	23%	13.60
Total Portfolio	**839,638**	**83.9%**	**119.6**	**100%**	**14.14**

By Location

Location	Lettable (sqm)	Occupancy %	Passing Rent €'million Annual	Passing Rent %	Passing Rent € per sqm/month
Frankfurt	257,291	91.4%	45.8	38%	16.22
Munich	188,249	82.8%	29.2	24%	15.62
Hamburg	75,349	93.3%	11.9	10%	14.09
Düsseldorf	60,012	97.3%	9.1	8%	13.07
Berlin	96,736	56.4%	9.0	8%	13.75
Subtotal—Top 5 Markets	**677,637**	**84.7%**	**105.0**	**88%**	**15.24**
Remaining West	156,332	82.9%	14.5	12%	9.30
Remaining East	5,669	16.1%	0.1	0%	7.74
Total Portfolio	**839,638**	**83.9%**	**119.6**	**100%**	**14.14**

INVESTMENT PROPERTY—MARS LEASE EXPIRY DATA

By Use Use	Average Lease Term	Passing Rent on Expiring Leases (€'million) Yr 1	Yr 2–3	Yr 4–6	Yr 7–10	Yr 10+
Office	2.7	13.6	41.0	19.7	3.1	0.9
Retail	3.5	3.6	2.8	5.7	1.4	0.3
Other	11.4	3.7	5.4	4.0	0.8	13.6
Total Portfolio	**4.8**	**20.9**	**49.2**	**29.4**	**5.3**	**14.8**

By Location Location	Average Lease Term	Passing Rent on Expiring Leases (€'million) Yr 1	Yr 2–3	Yr 4–6	Yr 7–10	Yr 10+
Frankfurt	4.2	6.6	23.2	8.2	2.1	5.6
Munich	6.8	5.4	10.4	6.5	1.6	5.3
Hamburg	2.9	2.7	6.3	1.9	0.5	0.5
Düsseldorf	7.5	0.7	0.8	5.5	0.2	1.9
Berlin	3.1	2.7	3.2	2.0	0.4	0.7
Subtotal—Top 5 Markets	**5.0**	**18.1**	**43.9**	**24.1**	**4.8**	**14.0**
Remaining West	3.4	2.6	5.3	5.3	0.5	0.8
Remaining East	0.2	0.2	—	—	—	—
Total Portfolio	**4.8**	**20.9**	**49.2**	**29.4**	**5.3**	**14.8**

INVESTMENT PROPERTY—MARS ACQUISITION DATA

Markets	Properties	Lettable Space (sqm)	Property Cost (€m)	% of Portfolio	Gross Rental Income (€m)	Net Operating Income (€m)	Net Operating Income yield on cost (%)
Top 5 Markets							
Frankfurt	17	257,291	781	36%	45.8	43.5	5.6%
Munich	10	188,249	527	25%	29.2	27.8	5.3%
Hamburg	5	75,349	205	10%	11.9	11.3	5.5%
Düsseldorf	4	60,012	180	8%	9.0	8.5	4.7%
Berlin	4	96,736	194	9%	9.2	8.6	4.4%
Subtotal—Top 5 Markets	**40**	**677,637**	**1,887**	**88%**	**105.1**	**99.7**	**5.3%**
Remaining West	15	156,332	252	12%	14.5	13.7	5.5%
Remaining East	1	5,669	2	0%	0.1	0.1	4.2%
Total Portfolio	**56**	**839,638**	**2,141**	**100%**	**119.7**	**113.5**	**5.3%**

Set out below are tables showing the impact of Mars on the portfolio as at 31 December 2006.

The total pro forma portfolio has lettable space of approximately 2.5 million square meters, occupancy of 86.3% (slightly lower than the year end occupancy of 87.5%) and an NOI yield of 5.5%. The pro forma average lease term is 6.2 years, approximately one year shorter than the year end portfolio. Concentration in the top five markets is 65%, compared to 52% at the year end. The increased concentration in the top five markets is consistent with Eurocastle's focus on high quality class A office space in those markets and, together with the shorter lease terms, means that Eurocastle is well positioned to benefit from improvements in the related rental markets.

INVESTMENT PROPERTY—PRO FORMA PORTFOLIO RENTAL DATA INCLUDING MARS

By Use

			Passing Rent		
Use	Lettable (sqm)	Occupancy %	€'million Annual	%	€ per sqm/ month
Office	1,450,601	84.4%	191.5	60%	13.04
Retail	409,801	93.8%	53.3	17%	11.56
Bank Hall	145,741	95.1%	26.2	8%	15.76
Other	465,037	82.8%	48.5	15%	10.50
Total Portfolio	**2,471,180**	**86.3%**	**319.5**	**100%**	**12.49**

By Location

			Passing Rent		
Location	Lettable (sqm)	Occupancy %	€'million Annual	%	€ per sqm/ month
Frankfurt	587,445	91.8%	108.9	34%	16.82
Munich	230,488	85.7%	37.3	12%	15.72
Hamburg	130,884	95.0%	22.3	7%	14.96
Düsseldorf	109,402	94.8%	18.2	6%	14.62
Berlin	171,667	69.5%	21.2	7%	14.84
Subtotal—Top 5 Markets	**1,229,886**	**88.2%**	**207.9**	**66%**	**15.98**
Remaining West	927,137	88.0%	89.6	28%	9.15
Remaining East	314,157	73.8%	22.0	6%	7.92
Total Portfolio	**2,471,180**	**86.3%**	**319.5**	**100%**	**12.49**

INVESTMENT PROPERTY—PRO FORMA PORTFOLIO LEASE EXPIRY DATA

By Use

Use	Average Lease Term	Passing Rent on Expiring Leases (€'million) Yr 1	Yr 2–3	Yr 4–6	Yr 7–10	Yr 10+
Office	5.3	16.7	55.7	60.2	19.1	39.8
Retail	6.6	4.8	7.6	12.4	17.5	11.1
Bank Hall	6.6	—	3.4	9.8	8.7	4.3
Other	9.3	6.0	8.7	9.8	4.4	19.6
Total Portfolio	**6.2**	**27.5**	**75.4**	**92.2**	**49.7**	**74.8**

By Location

Location	Average Lease Term	Passing Rent on Expiring Leases (€'million) Yr 1	Yr 2–3	Yr 4–6	Yr 7–10	Yr 10+
Frankfurt	6.1	7.7	27.2	33.7	5.2	35.0
Munich	6.9	5.5	10.5	11.5	2.2	7.5
Hamburg	5.8	3.1	9.2	2.7	0.7	6.6
Düsseldorf	9.4	1.3	1.0	6.7	0.4	8.7
Berlin	4.1	3.6	6.5	5.2	4.9	1.0
Subtotal—Top 5 Markets	**6.3**	**21.2**	**54.4**	**59.8**	**13.4**	**58.8**
Remaining West	6.2	4.7	14.4	27.7	28.7	14.2
Remaining East	5.4	1.6	6.6	4.7	7.6	1.8
Total Portfolio	**6.2**	**27.5**	**75.4**	**92.2**	**49.7**	**74.8**

INVESTMENT PROPERTY—PRO FORMA PORTFOLIO DATA

Markets	Properties	Lettable Space (sqm)	Property Cost (€m)	% of Portfolio	Gross Rental Income (€m)	Net Operating Income (€m)	Net Operating Income yield on cost (%)
Top 5 Markets							
Frankfurt	56	587,445	1,860	35%	109.7	101.6	5.5%
Munich	18	230,488	685	13%	37.5	35.1	5.1%
Hamburg	16	130,884	405	8%	23.0	21.1	5.2%
Düsseldorf	8	109,402	354	7%	18.4	16.9	4.8%
Berlin	13	171,667	408	8%	21.3	19.8	4.9%
Subtotal—Top 5 Markets	**111**	**1,229,886**	**3,712**	**71%**	**209.9**	**194.5**	**5.2%**
Remaining West	385	927,137	1,349	25%	90.3	80.8	28.8%
Remaining East	121	314,157	281	4%	22	19.5	1.4%
Total Portfolio	**617**	**2,471,180**	**5,342**	**100%**	**322.2**	**294.8**	**5.5%**

Real Estate Fund Units

As of 31 December 2006, Eurocastle had a total interest of €148 million (including cumulative unrealised fair value gains of €2.9 million since acquisition) in a real estate investment fund that owns a portfolio of approximately 400 Italian properties. The properties are let to Italian government agencies. The original term of the lease agreement is 9 years (approximately 7 years remaining), with an extension option for a further 9 years. The properties are 100% occupied.

DEBT INVESTMENT PORTFOLIO

Overview of Real Estate and Other ABS Securities and Real Estate Loans

	As of 31 December 2006	As of 31 December 2005
Total debt investments (excluding restricted cash) (€'000)	1,967,969	1,537,945
Weighted average asset margin (above Euribor)	1.88%*	1.88%*
Weighted average liability spread	0.56%*	0.53%*
Weighted average net spread	1.32%*	1.35%*
Weighted average credit rating	BBB–	BBB+
Percentage investment grade of debt investment portfolio	66%	87%
Number of securities and loans	158	127

**Includes assets and liabilities referenced under total return swaps.*

Portfolio

As of 31 December 2006, Eurocastle's total debt investment portfolio totalled approximately €2.0 billion and included €742 million of CMBS, €796 million of other asset backed securities (including €356 million of RMBS) and €431 million of real estate loans. The debt investment portfolio is well diversified with 158 securities and loans and an average life of approximately 4.52 years; approximately 94% of the portfolio comprises floating-rate securities. The portfolio is geographically diversified with direct exposures of 49% in the UK, 13% in Italy, 20% in Germany, 5% Pan European and 5% in France. The average credit quality of the debt investment portfolio is BBB– and approximately 66% of the investments are rated investment grade. The portfolio's weighted average credit spread was approximately 1.88% as of 31 December 2006.

Eurocastle's debt investment portfolio has continued to perform well. As of 31 December 2006, none of the Group's securities or loans had defaulted, and there have been no principal losses to date. Within Eurocastle's debt investment portfolio, the group continues to seek investments that will generate superior risk-adjusted returns with a long-term objective of capital preservation and earnings stability in varying interest rate and credit cycles.

Acquisitions

In the year ended 31 December 2006, Eurocastle purchased approximately €852 million of real estate related securities and loans. The securities and loans purchased have an average credit rating of BB and a net credit spread of 2.10%.

After allowing for sales of securities and principal redemptions, the net increase in face amount of real estate related securities and real estate related loans during year ended was €433.9 million, increasing the net face amount of real estate related securities and real estate related loans to €2 billion at 31 December 2006 with an average credit rating of BBB–.

FINANCING

Debt Financing

In December 2004, the Group financed the Deutsche Bank portfolio (“Wave”) with a €246.5 million facility of which €242.8 million had been drawn down at 31 December 2006. The loan is for 8.4 years at signing and, after allowing for an interest rate swap on €210 million, has an effective interest cost of 4.72%.

The Dresdner Bank portfolio (“Drive”) is financed with a 7 year (at signing) €1,525 million facility consisting of a senior and junior loan of €841 million and €684 million respectively. €50 million of the junior loan bears interest at Euribor to match a liquidity reserve maintained by Dresdner Grund-Fonds, whereas the remaining portion bears a fixed rate. The senior loan has a weighted average funding cost of 3.83% and the junior loan has a weighted average funding cost of 4.64%, giving an overall funding cost of 4.20%.

The retail property portfolio comprises four separate portfolios (“Bastion”, “Belfry”, “Truss” and “Turret”) for financing purposes. All of the portfolios have been financed with non-recourse fixed interest term loans. The loans drawn at 31 December 2006 and the related weighted average funding costs are as follows:

Belfry—€56.2 million at 4.81% per annum
Bastion—€26.5 million at 4.42% per annum
Truss—€85.3 million at 4.86% per annum
Turret—€147.6 million at 4.94% per annum

The Group financed the portfolio of 6 office properties (“Bridge”) acquired for an all-in purchase price of €502 million in the fourth quarter of 2006 with a 7 year (at signing) €372 million term loan at a fixed funding cost of 4.74%.

In addition, the Group entered into an arrangement to finance a €2,140 million committed acquisition of 56 properties from DB Grundbesitz Invest (“Mars”) with a term loan of €1,029 million at a fixed funding cost of 4.72% on the core portfolio and a floating loan of €550 million at a funding cost of Euribor 3M + 0.77% on the non-core portfolio. The weighted average funding cost of the total debt of €1,579 million is 4.68%. The transaction will be accounted for in the year ending 31 December 2007.

Eurocastle continues to finance its core real estate portfolio with fixed term loans, which has substantially eliminated its exposure to increased interest rates. This is consistent with the objective of locking in the spread between the yield on our investments and the cost of financing those investments.

Eurocastle Investment Limited
2006 Financial Review

Financial Review

Financial Highlights

Income Statement

(in €'000, except per share data)	Year Ended 31 Dec 2006	Year Ended 31 Dec 2005
Interest income	**95,970**	65,538
Rental income	**152,454**	28,128
Service charge income	**31,903**	6,545
Real estate fund unit interest income	**18,636**	8,406
Increase in fair value of investment properties	**78,119**	1,961
(Decrease)/increase in fair value of real estate fund units	**(5,217)**	8,098
Interest expense	**(150,282)**	(58,141)
Other operating expenses	**(26,023)**	(10,032)
Service charge expense	**(41,237)**	(8,599)
Operating profit before taxation	**147,557**	41,936
Operating profit after taxation	**143,819**	39,658
Earnings per weighted average basic share	**3.20**	1.85
Earnings per weighted average diluted share	**3.08**	1.79

Balance Sheet

(in €'000, except per share data)	As of 31 Dec 2006	As of 31 Dec 2005
Cash and cash equivalents	**122,699**	13,640
Asset backed securities (includes cash to be invested and securities pledged under repurchase agreements)	**1,560,307**	1,452,547
Real estate loans	**428,370**	92,649
Real estate fund units	**148,077**	189,591
Investment property	**3,308,872**	463,540
Total assets	**5,662,380**	2,273,980
Debt obligations	**3,966,328**	1,916,189
Shareholders' equity	**1,570,719**	298,866
Book value per ordinary share	**24.73**	12.34

Key Performance Indicators

- Net profit after tax of €143.8 million for the financial year 2006 increased by 262% from €39.7 million in 2005.
- Earnings per ordinary share of €3.20 or €3.08 per diluted share for 2006 compared to €1.85 per share or €1.79 per diluted share for 2005.
- Funds from operations ("FFO") increased by 137% from €31.6 million in 2005 to €74.7 million in 2006.
- FFO of €1.66 per ordinary share or €1.60 per diluted share for 2006 compared to €1.48 per ordinary share or €1.43 per diluted share for 2005.
- FFO return on average invested capital* was 9.1% for 2006.
- More than doubled equity book value per share from €12.34 per share at year end 2005 to €24.73 per share at year end 2006.

**Invested capital represents capital and reserves less hedging reserves, fair value of interest rate swaps and net unrealised gains on available-for-sale securities, real estate fund units and investment properties (net of attributable deferred taxation).*

Funds from Operations (FFO)

One of the Group's key performance measures is FFO. FFO is an appropriate measure of the underlying operating performance of companies primarily involved in real estate because it provides investors information regarding the Group's ability to service debt and make capital expenditures. Furthermore, FFO is used to compute incentive compensation to the manager. FFO, as defined by Eurocastle, represents net profit after taxation (computed in accordance with IFRS), excluding changes in the fair value of investment properties net of attributable deferred taxation, changes in the fair value of interest rate swaps that are taken to the income statement and mark-to-market fluctuations in real estate fund units. The Group considers gains and losses on resolution of its investments to be a normal part of its recurring operations and therefore does not exclude such gains and losses when arriving at FFO. FFO does not represent cash generated from operating activities in accordance with IFRS and therefore should not be considered an alternative to cash flow as a measure of liquidity, and is not necessarily indicative of cash available to fund cash needs. Eurocastle's calculation of FFO may be different from the calculation used by other companies and, therefore, comparability may be limited.

The table below illustrates the year on year growth in the Group's FFO since the year ended 31 December 2005, and gives reconciliation between net profit after taxation and FFO.

(in €'000, except per share data)	Year Ended 31 Dec 2006	Year Ended 31 Dec 2005
Reconciliation of FFO to net profit after taxation		
Net profit after taxation	143,819	39,658
(Increase)/decrease in fair value of investment properties	(78,119)	(1,961)
Decrease in fair value of interest rate swaps	425	—
(Increase)/decrease in fair value of real estate fund units	5,217	(8,098)
Deferred tax charge on investment properties	3,366	1,989
Funds from operations (FFO)	74,708	31,588
% increase on previous year in FFO	137%	163%
FFO per weighted average basic share	1.66	1.48
FFO per weighted average diluted share	1.60	1.43

In the year ended 31 December 2006, FFO increased 137% as compared to year end 2005. This increase was mainly due to the increase in revenues and improved cost:income ratio (total operating expense:total operating income). This was achieved through acquisitions of commercial property portfolios and debt investments, together with improved occupancy rates within the Drive and Wave portfolios.

The increase in FFO per share is largely due to the accretive impact of deploying equity issued in January and December 2006 in acquiring additional commercial property and debt investments.

Dividends

Including a dividend of €0.14 per share declared on 7 March 2007, the Group declared total dividends of €1.56 per share in respect of the year ended 31 December 2006. This represented an increase of 9.9% compared to the aggregated dividend per share of €1.42 per share for the year ended 31 December 2005.

Profits for the Year

The table below illustrates the year on year growth in the Group's operating profits since 31 December 2005.

	Year End 2006 €'000	Year End 2005 €'000
Operating profit before taxation	147,557	41,936
% Increase on previous year	252%	249%
Operating profit %	39.4%	34.3%

Operating profit before taxation increased from €41.9 million to €147.6 million. The growth in profit is primarily a reflection of the continued growth of the business due in particular to an increase in the investment property portfolio and to a lesser extent the increase in the debt investment portfolio. The increase in the fair value of real estate investment properties has also had a significant impact on the earnings, accounting for €78 million of operating profit in 2006 compared to €2 million in 2005.

Operating profit margins (operating profit before tax as a percentage of total operating income) have increased from 34.3% to 39.4% in the year ended 31 December 2006. This is due to unrealised gains on the commercial property portfolio, partly offset by a significant increase in service charge expenses and other property operating expenses.

Revenues

The Group's revenue mainly consists of rental income from German commercial property, interest income from debt investments and income from real estate fund units.

In the year ended 31 December 2006, total revenues increased 175% to €299.0 million as compared to €108.6 million for the year ended 31 December 2005. Revenue includes the following items: interest income, rental income, service charge income and real estate fund unit interest income. Since 31 December 2005, interest income increased from €65.5 million to €96.0 million; rental income increased from €28 million to €152.5 million; service charge income increased from €6.5 million to €31.9 million, and real estate fund unit income increased from €8.4 million to €18.6 million. A breakdown of these items is set out in the income statement on page 30 and accompanying notes.

Interest income has increased due to the increase in the debt investment portfolio (asset backed securities and real estate related loans), as well as the increase in Euro and Sterling interest rates. Real estate fund unit income has increased in 2006 in comparison to 2005 as Eurocastle gained a full year's return in 2006 compared with a half year return in 2005. The fund units were acquired between July and October 2005.

Rental income has increased due to increases in the property portfolio, increased occupancy levels and increases in rental income pursuant to the terms of existing leases. The Group's revenues have benefited from increased occupancy within the Deutsche Bank Portfolio, up from 74.6% as at 31 December 2005 to 81.3% as at 31 December 2006. In a short period of time, the Group has successfully integrated the Dresdner Portfolio and has increased occupancy from 80.7% on acquisition in February 2006 to 83.6% at 31 December 2006.

The Group's revenue has grown substantially year on year since it commenced operations in October 2003. This growth in revenues has in turn driven growth in net income and cash available for distribution. The Group's increase in revenue and FFO is achieved through a combination of accretive growth and organic growth. Accretive growth occurs by acquiring additional investments generating income above the expected cost of capital, whereas organic growth mainly comes from leasing up vacant space within the portfolio and controlling costs. One of the key factors underpinning the growth in revenues is growth in the size of the Group's investment portfolio or accretive growth.

The Group expects to continue to grow its revenue through acquisitions of real estate portfolios. In the short term the Group continues to see strong deal flow in Germany and believes the German real estate market will provide further attractive investment opportunities. Since the year ended 31 December 2006, the Group has acquired a further €2.2 billion of German commercial real estate investments which will result in significant increases in revenue in 2007 and beyond. In the longer term, however, the performance of investments will depend upon market conditions, the competitive environment in which the Group operates, and the ability of the Group to identify and acquire appropriate investments.

The Group's commercial real estate in Germany benefits from leases indexed to the German consumer price index ("CPI"). Substantially all of the leases in the Retail Portfolio are indexed to the German CPI with a rental adjustment being made once the index has moved 10% from a reference point level set on signing of each lease. The size of the adjustment is generally between 50% and 100% of the index movement depending on the tenant and form of the lease. The leases to Deutsche Bank within the Deutsche

Portfolio, which account for 69% of the portfolio's revenue, are also indexed to German CPI. A movement of 5% in the index will result in a rent adjustment of 100% of such index movement. The leases to Dresdner Bank within the Dresdner Portfolio have a fixed upwards rent adjustment of 1% in each year from 2007 to 2009 and thereafter from 2010, the rent adjustment is equal to 100% of the change in German CPI determined on an annual basis.

A significant proportion of the Group's revenues are derived from a limited number of tenants and counterparties. As at 31 December 2006, 79% of the Group's rental income was being derived from credit worthy tenants (including Dresdner Bank, Deutsche Bank and anchor tenants in the Retail Portfolio).

Operating Expenses

The Group's costs have increased period on period since it commenced operations, again reflecting the underlying growth in the size of its portfolio. However, the cost to income ratio (total operating income:total operating expenses) has improved from 1.52 in the year ended 31 December 2005 to 1.65 in the year ended 31 December 2006. The improvement in the ratio is primarily a result of the increased proportion of the Group's portfolio that comprises direct real estate investments being less leveraged than the debt portfolio.

A significant proportion of the Group's expenses represent interest expense (66.4% for the period ended 31 December 2006, against 72.3% as at 31 December 2005). Interest expense of the Group in the year to 31 December 2006 amounted to €150.3 million compared to €58.1 million for the same period in 2005, an increase of 159%. The increase was due principally to additional debt taken on to finance the commercial property acquisitions and debt investments completed during the year, as well as from increases in market interest rates.

Service charge expenses accounted for 18.2% of the Group's expenses (2005: 10.7%) and amounted to €41.2 million for 2006, compared to €8.6 million for 2005. The increase was due mainly to the growth in the commercial property portfolio during the year. The service charge expense recovery ratio in 2006 was 77.4% compared to 76.1% for 2005, reflecting increased portfolio occupancy.

The Group has structured its investments in a tax efficient manner but changes in tax legislation in relevant jurisdictions (including Guernsey, Luxembourg, Ireland and Germany) could affect the Group's effective rate of taxation.

Cash Flow from Operations

The following summaries the Group's cash flows for the years ended 31 December 2006 and 2005.

	2006 €'000	2005 €'000
Net cash inflow from operating activities	118,650	4,486
Net cash flows from investing activities	(3,156,569)	(832,010)
Net cash flows from financing activities	3,146,978	828,059
Net increase in cash and short term deposits	109,059	535

The cash outflow from investing activities reflects the acquisition of additional German commercial real estate portfolios and increased debt investment. The cash flow generated from financing activities reflects the increased bank borrowings to finance the expansion of the Group's commercial property portfolio and the issuance of Ordinary Shares. The Group's cash position at 31 December 2006 resulted in a positive balance of €122.7 million (2005: €13.6 million).

Total Assets

Total assets at 31 December 2006 amounted to €5,662 million, representing a 149% increase from €2,274 million as at 31 December 2005. This primarily reflects the acquisition of further German commercial property investments by the Group.

Real Estate Investments

As at 31 December 2006, the Group's real estate portfolio comprised €3,457 million of commercial property investments including the real estate fund (FIP) units compared with €653 million as at 31 December 2005. This represents an increase of 429% over the twelve month period. Of this increase, €72.9 million represented the unrealised gain on revaluation of underlying assets. The balance (excluding the sale of real estate fund units) of €2,731.10 million represents additional assets acquired by the Group amounting to €2.744 million.

As at 31 December 2006, the Group carried the FIP units at €148 million (which figure includes the costs related to investment). In September 2006, 300 FIP units were sold and this resulted in gain of €2.2 million. Currently the Group owns 1,200 FIP units.

Debt Investments

As at December 2006, the Group carried debt investments valued at €1,989 million compared to €1,545 million as at 31 December 2005. Of this €1,560 million represented asset backed securities (an increase of 7% on the amount held as at 31 December 2005) and €428 million represented real estate loans including real estate related B notes and mezzanine loans (2005: €93 million).

Interest income from debt portfolio increased by 43% from €65.5 million for the year ended 31 December 2006 to €93.4 million.

The growth in both asset values and income was achieved through further growth in the Group's portfolio of debt investments.

CDO Bonds Payable and Repurchase Agreements

As at 31 December 2006, the Group had in issue €1,210 million of CDO bonds payable (comprising bonds issued by Eurocastle CDO I, II, and III) representing an increase of 24% on the amount of CDO bonds payable in issue at 31 December 2005 (€977 million). This was as a result of Eurocastle CDO II and Eurocastle CDO III issuing further notes to finance the purchase of additional asset backed securities.

As 31 December 2006, the Group owed €75.5 million under repurchase agreements, a decrease of 27% as compared to 31 December 2005 (€103.5 million) primarily due to the sale of debt investments previously financed under repurchase agreements.

Bank Borrowings

As at 31 December 2006, the Group's bank borrowings had increased to €2,681 million, compared to €835 million as at 31 December 2005 reflecting principally the term financing of additional acquisitions of commercial property portfolios and real estate related loans.

Risks

Interest Rate Risk

The Group's primary interest rate exposure relates to its real estate and other asset backed securities, loans and floating rate debt obligations, as well as its interest rate swaps. Changes in the level of interest rates also can affect the Group's ability to acquire securities and loans and its ability to realise gains from the disposal of such assets.

The Group seeks to manage its interest rate exposure and consequently expects to suffer minimal changes in net income as a result of changes in interest rates. The Group generally finances its real estate portfolio with fixed rate loans for original terms ranging from 7–13 years, or where it takes out floating rate term loans, it enters into hedging instruments (such as interest rate swaps), to lock in a fixed rate for the duration of the loan.

Foreign Currency Risk

The Group's primary foreign currency exchange rate exposure relates to its non-euro denominated portfolio of securities and loans. Changes in the exchange rates can adversely impact the fair values and earnings streams of the Group's non-euro denominated assets and liabilities. The Group has mitigated this impact through a combination of (i) non-euro denominated financing and (ii) rolling forward foreign exchange contracts to hedge its net non-euro investments.

In connection with the Group's purchase of its asset backed securities and real estate related loans, the foreign currency risk is hedged through forward foreign currency exchange contracts.

Market Risk

The Group's exposure to market risk arises mainly due to potential movements in the value of its real estate and debt investments.

The Group's real estate investment assets are based in Germany and Italy and are subject to general property market risks. These risks are assessed by management at the point of acquisition and are then monitored on an ongoing basis. In addition, external valuations of the Group's real estate assets are obtained during each financial year.

The Group's debt investments are predominantly floating rate and as such are valued based on a market credit spread over Euribor and other benchmarks for euro and non-euro denominated assets respectively. Increases in the credit spreads above such benchmarks may affect the Group's net equity, net income or cash flow directly through their impact on unrealised gains or losses on available-for-sale securities, and therefore its liability to realise gains on such securities, or indirectly through their impact on its ability to borrow and access capital.

Credit Risk

The Group is subject to credit risk with respect to its investments in real estate and other asset backed securities and loans.

The securities the Group invests in are generally junior in right of payment of interest and principal to one or more senior classes, but benefit from the support of one or more subordinate classes of securities or other form of credit support within a securitisation transaction. While the expected yield on these securities is sensitive to the performance of the underlying assets, the more subordinated securities are designed to bear the first risk of default and loss.

The Group further minimises credit risk by actively monitoring its securities portfolio and the underlying credit quality of its holdings and, where appropriate, repositioning its investments to upgrade the credit quality and yield on the investments. The Group's debt portfolio is diversified by asset type, industry, location and issuer. This diversification minimises the risk of capital loss. At 31 December 2006, the Group's securities, which serve as collateral for its CDO financings and other borrowings, had an overall weighted average credit rating of approximately BBB-.

Liquidity and Capital Resources

The Group's ability execute its business strategy and, in particular to grow its investment portfolio, depend to a significant degree on its ability to obtain additional capital.

The Group's primary sources of funds consist of cash provided by operating activities, borrowings under loans and credit facilities and the issuance of debt and equity securities. The Group's loans and debt securities are generally secured directly over its assets. The Group expects that its cash on hand and cash flow provided by operations will satisfy its liquidity needs with respect to its current investment portfolio over the next twelve months. The Group expects that its long-term liquidity requirements, specifically to fund the repayment of its debt obligations, will be met through additional borrowings and the liquidation or refinancing of its assets at maturity.

A significant portion of the Group's debt investments are financed in the capital markets through the issuance of collateralised debt obligations, known as CDOs. The Group finances some of its debt investments with short term repurchase agreements with a number of investment banks.

Report of the Directors

Incorporation

Eurocastle Investment Limited (the "Group") was incorporated in Guernsey, Channel Islands on 8 August 2003 and commenced its operations on 21 October 2003.

Activities

The principal activities of the Group include investing in, financing and management of high quality German commercial properties. In addition, the Group also invests in European real estate related debt which is complementary to its core business. The Group is externally managed by its manager (the "Manager"), an affiliate of Fortress Investment Group LLC, a global alternative asset manager with approximately US$35.1 billion of assets under management as of 31 December 2006. The Group has entered into a management agreement (the "Management Agreement") under which the Manager advises the Group on various aspects of its business and manages its day-to-day operations, subject to the supervision of the Group's Board of Directors. The Group has no direct employees. For its services, the Manager receives an annual management fee (which includes a reimbursement for expenses) and incentive compensation, as defined in the Management Agreement. The Group has no ownership interest in the Manager.

Review of Business

The consolidated income statement for the year is set out on page 28. A review of the development and performance of the business has been set out in the letter to shareholders, business review and financial review. This includes an analysis of the performance and position of the business. Principal risks facing the business have been set out in the financial review.

Dividends

On 7 March 2007 the Board of Directors declared a second fourth quarter dividend of €0.14, which represents a total quarter four dividend of €0.43 per share (2005: €0.37). It is the Company's policy to recommend paying stable growing dividends. The aggregate dividend for the year was €1.56 compared to €1.42 in 2005.

Management Agreement

The Independent Directors have reviewed the continued appointment of the Manager. In carrying out the review the Independent Directors considered the past performance of the Group and the capability and resources of the Manager to deliver satisfactory investment performance. The Independent Directors also considered the length of notice period of the Management Agreement and the management and incentive fees payable to the Manager, together with the standard of the other services provided.

The Independent Directors conclude that the continued appointment of the Manager was in the best interest of the shareholders.

Directors

The Directors who held office during the year and subsequently were:

Wesley R. Edens
Randal A. Nardone
Keith Dorrian
Paolo Bassi
Simon Thornton
Udo Scheffel

Directors' Interests

The interests of the Directors in the ordinary shares of the Company as at 31 December 2006 were as follows:

	31 December 2006	31 December 2005
Keith Dorrian	3,000	2,000
Paolo Bassi	36,800	31,800
Wesley R. Edens*	50,000	50,000
Randal A Nardone*	20,000	—

**Wesley R. Edens and Randal A. Nardone are members of Fortress Principal Investment Holdings II LLC which is the registered holder of 1,005,000 Shares and as a result of this relationship Wesley R. Edens and Randal A. Nardone are interested in the shares owned by this entity or in some of such shares.*

Substantial Shareholdings

As at 23 April 2007, the Group had notification that the following shareholders had an interest in 3% or more of Eurocastle Investment Limited's share capital:

	% Holding
Nederlands Centraal Instituut Voor Giraal Effectenverkeer Bv*	61.75
Goldman Sachs Securities (Nominees) Limited	19.87
Euroclear Nominees Limited	6.82
Fortress Investment Fund III LP	4.75
Fortress Investment Fund III (Fund B) LP	4.06

**Nederlands Centraal Instituut Voor Giraal Effectenverkeer Bv is the Dutch central securities depositary (otherwise known as Euroclear Netherlands).*

Auditors

Ernst & Young LLP were re-appointed during the period. Ernst & Young LLP have expressed their willingness to continue in office.

Annual General Meeting

The AGM of Eurocastle Investment Limited will be held on 5 June 2007 in Guernsey at the registered office.

Registered Office

International Administration (Guernsey) Limited
Regency Court
Glategny Esplanade
St. Peter Port, Guernsey, GY1 1WW

On behalf of the Board

Wesley R. Edens
Date: 26 April 2007

Statement of Directors' Responsibility in Respect of the Financial Statements

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable Companies (Guernsey) Law 1994 and International Financial Reporting Standards.

The Directors are required to prepare financial statements for each financial year which present fairly the financial position of the Group and the financial performance and cash flows of the group for that period. In preparing those financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Present information, including accounting policies, in a manner that provides relevant, reliable comparable and understandable information;
- Provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- State that the company has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the financial statements comply with the Companies (Guernsey) Law 1994. 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.

Independent Auditors' Report

To the members of Eurocastle Investment Limited

We have audited the group financials (the "Consolidated financial statements") of Eurocastle Investment Limited and its subsidiaries for the year ended 31 December 2006 which comprise the Consolidated Income Statement, Consolidated Balance Sheet, Consolidated Cash Flow Statement, Consolidated Statement of Change in Shareholder's Equity, and the related notes 1 to 31. 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) 1994. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state them in an auditor's report and for no other purpose. To the fullest extent permitted by the law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we formed.

Respective Responsibilities of Directors and Auditors

The directors are responsible for preparing the Annual Report and then group financial statements in accordance with applicable Guernsey law and International Financial Reporting Standards (IFRS).

Our responsibility is to audit the financial statements and 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 give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies (Guernsey) Law 1994. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have received all the information and explanations we require for our audit, or if the information specified by law or the listing rules.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Director's Report and Chairman's Statement. 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 out audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practises 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 judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group'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 International Financial Reporting Standards, of the state of the Group's affairs as at 31 December 2006 and of its profit for the year then ended; and have been properly prepared in accordance with the Companies (Guernsey) Law 1994.

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
London
Date: 30 April 2007

Consolidated Income Statement

	Notes	Year Ended 31 December 2006 €'000	Year Ended 31 December 2005 €'000
Operating income			
Interest income	3	**95,970**	65,538
Rental income	4	**152,454**	28,128
Service charge income	5	**31,903**	6,545
Real estate fund unit interest income		**18,636**	8,406
Realised gain on disposal of available-for-sale securities		**314**	2,472
Realised gain on disposal of real estate fund units		**2,163**	731
Increase in fair value of investment properties	15	**78,119**	1,961
(Decrease)/increase in fair value of real estate fund units	14	**(5,217)**	8,098
(Decrease) in fair value of interest rate swaps		**(425)**	—
(Decrease)/increase in fair value of total return swap		**(150)**	477
Total operating income		**373,767**	122,356
Operating Expenses			
Interest expense	6	**150,282**	58,141
Losses on foreign currency contracts/currency translation		**1,211**	1,712
Service charge expenses	5	**41,237**	8,599
Property operating expenses	4	**7,457**	1,936
Other operating expenses	7	**26,023**	10,032
Total operating expenses		**226,210**	80,420
Operating Profit before Taxation		**147,557**	41,936
Taxation expense	8	**3,738**	2,278
Net Profit after Taxation		**143,819**	39,658
Earnings Per Ordinary Share			
Basic		**3.20**	1.85
Diluted		**3.08**	1.79
Weighted Average Ordinary Shares Outstanding			
Basic	21	**44,956,083**	21,392,936
Diluted	21	**46,760,626**	22,165,864

See notes to the consolidated financial statements.

Consolidated Balance Sheet

	Notes	31 December 2006 €'000	31 December 2005 €'000
Assets			
Cash and cash equivalents	9	**122,699**	13,640
Other assets	12	**69,537**	50,001
Asset backed securities, available-for-sale (includes cash to be invested)	10	**1,481,661**	1,342,638
Asset backed securities, pledged under repurchase agreements	10	**78,646**	109,909
Real estate related loans	11	**428,370**	92,649
Real estate fund units	14	**148,077**	189,591
Derivative assets	13	**22,690**	11,470
Investment property	15	**3,308,872**	463,540
Intangible assets	16	**1,828**	542
Total assets		**5,662,380**	2,273,980
Equity and liabilities			
Capital and reserves			
Issued capital, no par value, unlimited number of shares authorised, 63,519,083 shares issued and outstanding at 31 December 2006	22	**1,439,517**	286,801
Accumulated profit		**88,458**	18,442
Net unrealised gain on available-for-sale securities	10	**1,882**	4,703
Hedging reserve	23	**23,542**	(12,100)
Other reserves	22	**17,320**	1,020
Total shareholders' equity		**1,570,719**	298,866
Minority interest		**6**	2
Total equity		**1,570,725**	298,868
Liabilities			
Trade and other payables	20	**93,299**	41,396
CDO bonds payable	17	**1,210,275**	977,485
Bank borrowings	18	**2,680,563**	835,162
Repurchase agreements	19	**75,490**	103,542
Derivative liabilities		**212**	12,297
Finance lease payable	15	**25,800**	2,952
Current taxation payable	8	**539**	167
Deferred taxation payable	8	**5,477**	2,111
Total liabilities		**4,091,655**	1,975,112
Total equity and liabilities		**5,662,380**	2,273,980

See notes to the consolidated financial statements.

Consolidated Statement of Cash Flows

	Year Ended 31 December 2006 €'000	Year Ended 31 December 2005 €'000
Cash Flows From Operating Activities		
Operating profit before taxation	147,557	41,936
Adjustments for:		
Unrealised loss/(gain) on foreign currency contracts	1,211	(548)
Accretion of premiums/(discounts) on securities	434	(4,026)
Amortisation of borrowing costs	3,458	1,214
Realised gain on disposal of real estate fund units	(2,163)	—
Realised gain on disposal of available-for-sale securities	(887)	(2,540)
Realised gain on disposal of investment properties	—	(731)
Shares granted to Directors	172	108
Amortisation of intangibles	144	9
Revaluation loss/(gain) of real estate fund units	5,217	(8,098)
Revaluation gain on investment properties	(78,119)	(1,961)
Revaluation loss/(gain) of total return swap	150	(477)
Revaluation loss of interest rate swap	425	—
Increase in other assets	(9,744)	(51,861)
Increase in trade and other payables	50,795	31,461
Net cash flows from operating activities	118,650	4,486
Cash Flows From Investing Activities		
Purchase of investment property	(2,744,365)	(143,524)
Proceeds from disposal of investment properties	—	1,190
Minority interest movement	4	—
Acquisition of real estate fund units	—	(181,493)
Disposal of available-for-sale securities	245,049	—
Purchase of available-for-sale securities	(389,829)	(540,934)
Disposal of securities pledged under repurchase agreements	65,398	104,013
Purchase of securities pledged under repurchase agreements	(34,135)	—
Increase in real estate related loans	(427,635)	(70,711)
Repayment of real estate related loans	91,914	—
Proceeds from disposal of real estate fund units	38,460	—
Purchase of intangible assets	(1,430)	(551)
Net cash flows used in investing activities	(3,156,569)	(832,010)
Cash Flows From Financing Activities		
Proceeds of issuance of ordinary shares	1,195,401	99,015
Costs related to issuance of ordinary shares	(26,557)	(4,011)
Proceeds from issuance of bonds	235,458	635,362
Costs related to issuance of bonds	(1,970)	(6,556)
Borrowings under repurchase agreements	33,215	(94,042)
Repayments under repurchase agreements	(61,267)	—
Increase of bank borrowings	1,846,501	225,901
Dividends paid to shareholders	(73,803)	(27,610)
Net cash flows from financing activities	3,146,978	828,059
Net Increase in Cash and Cash Equivalents	109,059	535
Cash and Cash Equivalents, Beginning of Period	13,640	13,105
Cash and Cash Equivalents, End of Period	122,699	13,640

See notes to the consolidated financial statements.

Consolidated Statement of Changes in Equity

	Attributable to Equity Holders of the Company							
	Ordinary Shares (Adjusted for Share Consolidation) Number	Share Capital €'000	Other Reserves €'000	Net Unrealised Gains/ (Losses) €'000	Hedging Reserves €'000	Accumulated Profit/(Loss) €'000	Minority Interest €'000	Total Equity €'000
At 1 January 2005	18,463,670	192,309	400	6,604	713	6,394	2	206,422
Net unrealised gain on available-for-sale securities	—	—	—	211	—	—	—	211
Issuance of shares—June 2005	5,740,000	99,015	—	—	—	—	—	99,015
Costs related to issue of shares—June 2005	—	(4,011)	—	—	—	—	—	(4,011)
Issuance of ordinary shares to Directors	6,000	108	—	—	—	—	—	108
Realised gains reclassified to the income statement	—	—	—	2	—	—	—	2
Realised losses reclassified to the income statement	—	—	—	(2,114)	—	—	—	(2,114)
Net unrealised loss on hedge instruments	—	—	—	—	(12,813)	—	—	(12,813)
Costs related to issue of options on follow on share issue	—	(620)	620	—	—	—	—	—
Net gains/(losses) not recognised in the income statement	—	—	1,020	4,703	(12,100)	—	2	(6,375)
Net profit for the year	—	—	—	—	—	39,658	—	39,658
Total income and expense for the year	—	—	620	(1,901)	(12,813)	39,658	—	25,564
Dividends paid	—	—	—	—	—	(27,610)	—	(27,610)
At 31 December 2005	**24,209,670**	**286,801**	**1,020**	**4,703**	**(12,100)**	**18,442**	**2**	**298,868**
At 1 January 2006	**24,209,670**	**286,801**	**1,020**	**4,703**	**(12,100)**	**18,442**	**2**	**298,868**
Net unrealised loss on available-for-sale securities	—	—	—	(2,850)	—	—	—	(2,850)
Issuance of shares	39,232,267	1,194,690	—	—	—	—	—	1,194,690
Costs related to issue of shares	—	(26,557)	—	—	—	—	—	(26,557)
Share options exercised—June 2006	71,146	711	—	—	—	—	—	711
Ordinary shares issued to Directors	6,000	172	—	—	—	—	—	172
Realised losses reclassified to the income statement	—	—	—	29	—	—	—	29
Net unrealised gain on hedge instruments	—	—	—	—	35,051	—	—	35,051
Amortisation of novated swaps	—	—	—	—	591	—	—	591
Cost related to issue of options on follow on share issue	—	(16,300)	16,300	—	—	—	—	—
Movement in minority interest							4	4
Net gains not recognised in the income statement	—	—	17,320	1,882	23,542	—	6	42,750
Net profit for the year	—	—	—	—	—	143,819	—	143,819
Total income and expense for the year	—	—	16,300	(2,821)	35,642	143,819	—	192,940
Dividends paid	—	—	—	—	—	(73,803)	—	(73,803)
At 31 December 2006	**63,519,083**	**1,439,517**	**17,320**	**1,882**	**23,542**	**88,458**	**6**	**1,570,725**

Notes to Consolidated Financial Statements

1. BACKGROUND

Eurocastle Investment Limited (the "Group") was incorporated in Guernsey, Channel Islands on 8 August 2003 and commenced its operations on 21 October 2003. Eurocastle Investment Limited is a euro denominated Guernsey closed-end investment company listed on Euronext Amsterdam (formerly listed on the London Stock Exchange). The activities of the Group include the investing in, and financing and managing of European real estate assets and European real estate related debt.

The Group is externally managed by its manager, FIG LLC (the "Manager"). The Group has entered into a management agreement (the "Management Agreement") under which the Manager advises the Group on various aspects of its business and manages its day-to-day operations, subject to the supervision of the Company's Board of Directors. The Group has no direct employees. For its services, the Manager receives an annual management fee and incentive compensation (as well as reimbursement for expenses, including expenses of certain employees providing property/asset management and finance services), as described in the Management Agreement. The Group has no ownership interest in the Manager.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of Compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS). The financial statements have been prepared under the same accounting principles and methods of computation as in the financial statements as at 31 December 2005 and for the year then ended. The consolidated financial statements are presented in euros, the functional currency of the Group, because the Group conducts its business predominantly in euros.

Basis of Preparation

The consolidated financial statements are prepared on a fair value basis for derivative financial instruments, investment property, financial assets and liabilities held for trading, and available-for-sale assets. Other financial assets and liabilities and non-financial assets and liabilities are stated at amortised or historical cost.

The preparation of these financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Although these estimates are based on the Group's management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

Where such judgements are made they are indicated within the accounting policies below.

Basis of Consolidation

The consolidated financial statements comprise the financial statements of Eurocastle Investment Limited and its subsidiaries for the year ended 31 December 2006. Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred from the Group.

At 31 December 2006, the Group's subsidiaries consisted of a number of subsidiaries in Ireland, Luxembourg and Germany.

Eurocastle Funding Limited ("EFL"), Eurocastle CDO I PLC ("CDO I"), Eurocastle CDO II PLC ("CDO II"), Eurocastle CDO III PLC ("CDO III"), Eurocastle CDO IV PLC ("CDO IV"), Duncannon CRE CDO PLC ("Duncannon") and FECO SUB SPV PLC ("Feco") are all limited companies incorporated in Ireland. The ordinary share capital of these vehicles is held by outside parties and the Company has no voting rights. In accordance with the Standing Interpretations Committee Interpretation 12 Consolidation – Special Purpose Entities, the Group consolidates EFL, CDO I, CDO II, CDO III, CDO IV, Duncannon and Feco as it retains control over these entities and retains the residual risks of ownership of these entities.

Eurocastle owns either directly or indirectly a 100% equity interest in a number of significant operating subsidiaries in Luxembourg, Germany and Ireland, as disclosed in Note 29, which are consolidated into these financial statements.

Eurocastle's investment in real estate fund units are held by Finial Sàrl ("FIP"), a Luxembourg limited company, which is 100% owned by Luxgate Sàrl. Eurocastle owns 100% of Luxgate Sàrl.

Financial Instruments

Classification

Financial assets and liabilities measured at fair value through the income statement are principally those instruments that the Group holds for the purpose of short-term profit taking. These include total return swaps, real estate fund units, interest rate swaps and forward foreign exchange contracts that are not designated as effective hedging instruments.

Available-for-sale assets and restricted short term investments are financial assets that are not classified as instruments held at fair value through the income statement, loans and advances, or held to maturity. Available-for-sale instruments include real estate loans and other asset backed securities.

Recognition

The Group recognises financial assets that are classified as held at fair value through the income statement and available-for-sale assets on the date it commits to purchase the assets (trade date). From this date any gains and losses arising from changes in the fair value of the assets are recognised.

A financial liability is recognised on the date the Group becomes party to contractual provisions of the instrument.

Measurement

Financial instruments are measured initially at fair value plus, in the case of a financial asset or liability not measured at fair value through the income statement, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Subsequent to initial recognition all instruments that are classified as held at fair value through the income and available-for-sale assets are carried at fair value.

All financial assets other than trading instruments and available-for-sale assets are measured at amortised cost less impairment losses. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Fair Value Measurement Principles

The fair value of financial instruments is based on their quoted market price at the balance sheet date without any deduction for transaction costs. If a quoted market price is not available, the fair value of the instrument is calculated using pricing models or discounted cash flow techniques, as applicable.

Where discounted cash flow techniques are used, expected future cash flows are based on our manager's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.

The fair value of derivatives that are not exchange traded is calculated at the amount that the Group would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

Gains and Losses on Subsequent Measurement

Gains and losses arising from a change in the fair value of instruments that are classified as held at fair value through the income statement are recognised directly in the income statement. Gains and losses arising from a change in the fair value of available-for-sale securities are recognised directly in equity until the investment is derecognised (sold, collected, or otherwise disposed of) or impaired, at which time the cumulative gain or loss previously recognised in equity is included in the income statement for the period.

Derecognition of Financial Assets and Liabilities

Financial Assets

A financial asset is derecognised when:

- the rights to receive cash flows from the asset have expired;
- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred the control of the asset.

Where the Group has transferred its right to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except that in the case of a written put option (including a cash settled option or similar provision) on an asset measured at fair value, the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial Liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the income statement.

Impairment

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the calculated future cash flows of the financial asset or group of financial assets that can be reliably measured.

In the case of financial assets classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss, measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement, is removed from equity and recognised in the income statement.

Subsequent increases in the fair values of both debt instruments classified as available-for-sale and financial assets measured at amortised cost, which can be objectively related to an event occurring after previous impairment losses have been recognised in the income statement, are recorded in the income statement. Such reversals are then taken through the income statement only to the extent previous impairment losses have been taken through the income statement.

Hedge Accounting

Where there is a hedging relationship between a derivative instrument and a related item being hedged, the hedging instrument is measured at fair value.

Where a derivative financial instrument hedges the exposure to variability in the cash flows of recognised assets or liabilities, the effective part of any gain or loss on re-measurement of the hedging instrument is recognised directly in equity. The ineffective part of any gain or loss is recognised in the income statement.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

The gains or losses that are recognised in equity are transferred to the income statement in the same period in which the hedged items affect the net profit or loss.

Repurchase Agreements

Securities and real estate loans subject to repurchase agreements are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral. The counterparty liabilities have been classified as repurchase agreements.

Cash and Cash Equivalents

Cash and cash equivalents comprise cash at banks and in hand, short-term deposits, and restricted cash with an original maturity of three months or less.

Restricted Cash

Restricted cash comprises margin account balances held by derivative counterparties as collateral for forward foreign exchange contracts, as well as cash held by the trustees of CDO I, II and III securitisations as a reserve for future trustee expenses. In addition, restricted cash comprises cash held as part of the minimum liquidity requirement for the Dresdner Grund-Fonds. As such, these funds are not available for use by the Group.

Investment Properties

Investment properties comprise land and buildings. In accordance with IAS 40, property held to earn rentals and/or for capital appreciation is categorised as investment property. Investment properties are measured initially at cost, including transaction costs and recognised when the customary conditions precedent under the relevant purchase agreement have been satisfied and the purchase price is paid to the vendor. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met; and excludes the costs of day-to-day servicing of an investment property. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the balance sheet date. Gains or losses arising from changes in the fair values of investment properties are included in the income statement in the year in which they arise.

Investment properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in the income statement in the year of retirement or disposal.

Properties held under operating leases are accounted for as investment property when they meet the definition of investment property. In such cases the operating leases are accounted for as if they were finance leases with an associated liability representing the present value of future minimum lease payments included in finance lease liabilities on the balance sheet.

Finance Leases

The determination of whether an arrangement is, or contains a finance lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and the reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to the income statement as they arise.

Real Estate Fund Units

Real estate fund units are recorded at fair value in the consolidated balance sheet, with any change in fair value recognised in the consolidated income statement. The interest income is recognised in the income statement as it accrues, taking into account the effective yield of the real estate fund units.

Intangible Assets

Software development costs are capitalised when, they meet certain criteria relating to identifiability, it is probable that future economic benefits will flow to the enterprise, and the cost can be measured reliably. These software costs are recognised in income statement through amortisation of the capitalised software costs on a straight line basis over their expected useful life of 5 years.

Interest-Bearing Loans and Borrowings

All loans and borrowings, including the Group's repurchase agreements, are initially recognised at fair value, being the fair value of consideration received, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Minority Interests

Minority interests represent interests held by outside parties in the Group's consolidated subsidiaries.

Revenue Recognition

The Company considers revenue to comprise interest income and rental income as its principal business is investing in, financing and management of European real estate and other asset backed securities and other real estate related assets.

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured.

Interest income and expenses are recognised in the income statement as they accrue, taking into account the effective yield of the asset/liability or an applicable floating rate. Interest income and expense include the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Rental income arising from operating leases on investment properties is recognised on a straight-line basis over the lease term. Incentives given to enter into lease agreements are spread evenly over the lease term as a reduction of rental expense, even if the payments are not made on such a basis.

Service Charges

The Company acts as a principal bearing the risk of over/under charging of service costs to its tenants. The service income earned from the tenants and the service costs incurred are shown separately in the income statement.

Service Income

Service income represents service costs recoverable from tenants and is recognised on the basis of services being provided.

Service Costs

Service costs represent service contracts entered into for the operation of the property, and are expensed on an accrual basis.

Property Expenses

Property expenses are expenses that are incurred on the property portfolio that are not able to be recovered from tenants. Property expenses are recognised on an accruals basis in the income statement.

Income Tax

The Company is a Guernsey, Channel Islands limited company and is not subject to taxation. The Company's subsidiaries, EFL, CDO I, CDO II, CDO III, CDO IV, Duncannon and Feco are Irish registered companies and are structured to qualify as securitisation companies under section 110 of the Taxes Consolidation Act 1997. It is envisaged that these companies will generate minimal net income for Irish income tax purposes and no provision for income taxes has been made for these companies.

The Group's German subsidiary companies, Longwave and Shortwave, are subject to German income tax on income arising from their investment properties, after the deduction of allowable debt financing costs and other allowable expenses. The taxation accrual for the year ended 31 December 2006 relates to these subsidiaries.

The Group's subsidiaries Bastion, Belfry, Truss, Bridge and Turret are also subject to German income tax on rental income net of interest and other expense deductions. A small taxable income has been generated, within these entities, which has generated a small tax accrual, which includes deferred tax, for the year ended 31 December 2006.

The Group's investment in the underlying properties in relation to the Drive portfolio and the Real Estate Fund Units is by way of units in an open-ended real estate fund. No corporation tax is due on income generated from its investment in these units.

Certain Luxembourg subsidiaries are subject to Luxembourg tax on a small amount of net interest which is attributable to shareholder loans and other debt instruments used within each of the structures supporting the different investment property portfolio.

Deferred Taxation

Deferred income tax is provided in full, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

Deferred income tax is recognised for all temporary differences arising between the tax base of assets and liabilities and their carrying amounts in the financial statements, with the following exceptions:

- where the temporary difference arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss;
- in respect of taxable temporary differences associated with investments in subsidiaries, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future; and
- deferred income tax assets are recognised only to the extent that it is probable that taxable profit will be available against which deductible temporary differences, carried forward tax credits or tax losses can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance sheet date.

Notes to Consolidated Financial Statements *(continued)*

Income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

Foreign Currency Translation

The functional and presentation currency of the Group and its subsidiaries is the euro. Transactions in foreign currencies are initially recorded in the functional currency rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Segmental Reporting

A business segment is a group of assets and operations engaged in providing services that are subject to risks and returns that are different from those of others business segments.

A geographical segment is engaged in providing services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

Share-Based Payments

Share-based payments are accounted for based on their fair value on grant date. The fair value is calculated by using a trinomial pricing model. The fair value of the share options granted in relation to capital raises has been fully recognised (vested) on the date of grant as a cost relating to the issue of shares with a corresponding increase to other reserves.

Share options granted to Directors are recognised in the income statement over the period that the services are received.

Comparatives

Certain comparative figures have been reclassified (derivative assets, derivative liabilities, finance lease payables, are now classified as separate line items from other assets and trade and other payables on the balance sheet, and service charge income and expense have been grossed up and disclosed as separate line items from property operating expenses in the income statement) to provide better understanding of the Group's financial position and conform with the presentation adopted in these financial statements.

International Financial Reporting Standards to be Adopted in 2007 and Later

IAS 1 Amendment—Presentation of Financial Statements: Capital Disclosures and IFRS 7 Financial Instruments: Disclosures

Upon adoption of IAS 1 Amendments and IFRS 7, the Group will have to disclose additional information about its policies and processes for managing capital, as well as financial instruments, their significance and the nature and extent of risks that they give rise to. More specifically the Group will need to disclose the fair value of its financial instruments and its risk exposure in greater detail. There will be no effect on reported income or net assets.

3. INTEREST INCOME

Interest income for the year ended 31 December 2006 of €95.97 million (31 December 2005: €65.54 million) is primarily interest income earned on the asset backed securities, available-for-sale and asset backed securities pledged under repurchase agreements.

4. RENTAL INCOME

Rental income for the year ended 31 December 2006 of €152.45 million (31 December 2005: €28.13 million) represents rental income earned on investment properties.

Property operating expenses, including repairs and maintenance, arising from investment properties that generated rental income during the year for the year ended 31 December 2006 was €7.46 million (2005: €1.94 million).

5. SERVICE CHARGE INCOME AND EXPENSE

Service charge income for the year ended 31 December 2006 of €31.90 million (31 December 2005: €6.55 million) represents the service costs recoverable from tenants.

Service charge expense for year ended 31 December 2006 of €41.24 million respectively (31 December 2005: €8.60 million) represents the costs relating to the service contracts entered into for the operation of the properties.

6. INTEREST EXPENSE

Interest expense for year ended 31 December 2006 of €150.28 million (31 December 2005: €58.14 million) comprises interest expense incurred on the CDO bonds payable, bank borrowings and repurchase agreements.

7. OTHER OPERATING EXPENSES

	31 December 2006 €'000	31 December 2005 €'000
Professional fees	5,764	1,959
Management fees	12,191	3,626
Incentive fees	2,717	3,834
Amortisation of intangible assets	144	9
Other*	5,207	604
	26,023	10,032

**Included within other operating expenses for the year are reimbursement property related asset management services of €3.9 million (2005: €54,000) to FIG LLC.*

8. TAXATION EXPENSE

	31 December 2006 €'000	31 December 2005 €'000
Current tax		
Germany	9	40
Luxembourg	363	127
Total current tax	372	167
Deferred tax		
Germany	3,366	2,111
Total deferred tax	3,366	2,111
Total tax expense	3,738	2,278

Reconciliation of the Total Tax Expense

The tax expense in the income statement for the year is higher than the standard rate of corporation tax in Guernsey of 0%. The difference is reconciled below:

	31 December 2006 €'000	31 December 2005 €'000
Net profit before taxation	147,557	41,936
Profit on ordinary activities based on Guernsey tax of 0% (2005: 0%)	—	—
Overseas taxation	3,738	2,278
Total tax expense reported in the income statement	3,738	2,278

Notes to Consolidated Financial Statements *(continued)*

Analysis of Deferred Tax

	31 December 2006 €'000	31 December 2005 €'000
Tax losses carried forward	**(713)**	(1,567)
Short term timing differences		
Loan expense	**472**	956
Tenant improvements and leasing commissions	**208**	—
Other	**(15)**	—
Long term timing differences		
Accelerated capital allowance	**3,516**	1,426
Revaluation of investment properties	**(167)**	883
Acquisition expense	**65**	341
Other	**—**	72
Deferred tax expense	**3,366**	2,111

Movement in Taxation Payable

	31 December 2006 €'000	31 December 2005 €'000
Opening tax payable	**2,278**	—
Tax paid	**—**	—
Tax expense for the period	**3,738**	2,278
Closing taxation payable	**6,016**	2,278
Split between:		
Current tax	**539**	167
Deferred tax	**5,477**	2,111
Closing taxation payable	**6,016**	2,278

The taxation expense for the year ended 31 December 2006 relates to the Group's Luxembourg and German subsidiary companies as described in Note 2. The German tax charge is based on German tax on income arising from its investment properties, after the deduction of allowable debt financing costs and other allowable expenses. The Luxembourg tax charge is based on Luxembourg tax on a small amount of net interest which is attributable to shareholder loans and other debt instruments used within each of the structures supporting the different investment property portfolios.

9. CASH AND CASH EQUIVALENTS

	31 December 2006 €'000	31 December 2005 €'000
Cash on hand and balances with banks	**77,613**	13,640
Restricted cash DGF Liquidity requirement	**45,086**	—
Cash and cash equivalents	**122,699**	13,640

There is a minimum liquidity requirement of 5% of the value of Dresdner Grund-Fonds (DGF), the subsidiary through which the Drive portfolio is held, in accordance with German Investment Companies Act requirements. At 31 December 2006, the liquidity requirement was held as a short term deposit. Subsequent to 31 December 2006, the liquidity requirement of 5% has been invested in high grade debt securities of short duration.

10. AVAILABLE-FOR-SALE SECURITIES

The following is a summary of the Group's available-for-sale securities at 31 December 2006.

	Current Face Amount €'000	Amortised Cost Basis €'000	Gross Unrealised Gains €'000	Gross Unrealised Losses €'000	Carrying Value €'000	Weighted Average S&P Rating*	Weighted Average Coupon	Weighted Average Margin	Weighted Average Maturity (Years)
Portfolio I									
CMBS	140,407	140,391	687	(71)	141,007	BBB	5.19%	1.58%	3.83
Other ABS	259,885	260,404	1,329	(356)	261,377	BBB	5.46%	1.82%	4.25
	400,292	400,795	2,016	(427)	402,384	BBB	5.37%	1.74%	4.10
Portfolio II									
CMBS	222,651	222,738	364	(252)	222,850	BBB	4.98%	1.39%	5.34
Other ABS	199,197	199,581	316	(376)	199,521	BBB	4.98%	1.29%	4.32
	421,848	422,319	680	(628)	422,371	BBB	4.98%	1.34%	4.86
Portfolio III									
CMBS	244,209	244,307	564	(303)	244,568	BBB	5.58%	1.96%	5.25
Other ABS	227,747	227,883	549	(186)	228,246	BBB	5.09%	1.39%	3.86
	471,956	472,190	1,113	(489)	472,814	BBB	5.34%	1.69%	4.58
Portfolio IV									
CMBS	99,477	99,223	334	(57)	99,500	BBB	4.88%	1.63%	3.45
Other ABS	64,583	64,564	35	(715)	63,884	BBB	5.15%	1.70%	5.25
	164,060	163,787	369	(772)	163,384	BBB	4.99%	1.66%	4.16
Total Portfolio	1,458,156	1,459,091	4,178	(2,316)	1,460,953	BBB	5.20%	1.60%	4.48
Other Securities									
CMBS	34,126	34,126	20	—	34,146	AA+	4.02%	0.37%	8.03
Other ABS	44,500	44,500	—	—	44,500	AAA	4.74%	0.90%	0.73
	78,626	78,626	20	—	78,646	AAA	4.42%	0.67%	3.90
	1,536,782	1,537,717	4,198	(2,316)	1,539,599	BBB	5.16%	1.55%	4.45
Restricted Cash—Cash to be Invested					20,708				
Total Asset Backed Securities (Including Cash to be Invested)					1,560,307				

**Ratings are based on the minimum public or private rating obtained from Fitch, Moody's or S&P ratings agencies*

CMBS—Commercial Mortgage Backed Securities

Other ABS—Other Asset Backed Securities

The Securities Within Portfolio I, II and III Are Encumbered by CDO Securitisations (Note 17).

The following is a summary of the Group's available-for-sale securities at 31 December 2005.

	Current Face Amount €'000	Amortised Cost Basis €'000	Gross Unrealised Gains €'000	Gross Unrealised Losses €'000	Carrying Value €'000	Weighted Average S&P Rating	Weighted Average Coupon	Weighted Average Margin	Weighted Average Maturity (Years)
Portfolio I									
CMBS	152,096	151,956	1,592	(43)	153,505	BBB	4.13%	1.86%	3.16
Other ABS	248,300	248,813	2,258	(159)	250,912	BBB+	4.28%	1.95%	3.74
	400,396	400,769	3,850	(202)	404,417	BBB	4.23%	1.91%	3.52
Portfolio II									
CMBS	130,013	129,898	434	(527)	129,805	BBB	3.89%	1.67%	5.02
Other ABS	143,945	144,266	588	(350)	144,504	BBB	3.82%	1.40%	4.84
	273,958	274,164	1,022	(877)	274,309	BBB	3.85%	1.53%	4.93
Portfolio III									
CMBS	169,452	169,646	1,016	(254)	170,408	BBB-	4.26%	1.94%	4.81
Other ABS	211,768	212,038	628	(810)	211,856	BBB	3.87%	1.61%	3.56
	381,220	381,684	1,644	(1,064)	382,264	BBB	4.04%	1.75%	4.11
Portfolio IV									
CMBS	207,063	206,254	308	(139)	206,423	BBB+	4.00%	1.81%	5.30
Other ABS	67,952	68,025	137	(188)	67,974	A-	4.06%	1.82%	4.70
	275,015	274,279	445	(327)	274,397	BBB+	4.01%	1.81%	5.15
Total Portfolio	1,330,589	1,330,896	6,961	(2,470)	1,335,387	BBB	4.05%	1.77%	4.32
Other Securities									
CMBS	65,617	65,543	73	(207)	65,409	AA-	2.89%	0.58%	0.72
Other ABS	44,500	44,154	346	—	44,500	AAA	3.54%	0.90%	1.76
	110,117	109,697	419	(207)	109,909	AA	3.15%	0.71%	1.14
	1,440,706	1,440,593	7,380	(2,677)	1,445,296	BBB+	3.98%	1.69%	4.07
Restricted Cash—Cash to be Invested					7,251				
Total Asset Backed Securities (Including Cash to be Invested)					1,452,547				

Asset backed securities, available-for-sale at fair value of €78.65 million (31 December 2005: €109.91 million) have been pledged to third parties in sale and repurchase agreements. In accordance with the revisions to IAS 39 Financial Instruments: Recognition and Measurement, effective 1 January 2005, these securities have been reclassified as pledged securities as follows:

	31 December 2006 €'000	31 December 2005 €'000
Asset backed securities, available-for-sale (includes cash to be invested)	**1,481,661**	1,342,638
Asset backed securities pledged under repurchase agreements	**78,646**	109,909
Total Asset Backed Securities	**1,560,307**	1,452,547

Cumulative net unrealised gains on available-for-sale securities and hedge instruments recognised in the statement of changes in equity were as follows:

	31 December 2006 €'000	31 December 2005 €'000
Unrealised gains on available-for-sale securities	**4,198**	7,380
Unrealised losses on available-for-sale securities	**(2,316)**	(2,677)
	1,882	4,703

11. REAL ESTATE RELATED LOANS

The following is a summary of the Group's real estate loans at 31 December 2006.

	Current Face Amount €'000	Amortised Cost Basis €'000	Gross Unrealised Gains €'000	Gross Unrealised Losses €'000	Carrying Value €'000	Weighted Average S&P Rating	Weighted Average Coupon	Weighted Average Margin	Weighted Average Maturity (Years)
Real estate loans	**430,988**	**428,370**	**—**	**—**	**428,370**	**B+***	**6.38%**	**2.88%**	**4.78**

**57% of the Real Estate loan portfolio has ratings based on the minimum public or private ratings obtained from Fitch, Moody's or Standard & Poor's (S&P) ratings. 43% of the Real Estate loans have been assigned an internal credit rating in anticipation of a formal rating, which is currently being sought from S&P and Fitch and Moody's.*

As at 31 December 2005:

	Current Face Amount €'000	Amortised Cost Basis €'000	Gross Unrealised Gains €'000	Gross Unrealised Losses €'000	Carrying Value €'000	Weighted Average S&P Rating	Weighted Average Coupon	Weighted Average Margin	Weighted Average Maturity (Years)
Real estate loans	93,120	92,649	—	—	92,649	BB**	5.49%	3.48%	3.88

***Included in real estate loans are loans with a total current face amount of €47.0 million and with an average rating of BB from S&P.*
51% of the Real Estate loan portfolios have ratings based on the minimum public or private ratings obtained from Fitch, Moody's or Standard & Poor's (S&P) ratings. 49% of the Real Estate loans had been assigned an internal credit rating in anticipation of a formal rating.

12. OTHER ASSETS

	31 December 2006 €'000	31 December 2005 €'000
Unsettled security transactions	—	26,178
Interest receivable	**16,872**	18,963
Rent receivable	**5,551**	4,222
Prepaid expenses	**736**	254
Service charge receivable	**2,632**	384
Deposit fee*	**14,360**	—
Fund income receivable	**7,900**	—
Other accounts receivable and deferred income**	**21,486**	—
	69,537	50,001

**Deposit fee relates to acquisition fees paid prior to the purchase of the Mars portfolio.*

***Other accounts receivable includes €7.9 million relating to a VAT claw back and €7.9 million relating to purchase price adjustments.*

Included in other assets is €222,000 (2005: €310,000) due in more than one year, relating, in the current year, to deferred rent and in the prior year, to rent receivable.

13. DERIVATIVE ASSETS

	31 December 2006 €'000	31 December 2005 €'000
Derivative Assets	**22,690**	11,470
	22,690	11,470

13.1 Derivative Assets

Derivative assets represent the fair value of interest rate swaps and foreign exchange forward contracts.

13.2 Total Return Swaps

Included in the Derivative Assets are two total return swaps, the fair value of which as at 31 December 2006 is €288,313 (31 December 2005: €144,000) and the collateral deposit posted is €4.75 million (31 December 2005: €10.6 million). These total return swaps have been recorded as Derivative Assets and are treated as trading assets that are not designated as an Effective Hedging Instrument for accounting purposes and any gain or loss arising from the change in fair value of the assets is recognized through profit and loss.

Total Return Swap 1

In November 2006, Eurocastle entered into a total return swap with a major investment bank, whereby it receives the sum of all interest (at EURIBOR + 2.50%) and any positive changes in value from a referenced term loan with an initial notional amount of €10.70 million, and pays interest (at EURIBOR + 0.80%) on the notional amount plus any negative change in value amounts from such loan. Under the contract, the parent is required to post an initial collateral deposit equivalent to 14% of the notional amount and additional margin may be payable in the event of a decline in the value of the referenced term loan.

Total Return Swap 2

In December 2005, a subsidiary entered into a total return swap with a major investment bank, whereby it receives the sum of all interest (at EURIBOR + 4.00%) and any positive change in value from a referenced term loan with an initial notional amount of €25.85 million, and pays interest (at EURIBOR + 0.40%) on the notional amount plus any negative change in value amounts from such loan. In May 2006, the subsidiary increased its holding in the existing total return swap by €6.6 million. Under the contract, the parent is required to post an initial collateral deposit equivalent to 10% of the notional amount and additional margin may be payable in the event of a decline in the value of the referenced term loan.

Total Return Swap 3

In August 2005, a subsidiary entered into a total return swap with a major investment bank, whereby it receives the sum of all interest (at an average of Sterling LIBOR + 5.50%) and any positive change in value from a referenced term loan with an initial notional amount of £15 million, and pays interest (at Sterling Overnight Interbank Average—"SONIA") on the notional amount plus any negative change in value amounts from such loan. Under the contract, the subsidiary is required to post an initial collateral deposit equivalent to 36.7% of the notional amount and additional margin may be payable in the event of a decline in the value of the referenced term loan. In August 2006, the subsidiary sold 100% of its interest in this total return swap.

14. REAL ESTATE FUND UNITS

Between July and October 2005, the Group purchased an interest in 1,500 Class A real estate fund units backed by a portfolio of 394 properties in Italy. The original term of the Lease Agreement is 9 years, automatically renewable for a further 9 years, unless terminated by the Agenzia del Demanio (a public entity established by the Italian Ministry of Finance), with 12 months prior notice. The properties have a total occupancy of 100%. On 12 September 2006, 300 real estate fund units were sold.

	31 December 2006 €'000	31 December 2005 €'000
At 1 January	189,591	—
Purchase of real estate fund units	—	181,493
Additional acquisition costs	2	—
Sale of 300 Units	(36,299)	—
(Decrease)/increase in fair value	(5,217)	8,098
At 31 December 2006	148,077	189,591

15. INVESTMENT PROPERTY

The table below shows the items aggregated under investment property in the consolidated balance sheet:

	Freehold Land & Buildings €'000	Leasehold Property €'000	31 December 2006 Total €'000	31 December 2005 Total €'000
Opening balance	448,060	15,480	463,540	318,514
Additions	2,657,957	109,256	2,767,213	143,524
Disposals	—	—	—	(459)
Increase in fair value	76,113	2,006	78,119	1,961
Total	3,182,130	126,742	3,308,872	463,540

The value of investment properties incorporates 31 properties which are held by the Company under finance or operating leases. An associated liability is recognised at an amount equal to the fair value of the leased property, or if lower, the present value of the minimum lease payments, determined at the inception of the lease.

Investment properties are stated at fair value, which has been determined based on valuations performed by industry specialists in valuing these types of investment properties. The main factors the valuers consider when determining a fair valuation are the following: passing rent, void periods and relettability and marketability of properties. The fair value represents the amount at which the asset could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's-length transaction at the date of valuation, in accordance with international valuation standards.

Lease arrangements over the land on which the 31 investment properties are built have unexpired terms ranging from 9 years to 86 years.

A reconciliation of investment property valuations to the balance sheet carrying value of property is shown below:

	31 December 2006 €'000	31 December 2005 €'000
Investment property at market value as determined by external valuers	3,283,072	460,588
Minimum payments under head leases separately included in trade and other payables on the balance sheet	25,800	2,952
Balance sheet carrying value of investment property	3,308,872	463,540

Schedule of Minimum Lease Payments under Finance Leases

	Total Value 31 December 2006 €'000	Present Value 31 December 2006 €'000	Total Value 31 December 2005 €'000	Present Value 31 December 2005 €'000
Under 1 year	1,375	1,281	239	227
From 2 to 5 years	5,736	4,650	1,013	778
More than 5 years	99,423	19,869	27,710	1,947
Total	**106,534**	**25,800**	28,962	2,952

Additional Information

The tables below provide additional information for various portfolios within the group.

Portfolio	Passing Rent* €'000	Net Operating Income** €'000	Gross Rental Income €'000	Lettable Area Sq Metre	Vacancy %	Property Valuation €'000	Property Cost €'000	NOI Yield (Cost) %
Drive	111,965	101,032	114,395	841,682	16.4%	2,069,744	1,972,206	5.1%
Wave	26,435	23,159	26,435	294,486	18.7%	332,186	320,181	7.2%
Bridge	30,129	28,799	30,129	192,498	5.6%	496,120	501,886	5.7%
Retail	31,482	28,197	31,482	302,876	0.3%	410,822	408,769	6.9%
Total	**200,011**	**181,187**	**202,441**	**1,631,542**	**12.5%**	**3,308,872**	**3,203,042**	**5.7%**

Portfolio	Rent on Expiring Leases Yr 0–1 €'000	Rent on Expiring Leases Yr 2–3 €'000	Rent on Expiring Leases Yr 4–6 €'000	Rent on Expiring Leases Yr 7–10 €'000	Rent on Expiring Leases Yr 10+ €'000	Average Lease Length Years	Number of Properties
Drive	4,053	15,094	39,602	18,009	35,207	7.0	301
Wave	1,073	5,916	7,182	11,315	948	5.4	109
Bridge	1,251	4,286	10,975	1,162	12,456	6.7	6
Retail	164	951	4,995	13,921	11,451	9.0	145
Total	**6,541**	**26,247**	**62,754**	**44,407**	**60,062**	**7.1**	**561**

**Passing rent is defined as the annual gross rental income at the year end, excluding the net effects of straightlining for lease incentives.*

***Net Operating Income ("NOI") represents gross rental income less net service charge expenses and property operating expenses.*

16. INTANGIBLE ASSETS

	31 December 2006 €'000	31 December 2005 €'000
Cost		
Balance at 1 January	551	551
Additions	1,430	—
Balance at 31 December	1,981	551
Amortisation		
Balance at 1 January	(9)	—
Charge for the year	(144)	(9)
Balance at 31 December	(153)	(9)
Carrying amount		
At 1 January	542	551
At 31 December	1,828	542

The capital expenditure above represents intangible software, of which €1.18 million of additions is work in progress as at 31 December 2006.

17. BONDS PAYABLE

CDO Bonds

As at 31 December 2006

	Class	Rating	Current Face Amount €'000	Carrying Amount €'000	Weighted Average Cost of Financing	Weighted Average Margin	Weighted Average Maturity (in years)
CDO I	A and B Notes	AAA/AA	351,000	348,676	4.29%	0.59%	5.4
CDO II	A, B and C Notes	AAA/AA/A	406,278	402,879	4.33%	0.47%	8.5
CDO III	A, B and C Notes	AAA/AA/A	462,500	458,720	4.17%	0.47%	8.5
Total			**1,219,778**	**1,210,275**	**4.26%**	**0.51%**	**7.5**

As at 31 December 2005

	Class	Rating	Current Face Amount €'000	Carrying Amount €'000	Weighted Average Cost of Financing	Weighted Average Margin	Weighted Average Maturity (in years)
CDO I	A and B Notes	AAA/AA	351,000	348,271	3.08%	0.60%	6.3
CDO II	A, B and C Notes	AAA/AA/A	265,362	262,783	3.02%	0.53%	9.5
CDO III	A, B and C Notes	AAA/AA/A	370,000	366,431	2.97%	0.49%	9.5
Total			**986,362**	**977,485**	**3.02%**	**0.54%**	**8.4**

None of the CDO bonds are due to be repaid within one year of the balance sheet date.

18. BANK BORROWINGS

The bank borrowings comprises of:

		31 December 2006 €'000	31 December 2005 €'000
Term finance*	(Note 18.1)	**2,534,024**	782,031
Revolving credit facility	(Note 18.2)	**—**	18,578
Other bank financing—under 1 year	(Note 18.3)	**79,488**	34,553
Other bank financing—over 1 year	(Note 18.3)	**67,051**	—
		2,680,563	835,162

**All term financing is due within more than one year except €1.33 million which is due within one year.*

18.1 Term Financing

		Current Nominal Amount €'000		Carrying Amount €'000			
Real Estate Debt	Month Raised	31 December 2006	31 December 2005	31 December 2006	31 December 2005	Hedged Weighted Average Funding Cost	Maturity Date
CDO IV	Jul 2005	**—**	308,321	**—**	307,917	0.00%	
Investment Property							
Wave Portfolio	Dec 2004	**242,803**	245,900	**240,397**	242,762	4.72%	Apr 2013
Belfry Portfolio	Aug 2005	**56,240**	56,240	**55,433**	55,363	4.81%	Oct 2015
Bastion Portfolio	Sep 2005	**26,500**	26,500	**25,211**	26,202	4.42%	Sep 2012
Truss Portfolio	Dec 2005	**85,280**	30,163	**84,537**	29,607	4.86%	Feb 2016
Turret Portfolio	May 2006	**147,556**	—	**146,763**	—	4.94%*	May 2016
Drive Portfolio	Feb 2006	**1,525,000**	—	**1,511,443**	—	4.20%	Jan 2013
Bridge Portfolio	Oct 2006	**372,090**	—	**373,856**	—	4.74%**	Jan 2014
Real Estate Fund Units							
FIP Units	Jul 2005	**97,500**	121,875	**96,384**	120,180	5.53%	Jul 2018
Total		**2,552,969**	788,999	**2,534,024**	782,031		

**This is the fixed rate of the loan that is effective as from 7 February 2007 until maturity. The effective interest rate that applied during the year was 4.79%.*
***This is the fixed rate of the loan that is effective as from 15 January 2007 until maturity. The effective interest rate that applied during the year was 4.36%.*

Real Estate Debt

On 14 July 2005, the Group through Eurocastle CDO IV PLC entered into a €400 million 3 year extendable warehouse facility with a major UK bank. This facility was previously used to refinance a significant part of the portfolio previously financed under short-term repurchase agreements, and is currently being used to build and finance a portfolio of asset backed securities and real estate related loans. The lender uses a rating agency CDO model to determine the level of equity contribution the Group is required to make to support the portfolio from time to time. The facility is secured over, inter alia, the collateral making up the portfolio. The margin payable to the lender depends on the deemed rating levels of the portfolio as determined by the rating agency model.

As at 31 December 2006 there were no utilisations on the warehousing facility (2005: €308.3 million).

Investment Properties

In order to finance the Investment Property portfolios, the Group entered into non-recourse loan facilities as described in the table above. These facilities are secured in the customary manner for German real estate lending; granting security over, inter alia, the real estate purchased as well as rent receivables and bank accounts of the borrower. Interest in respect of these facilities is payable quarterly.

In December 2004, the Group financed the Wave Portfolio with a €246.5 million facility of which €242.8 million had been drawn down at 31 December 2006. The facility is for 8.4 years from the date of signature and, after allowing for an interest rate swap on €210 million, the average funding cost was 4.72%.

The Truss Portfolio is financed with a 10 year (at signing) non-recourse €85.3 million term loan which bears a fixed interest rate of 4.85%.

The Drive Portfolio is financed with a 7 year (at signing) €1,525 million facility consisting of a senior and junior loan of €840 million and €685 million respectively. €50 million of the junior loan bears interest at 1.13% to match a liquidity reserve maintained by Dresdner Grund-Fonds whereas the remaining portion bears a fixed rate. The senior loan has a weighted average funding cost of 3.83% and the junior loan has a weighted average funding cost of 4.64%.

The Bridge Portfolio is financed with a 7 year (at signing) €372 million term loan at an effective interest cost of 4.79%.

The Belfry Portfolio is financed with a 10 year (at signing) non-recourse €56.2 million term loan at an effective interest rate cost of 4.81%.

The Bastion Portfolio is financed with a 10 year (at signing) non-recourse €26.5 million term loan at an effective interest rate cost of 4.42%.

The Turret Portfolio is financed with a 10 year (at signing) non-recourse €150 million term loan which bears interest at Euribor + 0.9% up to February 7, 2007 and thereafter, has an effective interest cost of 4.94%.

Real Estate Fund Units

On 22 July 2005, the Group entered into a non-recourse 13 year loan facility to finance its acquisition of 1,450 Class A Units in Fondo Immobili Pubblici. The facility is secured over, inter alia, the 1,450 Class A Units, an assignment of receivables under the units, a pledge over bank accounts and over shares in the borrower. The interest rate on the loan is Euribor + 1.95%, payable semi-annually. On 21 October 2005, the Group acquired a further 50 Class A Units through the same facility. On 20 September 2006, the Group sold 300 Class A Units (20% of the total holdings), resulting in a pro-rated repayment of the finance facility.

18.2 Revolving Credit Facility

In December 2004, the Group entered into a revolving €35 million bank credit facility as a means of securing access to temporary working capital. The facility is secured by receivables flowing from CDO I, CDO II, CDO III and EFL, as well as from the Group's Luxembourg subsidiaries representing income from the investment properties and real estate fund units, and with security assignments of the Group's rights under its management agreement with FIG LLC. The facility contains a number of financial covenants including a maximum leverage ratio and a minimum interest cover ratio. The interest rate on drawn amounts is Euribor + 1.5% p.a., while on undrawn amounts it is 0.4% p.a. The facility was increased to €50 million on 26 May 2005. On 15 May 2006, the facility was further increased to €150 million. In October 2006, the facility was increased to €300 million until maturity in October 2007.

As at 31 December 2006, there were no utilisations on the credit facility (31 December 2005: €18.6 million).

18.3 Other Bank Financing

In May 2005, in order to finance the participation in a loan made in connection with a prime commercial property in Paris, the Group entered into a full recourse €10 million one year loan facility. The facility was backed by a security assignment over the financed asset. It also contained an obligation to ensure that loan to value remains below 75%. The loan bore a rate of Euribor + 1.85%. In May 2006, this loan facility matured and the financing was transferred to the revolving credit facility with Deutsche Bank as described below.

In August 2005, in order to finance the participation in a loan that had previously been made on certain properties leased to a leading financial institution in the United Kingdom, the Group entered into a full recourse €24.5 million one year loan facility. The participation had been transferred to the lender as security for the facility. It also contained an obligation to ensure that loan to value remained below 75% and bore a rate of Libor + 1.00%. On maturity of this facility, the financing was transferred to the revolving credit facility with Deutsche Bank as described below.

In May 2006, in order to finance the participation in certain B note loans, the Group entered into a 3 year revolving credit facility with Deutsche Bank. The facility contains a number of financial covenants. Its mark to market exposure is determined by the Investment manger, based on market quotations. Interest rates on drawn amounts depend upon the loan to value and collateral quality of the underlying lender with drawdowns currently bearing rates between 0.75% to 1.75% above Libor and Euribor. The security facility is backed by a security assignment over the financed asset. As at 31 December 2006, this facility was fully drawn in an amount of €67.1 million.

In August 2006, in order to finance the sub-participation in a real estate loan secured on properties leased to a leading German retailer, the Group entered into an €80 million, 364 day credit facility with Lehman Brothers. The facility contains a number of financial covenants including a requirement to deliver cash collateral to the lender equal to the excess of any mark to market decline over €200,000. Interest rates on the drawn amounts are 1.50% above Euribor. The security facility is backed by a security assignment over the financed asset and was drawn in an amount of €79.5 million at 31 December 2006.

19. REPURCHASE AGREEMENTS

The Company's consolidated subsidiary EFL has entered into master repurchase agreements with certain major investment banks to finance the purchase of available-for-sale securities. The obligations under those agreements are guaranteed by the Company. The terms of the repurchase agreements provide for interest to be calculated with reference to floating rate benchmarks (i.e., Euribor or Sterling Libor) which reset or roll monthly or quarterly, with the corresponding security coupon payment dates, plus an applicable spread.

As at 31 December 2006, the Group's carrying amount and weighted average financing cost of these repurchase agreements was approximately €75.49 million (31 December 2005: €103.54 million) and 3.84% (31 December 2005: 2.61%) respectively.

20. TRADE AND OTHER PAYABLES

	31 December 2006 €'000	31 December 2005 €'000
Security deposit	**5,421**	5,221
Unsettled security purchases	**—**	17,604
Interest payable	**22,869**	6,953
Due to manager (note 28)	**7,508**	4,555
Accrued expenses & other payables*	**57,501**	7,063
	93,299	41,396

**Accrued expenses & other payables includes: €19 million trade payables, €15 million capital expenditure provisions relating to improvement of conditions of the properties, €9 million accruals, €13 million of closing costs relating to current year acquisitions and €1 million ground rents payable.*

All amounts included above are due within less than one year except €5.4 million (2005: €5.2 million) security deposits due in more than five years and the remainder of €21,000 (2005: €Nil) due within one to five years. In the prior year accrued expenses included €1.3 million other payables due in more than one year.

21. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing net profit after taxation by the weighted average number of shares of ordinary stock outstanding during the period.

Diluted earnings per share is calculated by dividing net profit available to ordinary shareholders by the weighted average number of ordinary shares outstanding plus the additional dilutive effect of potential ordinary shares during the period.

The Group's potential ordinary shares during the period were the share options issued under its share option plan. There have been no other transactions involving ordinary shares or potential ordinary shares since the reporting date and before the completion of the financial statements.

The following is a reconciliation of the weighted average number of ordinary shares outstanding on a diluted basis.

	Year Ended 31 December 2006	Year Ended 31 December 2005
Weighted average number of ordinary shares outstanding, basic	44,956,083	21,392,936
Dilutive effect of ordinary share options	1,804,543	772,928
Weighted average number of ordinary shares outstanding, diluted	46,760,626	22,165,864

22. SHARE CAPITAL AND RESERVES

As at 31 December 2005, there were 24,209,670 shares issued and outstanding.

On 27 January 2006, the Group made a further public offering and issued 11,667,000 ordinary shares at a price of €30 each. On 1 February 2006, the over-allotment option relating to the January offering was exercised resulting in 1,156,000 ordinary shares being issued at €30 each.

On 15 February 2006, immediately prior to completion of the Dresdner Portfolio acquisition, 8,571,429 shares with aggregate nominal value of €8,571,429 were issued to certain funds managed by Fortress Investment Group LLC (the "Fortress Funds") at €17.50 each raising gross proceeds of €150 million. The principal terms of the Fortress Funds investment were agreed on 22 December 2005 and were, in relevant part, as follows:

The Fortress Funds would invest up to €300 million by subscribing for shares at €17.50 per share (representing an approximate 2.75% discount to the weighted average share price for the Group's shares over the 10 day period up to 21 December 2005), provided that the Group could reduce the amount of such subscription down to €150 million were it able to raise funds prior to completion of the Dresdner acquisition; as the Company was successful in raising additional capital prior to completion of the Dresdner portfolio acquisition in the offering described above, the Fortress Funds' subscription was reduced to €150 million.

The total number of shares issued in January and February 2006 was 21,394,429 ordinary shares, with net proceeds of €523.5 million being raised for the Group.

On 1 June 2006, 6,000 shares were issued to Independent Directors in accordance with the terms of their service contracts. The market value of the shares at the date of issue of €0.2 million was expensed in the income statement in accordance with IFRS 2 "Share Based Payments".

On 8 June 2006, 71,146 options with a strike price of €10 each were exercised.

On 1 December 2006, the Group made a further public offering of 17,837,838 shares at €37 each raising gross proceeds of €660 million (net €645 million).

As at 31 December 2006, there were 63,519,083 shares issued and outstanding.

Under the Company's Articles of Association, the Directors have the authority to affect the issuance of additional ordinary shares or to create new classes of shares as they deem necessary.

Profit due to minority interest is lower than the rounding threshold and has been eliminated during the consolidation process of the financial statements.

Other Reserves

Other reserves represent the fair value of share options at the grant date, granted to the Manager in December 2003, June 2004, June 2005, February 2006 and December 2006.

23. HEDGING ACCOUNTING

The Group's policy is to hedge its exposure to interest rates and foreign currencies on a case-by-case basis. Hedge accounting is applied to cash flow and fair value hedges of interest rate risk exposures. Interest rate swaps under which the Group pays a fixed rate and receives a floating rate have been used to hedge the interest rate risk on floating rate long-term bank borrowing. Interest rate swaps which the Group pays a fixed rate and receives a floating rate have been used to hedge the fair value of the available-for-sale assets in Feco Sub SPV Plc.

For the year ended 31 December 2006, unrealised gains on hedge instruments relating to cash flow hedges were €23.54 million (2005: losses of €12.1 million).

The gain or loss on measurement of the fair value of the interest rate swaps has been recognised in the statement of changes in equity to the extent that the swaps are effective, while gains and losses related to fair value hedges has been recognised in the income statement.

The details of interest rate swaps entered into by the Group in respect of certain of the term financing agreements are as follows:

Cash Flow Hedges

31 December 2006	Wave €'000	Bastion* €'000	Drive** €'000	FIP €'000	Truss*** €'000	Turret €'000	Huk €'000	Mars €'000	Unallocated Hedge**** €'000
Nominal amount	**210,000**	**—**	**—**	**97,500**	**—**	**58,108**	**39,586**	**1,000,000**	**83,324**
Pay rate	**3.47%**	**—**	**—**	**3.45%**	**—**	**3.96%**	**4.12%**	**3.87%**	**4.13%**
Receive rate	**3 Month Euribor**	**—**	**—**	**6 Month Euribor**	**—**	**3 Month Euribor**	**3 Month Euribor**	**3 Month Euribor**	**3 Month Euribor**
Remaining life	**6.3**	**—**	**—**	**11.0**	**—**	**9.4**	**6.9**	**7.4**	**7.1**
Fair value of swaps assets	**6,411**	**—**	**—**	**2,812**	**—**	**489**	**(212)**	**10,816**	**(479)**

31 December 2005	Wave €'000	Bastion* €'000	Drive** €'000	FIP €'000
Nominal amount	210,000	26,500	1,300,000	121,875
Pay rate	3.47%	3.05%	3.37%	3.34%
Receive rate	3 Month Euribor	3 Month Euribor	3 Month Euribor	6 Month Euribor
Remaining life	7.3	6.5	7.1	11.8
Fair value of swaps (liabilities)/assets	(3,831)	197	(7,214)	(1,252)

**As at 8 June 2006, the interest rate swap agreement relating to the Bastion portfolio was novated to ABN Amro Bank N.V. in conjunction with the loan agreement. The positive fair value of €1.1 million as at the date of novating the swaps has been recorded within the hedging reserve and will be recycled through the Income Statement.*

***As at 31 March 2006, the interest rate swap agreement relating to the Drive portfolio was novated to Deutsche Bank AG in conjunction with the loan agreement. The positive fair value of €6.4 million as at the date of novating the swap has been recorded within the hedging reserve. A corresponding amount has been included in the carrying value of the Drive loan within term financing (refer to Note 18.1). This fair value is being recycled through the Income Statement over the life of the loan. The carrying value of the novated amount is €5.6 million.*

****From the period of 3 April 2006 to 23 June 2006, the interest rate swap agreement relating to the Truss portfolio was novated to Morgan Stanley Bank International Limited in conjunction with the loan agreement. The positive fair value of €0.3 million as at the date of novating the swap has been recorded within the hedging reserve and will be recycled through the Income Statement.*

*****The unallocated hedge represents interest rate swaps undertaken to hedge the interest rate risk on forecasted transactions. The fair value of €0.5 million on the revaluation of the €83.3 million interest rate swap has been recorded within the hedging reserve.*

Fair Value Hedges

31 December 2006	Feco EURO B Notes €'000	Feco CHF B Notes CHF '000	Feco* CHF B Notes €'000	Feco GBP Notes €'000	Feco** GBP Notes €'000
Nominal amount	11,974	3,725	2,315	36,694	54,459
Pay rate	2.87%	2.00%	—	4.61%	—
Receive rate	3 Month Euribor	3 Month CHF Libor	—	3 Month Libor	—
Remaining life	3.6	3.8	—	4.4	—
Fair value of swap assets	455	78	48	1,049	1,557

**The amount stated is a euro notional, mark to market equivalent of CHF swaps.*
***The amount stated is a euro notional, mark to market equivalent of GBP swaps.*

There were no fair value hedges in year ended 31 December 2005.

24. FINANCIAL INSTRUMENTS

Risk Management

This section provides details of the Group's exposure to risk and describes the methods used by management to control risk. The most important types of financial risk to which the Group is exposed are market risk, credit, liquidity, interest rate and foreign currency risk.

Market Risk

The Group's exposure to market risk is comprised mainly of movements in the value of its debt securities, property investments and real estate fund units.

The Group's securities are predominantly floating rate and as such are valued based on a market credit spread over Euribor, Libor and CHF benchmarks for euro, sterling and Swiss denominated assets respectively. Increases in the credit spreads above such benchmarks may affect the Group's net equity, net income or cash flow directly through their impact on unrealised gains or losses on available-for-sale securities, and therefore its ability to realise gains on such securities, or indirectly through its impact on its ability to borrow and access capital.

Under the terms of the securities contract the Group was exposed to market risk on the underlying securities as, should the intended securitisation of such assets not be consummated, the Group would be required to either purchase the securities or pay the loss realised on the disposal up to the amount of any deposits made by the Group under the contract, less any interest earned on the deposits.

The Group's investment property assets are based in Germany and Italy and are subject to general property market risks. These risks are assessed by management at the point of acquisition as well as on an ongoing basis. In addition, external valuations of the property assets are obtained during each financial year.

Credit Risk

The Group is subject to credit risk with respect to its investments in real estate and other asset backed securities and loans.

The securities the Group invests in are generally junior in right of payment of interest and principal to one or more senior classes, but benefit from the support of one or more subordinate classes of securities or other form of credit support within a securitisation transaction. While the expected yield on these securities is sensitive to the performance of the underlying assets, the more subordinated securities are designed to bear the first risk of default and loss.

The Group further minimises credit risk by actively monitoring its securities portfolios and the underlying credit quality of its holdings and, where appropriate, repositioning its investments to upgrade the credit quality and yield on the investments.

The Group's securities portfolio is diversified by asset type, industry, location and issuer. This diversification minimises the risk of capital loss. At 31 December 2006, the Group's securities, which serve as collateral for its CDO financings and other borrowings, had an overall weighted average credit rating of approximately BBB.

The Group's available-for-sale asset backed securities and real estate loans portfolio was split between countries within Europe as follows:

	31 December 2006			31 December 2005		
	Number of Securities/Loans	Nominal Value €'000	Location Split	Number of Securities/Loans	Nominal Value €'000	Location Split
United Kingdom	72	962,894	48.9%	60	764,958	49.9%
Italy	14	250,846	12.7%	14	247,947	16.2%
Germany	31	396,076	20.1%	18	183,470	12.0%
Pan European	7	99,391	5.1%	10	141,622	9.2%
France	11	94,839	4.8%	9	79,525	5.2%
Other	23	163,724	8.4%	16	116,304	7.5%
	158	1,967,770	100%	127	1,533,826	100%

The Group's hedging transactions using derivative instruments also involve certain additional risks such as counterparty credit risk, the enforceability of hedging contracts and the risk that unanticipated and significant changes in interest rates will cause a significant loss of basis in the contract. The counterparties to the Group's derivative arrangements are major financial institutions with investment grade credit ratings with which the Group and its affiliates may also have other financial relationships. As a result, it is not anticipated that any of these counterparties will fail to meet their obligations.

The Group's German real estate portfolio holds the following type of real estate: office, retail, banking halls and other. As at 31 December 2006, the Group derived its rental income from the following sources: Dresdner Bank 43.7%, Deutsche Bank 8.8%, Deutsche Bahn AG 3.5%, Edeka 3.3%, Arcor AG 3.3% and Other 37.4%. As at 31 December 2005, the Group derived its rental income from the following sources: Deutsche Bank 49.3%, Edeka 8.8%, REWE 5.5% PLUS 3.0% Peek and Cloppenburg 2.1% and Other 31.3%.

The Group's Italian real estate assets comprise an investment in a real estate investment fund that owns a portfolio of 394 properties in Italy that are let to Italian government agencies.

Liquidity Risk

The Group's ability to execute its business strategy, particularly the growth of its investment portfolio, depends to a significant degree on the Group's ability to obtain additional capital.

The Group's primary source of funds for liquidity consist of net cash provided by operating activities, borrowings under loans and the issuance of debt and equity securities. The Group's loans and debt securities are generally secured directly over its assets. The Group expects that its cash on hand and cash flow provided by operations will satisfy its liquidity needs with respect to its current investment portfolio over the next twelve months. The Group expects to meet its long-term liquidity requirements, specifically the repayment of its debt obligations, through additional borrowings and the liquidation, refinancing or repayment of its assets at maturity.

A significant portion of the Group's investments are financed with collateralised debt obligations, known as CDOs. If spreads for CDO liabilities widen or if demand for such liabilities ceases to exist, then the ability to execute future CDO financings will be restricted. Proceeds from the sale of real estate and other asset backed securities which serve as collateral for the Group's CDO financings, including gains thereon, are required to be retained in the CDO structure until the related bonds are retired and are therefore not available to fund current cash needs.

The Group's real estate securities are financed long-term and their credit status is continuously monitored; therefore, these investments are expected to generate a generally stable current return, subject to interest rate fluctuations. The Group's operating real estate is also financed long-term and primarily leased to credit tenants with long-term leases and is therefore also expected to generate generally stable current cash flows.

As described in Note 18, the Group has access to temporary working capital through a revolving €300 million credit facility.

Interest Rate Risk

The Group's primary interest rate exposures relate to its real estate and other asset backed securities, loans and floating rate debt obligations, as well as its interest rate and total return swaps. Changes in the level of interest rates also can affect the Group's ability to acquire securities and loans and its ability to realise gains from the settlement of such assets.

The Group's general financing strategy focuses on the use of match-funded structures, meaning that it seeks to match the maturities of its debt obligations with the maturities of its investments to minimise the risk that the Group will have to refinance its liabilities prior to the maturities of its assets, reducing the impact of changing interest rates on its earnings. In addition, the Group match funds interest rates on its investments with like-kind debt directly or through the use of interest rate swaps. However, based on a variety of factors, the Manager finances certain assets on a short term basis, including the use of repurchase agreements.

The interest rate profile of the Group at 31 December 2006 and 31 December 2005 was as follows:

31 December 2006

Type	Total Per Consolidated Balance Sheet €'000	Non-Interest Bearing Assets €'000	Within 1 Year Fixed %	Within 1 Year Variable %	1 to 5 Years Fixed %	1 to 5 Years Variable %	Over 5 Years Fixed %	Over 5 Years Variable %
Assets								
Cash and cash equivalents	122,699	—	—	122,699	—	—	—	—
Asset backed securities, available-for-sale (includes cash to be invested)	1,481,661	—	22,892	103,727	18,942	808,867	—	527,233
Asset backed securities, pledged under repurchase agreements	78,646	—	—	44,500	—	—	—	34,146
Real estate related loans	428,370	—	—	—	53,851	208,182	12,887	153,450
Real estate fund units	148,077	—	148,077	—	—	—	—	—
Investment property	3,308,872	3,308,872	—	—	—	—	—	—
Intangible assets	1,828	1,828	—	—	—	—	—	—
Other assets	69,537	37,961	422	31,154	—	—	—	—
Derivative assets	22,690	—	—	—	—	—	22,690	—
Total Assets	5,662,380	3,348,661	171,391	302,080	72,793	1,017,049	35,577	714,829
Liabilities								
CDO bonds payable	1,210,275	—	—	—	—	—	12,244	1,198,031
Bank loans	2,680,563	—	—	79,488	—	67,051	2,451,221	82,803
Repurchase agreements	75,490	—	—	75,490	—	—	—	—
Taxation payable	6,016	6,016	—	—	—	—	—	—
Trade and other payables	93,299	70,406	—	22,869	—	—	24	—
Derivative liabilities*	212	—	—	—	—	—	212	—
Finance lease payable	25,800	—	1,281	—	4,650	—	19,869	—
Total liabilities	4,091,655	76,422	1,281	177,847	4,650	67,051	2,483,570	1,280,834

**Net interest rate swap payable related to the cash flow hedges as described in Note 23.*

Notes to Consolidated Financial Statements *(continued)*

31 December 2005

Type	Total Per Consolidated Balance Sheet €'000	Non-Interest Bearing Assets €'000	Within 1 Year		1 to 5 Years		Over 5 Years	
			Fixed %	Variable %	Fixed %	Variable %	Fixed %	Variable %
Assets								
Cash and cash equivalents	13,640	—	—	13,640	—	—	—	—
Asset backed securities, available-for-sale (includes cash to be invested)	1,342,638	—	8,203	99,452	39,985	716,625	—	478,373
Asset backed securities, pledged under repurchase agreements	109,909	—	—	59,593	—	44,500	—	5,816
Real estate related loans	92,649	—	—	13,478	—	79,171	—	—
Real estate fund units	189,591	—	189,591	—	—	—	—	—
Investment property	463,540	463,540	—	—	—	—	—	—
Intangible assets	542	542	—	—	—	—	—	—
Other assets	50,001	31,586	568	17,650	—	—	197	—
Derivative assets*	11,470	—	—	11,470	—	—	—	—
Total Assets	2,273,980	495,668	198,362	215,283	39,985	840,296	197	484,189
Liabilities								
CDO bonds payable	977,485	—	—	—	—	—	—	977,485
Bank loans	835,162	—	—	53,131	—	307,917	441,352	32,762
Repurchase agreements	103,542	—	—	103,542	—	—	—	
Taxation payable	2,278	2,278	—	—	—	—	—	—
Trade and other payables	41,396	34,443	—	6,953	—	—	—	—
Derivative liabilities*	12,297	—	—	—	—	—	12,297	—
Finance lease payable	2,952	—	227	—	778	—	1,947	—
Total liabilities	1,975,112	36,721	227	163,626	778	307,917	455,596	1,010,247

**Net interest rate swap payable related to the cash flow hedges as described in Note 23.*

Foreign Currency Risk

The Group's primary foreign currency exchange rate exposures relate to its sterling and Swiss franc denominated portfolio of securities and loans. Changes in the currency rates can adversely impact the fair values and earnings streams of the Group's non-euro denominated assets and liabilities. The Group has mitigated this impact through a combination of (i) sterling denominated financing and (ii) rolling forward foreign exchange contracts to hedge its net sterling equity investment.

In connection with the Group's purchase of its available-for-sale real estate and other asset backed securities and real estate loans, the foreign currency risk is covered through forward foreign currency exchange contracts.

Fair Values of Financial Assets and Financial Liabilities

Set out below is a comparison by category of carrying amounts and fair values of all of the Company's financial instruments that are carried in the financial statements.

	31 December 2006 €'000 Carrying Value	31 December 2005 €'000 Carrying Value	31 December 2006 €'000 Fair Value	31 December 2005 €'000 Fair Value
Financial Assets				
Cash and cash equivalents	122,699	13,640	122,699	13,640
Asset backed securities, available-for-sale (includes cash to be invested)	1,481,661	1,342,638	1,481,661	1,342,638
Asset backed securities, pledged under repurchase agreements	78,646	109,909	78,646	109,909
Real estate related loans	428,370	92,649	428,370	92,649
Real estate fund units	148,077	189,591	148,077	189,591
Derivative assets	22,690	11,470	22,690	11,470
Financial Liabilities				
CDO bonds payable	1,210,275	977,485	1,210,275	977,485
Bank loans	2,680,563	835,162	2,674,931	836,393
Repurchase agreements	75,490	103,542	75,490	103,542
Derivative liabilities	212	12,297	212	12,297
Finance lease payable	25,800	2,952	25,800	2,952

25. SHARE OPTION PLAN

In December 2003, Eurocastle Investments Limited, the parent company (the "Company") (with the approval of the Board of Directors and pursuant to the confidential information memorandum dated August 2003) adopted a nonqualified share option plan (the "Company Option Plan") for officers, Directors, employees, consultants and advisors, including the Manager. In December 2003, for the purpose of compensating the Manager for its successful efforts in raising capital for the Company, the Manager was granted options representing the right to acquire 1,185,767 ordinary shares at an exercise price of €10 per share (number of shares and exercise price adjusted for share consolidation). The fair value of the options at the date of grant was €0.2 million and was calculated by reference to an option pricing model.

In June 2004, following the IPO, the Manager was granted an additional 660,000 options at an exercise price of €12 per share. The fair value of the additional options at the date of grant was €0.2 million and was also calculated by reference to an option pricing model.

In June 2005, following the secondary public offering, the Manager was granted an additional 574,000 options at an exercise price of €17.25 per share. The fair value of the additional options at the date of grant was €0.6 million. The Manager's options represent an amount equal to 10% of the ordinary shares issued by the Company. The options granted to the Manager were fully vested on the date of grant and expire ten years from the date of issuance.

In February 2006, following the third public offering, the Manager was granted 1,282,300 options at €30.00 per share and, pursuant to December 2005 Board action, an additional 857,142 options at an exercise price of €18.00 per share. The fair value of the additional options at the date of grant was €2.1 million and €4.8 million respectively. The Manager's options represent an amount equal to 10% of the ordinary shares issued by the Company in respect of the public and private offerings that preceded the Drive acquisition. The options granted to the Manager were fully vested on the date of grant and expire ten years from the date of issuance.

In December 2006, following the fourth public offering, the Manager was granted an additional 1,783,748 options at €37.00 per share. The fair value of the additional options at the date of grant was €9.4 million. The Manager's options represent an amount equal to 10% of the ordinary shares issued by the Company. The options granted to the Manager were fully vested on the date of grant and expire ten years from the date of issuance.

The fair value at the date of grant of options granted to the Manager has been offset against the proceeds from issuance of ordinary shares as the grant of options is a cost of capital.

On 8 June 2006, 71,146 share options were exercised at a strike price of €10 per share.

All share options granted, have been granted to the manager. The exercise price of the granted options has been determined as stated above.

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

Date of Grant	Number of Options Issued	Exercised in the Year	Options Remaining at 31 December 2006	Exercise Price	Date of Expiration	Fair Value of Share Options
31 Dec 2003	1,185,767	(71,146)	**1,114,621**	€10.00	31 Dec 2013	200,000
23 Jun 2004	660,000	—	**660,000**	€12.00	23 Jun 2014	200,000
24 Jun 2005	574,000	—	**574,000**	€17.25	24 Jun 2015	620,000
27 Jan 2006	857,142	—	**857,142**	€18.00	27 Jan 2016	4,800,000
27 Jan 2006	1,282,300	—	**1,282,300**	€30.00	27 Jan 2016	2,100,000
1 Dec 2006	1,783,783	—	**1,783,783**	€37.00	1 Dec 2016	9,400,000
Total	6,342,992	(71,146)	**6,271,846**			17,320,000

The weighted average fair value of the options granted during the year was determined using a trinomial model. The significant inputs into the model were the weighted average share price at the grant date, the exercise price as shown above, volatility of 21%, expected option life of 5 years, dividend yield, and a risk fee rate of 3.92%. The volatility is measured at the standard deviation of continuously compounded share returns. It is based on a statistical analysis of the daily share price since the date of the initial public offering of Eurocastle Investments Limited.

26. SEGMENTAL REPORTING

The Group operates in one geographical segment, being Europe. The Group has conducted business through three primary segments: debt investments, real estate fund units and investment properties.

Summary financial data of the Group's business segments is provided below:

31 December 2006	Debt Investment €'000	Real Estate Fund Units €'000	Investment Properties €'000	Unallocated €'000	Total €'000
Operating income*	**93,176**	**15,607**	**265,172**	**(188)**	**373,767**
Interest expense	**(63,398)**	**(6,466)**	**(77,740)**	**(2,678)**	**(150,282)**
Other operating expenses	**(2,105)**	**(90)**	**(52,499)**	**(21,234)**	**(75,928)**
Segment result	**27,673**	**9,051**	**134,933**	**(24,100)**	**147,557**
Taxation expense	**—**	**—**	**—**	**(3,738)**	**(3,738)**
Net profit	**27,673**	**9,051**	**134,933**	**(27,838)**	**143,819**

**Operating income includes fair value gains /(losses) for Real Estate Fund Units of (€5.2 million) and Investment Properties of €78.1 million.*

31 December 2005	Debt Investment €'000	Real Estate Fund Units €'000	Investment Properties €'000	Unallocated €'000	Total €'000
Operating income *	68,486	16,504	37,366	—	122,356
Interest expense	(42,158)	(2,876)	(12,274)	(833)	(58,141)
Other operating expenses	(1,956)	—	(10,850)	(9,473)	(22,279)
Segment result	24,372	13,628	14,242	(10,306)	41,936
Taxation expense	—	—	—	(2,278)	(2,278)
Net profit	24,372	13,628	14,242	(12,584)	39,658

**Operating income includes fair value gains for Real Estate Fund Units of €8.1 million and Investment Properties of €1.9 million.*

31 December 2006	Debt Investment €'000	Real Estate Fund Units €'000	Investment Properties €'000	Unallocated €'000	Total €'000
Total assets	**2,011,490**	**158,784**	**3,461,857**	**30,249**	**5,662,380**
Total liabilities	**(1,436,424)**	**(98,027)**	**(2,540,696)**	**(10,492)**	**(4,085,639)**
Segment net assets	**575,066**	**60,757**	**921,161**	**19,757**	**1,576,741**
Tax liability	**—**	**—**	**—**	**(6,016)**	**(6,016)**
Minority interest	**(2)**	**(4)**	**—**	**—**	**(6)**
Net assets	**575,064**	**60,753**	**921,161**	**13,741**	**1,570,719**

31 December 2005	Debt Investment €'000	Real Estate Fund Units €'000	Investment Properties €'000	Unallocated €'000	Total €'000
Total assets	1,602,455	189,591	480,754	1,180	2,273,980
Total liabilities	(1,470,524)	(128,619)	(359,123)	(14,568)	(1,972,834)
Segment net assets	131,931	60,972	121,631	(13,388)	301,146
Tax liability	—	—	—	(2,278)	(2,278)
Minority interest	(2)	—	—	—	(2)
Net assets	131,929	60,972	121,631	(15,666)	298,866

The unallocated portion consists primarily of general and administrative expenses and management fees pursuant to the Management Agreement.

27. DIVIDENDS PAID & DECLARED

	31 December 2006 €'000	31 December 2005 €'000
Equity dividends on ordinary shares:		
Fourth quarter dividend for 2005: €0.37 (2004: €0.33)	**8,958**	6,093
First quarter dividend for 2006: €0.30 (2005: €0.33)	**13,682**	6,095
Second quarter dividend for 2006: €0.40 (2005: €0.35)	**18,272**	6,464
Third quarter dividend for 2006: €0.43 (2005: €0.37)	**19,643**	8,958
First interim dividend for fourth quarter of 2006: €0.29 (2005: €Nil)	**13,248**	—
Paid during the year ended 31 December	**73,803**	27,610
Fourth quarter dividend declared on 7 March 2007: €0.14 (2005: €0.37)	**8,929**	8,958

28. MANAGEMENT AGREEMENT & RELATED PARTY TRANSACTIONS

Eurocastle Investments Limited, the parent company (the "Company") entered into the Management agreement with the Manager in August 2003, which provides for an initial term of ten years with automatic three year extensions, subject to certain termination rights. The Management agreement may be terminated by the Company by payment of a termination fee, as defined in the Management agreement, equal to the amount of management fees earned by the Manager during the twelve consecutive calendar months immediately preceding the termination, upon the vote of a majority of the holders of the outstanding ordinary shares. Pursuant to the Management agreement, the Manager, under the supervision of the Company's Board of Directors, will formulate investment strategies, arrange for the acquisition of assets, arrange for financing, monitor the performance of the Group's assets and provide certain advisory, administrative and managerial services in connection with the operations of the Group. For performing these services, the Company will pay the Manager an annual fee (payable monthly in arrears) of 1.5% of the gross equity of the Company, as described in the Management agreement.

The Management agreement provides that the Company will reimburse the Manager for various expenses incurred by the Manager or its officers, employees and agents on the Company's behalf, including the cost of legal, accounting, tax, auditing, finance, administrative, asset management, property management and other similar services rendered for the Company by providers retained by the Manager or, if provided by the Manager's or its affiliates' employees, in amounts which are no greater than those that would be payable to external professionals or consultants engaged to perform such services pursuant to agreements negotiated on an arms-length basis. Such expenses have been included in the consolidated income statement.

To provide an incentive for the Manager to enhance the value of the Company's ordinary stock, the Manager is entitled to receive incentive compensation on a cumulative, but not compounding, basis in an amount equal to the product of (A) 25% of the euro amount by which (1) funds from operations ("FFO") of the Company before the incentive compensation per ordinary share exceeds (2) an amount equal to (a) the weighted average of the price per ordinary share in any offerings by the Company (adjusted for any prior capital dividends or distributions) multiplied by (b) a simple interest rate of eight percent (8%) per annum multiplied by (B) the weighted average number of ordinary shares outstanding during such period.

FFO is used to compute the Company's incentive compensation to the Manager. FFO, for these purposes, represents net income (computed in accordance with the Management agreement), excluding changes in the fair value of investment properties net of attributable deferred taxation, changes in the fair value of interest rate swaps that are taken to the income statement and mark to market fluctuations in real estate fund units.

At 31 December 2006, management fees, incentive fees and expense reimbursements of approximately €7.5 million, note 20, (31 December 2005: €4.5 million) were due to the Manager. For the year ended 31 December 2006, management fees of €12.1

million (31 December 2005: €3.6 million), incentive fees of €2.7 million (31 December 2005: €3.8 million), reimbursement fees of €3.9 million, note 7, (31 December 2005: €54,000) were charged to the income statement.

Keith Dorrian and Paolo Bassi each currently receive €30,000 per annum payable semi-annually in equal installments. On 22 August 2006, Randal Nardone, Udo Scheffel and Simon Thornton were appointed to the Eurocastle Board of Directors. Udo Scheffel and Simon Thornton will receive remuneration of €30,000 per annum. Wesley R. Edens and Randal Nardone do not receive any remuneration from the Company.

As stated in Note 22, the Company issued 5,000 shares to Paolo Bassi and 1,000 shares to Keith Dorrian in their capacity as Directors of the Company. The shares issued to the Directors were non-cash shares, and were issued with nil proceeds.

During 2006, Eurocastle Investments Limited acquired consultancy services from Mapeley Limited, a company owned in part by funds also managed by the Manager. Total services amounted to €97,532 of which €68,897 was owed at 31 December 2006.

All share options granted have been granted to the Manager. For further details please see note 25.

29. INVESTMENT IN SUBSIDIARIES

The legal entity group structure of Eurocastle is designed to support the Group's businesses within an efficient legal, tax, regulatory and funding framework.

The significant operating subsidiaries, in which the Company owns directly or indirectly a 100% equity interest, are listed by jurisdiction below:

Luxembourg:
Luxgate s.a.r.l.
Drive s.a.r.l.
Eurobarbican s.a.r.l.
Bastion Participation s.a.r.l.
Belfry Participation s.a.r.l.
Truss Participation s.a.r.l.
Finial s.a.r.l.
Turret Participation s.a.r.l.
Undercroft s.a.r.l.
Marathon s.a.r.l. (formerly Turret LP s.a.r.l.)
Mars Holdco 1 s.a.r.l.

Germany:
Dresdner Grund-Fonds
Shortwave Acquisition GmbH
Longwave Acquisition GmbH
Bastion GmbH & Co.KG
Belfry GmbH & Co.KG
Truss GmbH & Co.KG
Turret GmbH & Co.KG
Bridge GmbH & Co.KG

Additionally, the Company has investments in Eurocastle Funding Limited, Eurocastle CDO I PLC, Eurocastle CDO II PLC, Eurocastle CDO III PLC and Eurocastle CDO IV PLC, Duncannon CRE CDO PLC and Feco SUB SPV PLC that it consolidates in accordance with SIC 12.

30. SUBSEQUENT EVENTS

Fourth Quarter 2006 Dividend

On 7 March 2007, the Directors declared a fourth quarter 2006 dividend of €0.14 per share to all holders of shares, the record date is 7 March 2007.

Exercise of Options

On 19 January 2007, 20,000 share options were exercised by the Manager.
On 7 March 2007, 237,445 share options were exercised by the Manager.

31. COMMITMENTS

As at 31 December 2006, amounts contracted for but not provided in the financial statements for the acquisition of investment property amounted to:

- Entered into an agreement to acquire a further €2,148 million, representing 56 commercial properties within the Mars portfolio.
- Entered into an agreement to acquire a further €53 million, representing 8 commercial properties within the HUK portfolio.

CORPORATE INFORMATION

Board of Directors

Wesley R. Edens
Chairman of the Board

Paolo Giorgio Bassi

Keith Dorrian

Randal A. Nardone

Dr. Udo Scheffel

Dr. Simon J. Thornton

Executive Officers

Stephen Charlton
Chief Financial Officer

Investment Manager
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Notice of Annual Meeting
5 June 2007
Guernsey

Forward-Looking Statements

This report contains statements that constitute forward-looking statements. Such forward-looking statements relate to, among other things, availability of attractive investment opportunities, methods of funding portfolios, the operating performance of our investments and financing needs. Forward-looking statements are generally identifiable by use of forward-looking terminology such as "may," "will," "should," "potential," "intend," "expect," "endeavor," "seek," "anticipate," "estimate," "overestimate," "underestimate," "believe," "could," "project," "predict," "continue," "plan," "forecast" or other similar words or expressions. Forward-looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain projections of results of operations or of financial condition or state other forward-looking information. Our ability to predict results or the actual effect of future plans or strategies is limited. Although we believe that the expectations reflected in such forward-looking statements are based on reasonable assumptions, our actual results and performance may differ materially from those set forth in the forward-looking statements. These forward-looking statements are subject to risks, uncertainties and other factors that may cause our actual results in future periods to differ materially from forecasted results or stated expectations including the risk that Eurocastle will be unable to exploit opportunities to acquire high quality office and retail property in Germany or increase occupancy of its portfolio.

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