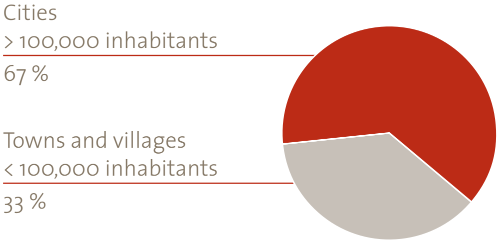
2006 Annual Report

DEUTSCHE ANNINGTON

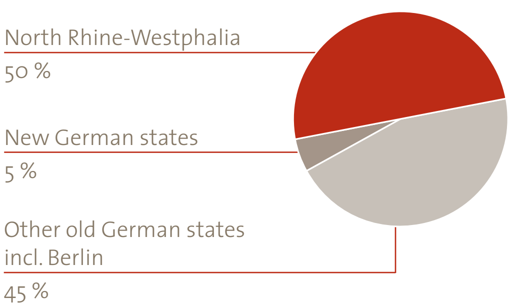
		Residential units	Other rental units	Fair values in € million
Deutsche Annington Nord GmbH	1	18,370	4,232	823.8
Deutsche Annington Westfalen GmbH	2	43,460	6,477	1,984.5
Deutsche Annington Ruhr GmbH	3	36,991	6,296	1,684.9
Deutsche Annington Rheinland GmbH	4	19,920	6,315	1,270.6
Deutsche Annington Süd-West GmbH	5	31,658	7,313	1,940.9
Deutsche Annington Ost GmbH	6	18,073	2,803	733.3
Deutsche Annington Süd GmbH	7	16,966	8,285	1,164.1

The Deutsche Annington properties are spread throughout Germany. They are managed by seven regional companies. The main regions are North Rhine-Westphalia and the Rhine-Main region.

Portfolio structure
Nationwide presence in 670 cities, towns and villages



Portfolio structure
with a clear focus on western Germany



We successfully combine real estate portfolios throughout Germ

2001	2003	2004	
Acquisition of eleven railway housing companies with roughly 65,000 units from the German state	Acquisition of some 10,000 units from Heimbau AG, Kiel	Acquisition of about 4,500 units from RWE Systems, Essen	Take

y.

2005	2006	Goal
f Viterra AG, Essen, 38,000 units	Viterra integration completed	Further expansion of portfolio and earning power

Profile

Deutsche Annington is one of the leading residential property companies in Germany, managing some 221,000 units. As a fully integrated real estate company, we pursue three core activities: the acquisition of attractive housing stocks, their value-enhancing management and the selective sale of residential units, primarily to tenants.

We see ourselves as a property holder and intend to **grow profitably** in the years to come: To achieve this, we will expand our portfolio through selective acquisitions and further improve the quality of our tenants' living conditions by offering attractive services.

Key Figures for the Group

€ million	2005	2006	Change in %
Income from property management	681.7	898.8	31.8
Profit on disposal of properties	183.4	131.3	–28.4
EBITDA	311.3	765.9	146.0
Profit before tax	58.3	428.7	635.3
Profit for the year	170.6	207.1	21.4
Total assets	10,816.6	10,932.2	1.1
Non-current assets	6,757.1	7,059.9	4.5
Current assets	4,059.5	3,872.3	–4.6
Total equity	1,031.7	1,688.7	63.7
Return on equity in %	9.5	15.4	–
Investments	3,553.7	133.4	–96.2
Cash flow from operating activities	549.5	789.9	43.7
Cash flow used in/from investing activities	–3,296.3	20.9	–100.6
Cash flow from/used in financing activities	3,165.2	–589.1	–118.6
Number of employees (as at Dec. 31)	1,889	1,385	–26.7
Number of residential units in portfolio (as at Dec. 31)	189,886	185,438	–2.3
Number of units sold (recorded sales)	12,378	7,601	–38.6
of which sold individually	7,072	4,763	–32.6
of which sold en bloc	5,306	2,838	–46.5

Contents

Ladies and Gentlemen,

We can look back on a successful business year in 2006 and state with confidence that Deutsche Annington is on course. We have optimised our structures and successfully completed one of the largest integration projects in the history of the German real estate industry. At the same time, we have improved our customer service, thus strengthening our customer ties. We have therefore created a solid foundation for further growth. On the operational side, we also performed very well. In 2006, we recorded a net profit of € 207.1 million. Parallel to this, we managed to reduce our liabilities by € 541.4 million and achieve a sustained improvement in our return on equity. In 2007, we will continue on our successful course and grow further.

We are an integrated residential real estate company with clear objectives

Last year, we were mainly concerned with the integration of the two companies, Deutsche Annington and Viterra. We felt it was important to first of all carefully create a suitable platform for our planned growth. We not only restructured our entire housing stocks in the regions but also optimised and standardised our processes. At the same time, we considerably reduced our costs by centralising key business functions and controlling our workflows more efficiently.

The completion of the comprehensive integration process in 2006 was an important step, setting the future course for our company and greatly enhancing our efficiency. Attractive offerings and services, improved processes and well-trained staff now enable us to successfully expand our market position, both in terms of the quantity and quality of our daily work. Our strategy focuses on three core areas: the long-term, value-enhancing management of our real estate portfolio, the selective sale of units in a socially acceptable manner, primarily to tenants, and the strategic acquisition of housing portfolios which can be integrated into the Deutsche Annington stocks.

We think nationally but act locally

Thanks to our new platform, we can quickly and smoothly integrate the housing portfolios we acquire wherever they are. We now have properties in over 670 cities, towns and villages from Flensburg to Munich. Despite the fact that we operate throughout Germany, our company has a very strong local character. Our structure with seven independent regional companies with some seventy customer centres and service offices guarantees a customer-oriented local service: Tenants, local authority staff, local suppliers and service-providers can all contact a local office with reliable staff who speak their language.

We see ourselves as a property holder with a long-term view

In 2006, we made a course adjustment as regards house sales, sharply reducing the number of properties we sold. We will, in future, be concentrating more on buying further housing portfolios and managing them in the long term. Our Group has a good portfolio of properties in non-prime locations at attractive prices which can be readily let. More than two-thirds of our units are situated in cities, which means there is a good demand for them. Our high customer loyalty also shows this: On average, our tenants live in our apartments for 16 years, that's six years more than the national average. Our success in the letting business is also reflected in our figures: We generated approx. € 900 million in income from property management last year.

We also want to grow significantly in 2007

Deutsche Annington's aim is long-term, steady growth. The acquisition of the Viterra Group enabled us to considerably increase our share of the private housing market in Germany. We intend to acquire housing portfolios of all sizes throughout Germany and thus greatly expand our housing stocks in the medium term. Trading in real estate is not our primary concern.

In 2007, we will continue selective sales of residential units to tenants, owner-occupiers and capital investors. However, unlike in the past, we currently have no interest in large, so-called en bloc sales. Deutsche Annington has many years of experience in the purchase and integration of housing portfolios. We have proved that in our daily work over the years.

We take our social responsibility as a lessor seriously

An apartment will always be a valuable asset. Our tenants are interested in what is happening with their apartments and in their direct vicinity, in their neighbourhood. And so are the local authorities. Deutsche Annington has always taken its responsibility as a landlord seriously. We are and will remain committed to our social responsibility: For example, we give special protective rights to tenants who have lived in our properties for many years, we support regional social projects in our residential estates and constantly seek dialogue with the local people responsible. In the Ruhr area, for example, we have established a structured, moderated process for the sale of properties based on specially developed estate privatisation agreements which are accepted by everyone. We also treat our properties with respect, investing in them to retain their value.

High customer satisfaction is one of our most important goals. Only with satisfied customers can we continue on our hitherto so successful course and grow further.

Deutsche Annington has already been on the market for six years and our owners, the investment company Terra Firma, have continually supported our course of growth, always stressing the long-term nature of their investment. Deutsche Annington will continue to be a reliable partner for tenants and local authorities alike.

We want both: satisfied customers and high-yield growth

We are the leaders on the German residential real estate market. And we intend to retain this position. Our two most important goals for 2007 are even greater customer orientation and further growth. We plan to steadily expand our housing portfolio. In doing so, we will further develop our professional service to the benefit of our customers, for quantitative growth is not to be achieved at the expense of quality. Our clear organisational structure provides us with an excellent platform to do so.

Naturally, we are also setting ourselves yield targets as only an economically successful company can invest in good customer service. The development of vacancies shows that we are on the right track here: In 2006 alone, we managed to cut vacancies from 6.3 % to 5.7 % – and we achieved this despite the disproportionately high numbers of empty apartments in the new German states. In future, we will continue to show that professional management of a housing company and customer-oriented action can indeed be combined.

We want to have a clear lead tomorrow as well

The motto of our 2006 Annual Report is “With a Clear Lead“. We are currently the largest residential real estate company in Germany but above all we manage our stocks with broad-based expertise and extensive experience. We are in the lead. And that’s where we intend to stay. That’s why our tenants are so important to us, for satisfied customers are the basis of our success. We know that loyal tenants guarantee steady income. This knowledge also determines our plans for the future.

We would like to thank our staff, suppliers and service-providers and our tenants for the trust they have placed in us and their support in the past business year and look forward to another equally successful year of working together in 2007.

Boards

Managing Directors

Georg Kulenkampff
Senior Managing Director
until May 9, 2007

Responsible for:
Business Development, Corporate Communications, Auditing, Human Resources Management, Procurement/Technology, Regional Companies

Born in 1951; degree in economics; extensive international management experience at various companies incl. Raab Karcher, VEBA and Metro; in 2002 moved to Terra Firma Capital Partners in London and Frankfurt am Main; since 2006 Senior Managing Director of Deutsche Annington

Wilhelmus (Wijnand) P. Donkers
Senior Managing Director
since May 10, 2007

Responsible for:
Business Development, Corporate Communications, Auditing, Human Resources Management, Procurement/Technology, Regional Companies

Born in 1962; Master of Business Administration; international management experience at BP p.l.c. with career steps in Europe and North America; last: Managing Director, BP Gas Marketing

Dr Manfred Püschel

Responsible for:
Controlling, Finance, Accounting/Taxes, Legal Affairs and Shareholdings, Deutsche Annington Verwaltungs GmbH, Deutsche Annington Informationssysteme GmbH

Born in 1953; PhD in business economics; many years of management experience in the fields of planning and finance at various companies incl. VEBA, Stinnes and Raab Karcher; from 1998 to 2005 CFO of Viterra AG; since 2005 Managing Director of Deutsche Annington

Supervisory Board

Guy Hands
Chairman
Chief Executive Officer of Terra Firma Capital Partners Limited, London

David Pascall (until December 1, 2006)
Managing Director of Terra Firma Capital Partners Limited, London
Managing Director of terrafirma GmbH, Frankfurt am Main

Georg Kulenkampff
(December 1, 2006 until December 18, 2006)
Managing Director of Terra Firma Capital Partners Limited, London
Managing Director of terrafirma GmbH, Frankfurt am Main

Fraser Duncan
Executive Officer of Terra Firma Capital Partners Limited, London

Phillip Burns
Managing Director of Terra Firma Capital Partners Limited, London

Joseph E. Azrack
President & Chief Executive Officer of Citigroup Property Investors, New York

Sir Thomas Macpherson
Chairman of Annington Holdings PLC, London

Wolfgang König (since July 6, 2006)
Corporate Consultant, Esslingen

With a clear lead

The German residential real estate market is on the move – and we are moving successfully with it! New tenant demands make it necessary to consider new service and thus earnings concepts. The market is also on the move in the financial respect: For example, the dividing line between our business and the capital markets is becoming increasingly blurred. **All this opens up new opportunities for us. And we intend to seize them!**

We are big: Managing a portfolio of some 221,000 residential units, we are one of the market leaders. Our size stands for decades of experience gained in the real estate business and 1,385 employees dedicated to putting this knowledge to good use in their work – day in, day out.

Drive and profit-orientation – these were the two qualities which Deutsche Annington started out with in 2001. It was with these two qualities that we ventured into a market segment which tends to plan for the long term rather than the short term and where yield-oriented management is traditionally viewed with some scepticism.

Since then we have developed strongly. We have grown considerably and have created a sound foundation. We have networked structures but also streamlined where necessary. We have pooled resources and optimised processes. On our way we have managed to exploit many synergies. **Today we are an integrated company** which combines the size and stability of a residential real estate company with the dynamism of a modern, efficiently managed enterprise.

We are broad-based: Through our seven regional companies we are present throughout Germany – both in the old West German states and in the five new states, in 670 cities, towns and villages. Our proximity to our tenants helps us to forge and strengthen bonds with our customers. This makes us strong on the ground. Thanks to the close networking of our companies, we ensure that not just some but all parts of our Group develop successfully. This makes us strong as a Group.

We move with the times: With a feel for the market, we were at the right place at the right time. And so, within a short space of time, we were able to build up a successful company which has carved out a leading position for itself in the market. With a sure feel for what our tenants want, we will continue to build on our strengths. **We are on the right road –** a road leading to profitable expansion.

Today, we manage more than 185,000 residential units of our own and nearly 35,000 on behalf of others. Furthermore, we have just under 1,200 commercial properties and more than 40,000 garages and parking spaces. This makes us the largest residential real estate company in Germany. But we do not claim to have a clear lead just because of our size. We have earned our lead by using our in-depth knowledge and wide experience to manage our housing stocks.

With a clear lead

We have optimised our structures and work on this clearly coordinated basis. Following the acquisition of Viterra, we managed to successfully complete one of the largest integration projects in the history of the German real estate industry in just one year. With our seven regional companies, we have a sound structure throughout Germany. So we can meet our tenants' needs at any time and also quickly integrate new portfolios into our structures.

With a clear structure

We are reliable and act according to firm principles. This makes us predictable – for our tenants by acting as socially responsible property owners as well as for private owners and local authorities with whom we negotiate to purchase their properties. We keep the agreements we make. And because we know where we are headed, we always stay on course in our daily business. We think clearly. And we are true to our word. After all, our business is all about commitment.

With clear actions

We are always at our customers' side. Not only because we are physically present in 670 cities, towns and villages but because we try and see things their way. We invest in good relations. This is an investment which pays off for both sides: For loyal tenants guarantee steady income. Therefore, we are always looking to introduce new offers and services to keep our tenants satisfied and loyal.

With clear bonds

We want to grow profitably! We will steadily increase the number of our residential units by integrating further portfolios. To do this, we are always watching market developments and looking to see which properties would fit in our portfolio. From the business point-of-view, we are of course mainly looking for properties which will generate a steady, attractive income. To achieve this, we keep powering at all levels of our company. After all, success has to be earned.

With a clear strategy

Residential Real Estate – a Market

German residential real estate: The housing market is in a state of upheaval

Banks and analysts currently estimate that residential portfolios with up to some three million units will be offered for sale in Germany in the medium term, mostly by public authorities. The much-publicised high debts of most local authorities and the attraction of high income are forcing them to sell to get their budgets under control.

This intention to sell, particularly on the part of local authorities, is creating growing interest among private housing companies and investors who see good growth opportunities in the German residential real estate market due to the attractive prices and low home ownership in Germany. This has meanwhile led, in contrast to past practice, to premiums being paid for large portfolios; at the same time, portfolio prices have risen sharply since 2004.

The increasing competition among the new, privately run residential real estate companies has, however, not only led to bidders competing for residential portfolios but also to greater professionalism in the entire industry. The years of reconstruction in Germany when it was the government's task to ensure the basic provision of reasonably priced accommodation are over. Today, the housing market is largely saturated and it seems economically sensible and socially more effective to give direct support to those in need. What's more, local-authority housing companies not only work less profitably than private industry in many cases, they are also facing an investment backlog since they are in debt and therefore do not have the funds to invest in their housing stocks.

A new age: Institutional investors are discovering German residential real estate

Nowadays, housing companies must be run according to the same business principles as all private-sector enterprises as only efficient, profitable, high-earning companies are in a position to invest – also in the interests of their customers.

The stable cash flows from rental income are interesting for institutional investors. Large pension funds therefore often invest in real estate as they are looking for security for their many thousands of small investors. The growing interest of such investors in German residential real estate is also having a positive impact on the value of German houses and apartments. Rising construction costs and attractive rent returns are also contributing to the overall favourable constellation for real estate owners. The prices for residential real estate in Germany have, on balance, hardly changed since the beginning of the 1990s. Measured by the development of per capita income, houses and apartments are today even cheaper than 15 years ago. Germany is therefore an exception compared with many of its neighbours where prices have risen, in some cases exorbitantly. For example, the price of residential real estate in the United Kingdom has risen by more than 100 % in the same period.

Despite a slow-down in the growth of the population, the demand for accommodation in Germany will still rise in the next 15 years as the number of households will continue to increase; the age of the big family is over, single people, elderly couples, patchwork families, single parents and unmarried

with Opportunities

couples dominate the picture. This development is boosting the demand for small apartments. It is estimated that two million new households will be looking for a home in the period up to 2020. In addition, people are slowly becoming aware that they need to provide for retirement. Between 1993 and 2006, the home ownership rate in Germany rose from 39 % to approx. 43 % – good opportunities for an investment in residential real estate.




New sources of capital: Earnings orientation opens up opportunities for companies and tenants

Professional management of residential property does not mean aimlessly saving money at all costs. Good housing managers, however, pursue a market-oriented maintenance strategy and optimise their procurement costs (for example, by centralising the purchase of repair services). This brings cost savings. Leaner processes and lower staff costs reduce administration costs, better vacancy management and faster reletting boost returns.

Competing for residential portfolios: Companies who offer the right concepts win

High-earning housing companies offer good prospects: for tenants, local authorities and companies they work with. Housing is a valuable asset in Germany: In the past, this has led to a strictly regulated market. Faced with the acute shortage of housing in the post-war years, German legislators established strong tenant protection and enabled housing companies to acquire the tax-privileged status of non-profit organisations. When the housing companies lost this status in 1990, times started to change: Customer proximity instead of bureaucracy, efficiency instead of mere management are now the order of the day. In view of the demographic change in our society, the housing industry must now answer the question as to how people are going to live in future. Housing concepts for the aged are in demand as well as ideas for the social management of urban districts. Housing companies have to meet their responsibilities as owners. With the right partner, the local authorities can develop workable, long-term concepts which allow them to concentrate on their core competence, looking after the well-being of their citizens.

New housing and service concepts: Creativity can open up new opportunities to earn money

Housing is not only a valuable asset, it is and always will be a much sought-after asset. Everybody needs a roof over their head. The question is therefore not whether this asset will be sought-after tomorrow but who will be doing the searching and what they will be willing to pay. The German residential real estate market is currently changing from an administrated, regulated market into a customers' market. As there is plenty of accommodation on offer, it is the customers who can afford to decide where they will live and who they will rent from. And they will make this decision several times during their lives. It is becoming more and more unusual for people to live in the one place their whole lives. Here customer loyalty concepts are very much in demand. Be it housing for the elderly, the selling of apartments to tenants, district management to maintain the attractiveness of a particular location or simply customer orientation – these are all concepts and facets of the new housing industry. Private enterprise involvement in the housing industry is not automatically a negative thing as public criticism would suggest. The market will punish those who lose sight of the customers' interests.

Management Report

Integrated platform
created for further growth

Income from property management
rises to € 898.8 million

Profit for the year
increases to € 207.1 million

Company on course
to further expand its portfolio

2006 was above all a year of restructuring in the Deutsche Annington Real Estate Group following the acquisition of the Viterra Group in mid-2005. Thanks to the comprehensive reorganisation of our processes as a result of our pan-Group integration project, we have improved the efficiency of Deutsche Annington and created a platform for rapid, sustained growth. At the same time, we have successfully developed business operations and increased our earning power. Deutsche Annington has started 2007 with an efficient organisation and a clear strategic direction.

Structure and Strategy

The Deutsche Annington Real Estate Group – a leading integrated housing company

As an integrated real estate company, the Deutsche Annington Real Estate Group pursues three core activities: the value-enhancing management of its nationwide residential real estate portfolio, the selective sale of residential units, predominantly to tenants, and the acquisition of attractive housing stocks.

With a portfolio of some 260,000 rental units managed, the Deutsche Annington Real Estate Group is one of the leading residential real estate companies in Germany. In total we manage 185,438 own apartments, 40,552 garages and parking spaces as well as 1,169 small commercial units. In addition, we manage 34,592 residential units on behalf of other companies.

Our Group consists of seven regional companies located in Kiel, Berlin, Dortmund, Essen, Düsseldorf, Frankfurt am Main and Munich. The company is run by Deutsche Annington Immobilien GmbH. However, the managing directors of the regional and service companies are responsible for the business operations of their own units and report regularly to the company's management.

The Group also has four service companies: The central service functions are pooled in Deutsche Annington Verwaltungs GmbH; Deutsche Annington Service GmbH manages the common property for apartment owners in accordance with the German Condominium Act; we have pooled our decentralised sales team in Deutsche Annington Vertriebs GmbH and Deutsche Annington Informationssysteme GmbH operates the IT infrastructure for the entire Group as our IT service provider.

The regional companies each have responsibility for their own local markets. They benefit from the centralisation of key business functions such as service charge billing, accounting and procurement. This enables us to exploit synergies and at the same time create centres of competence, enhancing the efficiency of our Group and accelerating integration of newly acquired stocks. Above all, however, the regional companies can concentrate on their main real estate management tasks.

From a railway housing company to a modern real estate group

The history of Deutsche Annington is one of continual growth. Following the purchase of ten railway housing companies in 2001 (with 63,626 apartments), we had acquired and successfully integrated another 156,013 residential units into our company by the end of 2006:

2002: 319 units in Regensburg
2003: 10,025 units from Heimbau AG in Schleswig-Holstein and the metropolitan area of Hamburg
2004: 322 units in Ahrensburg
2005: 4,365 units from RWE Systems in Essen and Cologne, 137,671 units through the acquisition of Viterra
2006: 748 units in Leverkusen, 940 units in North Rhine-Westphalia, 1,623 units in Frankfurt am Main and the Rhineland

At the end of 2006, we acquired another 1,164 units in Düsseldorf; transfer of title and economic ownership of these units to Deutsche Annington will not, however, take place until March 2007.

Represented throughout Germany with a uniform structure

The Deutsche Annington stocks are now spread over 670 cities, towns and villages throughout Germany. The majority of the residential units (more than 67%) are located in cities with more than 100,000 inhabitants, about 33% in medium-sized and small towns and villages. 61% of our portfolio is concentrated in 20 cities. We have between 2,000 and 18,000 units in each of these cities. The four biggest locations are Dortmund, Frankfurt am Main, Essen and Berlin. Our focus is on the old West German states (95% including the capital of Germany, Berlin) and particularly on North Rhine-Westphalia (over 50%), Germany's most populated state.

Regional distribution of the residential real estate portfolio of the Deutsche Annington Real Estate Group

Regional company	Town/City	Residential units	Average monthly rent per square metre in €
Deutsche Annington Westfalen GmbH	Dortmund	18,253	
	Bochum	7,775	
	Herne	4,752	
	Bergkamen	2,031	
	Others	10,649	
		43,460	4.33
Deutsche Annington Ruhr GmbH	Essen	10,833	
	Gelsenkirchen	8,815	
	Duisburg	4,588	
	Gladbeck	4,043	
	Herten	3,181	
	Marl	2,636	
	Bottrop	2,361	
	Others	534	
		36,991	4.36
Deutsche Annington Süd-West GmbH	Frankfurt am Main	11,000	
	Wiesbaden	2,259	
	Kassel	2,044	
	Others	16,355	
		31,658	5.24
Deutsche Annington Rheinland GmbH	Cologne	4,681	
	Bonn	4,658	
	Others	10,581	
		19,920	5.00
Deutsche Annington Ost GmbH	Berlin	9,294	
	Others	8,779	
		18,073	4.62
Deutsche Annington Nord GmbH	Geesthacht	1,978	
	Others	16,392	
		18,370	4.75
Deutsche Annington Süd GmbH	Munich	5,467	
	Nuremberg	2,079	
	Others	9,420	
		16,966	4.61
		185,438	4.67

Long-term loyal tenants

Our tenants are particularly loyal: On average a tenant lives in a Deutsche Annington apartment for about 16 years, the average tenure in Germany is about ten years. As the majority of our stocks were built either as accommodation for German miners, post office workers and railway staff or come from the large housing construction programmes of the 1950s and 60s for people with low incomes, we have many residential estates with homogeneous, stable social structures. In the big cities such as Dortmund or Berlin, the Deutsche Annington residential estates dominate entire districts. The average apartment size is approx. 64 square metres, the average monthly rental income is € 4.67 per square metre.

Positioning as a leading residential real estate company in Germany

In recent years, Deutsche Annington has pooled the expertise and knowledge of companies which have already been operating successfully on the market for many years. Therefore, we can draw on many years of experience and long-established tenant and business relationships despite the fact that the Group in its present structure is still young. We concentrate on the German market where we pursue a long-term, value-oriented business model. Thanks to our active portfolio management, we are in a position to continually adjust our rents in line with market developments while complying with statutory regulations, tenant protection laws and our contractual obligations. Another important focus is to reduce our vacancies and enhance the efficiency of our internal workflows.

At the same time, we seize opportunities for growth by acquiring new portfolios, constantly exploiting any synergies presented by the integration of these new portfolios. Thanks to our extensive experience in the acquisition and integration of housing stocks of all sizes and our efficient platform, we can perform the necessary integration processes both quickly and efficiently. Our nationwide portfolio and our regionalised Group structure enable us to incorporate housing stock acquired in any region of Germany quickly into our organisational structure as we already have the necessary local infrastructure in place. We currently have 69 customer centres and service offices throughout Germany to look after our customers.

Successful expansion of market position thanks to clear growth strategy

Deutsche Annington has set itself quantitative and qualitative growth targets for the medium term. In the next few years, we intend to buy further residential real estate portfolios and thus increase our housing stocks in the medium term. Parallel to this, we are aiming to further enhance the quality of our work and services, thus underscoring our claim to market leadership.

Our strategy focuses on three core areas:

- Long-term value-enhancing management: As a high-performing company with an attractive range of property for let, we aim to provide an excellent service for our tenants. We offer a wide range of local services and are also introducing new ones. We are creating a strong brand in the housing industry and the same standard throughout Germany. We invest in our properties to maintain their value as we can only expect to have high letting rates if we offer attractive residential properties. By targeted exploitation of earnings potential in our portfolio, we improve our company's business performance and generate high cash flows.

- Selective sales of units in a socially acceptable manner, primarily to tenants: As a socially responsible company, we offer a large cross-section of the population the chance to buy property at attractive prices. We sell selectively. We have largely stopped the so-called en bloc sales. We announce planned sales of our residential properties at an early stage and, where necessary, make use of a moderated procedure involving tenants and local authorities in the processes.

- Strategic acquisition of housing portfolios: As a residential real estate company driven by long-term considerations, we want to considerably expand our housing stocks in Germany in order to achieve further economies of scale. We are represented throughout Germany but concentrate above all on portfolios in urban centres. The key criteria in the decision to purchase a portfolio are whether it can be integrated into our portfolio and whether it can provide an adequate return.

Given the high debts of local councils, we expect up to about 1.5 million residential units to come up for sale as portfolio transactions in the next few years. Furthermore, market analysts predict that companies, investors and private owners will be selling properties on a large scale. Therefore, we believe that the conditions for attractive acquisitions are likely to improve further.

In our acquisitions, we are, however, selective as the strong demand in the housing industry has already led to a marked rise in prices for larger portfolios. Thanks to our ability to efficiently integrate portfolios of all sizes into our organisation, Deutsche Annington can not only acquire large portfolios but also smaller stocks of units where price competition is currently less stiff.

In the selective sale of residential units, we are focusing on sales to tenants and small capital investors. In order to optimise the yield from the sale of an individual unit, we have defined clear value-driven criteria for our selling decisions.

With attractive offerings and services, improved processes and well-trained staff, we are convinced we have the necessary capability to further reduce vacancy rates and boost our earnings potential. However, the economic environment and demographic developments set us limits: for example, in the new German states and in the rural, structurally weak areas of the old West German states, vacancy rates will always be above the national average. Our sustained rent policy is geared to the local market and combines the gradual raising of rents to local market levels while complying with tenant protection laws.

One of our main control instruments is permanent cost management. Thanks to the large volumes which we purchase, we can generally negotiate better prices for the goods and services we buy in. Wherever it would seem sensible, we outsource work which is not part of our core competence. Modern information technology supports us in the optimisation of processes.

Economic Environment

German economy expected to recover further in 2007

The German economy showed a surprisingly positive development in 2006: GDP rose more sharply than it had done since 2000. The growth rate was 2.7%. Thus, the increase was not only much bigger than the moderate growth of 0.9% in 2005 but also well above the forecasts. The economic recovery also had an appreciable impact on the domestic market for the first time. The labour market started to pick up so un employment fell and the number of people paying social insurance contributions increased again.

As in the years before, foreign trade again developed positively. For example, investments in plant and equipment rose again. It was notable that companies focusing on the domestic market also started to invest again in 2006. In the second half of the year, the rise in private consumption was also boosted by people buying products ahead of the forthcoming increase in VAT at the beginning of 2007. In addition, the revival of the labour market and the diminishing fear of unemployment also had a positive influence on consumption.

At the time of publication of this management report, both market research institutes and the companies themselves regarded the economic climate as favourable: In its annual report for 2006/2007, the government's Council of Economic Experts forecasts that, despite the increase in VAT and insurance tax and the further phasing-out of tax benefits, the economy will not slump but grow further – albeit only moderately. It is expecting GDP to rise by 1.8% in 2007.

The last ifo business climate index shows that German industry started the 2007 business year with full order books. According to the Council of Economic Experts, the results of surveys indicate that in 2007 it will not only be possible to increase the export and investment volumes but also to further increase the number of people in work.

No growth in private consumption expenditure and the residential real estate construction market are expected in 2007. Here, the purchases made last year in advance of the increase in VAT are likely to dampen demand.

Housing construction: First positive signs on the housing construction market but influence of extraordinary factors

A reversal in the trend in investments in construction activity is now evident. Last year, they increased by 2.5%, making a positive contribution to growth for the first time since 1999. Housing construction was, however, influenced by extraordinary factors. Since the subsidies for first-time buyers were phased out in 2006, according to the Council of Economic Experts, a larger number of building permits were granted at the end of 2005 and during 2006 which consequently led to more owner-occupier homes being built. Investments made in advance of the rise in VAT also had a positive impact.

In 2007, private housing construction activity is not likely to reach the 2006 level: The investments brought forward last year will be missing this year and the purchasing power of private households is likely to be reduced as a result of higher VAT. According to experts, the future trend in the number of buildings completed in the next few years will depend less on interest rates, which will only increase minimally, and more on the development of disposable incomes and how people rate the risk of losing their jobs.

Despite the revival last year, the amount of accommodation on offer will remain on a low level overall – measured by the number of homes being completed. According to a study published by a German building society, Bausparkasse LBS, 270,000 to 300,000 new homes will be built a year in Germany in the period from 2005 to 2010. However, a study prepared by Empirica predicts that annual demand for new homes will go up to 330,000 in the period up to 2010. Therefore, the LBS experts are expecting a housing shortage in the medium term, which should have a positive influence on prices and rents for accommodation.

Housing rents: Stronger rise in rents overall but regional patterns differ

Against the backdrop of the economic revival, rents are also continuing to rise in Germany. In 2006, rents rose on average by a good 1% compared with the previous year. However, average rent rises were still below price inflation and were still moderate compared with the general increase in consumer prices of 1.6%.

There are still sharp differences in the development of rents depending on the location, segment and region. In general, it can be said that in the big cities the trend towards higher rents is greater than in towns with less than 100,000 inhabitants and, particularly in a five-year comparison, the rents for apartments in non-prime locations have risen disproportionately. Both are market data which apply to the Deutsche Annington housing stocks.

Different conditions impacting on regional rent markets

The regional demographic and economic conditions have different influences on the respective regional rent markets. The regions below are the areas of the Deutsche Annington regional companies; the average rents mentioned below are market rents for residential units with an average standard of comfort.

Ruhr and Westphalia (Ruhr area):

The Ruhr and Westphalia regional companies mainly manage our properties in the Ruhr area. The Ruhr area has a high population density (approx. 5.3 million inhabitants, approx. 1,200 inhabitants per square kilometre). Structural changes in recent years, such as a decline in the population and high unemployment, are having a direct impact on disposable income. The market rents vary from city to city: at € 5.50 per square metre, Bochum has the highest rent, followed by Dortmund and Essen at approx. € 5.00 per square metre. Overall, rents have tended to stabilise in these areas in recent years. We are expecting rents to continue to increase slightly in this region.

Rhineland:

The areas along the river Rhine are, comparatively speaking, in a better position than the Ruhr area with higher average incomes, lower unemployment and greater earning power. In recent years, average rents have risen steadily in metropolitan areas such as Düsseldorf, Cologne and Bonn and are currently among the highest in Germany. At € 7.35 per square metre, Cologne has the highest rents, followed by Bonn and Düsseldorf. The market rents in the other main cities of the Rhineland such as Aachen, Koblenz and Mönchengladbach are around € 5.50 per square metre. We are expecting a further slight rise in rents in the metropolitan areas of the Rhineland and at above-average locations in the region.

Southwest:

Our Southwest region mainly covers Hesse and Baden-Württemberg. This region is in our opinion one of the most attractive markets for residential real estate in Germany, covering both the populous Rhine-Main area in the north and the Stuttgart region in the south. In our opinion, the economic conditions in the Rhine-Main region are good, regional GDP is forecast to grow further as is the population in the region. There has been a general increase in the rents in Hesse and Baden-Württemberg in recent years. In Frankfurt am Main and Wiesbaden, rents for residential units with an average standard of comfort are around € 7.20 and € 7.60 per square metre, respectively. We expect a further increase in market rents in the Southwest region.

North:

Our North region covers Hamburg, Bremen and the states of Schleswig-Holstein and Lower Saxony as well as parts of Mecklenburg-Western Pomerania. This includes the mainly export-driven metropolitan area of Hamburg. Overall, market rents in Hamburg are at a high level, averaging € 6.70 per square metre. Smaller towns such as Geesthacht in the vicinity of Hamburg are profiting from the economically strong region and also have very high average market rents of € 5.50 per square metre. The development of rents in Lower Saxony and Schleswig-Holstein has tended to be stable in recent years; the rents in Hanover are currently under € 5.00 per square metre. We still see fairly good potential for the development of rents in the catchment area of the Free Hanseatic City of Hamburg.

East:

Our East region manages the housing stocks of Deutsche Annington in the capital, Berlin, and in the five new German states. The five new states are rather structurally weak compared with the older German states and have to contend with high unemployment and lower purchasing power. Berlin has seen its population grow in recent years and apartment rents have also tended to rise there. However, no such trend towards higher rents has been recorded in the new German states. Rents in Berlin are currently around € 5.70 per square metre. We can confirm the above-average attractiveness of the capital and the surrounding area and therefore expect rents to rise slightly there.

South:

The South region of Deutsche Annington mainly covers the economically powerful state of Bavaria. Continued strong economic growth and an increase in the population are predicted for this region, with the trend stronger in the south of Bavaria than in the north. The steady migration of people to the region in recent years has helped to push up rents; apartments in Munich currently fetch rents of about € 8.75, and those in Nuremberg about € 6.20 per square metre. Thanks to the positive development of the economy, we are expecting considerable potential for higher rents in the medium term in the large and mid-sized centres of Bavaria, particularly in Munich and its catchment area.

Buying a home: No uniform trend in the prices for residential real estate

There is still no uniform trend in the development of prices for residential property: In 2006, the prices for used housing fell compared with 2005 but the price drop was half than seen in the previous year. In general, it is, in our opinion, a good time to buy an owner-occupier apartment.

Regionally there are sharp differences in the development of prices and no uniform trends. The highest prices for used owner-occupier apartments with an average standard of comfort are paid in the metropolitan areas of Munich, Düsseldorf and Frankfurt am Main.

Purchasing property: Continued strong demand for residential real estate

Used housing in average to good locations and with good returns can still be expected to find buyers in the future. The great interest from investors in acquiring large residential real estate portfolios in Germany seen since about 2004 continued in 2006. The reasons for this interest are the low home ownership level in Germany (about 43%), the increasing number of households as well as the fact that real estate offers good opportunities to maintain or increase the value of the investment. Furthermore, the economic environment in Germany is favourable.

Demographic development: Growing number of small households leading to greater demand for accommodation

The demographic development in Germany is a major factor determining demand for accommodation. In addition to the development of the population, which according to the Federal Statistical Office will start declining from about 2012 despite immigration, the demand for accommodation is determined directly by the number of households. In spite of decreasing population figures, the number of households in Germany is rising steadily. It is forecast that the number of households in Germany will increase from about 39 million today to about 41 million by 2020. According to the Federal Statistical Office, it is particularly the small households (one-person and two-person households) which are the growth drivers.

The trend towards smaller households depends on various factors. The main reasons are the demographic structure in Germany, growing affluence and the resultant increasing demands on home comfort, people starting families later and more divorces. We believe that this trend towards smaller households will be beneficial for the letting business of Deutsche Annington as we mainly offer small and medium-sized apartments.

In the medium term, we expect a further increase in the demand for living space. According to a study by Bausparkasse LBS, living space per capita will rise by 22% or ten square metres in the old German states in the next 25 years and thus continue increasing albeit at a slower rate. In the new German states, a growth in living space per capita of 45% or 17 square metres is forecast. Overall, there are likely to be sharp regional differences in the demand for living space: particularly strong growth is predicted in the southern German states of Bavaria and Baden-Württemberg.

Business Review

Operational performance

€ million	2006	2005
Income from property management	898.8	681.7
Profit on the sale of trading properties	123.5	147.4
Profit on the disposal of investment properties	7.8	36.0
Profit on disposal of properties	**131.3**	**183.4**
EBITDA	765.9	311.3
Profit before tax	428.7	58.3
Profit for the year	207.1	170.6
Investments	133.4	3,553.7
Number of employees (as at Dec. 31)	1,385	1,889
Number of units sold individually	4,763	7,072
Number of units sold en bloc	2,838	5,306
Number of units sold (recorded sales)	**7,601**	**12,378**
Number of residential units in portfolio (as at Dec. 31)	185,438	189,886

Notice on scope of consolidation

The 2006 financial statements include the activities of Viterra AG (as well as MIRA), which were acquired in August 2005, for the first time for the entire period from January through December. The previous year's financial statements only included Viterra (and MIRA) for the period from August through December 2005. Therefore, the company's volume of business for the 2006 financial year is much larger and the comparability of the figures for 2006 and 2005 is only limited.

The pre-year figures have been adjusted as a result of the following:

- A change was made in the accounting and measurement policies with effect from January 1, 2006. In accordance with IFRS, the change was applied retrospectively at January 1, 2007. Investment properties are now carried at fair values and not, as previously, at cost of acquisition.

- In connection with the discontinued operations, the presentation of the comparative period in the income statement has been adjusted as if the discontinued operations had already been discontinued from the beginning of the comparative period. The items referring to the Development division are shown separately in the income statement.

Development of our core activities

Deutsche Annington has divided its business operations into three core areas in order to ensure optimal control.

Real eatate management: Innovative measures secure continued strong earnings

The income from property management rose from € 681.7 million in 2005 to € 898.8 million in 2006. This increase is mainly due to the first-time inclusion of the Viterra activities for the full 2006 financial year; our action taken to reduce the number of vacant units, raise rents and cut costs as well as optimise our purchasing processes also helped to further improve the result.

Our Real Estate Management division covers letting and real estate management activities. As one of the largest residential real estate letting companies in Germany, we set ourselves quantitative and qualitative goals. We see ourselves, above all, as a property holder and classic letting company for residential real estate. That's why high customer satisfaction and customer loyalty are among our most important goals. In the past year, we successfully reduced our vacancy rates.

To achieve this, we did not just rely on classic letting strategies but also adopted new, innovative approaches. Thanks to our regional structure, we can steer our marketing activities to suit the requirements of the particular region and the specific target group, try out measures in test markets and later use them throughout Germany. For example, we have special offers for target groups such as families, senior citizens and students and also make use of product-specific advertising campaigns (e.g. for attic flats).

Still regional differences in vacancy rates

The regional differences in the demand for accommodation are also reflected in the vacancy rates. Although we managed to reduce vacancy rates for the Deutsche Annington housing stocks in the new German states, they are still much higher than in the rest of Germany. By contrast, the residential units of our companies in the south and southwest of Germany are virtually fully let. In the other regions, in particular in the Rhine/Ruhr metropolitan area, the vacancy rate has stayed more or less at the 2005 level. Overall, 5.7% (2005: 6.3%) of our properties were vacant at the end of the year. This figure also includes the apartments earmarked for sale and therefore vacant. We do not re-let such apartments planned for sale as it is easier to sell empty apartments to owner-occupiers and we can get a higher price for them.

Rental income grew in 2006

In 2006, we achieved a slight increase in our rental income. One third of our residential units now fetch average monthly rents of more than € 5.00 per square metre; the average rent for our portfolio as a whole is € 4.67.

The majority of our housing stocks are standard apartments with 60 square metres of living area or more (58%); there is good demand for them if they are located in inner cities or in residential areas near cities. Most of our units were built between 1946 and 1980 (nearly 75%).

We expect this market segment of small to medium-sized residential units to profit most from the demographic development and the trend towards an increase in the number of households. Furthermore, our units are mainly (90%) in small blocks of up to eight apartments; experience shows that these smaller apartment blocks are more attractive for tenants and buyers alike than the classic high-rise blocks.

Maintaining customer loyalty by offering an after-sales service

Since the establishment of Deutsche Annington, the company has sold a large number of residential units; most of them individually. We offer these customers our service even after they have purchased their property. Our subsidiary, Deutsche Annington Service GmbH, Frankfurt am Main, manages the common property for apartment owners in accordance with the German Condominium Act. It handles the efficient management of the entire property, implements the decisions of the condominium owners' associations and is the contact for owners at the interface between separate property and common property. Deutsche Annington Service GmbH offers capital investors a full management service for their separate property. In addition, it provides the owners with a wide range of services such as the maintenance and modernisation of separate and common property in apartment buildings including alterations to the apartments to suit the owners' new needs as they get older. At the end of 2006, Deutsche Annington Service GmbH looked after approx. 2,200 (2005: 800) condominium owners' associations with a total of more than 56,750 residential units and condominiums (2005: 18,380).

Demographic changes exploited as an opportunity with Annington Wohnen Plus

In our opinion, German society is about to undergo a demographic change: About 19% of the population is already over 65. In 2020, this figure will have risen to about 25%. At the same time, we believe that people's ideas about how they want to spend their old age are also changing: Fewer and fewer people find the prospect of spending their old age in a senior citizens' home attractive. According to a recent Emnid survey carried out by Bausparkasse BHW, 87% of all Germans over 50 want to stay in their own home. Deutsche Annington has already responded to this growing market segment and developed the senior citizens' sheltered accommodation programme, Annington Wohnen Plus. Specially trained staff arrange support for elderly residents to cope with day-to-day problems surrounding life and care in the community. To provide this support, we have set up advice centres in seven cities (Frankfurt am Main, Duisburg, Geesthacht, Dortmund, Essen, Cologne and Nuremberg). The high demand for this service confirms our market analysis.

Residential sales: Shift in focus towards retaining housing stocks

As expected, profit on disposal of properties fell from € 183.4 million in 2005 to € 131.3 million. We have shifted the focus of our sales strategy sharply. Deutsche Annington already announced at the end of 2005 that it would only be selling units en bloc to third parties in exceptional cases. 5,306 units were sold en bloc in 2005. In 2006, we reduced these package sales to 2,838 units and the apartments that were sold en bloc were largely in the new German states. Parallel to this, we also reduced our so-called privatisation programme (sales to tenants, other owner-occupiers and small investors) in 2006. In future, we will continue to be selective in our new sales projects. In 2006, we sold 4,763 units (2005: 7,072) throughout Germany under our privatisation programme.

The careful preparation of our sales programme accompanied by early notification of the local people affected has meant that our plans to sell individual apartments have been successful and met with broad acceptance. This practice has, for example, gone so well in Dortmund that the decision-makers on the Dortmund city council now talk of the "Dortmund approach" to the selling of units in residential estates.

Acquisitions: High demand for local authority portfolios pushes up prices

As the first private equity-funded residential real estate company in Germany, Deutsche Annington started acquiring the housing stocks of railway companies in 2001. Since then, we have systematically pursued our strategy of growth by continually purchasing new portfolios of all sizes. The acquisition of attractive portfolios and their integration into our Group are a key part of our business strategy. With the Deutsche Annington Real Estate Group, we now have a platform which permits us to already exploit the synergies of newly acquired portfolios within a short time of their purchase. With our acquisitions, we not only want to achieve our growth targets but also to round off our regional residential portfolios where this makes sense.

Due to the growing demand from investors for residential real estate, prices for larger portfolios rose last year. Therefore, Deutsche Annington did not put in an offer for portfolios which we considered to be unprofitable. At the same time, there were sometimes considerable delays in the privatisation of portfolios owned by local authorities.

Owing to the comprehensive integration measures in our company in the first half of 2006, we did not refocus our attention on acquisitions until the second half of the year. As a result of these activities, we managed to acquire about 2,500 units at the end of 2006 and another roughly 1,200 at the beginning of 2007.

Development division sold as part of our focusing strategy

As part of the integration process, we decided to concentrate solely on the residential real estate business and therefore to sell the real estate development activities. Therefore, with effect from June 23, 2006 we sold Viterra Development to the German subsidiary of the Orco Property Group, a company listed on the Paris stock exchange. All projects and branches and therefore all staff were taken over by Orco.

Viterra Development successfully concentrated on the development and sale of office real estate and owner-occupier apartments in inner-city locations of German metropolitan areas such as Hamburg, Berlin, Düsseldorf, Frankfurt am Main and Munich. Outside Germany, Viterra Development is also active in the two capital cities, Warsaw and Prague. The company is still operating under the brand name, Viterra. Orco has acquired the trademark rights for Viterra Development until June 2011.

2006: One of the biggest integration projects in the German housing industry completed

2006 was dominated by the integration of Viterra into the Deutsche Annington Real Estate Group. Following the acquisition of Viterra in August 2005, we started a comprehensive project. On January 1, 2006, the previously separate companies (including Deutsche Annington, Viterra, Viterra Rhein-Main and Deutschbau) were united under the umbrella of the new Deutsche Annington Real Estate Group.

Regional reorganisation of housing stocks

One important goal of our integration project was the regional reorganisation of our housing stocks by allocating all units to one of seven regional companies. Parallel to this, all main processes were reviewed and improved. For example, we separated the real estate management and re-letting activities organisationally from each other. This has given our customer care team the necessary manpower resources to concentrate on their core work, maintaining good customer contacts, while our re-letting staff can make sure vacant units are re-let quickly and smoothly. Thanks to this clear organisational separation of functions, we can introduce better and more easily measurable re-letting incentives and also engage external estate agents where necessary.

Cost-cutting saves double-digit millions

The successful integration of Viterra has enabled us to achieve considerable cost savings. This has been mainly achieved by cutting personnel, IT, purchasing and administrative costs. Some of these measures will not take effect until 2007.

Key business functions centralised

Deutsche Annington took further action to optimise processes and save costs by setting up centralised service and control departments. The following operational business is now handled centrally for all regional companies:

- heating and ancillary cost billing
- the purchase of all goods and services, organisation of necessary technical work (maintenance and repairs)
- advice in all legal questions including dunning and legal action
- accounting
- rent account and claims management
- personnel work and the looking-after of trainees and apprentices

These service functions are all provided by Deutsche Annington Verwaltungs GmbH. Deutsche Annington Immobilien GmbH acts as a pure holding company. Other functions such as IT, residential sales and condominium management were hived off into separate companies.

More efficient control of maintenance work

By introducing standardised processes, Deutsche Annington has in our opinion organised maintenance more effectively. Our central purchasing department signed framework agreements for all maintenance and repair work with local service providers and set flat rates for important work. Deutsche Annington provides a basket of brand products for the materials to be used. This ensures the same quality of repairs throughout the Group and also avoids time-consuming purchasing processes for individual work. Our central technical department has set up a 24-hour repair hotline for all regional companies. This is run mainly by external service providers and promises our customers that their repairs will be performed within four days. We continually monitor online the availability of the hotline and the quality of the service provided.

Competitive advantages thanks to integrated IT platform

Deutsche Annington relies on an efficient, integrated IT platform to control processes throughout the Group. In SAP R/3 we have a universal ERP (Enterprise Resource Planning) software solution. Furthermore, the SAP Real Estate solution specially designed for our industry allows effective, precise operational control of housing stocks. Thanks to the scalable platform, further acquisitions of all sizes can be rapidly integrated into the portfolio.

Promoting social interaction

Deutsche Annington takes its social responsibility as a residential real estate company seriously. For example, we support social projects in difficult residential districts, be it with debt counselling by a charity or the renovation of kindergartens in need of modernisation. One focus of our work is to promote community life and help children and teenagers.

We also help to deal with the special concerns of our tenants' associations with foundations which we run together with the German Tenants' Association, Foundation to Foster Community Life in Viterra Residential Complexes and the Deutsche Annington Foundation. Whilst the Deutsche Annington Foundation focuses on helping tenants who have fallen on hard times, the Viterra Foundation promotes social interaction in our residential estates.

Employees

Staff adjustments completed by the end of the year

With the integration of Viterra into the Deutsche Annington Real Estate Group, the organisation was completely restructured in the first quarter of 2006 both at Group and branch level. The necessary adjustments to the workforce structure were completed to schedule by December 31, 2006. At the end of the year, 1,385 people (in 2005: 1,889) were employed in the Deutsche Annington Real Estate Group.

As at December 31, 2006, 682 women were employed in the Deutsche Annington Real Estate Group; thus women now make up 49.2% of the workforce. 228 employees or 16.5% of the workforce have a part-time job. The average age in the Group is 42.3, the average number of years of service is 12.4.

As part of the restructuring of the organisation, the branch and works council structures were also adjusted to bring them into line with the new corporate structures.

Works regulations harmonised

The different collective works regulations were harmonised throughout the Group in order to make the employees of the different companies feel part of the one new organisation. We attach particular importance to continuity in the works regulations which apply to all employees of the Deutsche Annington Real Estate Group from January 1, 2007.

In addition, new works regulations are to be introduced in future, offering in particular measures in the field of health and family. As part of a strategic personnel policy, these measures are to meet the specific demands of our company and be permanently anchored in our processes. In 2007, a project group will identify the possible fields of action and work out appropriate measures together with the managers, works council and staff. Our aim is to put together and optimise the possibilities the company already offers such as flexible working hours and alternating telework and find more options for achieving an intelligent balance between the company's and employees' interests.

Using personnel development and further training as a strategic instrument

Developing our staff and helping them to improve their qualifications is a major strategic factor for ensuring our company's success. The aim of personnel development is to help the staff and managers to cope better with present and future demands and make sure that good employees stay with the company by giving them both career prospects and the opportunity for personal development.

In 2006, a number of staff development measures were introduced throughout the Group as part of strategic HR management. These instruments include "Management by Objectives", structured staff appraisal interviews as well as personnel development rounds. The introduction of "Management by Objectives" was accompanied by training courses for managers and introductory events for the staff in the different companies of our Group. "Management by Objectives" is a structured target agreement process which cascades the goals of the Deutsche Annington Real Estate Group into all levels of the workforce. Alongside the target agreements, the process also ensures further training and staff development.

All managers and staff are obliged to use the personnel development instruments. The HR department has ensured that the works councils can exercise their codetermination and participation rights for all processes and instruments.

The new instrument, personnel development rounds, gives the management a comprehensive overview of all staff and executives. The aim of these rounds is to identify potential candidates for key positions, emerging leaders and people for interdisciplinary project groups which the company now needs more and more. We want to offer our employees opportunities which suit their strengths and achievements. For us this is the expression of an appreciative personnel policy.

Establishing a uniform leadership culture

In this connection it was particularly important for us to also establish a uniform Deutsche Annington leadership culture in 2006. To achieve this, the senior managers got together to develop leadership principles which will be an important yardstick for assessing managers in the years to come. We set up internal management training courses as another component for implementing a uniform leadership culture. Some 70 executives of the 3rd and 4th management levels attended such a training course on “Management in Times of Change” in 2006. Further management training seminars to deepen our understanding of leadership are to follow in 2007.

Devising further training measures in line with the company’s strategy and goals is also part of staff development. A large number of such further training measures were already performed in 2006. The focus was on tailored in-house training courses and a range of external seminars for our specialists.

All employees to share in the company’s success

In future, all employees will share in the company’s success. In addition to the performance-related pay system for all non-pay-scale staff already in place, a variable pay system for all pay-scale staff was introduced on January 1, 2007. The variable pay component will be linked to the employee’s individual performance and the company’s success.

Compensation for non-pay-scale staff was also harmonised. The performance-related pay system for all non-pay-scale staff together with a single target agreement system for all function groups was introduced throughout the Group as part of the harmonisation process, the key performance figures were standardised and the old bonus systems replaced. All non-pay-scale staff were offered a new non-pay-scale employment contract.

Taking responsibility for the next generation by offering vocational training

In 2006, the department responsible for vocational training concentrated on integrating the trainees and apprentices working for the company all over Germany and harmonising the training processes. Another main point was the changes in the vocational training regulations for the real estate industry.

As at December 31, 2006, a total of 89 trainees and apprentices were employed in the Deutsche Annington Real Estate Group; that is 6.4% of the workforce. 20 young people were given a place for a traineeship or apprenticeship. 31 passed their final exams and 28 were given a fixed-term employment contract.

Financial Analysis

Notice on scope of consolidation

Due to the first-time inclusion of the activities of Viterra AG (and MIRA), which were acquired in 2005, for the first time for the entire financial year, the company's volume of business for 2006 is much larger and the comparability of the figures for 2006 and 2005 is only limited. Furthermore, the pre-year figures were restated (see page 36).

Income from property management rises again

The income from property management rose from € 681.7 million in 2005 to € 898.8 million in 2006. The action taken to reduce the number of vacant units, raise rents and cut costs as well as optimise our purchasing processes also helped to increase the result. The number of the company's own residential units managed fell slightly from 189,886 at the end of 2005 to 185,438 at the end of 2006.

Profit on disposal of properties falls slightly as the sales programme is cut back

As expected, profit on disposal of properties decreased from € 183.4 million in 2005 to € 131.3 million. At € 123.5 million (2005: € 147.4 million), sales of trading properties accounted for most of this figure. Profit on disposal of investment properties amounted to € 7.8 million (2005: € 36.0 million).

The main reason for this development is a decline in sales of residential units: At 7,601 units, Deutsche Annington sold a lot fewer units than in the previous year (2005: 12,378 units). This was due to a conscious change in our strategic focus away from privatisation towards stock management. As a residential real estate company with a long-term view, we see ourselves first and foremost as a company aiming to retain its stock of residential real estate. Given the current low capital market costs and the slow development of prices for used housing, we are continually reviewing whether it makes more sense to sell a property or to keep it. This strategy already led at the end of 2005 to an appropriate cutback in the sales programme for 2006. Furthermore, our policy not to continue with en bloc sales also played a role in the reduction of the sales programme.

Further sharp increase in EBITDA

EBITDA is our most important metric. It is used for internal management purposes and as an indicator of the earning power of our business activities. EBITDA is the acronym for earnings before interest, tax, depreciation and amortisation.

The Deutsche Annington Real Estate Group generated EBITDA of € 765.9 million in 2006. Compared with the previous year, EBITDA jumped by € 454.6 million or 146%.

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Consolidated net income

€ million	2006	2005
EBITDA	**765.9**	**311.3**
Depreciation and amortisation	4.0	3.9
EBIT	**761.9**	**307.4**
Interest expense	–333.2	–249.1
Profit before tax	**428.7**	**58.3**
Income taxes	–197.6	96.2
Profit from continuing operations	**231.1**	**154.5**
Loss/profit from discontinued operations	–24.0	16.1
Profit for the year	**207.1**	**170.6**
Attributable to:		
Equity holders of DAIG	207.1	170.3
Minority interests	0.0	0.3

The improvement in EBITDA is above all due to the increase in value of the investment properties and the first-time inclusion of Viterra for the entire 2006 financial year. The increase in EBIT from € 307.4 million to € 761.9 million is also largely due to the same reason. Pre-tax profit rose to € 428.7 million (2005: € 58.3 million).

Income taxes were particularly affected by the deferred tax expenses arising from the result of the measurement of investment properties at fair value. By contrast, in 2005 a different assessment of whether existing loss carryforwards could be used led to the recording of higher deferred tax assets and therefore to a positive income tax charge.

The consolidated profit for the year is thus well up on the figure for 2005.

Assets and Financial Situation

Group balance-sheet structure

€ million	2006	%	2005	%
Total non-current assets	7,059.9	64.6	6,757.1	62.5
Total current assets	3,872.3	35.4	4,059.5	37.5
Total assets	**10,932.2**	**100.0**	**10,816.6**	**100.0**
Total equity	1,688.7	15.4	1,031.7	9.5
Total non-current liabilities	7,758.9	71.0	8,707.3	80.5
Total current liabilities	1,484.6	13.6	1,077.6	10.0
Total equity and liabilities	**10,932.2**	**100.0**	**10,816.6**	**100.0**

In 2006, the Deutsche Annington Real Estate Group invested a total of € 133.4 million. In 2005, investments ran at € 3,553.7 million, most of this amount being used for the Viterra acquisition.

The increase in non-current assets in the reporting year compared with the previous year is mainly due to the fair value adjustment of investment properties in 2006.

Equity rose from € 1,031.7 million in 2005 to € 1,688.7 million in 2006. As a result, the capital-to-assets ratio increased to 15.4% as against 9.5% in 2005. This increase is partly due to the Group profit and partly to capital injections of € 479.5 million by the equity holders of Deutsche Annington.

Information on the Statement of Cash Flows

Statement of cash flows

€ million	2006	2005
Cash flow from operating activities	789.9	549.5
Cash flow from/used in investing activities	20.9	–3,296.3
Cash flow used in/from financing activities	–589.1	3,165.2
Net changes in cash and cash equivalents	**221.7**	**418.4**
Cash and cash equivalents at the beginning of the year	484.7	66.3
Cash and cash equivalents as shown in the balance sheet	**706.4**	**484.7**

The effect of the changes in the balance sheet on the cash flow from operating activities has been adjusted to eliminate the effects of changes in the scope of consolidation and non-cash items. Therefore, direct comparison with the corresponding changes in the published consolidated balance sheets is not possible.

At € 789.9 million, the cash flow from operating activities is well up on the previous year's figure and contains above all receipts from the letting business and from sales of trading properties. The rise in comparison to the previous year is mainly a result of the inclusion of the cash flow from Viterra for the whole of 2006.

The cash flow from investing activities rose sharply compared with the previous year by € 3,317.2 million to € 20.9 million. Whilst the previous year was affected by payment of the purchase price for Viterra, it was above all the sale of the Development division which had a positive impact on cash flow from investing activities in 2006.

The cash flow used in financing activities in 2006 reflects the current capital repayments on loans. In 2005, there was a much more positive cash flow from financing activities from the funding of company acquisitions.

Funding

Comprehensive recapitalisation completed in 2006

On August 3, 2006 a total of € 5,416 million was raised as part of a securitisation transaction. As part of this securitisation transaction, 29 companies of the Deutsche Annington Real Estate Group sold bearer bonds to German Residential Asset Note Distributor P.L.C. (GRAND). GRAND refinanced the acquisition of the bearer bonds by issuing interest-bearing securities on the capital market. The syndicated loans taken out in August 2005 and totalling € 5,898.5 million were repaid in full using the funds raised in this securitisation transaction as well as € 482.5 million of the company's own funds.

Of the amount repaid, € 1,570.9 million was used for repaying a Deutsche Annington recapitalisation measure performed in 2005, which was used to repay company borrowings and also partly to fund the Viterra acquisition. The remainder was used for repaying a syndicated loan of € 4,327.6 million taken out by subsidiaries the previous year for the Viterra acquisition (€ 3,562.5 million), the repayment of loans in connection with the Viterra acquisition (€ 715.1 million) as well as for market adjustment resulting from the transfer of interest rate swaps (€ 50.0 million).

On October 20, 2006, the Group entered into liabilities of € 393.5 million with GRAND as part of another securitisation measure. These funds were also raised by issuing bearer bonds to GRAND. These bonds were issued by two Group companies of Deutsche Annington. Some of the funds raised were used to repay company borrowings of € 170.0 million. The rest was retained by Group companies.

As part of the two securitisation transactions with GRAND, the companies involved provided securities in the form of land charges, account pledge agreements and assignments. Moreover, equity interests were also pledged. The average weighted interest rate achieved in the securitisation transactions is 3.36% to July 2010. According to the terms of the contracts, this interest rate increases to 4.66% from July 2010 to the end of the contracts in July 2013. The repayments for this transaction are to be met from future property sales and from normal cash flow from the re-letting business.

A loan for € 200.0 million was taken out with Barclays Capital in December 2006. The purpose of this loan was to finance portfolio acquisitions which had been made by subsidiaries of Deutsche Annington. As at December 31, 2006, a total of € 130.2 million of the total loan amount had been utilised. The remaining amount of € 69.8 million is available for further portfolio acquisitions (€ 64.8 million) and as a short-term credit line (€ 5.0 million).

Fair Values

Fair values increase transparency and are an important control instrument

Deutsche Annington calculated the fair values of the entire stock of residential buildings, small commercial units, garages/parking spaces and undeveloped land of the Deutsche Annington Real Estate Group as at December 31, 2006 in an internal valuation. The following criteria were applied in the valuation of the different segments of real estate:

Residential real estate

The value of the entire portfolio of residential properties was determined on the basis of the “International Valuation Standard Committee’s” definition of market value. Portfolio premiums and discounts which can be seen when portfolios are sold in market transactions were not allowed for, nor were time restrictions in the marketing of individual properties. The method used by Deutsche Annington to determine the fair values therefore complies with the IFRS standards.

In line with our business model, a distinction was made between apartments which are being sold individually or which, in our opinion, are basically suitable for being sold individually (privatisation portfolio) and the buildings which are to be considered as properties to be managed.

First, all buildings were valued according to a rating system with regard to their quality, their market attractiveness and their macro-location. The aspects considered in assessing the quality of the buildings included their age, the standard of their heating systems, the quality of the windows and heat insulation and an assessment of the technical condition of the buildings. The assessment of their market attractiveness was based on factors including the micro-location of the buildings, how built-up the area is, the average size of the residential units and the number of rooms. The quality of the macro-location was derwed from the purchasing power index for the particular postal code area.

The property management portfolio was valued using the income capitalisation approach. The basis of the valuation is the net annual income per building which results from the annual net rent minus non-allocable ancillary costs, maintenance expenses and administrative expenses following the II. BV (German Regulation on Calculations for Residential Buildings in Accordance with the Second Housing Construction Law). With properties on land with inheritable building rights, the annual ground rent was also deducted. Vacant properties were taken into consideration on the basis of future anticipated rental income from assumed re-letting scenarios. In order to determine the capitalised value of potential yield returns, the annual net yield at building level was capitalised using capitalised interest rates which were derived from the current German real estate market and allocated to the buildings with the aid of the previously determined ratings.

For the privatisation portfolio, it was assumed that, apart from the apartments in a building which can be sold directly to tenants, owner-occupiers and capital investors (privatisation share), there are a certain number of apartments which, depending on the attractiveness, quality and macro-location, can only be sold to capital investors at a discounted price (remainder share).

The value of the privatisation share per building was determined using the comparable method. In principle, the remainder share was valued in the same way as the properties in the property management portfolio.

A residential real estate portfolio acquired at the end of the year was not revalued but recognised at cost as this was, in our opinion, the fair value of the portfolio.

Commercial properties

The commercial properties in the portfolio were measured on the basis of individual experts' opinions, purchase contracts, offers made in the course of sales activities or appraisals of internal experts.

Undeveloped land

Undeveloped plots of land were measured according to their state of development, the likelihood of development and the local market situation on the basis of derived land guide prices.

Results of the valuation

In accordance with their engagement letter, the auditors of the consolidated financial statements included these fair values in their audit of the consolidated financial statements and the Group management report of the Deutsche Annington Real Estate Group for the financial year from January 1 to December 31, 2006.

The fair value of the stocks of residential units, small commercial units, garages and undeveloped land of the Deutsche Annington Real Estate Group as at December 31, 2006 was approx. € 9.9 billion (2005: € 9.4 billion).

The fair values of the real estate portfolio by region are as follows:

Fair Values of the Real Estate Portfolio of the Deutsche Annington Real Estate Group

	Residential units		Other rental units		Fair values in € million	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
Deutsche Annington Nord GmbH	18,370	18,731	4,232	4,497	823.8	848.6
Deutsche Annington Ost GmbH	18,073	20,707	2,803	3,355	733.3	727.0
Deutsche Annington Rheinland GmbH	19,920	18,805	6,315	5,339	1,270.6	1,061.5
Deutsche Annington Ruhr GmbH	36,991	37,249	6,296	7,230	1,684.9	1,667.9
Deutsche Annington Süd GmbH	16,966	18,190	8,285	7,948	1,164.1	1,127.8
Deutsche Annington Süd-West GmbH	31,658	32,430	7,313	7,367	1,940.9	1,781.8
Deutsche Annington Westfalen GmbH	43,460	43,774	6,477	6,590	1,984.5	1,825.3
Commercial units					207.5	234.0
Undeveloped land					80.5	76.7
	185,438	**189,886**	**41,721**	**42,326**	**9,890.1**	**9,350.6**

In addition, Cushman & Wakefield, an external valuer, performed an independent valuation of the Deutsche Annington real estate stock as at December 31, 2006. Commercial units and undeveloped land (internally valued at € 288.0 million) were not included. The Cushman & Wakefield valuation is a valuation at portfolio level and includes portfolio premiums and discounts. Therefore, this external valuation (adjusted to eliminate the small commercial units and undeveloped land) is about € 338.0 million higher than our internal valuation of the fair values in accordance with IFRS.

Risk Management

The risk policy of the Deutsche Annington Real Estate Group is geared to systematically and continuously increasing the company's value and achieving its medium-term financial objectives. Furthermore, the company has codes of conduct laid down in guidelines and other directives. Monitoring mechanisms are in place to ensure that these codes of conduct are observed. Speculative business transactions or other measures of a speculative nature are not permitted. We strive to conduct ourselves in a fair and responsible manner towards suppliers, customers and the company.

Risk management system

The company uses a comprehensive reporting system to identify and handle risks at an early stage which may be of significance to the economic situation of Deutsche Annington. In addition to detailed monthly controlling reports, the Chief Executive Officer and the Chief Financial Officer both give monthly reports to the Supervisory Board of Deutsche Annington. In addition to the quantitative reporting in the controlling reports, there is also qualitative reporting in standardised, weekly reports which the managers submit to the managing directors of the company. In our opinion, this standardised process ensures that all managers of the subsidiaries and the heads of department of the holding company report major issues regularly to the managing directors.

Risk situation and individual risks

Major risk fields or risks have been identified in the following areas:

Risks from changes in the business environment

Economic forecasts predict that the demographic development of German metropolitan areas will differ greatly: According to these forecasts, there are regions to which substantial numbers of people will migrate (e.g. the Rhine-Main region, Munich, Stuttgart). Here, the demand for accommodation is likely to rise. By contrast, there will, in our opinion, be regions, possibly including the Ruhr area, from which large numbers will move away. The population will also decrease here as a result of the expected fall in birth rates. However, this development is likely to be cushioned by a shift in the individual demand for living space: The number of one and two-person households is likely to rise steadily and demand for bigger apartments will, in our opinion, also grow parallel to this. Therefore, in future there may be fewer people but they will be living in bigger homes and the number of households will increase overall. Thus, a noticeable fall in demand for rented and owner-occupier accommodation is not likely to occur before 2020, even in the regions like the Ruhr area which people are leaving.

It is currently impossible to predict to what extent the increase in VAT on January 1, 2007 will lead to a fall in demand for residential real estate, particularly from threshold households in the next few years. Although there are very few government subsidies available to home buyers since the subsidy for threshold households was phased out at the beginning of 2006, we are expecting demand to remain stable thanks to the continued low interest rates on mortgages. Should the interest rates increase considerably in the next few years, this might have an effect on the demand for residential properties.

Changes in market prices may also affect demand for properties to buy and our acquisition strategy. Should the prices for residential portfolios increase more sharply than we expect, Deutsche Annington may possibly only be able to achieve its growth targets by incurring higher costs. Moreover, other market players could start selling off individual apartments on a large scale and thus cause prices to fall as a result of greater supply. Deutsche Annington is monitoring the development of demand closely and will, if necessary, step up its sales promotion activities.

Performance/Operational risks

As far as acquisitions are concerned, there are various government requirements restricting our rent increases and our sales programme for some of our housing stocks; furthermore, there are also contractual and legal requirements impacting on the adjustment of our workforce structure to the changed market conditions.

One major goal in our Real Estate Management division is to reduce vacancy rates. Should the macro-economic conditions deteriorate significantly, the vacancy rate may also increase in the medium term and thus cause a fall in rental income. As most of the residential properties of Deutsche Annington are in average locations, we do not expect demand to be affected much.

In the south of the Ruhr area, the many years of coal mining have left disused mine workings near the surface, which present a risk of mining damage to Deutsche Annington's land and buildings. At present, it is difficult to exactly estimate the associated economic risk as there are no or very few records for many of the old mine workings. Moreover, the law is not clear on the question of liability for any damage which might occur. Deutsche Annington is countering this risk by conducting a systematic analysis to identify potential mining damage. These results will provide the basis for Deutsche Annington to take suitable remedial action and clarify the legal situation where necessary.

Risk from the development of fair values

Our valuation of the fair values of our real estate was based on assumptions which may develop differently in the next few years than we currently expect. For example, the valuation included not only building-specific parameters but also the quality of the building location. Should the estimate of the micro-situation of the buildings and the quality of the macro-location (purchasing power index) change adversely as a result of developments in the next few years, the fair value of our entire real estate portfolio would also decrease.

Changes in the value of our investment properties are recorded as appreciation or impairments in the income statement and therefore have a direct impact on the earnings situation of our company.

Financial risks

The DAIG Group companies are financed by third-party and shareholder loans, taking into account current law and the present interpretation of the law on deductibility of interest by the applicable tax authorities. According to the current draft for a tax reform in 2008, the legislative framework may change and the overall tax burden for the DAIG Group companies may increase.

In its financing activities for its operational business, Deutsche Annington is exposed to risks arising from changes in interest rates. Deutsche Annington operates a systematic finance management system to limit these risks.

A description of the financial instruments used can be found in the Notes to the consolidated financial statements, Note 33.

Other risks

On February 22, 2006, the Federal Court of Justice made a landmark ruling on the subject of contracting (heat supplies) in a Viterra case. In this ruling, the Federal Court of Justice confirms that contracting is only admissible if it is provided for in the tenancy agreement. Therefore, together with the German Tenants' Association, Deutsche Annington has developed a procedure to ensure that part of the heat costs charged under heat contracting is refunded to the tenants. This applies only to former Viterra tenants in the Ruhr area whose tenancy agreement started before January 1, 1999 and whose heat costs were billed in accordance with Section 7(4) HKVO (Heating Cost Ordinance) in the period between 2001 and 2004.

The legal dispute with Deutsche Post AG about eight logistics centres, which Deutsche Annington took over as part of the Viterra acquisition, was settled on December 21, 2006.

Other legal disputes beyond those shown in the balance sheet which might have a substantial negative impact on the economic situation of Deutsche Annington are neither pending nor, to our knowledge, has such a case been threatened. No major risks for Deutsche Annington can currently be identified in the information technology and human resources sectors.

Outlook

Trend towards greater professionalism in the real estate industry will continue

HSH Nordbank estimates that about 1.5 million apartments will change hands in the next five years as part of portfolio transactions. These sales prospects are likely to attract growing interest from privately held housing companies as well as investors who see good opportunities for growth in the German residential real estate market given the current attractive prices and the low home ownership rate. In contrast to the past, large portfolios are currently being sold at a premium rather than at a discount and portfolio prices have risen sharply since 2004. Deutsche Annington will stick to its policy of concentrating on the acquisition of portfolios which fit in with its yield strategy.

In our opinion, the increasing competition among the new privately owned residential real estate companies will lead to greater professionalism in the residential real estate industry. Housing companies will be increasingly run according to the same commercial principles as other private-sector companies. At the same time, an increasingly critical public is keeping an eye on this development and lobbying politicians only to sell housing companies under certain restrictions. Deutsche Annington has successfully shown in the past that it takes such restrictions seriously and deals with the tenants in a responsible manner.

Now that our integration project has been completed, we see ourselves as one of the leading privately held housing companies with regard to our structure and our processes. Thanks to its efficient organisation, the Deutsche Annington Real Estate Group is well placed to make further acquisitions.

Residential real estate management will remain our core business

Deutsche Annington places a clear emphasis on keeping housing stocks. We remain selective when it comes to selling residential units. That means in every single case we check whether it makes sense to sell the property. For us the top priority is to increase our earnings by taking appropriate action in the core business, real estate management. Here, we mainly concentrate on three areas: Cutting vacancy rates, raising rents and reducing costs.

Many factors promoting the trend towards home ownership

In the Residential Sales division, Deutsche Annington shifted the accent sharply in 2006 and reduced the sales programme as our yield expectations are currently mainly being fulfilled in the Real Estate Management division. As long as the main parameters governing the market do not change (particularly rents, purchase prices for used properties and interest rates), we are also planning to keep the 2007 sales programme below the level of 2006. Thanks to our many years of experience in selling units to tenants and our experienced sales team, we can, however, step up sales again at any time.

Generally, we see good chances in the future for us to meet our yield expectations in the Residential Sales division as we see further good market opportunities in the long term for the sale of residential units to tenants in Germany. In our opinion, the steady liberalisation of the market for rented accommodation will, in the long term, make home ownership more attractive. The demographic trend will also boost demand for small apartments. The number of households will also increase. And people are becoming more aware that they need to make some private provision for retirement. Between 1993 and 2006, the percentage of home owners rose from 39% to about 43%; here Germany seems to be gradually coming up to the European average for home ownership.

Good economic prospects provide an important stimulus

The forecasts of economic experts for 2007 (including the Council of Economic Experts' report on the overall development of the economy) are largely positive. Despite the increase in VAT, they are expecting GDP to grow by 1.8% this year. The forecasts of the labour market experts are also positive, according to the Council of Economic Experts, and are backed up by the first surveys in industry (see ifo business climate index for January 2007).

Potential for raising rents rather limited

In 2007, we are again expecting that there will be no uniform pattern of development in the rents of the Deutsche Annington residential real estate portfolio. Thanks to careful management, we have succeeded in steadily bringing the rents up to market prices in the last few years. Thanks to our centralised rent management, we keep an eye on developments in the local markets and raise rents where we can. As a responsible landlord, we always keep strictly to the law. We are expecting rents to rise moderately in 2007 but the amount by which they can be raised will differ from region to region. Whilst we see chances for higher rents in growth regions like Hamburg, Frankfurt am Main and Munich, we believe that rents in the Ruhr area will stagnate or rise only slightly.

Introduction of REITs excluding the residential real estate industry regrettable

In January 2005, the German government launched an initiative to introduce Real Estate Investment Trusts (REITs) in Germany. REITs are to be permitted by law in Germany in the course of 2007 but, according to the latest draft bill, the residential real estate industry is to be expressly excluded for political reasons. An amendment to this law is still being discussed and is backed by Deutsche Annington. In our opinion, including the residential real estate industry would create important momentum for the still very small segment of German real estate shares.

Our goal for 2007 is growth

Through the acquisition of the Viterra Group, we managed to considerably increase our share of the private-sector housing market in Germany. In 2007, we are continuing to examine the possibilities of buying attractive housing portfolios. The decisive criterion is always whether the housing stocks on offer fit in with our strategy. Our aim is to enlarge our housing portfolio in the medium term. Deutsche Annington has many years of experience in the purchase and integration of large housing portfolios as well as the resale of individual units. This strength will stand us in good stead in the competitive market place.

Company looks to the future with optimism

The completion of the comprehensive integration process in 2006 was an important step, setting the future course for our company and greatly enhancing our efficiency. Our prime aim is to steadily expand the portfolio. This is also our top priority for 2007.

As we have decided not to sell residential units en bloc and want to get a higher return on property sales, we expect the number of residential units sold in 2007 not to exceed the figure for 2006. We have set out to increase EBITDA in 2007. In the medium term, we want to achieve further improvements in EBITDA. The development of our key performance indicators depends on the achievement of our internal targets for growing rental income and reducing vacancies as well as on the implementation of our acquisition strategy.

Consolidated Financial Statements

Total assets
increase slightly to € 10.9 billion

Total equity
rises to € 1.7 billion

Liabilities
reduced by € 541.4 million

Cash and cash equivalents
rise to € 706.4 million

Consolidated Income Statement

Jan. 1 to Dec. 31

€ million	Notes	2006	2005 restated*
Continuing operations			
Gross rental income		871.1	666.0
Other income from property management		27.7	15.7
Income from property management	6	**898.8**	**681.7**
Income from sale of trading properties		409.8	554.0
Carrying value of trading properties sold		–286.3	–406.6
Income from disposal of investment properties		44.8	206.4
Carrying value of investment properties sold		–37.0	–170.4
Profit on disposal of properties	7	**131.3**	**183.4**
Net valuation gains on investment property	8	**360.7**	**26.1**
Impairment losses on trading properties	9	–2.8	0.0
Cost of materials	10	–421.4	–437.9
Personnel expenses	11	–128.2	–110.0
Depreciation and amortisation	12	–4.0	–3.9
Other operating income	13	75.9	130.8
Other operating expenses	14	–150.4	–163.5
Financial income	15	25.0	17.9
Financial expenses	16	–356.2	–266.3
Profit before tax		**428.7**	**58.3**
Income tax	17	–197.6	96.2
Profit from continuing operations		**231.1**	**154.5**
Discontinued operation			
Profit (loss) from discontinued operation (net of income tax)	31	**–24.0**	**16.1**
Profit for the period		**207.1**	**170.6**
Attributable to:			
Equity holders of DAIG		207.1	170.3
Minority interests		0.0	0.3

* See change in accounting policy – note (5d); and discontinued operation – note (31)

Consolidated Balance Sheet

€ million	Notes	Dec. 31, 2006	Dec. 31, 2005 restated*
Assets			
Intangible assets	18	14.5	15.1
Property, plant and equipment	19	19.1	7.9
Investment properties	20	6,908.6	6,561.9
Financial assets	21	42.7	102.5
Other assets	22	21.9	18.8
Deferred tax assets	17	53.1	50.9
Total non-current assets		**7,059.9**	**6,757.1**
Inventories	23	2,630.7	2,948.3
Trade and other receivables	24	258.3	492.5
Financial assets	21	1.7	0.0
Other assets	22	28.5	68.6
Income tax receivables		69.7	65.4
Cash and cash equivalents	25	706.4	484.7
Assets classified as held for sale	31	177.0	–
Total current assets		**3,872.3**	**4,059.5**
Total assets		**10,932.2**	**10,816.6**
Equity and liabilities			
Subscribed capital		0.1	0.1
Capital reserves		682.2	202.7
Retained earnings		997.7	784.4
Other reserves		0.0	27.7
Total equity attributable to equity holders of DAIG		**1,680.0**	**1,014.9**
Minority interests		8.7	16.8
Total equity	26	**1,688.7**	**1,031.7**
Provisions	27	376.7	375.9
Trade and other payables	28	0.4	1.3
Financial liabilities	29	6,755.1	7,880.2
Other liabilities	30	3.9	5.9
Deferred tax liabilities	17	622.8	444.0
Total non-current liabilities		**7,758.9**	**8,707.3**
Provisions	27	304.8	389.8
Trade and other payables	28	32.0	44.2
Financial liabilities	29	501.5	157.6
Income tax liabilities		10.0	9.6
Other liabilities	30	462.0	476.4
Liabilities relating to assets classified as held for sale	31	174.3	–
Total current liabilities		**1,484.6**	**1,077.6**
Total liabilities		**9,243.5**	**9,784.9**
Total equity and liabilities		**10,932.2**	**10,816.6**

* See change in accounting policy – note (5d)

Consolidated Cash Flow Statement

Jan. 1 to Dec. 31

€ million	Notes	2006	2005 restated*
Profit for the period		207.1	170.6
Depreciation and amortisation	12	4.0	3.9
Interest expenses/income		343.2	253.8
Results from disposals of non-current assets		–32.8	–49.1
Loss on sale of discontinued operation, net of income tax	31	24.5	–
Net valuation gains on investment property	20	–373.7	–26.1
Other earnings not affecting net income	13	–	–109.5
Changes in inventories		187.0	470.8
Changes in receivables and other assets		159.1	–200.0
Changes in provisions		–47.9	128.5
Changes in liabilities		151.8	44.1
Changes in deferred taxes		183.2	–104.7
Income tax paid		–15.6	–32.8
Cash flow from operating activities		**789.9**	**549.5**
Proceeds from disposals of intangible assets, property, plant and equipment, and investment properties		48.4	247.2
Disposal of discontinued operation (net of cash disposed of)	31	60.0	–
Proceeds received from disposals of financial investments	13	25.5	0.2
Acquisition of intangible assets, property, plant and equipment, and investment properties	35	–133.3	–10.4
Acquisition of subsidiaries (net of cash acquired)		–0.1	–3,543.3
Interest received		20.4	10.0
Cash flow from/used in investing activities		**20.9**	**–3,296.3**
Cash proceeds from issuing loans and notes	29	5,942.8	5,904.9
Cash repayments of financial liabilities	29	–6,265.0	–2,344.1
Transaction costs		–76.6	–106.2
Capital contributions from the shareholder	26	214.6	1.0
Other financing transactions		–	–4.2
Interest paid		–404.9	–286.2
Cash flow used in/from financing activities		**–589.1**	**3,165.2**
Net changes in cash and cash equivalents		**221.7**	**418.4**
Cash and cash equivalents at beginning of year	25	484.7	66.3
Cash and cash equivalents at year-end	25	**706.4**	**484.7**

* See change in accounting policy – note (5d)

Consolidated Statement of Changes in Equity

€ million	Subscribed capital	Capital reserves	Retained earnings	Other reserves containing cumulative changes in equity not affecting net income: Total	From cash flow hedges	From currency translation	Equity before minority interests	Minority interests in equity	Total equity
As of Jan. 1, 2005	**0.1**	**201.7**	**225.4**	**–14.9**	**–14.9**	**0.0**	**412.3**	**19.2**	**431.5**
Impact of change in accounting policy*			386.7				386.7	0.3	387.0
As of Jan. 1, 2005, restated	**0.1**	**201.7**	**612.1**	**–14.9**	**–14.9**	**0.0**	**799.0**	**19.5**	**818.5**
Profit for the period			170.3				170.3	0.3	170.6
Changes in equity not affecting net income				42.6	41.9	0.7	42.6		42.6
Total recognised income and expense			170.3	42.6	41.9	0.7	212.9	0.3	213.2
Capital increase		1.0					1.0		1.0
Acquisition/disposal of minority interests			2.0				2.0	–3.0	–1.0
As of Dec. 31, 2005, restated	**0.1**	**202.7**	**784.4**	**27.7**	**27.0**	**0.7**	**1,014.9**	**16.8**	**1,031.7**
Profit for the period			207.1				207.1	0.0	207.1
Changes in equity not affecting net income				–27.7	–27.0	–0.7	–27.7		–27.7
Total recognised income and expense			207.1	–27.7	–27.0	–0.7	179.4	0.0	179.4
Capital increase		479.5					479.5		479.5
Acquisition/disposal of minority interests			6.2				6.2	–8.1	–1.9
As of Dec. 31, 2006	**0.1**	**682.2**	**997.7**	**0.0**	**0.0**	**0.0**	**1,680.0**	**8.7**	**1,688.7**

For further information on the statement of changes in consolidated equity, see note (26) Equity
* See change in accounting policy – note (5d)

Notes
to the Consolidated Financial Statements

Accounting Policies

1 Basis of Presentation

The Deutsche Annington Real Estate Group (DAIG) has positioned itself as a focused real estate company and concentrates on its core business, residential real estate. The company's focus is on the profitable letting, buying and selling of residential units. The parent company of the Deutsche Annington Real Estate Group is Deutsche Annington S.A., Luxembourg, the ultimate controlling parent is Monterey Capital I S.à.r.l., Luxembourg (Monterey). Deutsche Annington Immobilien GmbH (DAIG mbH) is incorporated and domiciled in Germany; its registered office is located in Düsseldorf. The head office (principal place of business) is located at Philippstrasse 3, Bochum.

DAIG mbH has made use of the option under Section 315a, para. 3 of the German Commercial Code (HGB) and is thus not obliged to prepare consolidated financial statements in accordance with German commercial law.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted in the EU. Allowance has also been made for the supplementary provisions in accordance with Section 315a, para. 1 of the German Commercial Code (HGB).

The consolidated financial statements have been prepared on the historical cost basis except for investment properties, derivative financial instruments, available-for-sale financial assets and financial liabilities arising from binding share purchase offers to minority shareholders, which are measured at fair value. The income statement has been prepared using the nature of expense method and follows the recommendations of the European Public Real Estate Association (EPRA).

These consolidated financial statements are presented in euro, which is the Group's functional currency. Unless stated otherwise, all figures are shown in million euros (€ million).

On March 26, 2007, the Management approved the consolidated financial statements of DAIG mbH for submission to the shareholders' meeting. It is the responsibility of the shareholders' meeting to examine the consolidated financial statements and declare whether it approves them.

2 Consolidation Principles

Entities that are under the control of DAIG mbH are included in the consolidated financial statements as subsidiaries. Control is exercised when DAIG mbH is able to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Any potential voting rights are taken into account when assessing control. Subsidiaries are included in the consolidated financial statements from the date on which DAIG mbH obtains control until the day control ceases.

Business combinations are accounted for using the purchase method. The identifiable assets, liabilities and contingent liabilities of the acquiree are recognised in the consolidated financial statements at fair value, except for non-current assets (or disposal groups) classified as held for sale, which are recognised at fair value less costs to sell. Any excess of the cost of a business combination over DAIG's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities is recognised as goodwill.

If DAIG's interest in the net fair value of the identifiable assets and liabilities exceeds the cost of the business combination, the values of the assets, liabilities and contingent liabilities as well as the costs of acquisition are reassessed and any remaining excess is recognised as income in the income statement.

The shares in the net assets of subsidiaries that are not attributable to DAIG are shown as a separate component of equity under minority interests.

Further share purchases after control has been obtained, i.e., the acquisition of minority interests, are accounted for as equity transactions. Any premiums or discounts on those purchases are recognised directly in equity.

For the term during which DAIG has made a binding offer to minority shareholders to purchase their shares in subsidiaries, such minority interests are recognised as financial liabilities and not as a separate component of equity. The financial liabilities are recognised at fair value, which corresponds to the price offered.

Entities over which DAIG mbH has significant influence but not control are accounted for as associates. This is generally the case when 20% to 50% of the voting rights are held. Investments in associates are of minor significance from a Group perspective and therefore are accounted for at cost.

A special purpose entity (SPE) is consolidated, if based on an evaluation of the substance of its relationship with DAIG mbH and the SPE's risks and rewards, DAIG mbH concludes that it controls the SPE.

The effects of the business transactions between the entities included in the DAIG consolidated financial statements are eliminated.The financial statements of DAIG mbH and all consolidated entities are prepared according to uniform accounting policies.

3 Scope of Consolidation

In addition to DAIG mbH, 102 domestic (2005: 83) and 0 foreign (2005: 3) companies have been included in the consolidated financial statements of DAIG as at and for the year ended December 31, 2006. The net assets, financial position and results of the operations of the Group do not include 3 subsidiaries (2005: 7), which are of minor significance from a Group perspective. The list of DAIG shareholdings is appended to these Notes to the consolidated financial statements.

In 2006, 53 companies (2005: 75) have been included in the consolidated financial statements for the first time as a result of their acquisition or new establishment mainly due to corporate restructuring as a consequence of the Group's refinancing measures. The disposals in 2006 were the result of 17 sales (2005: 0), 16 mergers (2005: 5) and 4 intra-Group legal reorganisations (Anwachsung) (2005: 2).

Although in 2005 DAIG mbH did not hold the majority of voting rights, MIRA was fully consolidated as a special purpose entity (SPE) in line with IAS 27 in conjunction with SIC-12 as DAIG mbH bore the main rewards and risks from MIRA and its business activities. Due to extensive restructuring and reorganising within the Group, DAIG mbH now holds a controlling interest in MIRA and MIRA is fully consolidated in line with the provisions of IAS 27.

As at December 31, 2006, DAIG mbH does not consolidate any SPEs.

4 Currency Translation

In the separate financial statements of DAIG mbH and the subsidiaries included in the consolidated financial statements, foreign currency transactions are translated into the functional currency at the exchange rate on the date of the transaction. Monetary assets and liabilities in foreign currencies are translated at the exchange rate prevailing on the balance-sheet date. Non-monetary items that are measured in terms of historical cost are recorded on the balance-sheet date at the exchange rate on the date when they were first recognised. Non-monetary items that are measured at fair value are translated using the exchange rate on the date when the fair value was determined. Any resulting translation gains and losses are recorded in the income statement.

Financial statements of foreign subsidiaries are prepared on the basis of the currency of the primary economic environment in which the company operates (functional currency). In principle the respective national currency is taken to be the functional currency. The financial statements of consolidated companies which are denominated in foreign currencies are translated into the Group's functional currency, the euro, as follows:

The balance sheet is translated at the closing rate on the balance-sheet date and the income statement at a rate that approximates the exchange rate at the dates of the transactions (average rate of the reporting period). Differences resulting from currency translation of assets and liabilities between the prior year-end and the current year-end as well as differences between balance sheet and income statement translation do not affect income and are included within equity until disposal of the subsidiary.

As part of the sale of the Development division, all foreign subsidiaries have been disposed of.

5 Significant Accounting Policies

(a) Recognition of income and expenses

Income from property management includes income from the letting of investment properties and trading properties which is recognised, net of discounts, sales incentives, customer bonuses and rebates granted, on a straight-line basis over the duration of the contracts when the remuneration is contractually fixed or can be reliably determined and collection of the related receivable is probable.

Furthermore, the income from property management includes payments for ancillary costs made by DAIG in the current and previous years which are billed to tenants in the current year when the cost and the amount of revenue can be measured reliably. Ancillary costs which have yet to be billed are shown under inventories. Advance payments made by tenants which cannot be offset against the ancillary costs are shown under other liabilities.

Income from property sales is recognised as soon as the material risks and rewards of ownership have been transferred to the buyer and DAIG has no substantive further obligations. If DAIG only retains insignificant risks of ownership, the proceeds are recognised at the time of sale and a provision is recognised for the probable risk.

Income from construction contracts is recognised under the percentage-of-completion method according to the progress of work completed. The progress of work is determined using the cost-to-cost method. If the percentage-of-completion method is not appropriate, proceeds are recognised using the completed-contract method, i.e. after completion and final acceptance of the project. As part of the sale of the Development division, all subsidiaries which engaged in construction contracts have been disposed of.

Expenses are recognised when they arise or at the time they are incurred. Interest is recognised as income or expense using the effective interest method.

(b) Intangible assets

Intangible assets are carried at cost less any accumulated amortisation and impairment losses. All intangible assets of DAIG have definite useful lives and are amortised on a straight-line basis over their estimated useful lives. Software and licences are amortised on the basis of a useful life of three years. Customer bases are amortised on a straight-line basis over 10 years.

(c) Property, plant and equipment

Items of property, plant and equipment are carried at cost less accumulated depreciation and impairment losses and are depreciated over their respective estimated useful lives on a straight-line basis.

Subsequent costs of replacing part of an item of property, plant and equipment are capitalised provided it is probable that future economic benefits associated with the item will flow to DAIG and the cost can be measured reliably.

Equipment, fixtures, furniture and office equipment are depreciated over periods of between 3 and 13 years.

(d) Investment properties

When DAIG acquires real estate properties, whether through a business combination or separately, the intended use determines whether those properties are classified as investment properties, trading properties or owner-occupied properties.

Investment properties are properties that are held for the purpose of earning rental income or for capital appreciation or both and are not owner-occupied or held for sale in the ordinary course of business. Investment properties include undeveloped land, land and land rights including buildings and land with inheritable rights of third parties. Properties which are capitalised under a finance lease in accordance with IAS 17 “Leases” and are covered by the definition of investment properties are also classified as investment properties. Property interests held under operating leases where DAIG acts as a lessee are not classified and accounted for as investment properties.

Investment properties are measured initially at cost. Related transaction costs, such as fees for legal services or property transfer taxes, are included in the initial measurement. Property held under a finance lease is recognised at the lower of the fair value of the property and the present value of the minimum lease payments upon initial recognition.

After initial recognition, investment properties are measured at fair value with any change therein recognised in profit or loss. In its financial statements for periods beginning before January 1, 2006, DAIG applied the cost model, i.e. investment properties were carried at their cost less any accumulated depreciation and any accumulated impairment losses. This voluntary change in accounting policy was made to provide reliable and more relevant information about the entity’s financial position, financial performance or cash flows. Moreover, the new policy is consistent with industry practice, making DAIG’s consolidated financial statements more comparable.

In accordance with IAS 8 “Accounting Policies, Changes in Accounting Estimates and Errors”, the change has been applied retrospectively and comparatives have been restated.

The change in accounting policy had the following impact on the comparative figures:

Consolidated income statement for the year ended December 31, 2005

€ million	
Decrease in gross rental income	–1.6
Increase in carrying value of trading properties sold	–31.2
Increase in carrying value of investment properties sold	–5.6
Increase in net valuation gains on investment property	26.1
Decrease in depreciation	60.3
Decrease in income tax	–18.2
Increase in profit from continuing operations	**29.8**

Consolidated balance sheet as at December 31, 2005

€ million	
Cumulative increase in investment properties	440.6
Cumulative decrease in deferred tax assets	–12.1
Cumulative increase in inventories	45.5
Cumulative decrease in other liabilities	46.2
Cumulative increase in deferred tax liabilities	–103.4
Cumulative increase in total equity	**416.8**
thereof: Cumulative increase in retained earnings	416.5
thereof: Cumulative increase in minority interests	0.3

The adjustment to retained earnings as at January 1, 2005 was an increase of € 386.7 million, minority interests increased by € 0.3 million.

Due to major system change-overs, which were necessary because of the change to fair value measurement, it is not possible to identify the amount of the adjustment for the current period.

The fair value of investment properties is calculated using internationally recognised measurement methods. One such method is the income approach, which is based on actual or market rents and a risk-adjusted capitalised interest rate. In addition, fair values are also determined by comparing market prices for comparable properties (sales comparison method). Both of these approaches to determine the fair values of investment properties are based on current market data. For a more detailed description of the determination of the fair values of investment properties, see note (20) Investment properties.

In line with the real estate trading strategy of DAIG, investment properties which are to be sold within the normal six-year business cycle and which are being prepared for sale, e.g. condominium declaration obtained after initial classification, are transferred to inventories.

Should these properties classified as trading properties not have been sold within the six-year business cycle as intended, they are re-transferred to the investment properties category in accordance with the provisions of IAS 8 "Changes in Accounting Estimates".

Investment properties are transferred to property, plant and equipment when there is a change in use evidenced by the commencement of owner-occupation. The properties' deemed cost for subsequent accounting corresponds to the fair value at the date of reclassification.

(e) Leases

Leases are either classified as finance leases or operating leases. Leases where substantially all risks and rewards incidental to ownership are transferred to the lessee are accounted for as finance leases.

DAIG as a lessee under a finance lease

The leased asset and a corresponding liability are recognised at an amount equal to the lower of the fair value of the asset and the present value of the minimum lease payments. Subsequently, the asset is accounted for in accordance with the accounting policy applicable to that asset. The minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability.

All leases where not substantially all risks and rewards incidental to ownership are transferred are accounted for as operating leases.

DAIG as a lessor under an operating lease

Lease payments are recognised in income on a straight-line basis over the lease term. The assets subject to operating leases are presented in the balance sheet according to their nature.

DAIG as a lessee under an operating lease

Lease payments are recognised as an expense on a straight-line basis over the lease term.

(f) Impairment of intangible assets and property, plant and equipment

In accordance with IAS 36 "Impairment of Assets", intangible assets as well as property, plant and equipment are tested for impairment whenever there is an indication for an impairment. An impairment loss is recognised when an asset's recoverable amount is less than its carrying amount. If the recoverable amount cannot be determined for the individual asset, the impairment test is conducted on the cash-generating unit to which the asset belongs. Impairment losses are recorded as expenses in the income statement.

An impairment loss recognised for prior periods is reversed if there has been a change in the estimates used to determine the asset's (or the cash-generating unit's) recoverable amount since the last impairment loss was recognised. The carrying amount of the asset (or the cash-generating unit) is increased to the newly estimated recoverable amount. The carrying amount is limited to the amount that would have been determined if no impairment loss had been recorded in prior years for the asset (or the cash-generating unit).

(g) Non-derivative financial assets

Financial assets are recognised when DAIG becomes a party to the contractual provisions of the asset. A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or the financial asset is transferred and DAIG neither retains control nor retains substantially all the risks and rewards of ownership of the financial asset.

Financial investments

Shares in associates not accounted for using the equity method and other investments are measured at amortised cost as there is no price quoted on an active market and the fair value cannot be determined reliably.

Available-for-sale financial assets

Available-for-sale financial assets are initially measured at fair value and any changes therein – other than impairment losses – are recognised in equity. The fair value of available-for-sale financial assets is based on quoted market prices at the reporting date. When the available-for-sale financial asset is derecognised, the cumulative gain or loss recognised in equity is transferred to profit or loss. Regular way purchases or sales are accounted for at the date of the economic transfer of the asset to the purchaser.

Loans and receivables

Loans and receivables are stated at amortised cost using the effective interest method less impairment losses. Allowance is made for all discernible risks by appropriate deductions. An appropriate valuation allowance is made when it is estimated that certain receivables will be uncollectible.

Trade receivables

Trade receivables are measured at amortised cost using the effective interest method less impairment losses. An impairment loss is recognised when there is objective evidence that DAIG will not be able to collect all amounts due according to the original terms of the receivables.

Customer-specific construction contracts are, when certain conditions are met, recognised under the percentage-of-completion method according to the progress of work completed. Construction contracts where the balance shows an amount owed by the customer are shown under trade receivables. Any negative balance on a construction contract is recorded under other liabilities as advance payments made on construction contracts.

The stage of completion is determined in accordance with the expenses incurred (cost-to-cost method). Anticipated losses from orders are covered by value adjustments or provisions; they are determined allowing for all discernible risks. The contractual income is shown as income from contracts in line with the percentage of completion under income from sale of trading properties. As part of the sale of the Development division, all subsidiaries which engaged in construction contracts have been disposed of.

(h) Inventories

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

In line with the real estate trading strategy of DAIG, residential properties which are to be sold within the normal six-year business cycle and for which a condominium declaration has been obtained are shown as trading properties under inventories. If these properties have not been sold within the six-year business cycle as intended, they are transferred to the investment properties category in accordance with IAS 8 “Changes in Accounting Estimates”. Any difference between the fair value of the property at that date and its previous carrying amount is recognised in profit or loss.

(i) Borrowing costs

Borrowing costs are recognised as expense when incurred.

(j) Cash and cash equivalents

Cash and cash equivalents include cash on hand, cheques and deposits on bank accounts with an original term of up to three months.

(k) Deferred taxes

Deferred tax is recognised using the liability method, providing for all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. A deferred tax asset is recognised to the extent that future taxable profits will be available against which the temporary difference can be utilised. The carrying amount of a deferred tax asset is reviewed at each balance-sheet date. If necessary, the carrying amount of the deferred tax asset is reduced to the extent that it is no longer probable that sufficient taxable profit will be available.

Deferred taxes are measured at tax rates that have been enacted or substantially enacted and that are expected to apply to the period when the tax asset is realised or the liability is settled. A tax rate of 40% is used to calculate domestic deferred taxes. In addition to corporate income tax and the solidarity surcharge together totalling 26.4%, the average trade earnings tax rate for DAIG was taken into consideration.

Tax assets and liabilities are offset against each other only if DAIG has a legally enforceable right to set off the recognised amounts, when the same tax authority is involved and when the realisation period is the same. In accordance with the regulations of IAS 12 “Income Taxes”, deferred tax assets and liabilities are not discounted.

(l) Provisions

Provisions for pensions and similar obligations

The values of the pension obligations and the expenses necessary to cover these obligations are determined using the projected unit credit method according to IAS 19 “Employee Benefits” whereby current pensions and vested pension rights at the balance-sheet date as well as future increases in salaries and pensions are included in the valuation. An actuarial valuation is performed at every balance-sheet date.

The amount shown in the balance sheet is the present value of the defined benefit obligation after elimination of unrecognised actuarial gains and losses and past service cost and after offsetting against the fair value of the plan assets.

Actuarial gains and losses arising are recognised using the corridor method. They are only recorded to income or expense when the balance of the accumulated unrecognised actuarial gains and losses exceeds the corridor of 10% of the greater of defined benefit obligation (DBO) and the fair value of plan assets. The excess is recognised in future periods over the expected average remaining working lives of the participating employees.

Service cost is shown in personnel expenses. The interest share of the addition to provisions is recorded in the financial result.

Reinsurance policies that qualify as plan assets have been taken out to cover the pension obligations towards particular persons. Where the value of those reinsurance policies exceeds the related pension obligations, the excess is recognised as an asset and shown under other assets.

Other provisions

Other provisions are established when there is a present obligation, either legal or constructive, as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Non-current provisions are discounted if the resulting effect is material. The carrying amount of discounted provisions increases in each period to reflect the passage of time and the unwinding of the discount is recognised within interest expense. The discount rate is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Provisions for environmental liabilities are recognised when it is probable that an outflow of resources will be required to settle the obligation and the amount of the liability can be reliably estimated.

Provisions for restructuring are recognised when the Group has set up a detailed formal plan for restructuring and has announced the main features of the plan to those affected.

Provisions for onerous contracts are recognised when the expected benefits from a contract are lower than the unavoidable cost of meeting the obligations under the contract. The provision is stated at the present value of the lower of the net cost of continuing with the contract and the cost of terminating the contract, i.e., a possible indemnity or fine for breach or non-fulfilment of contract.

Provisions for warranties are recognised when the related goods or services are sold. The amount recognised is based on historical warranty data.

(m) Financial liabilities

Financial liabilities are recognised when DAIG becomes a party to the contractual provisions of the liability. Financial liabilities are derecognised when DAIG's obligations specified in the contract expire or are discharged or cancelled.

With the exception of derivative financial instruments and financial liabilities arising from binding share purchase offers to minority shareholders, financial liabilities are shown at amortised cost using the effective interest method.

Loans bearing no interest or interest below market rates in return for occupancy rights at rents below the prevailing market rates are recorded at present value.

Debt discounts and debt issue costs are directly allocated to financial liabilities. Liabilities from finance leases are recognised at the fair value of the leased object or the lower present value of the minimum lease payments.

Financial liabilities arising from binding share purchase offers to minority shareholders are measured at fair value. Fair value is determined using mathematical financial models, e.g. the income approach.

(n) Derivative financial instruments and hedge accounting

All derivative instruments, irrespective of the purpose or the intended use, are accounted for at their fair values as assets or liabilities in the balance sheet. The fair values of the derivative financial instruments are calculated using standard market valuation methods for such instruments on the basis of the market data available on the valuation date. The fair values of instruments which are used to hedge interest rate risks are determined by discounting future cash flows using market interest rates over the remaining term of the instruments.

With derivatives that are not designated as a hedging instrument, changes in the fair value are recorded in profit or loss.

With derivatives designated as hedging instruments, the recording of changes in the fair value depends on the type of hedge:

With a fair value hedge, the changes in the fair value of the derivative financial instruments and of the underlying hedged items attributable to the hedged risk are recognised in the income statement.

With a cash flow hedge, the changes in fair value of the derivative hedging instrument are recognised in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, the change in fair value is immediately recognised in profit or loss.

Amounts accumulated in equity are recycled in the income statement at the same time the underlying hedged item affects net income.

(o) Government grants

The companies of DAIG receive grants from public authorities in the form of construction subsidies, expenses subsidies, expenses loans and low-interest loans.

Government grants are regularly recorded as income over the periods necessary to match them with the related costs which they are intended to compensate.

Construction cost subsidies are, where they relate to construction measures, deducted from the construction costs and amortised as income over the useful life of the relevant assets. Construction cost subsidies relating to maintenance work which cannot be capitalised are immediately recognised in income.

Expenses subsidies granted in the form of rent, interest and other expenses subsidies are recorded as income and shown within other income from property management.

The low-interest loans are grants from public authorities, which are recorded at net present value. The difference between nominal value and net present value is recognised in income over the maturity term of the corresponding loans.

(p) **Contingent liabilities**

A contingent liability is a possible obligation toward third parties that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity or a present obligation that arises from past events for which an outflow of resources is not probable or the amount of which cannot be estimated with sufficient reliability. According to IAS 37 “Provisions, Contingent Liabilities and Contingent Assets”, contingent liabilities are not recognised.

(q) **Assets and disposal groups classified as held for sale and discontinued operations**

If the carrying amount of a non-current asset or a disposal group is expected to be recovered primarily through a sale transaction rather than through continuing use, the non-current asset or disposal group is classified as held for sale. The non-current asset or the disposal group must be available for immediate sale and the sale must be highly probable.

Immediately before classification as held for sale, the carrying amounts of the non-current assets (and all assets and liabilities of a disposal group) are measured in accordance with applicable IFRSs. Upon initial classification as held for sale, non-current assets and disposal groups are recognised at the lower of carrying amount and fair value less costs to sell.

Non-current assets that are classified as held for sale or are part of a disposal group held for sale are not depreciated; however, interest and other expenses attributable to the liabilities of a disposal group classified as held for sale are recognised.

A discontinued operation is a component of an entity which represents a separate major line of business or geographical area of operations that has been disposed of or is held for sale. A subsidiary acquired exclusively with a view to resale is also classified as a discontinued operation. Classification as a discontinued operation occurs upon disposal, e.g. when the operation is sold or abandoned, or when the operation meets the criteria to be classified as held for sale.

The comparative income statement is restated as if the operation had been discontinued from the start of the comparative period.

(r) **Estimates, assumptions and management judgment**

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and contingent liabilities at the balance-sheet date as well as reported amounts of revenues and expenditures during the reporting period. These estimates and assumptions mainly relate to the uniform definition of useful lives, the assumptions made on the value of land and buildings, the recognition and measurement of provisions as well as the realisation of future tax benefits. The actual amounts may differ from the estimates as the business environment may develop differently than assumed. In this case, the assumptions and, where necessary the carrying amounts of the assets or liabilities affected are adjusted accordingly.

Assumptions and estimates are reviewed on an ongoing basis and are based on historical experience and other factors, including expectations regarding future events which appear reasonable under the given circumstances.

The estimates and assumptions which may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities mainly relate to the determination of the fair value of investment properties.

The best evidence of fair value of investment properties is current prices in an active market for similar properties. If, however, such information is not available, DAIG uses valuation techniques such as the income capitalisation method. In determining the fair value by using the income capitalisation method, DAIG takes, among others, the following assumptions into consideration: the annual net rent, future anticipated rental income, void periods and administrative and maintenance expenses. The interest rate to determine the capitalised value is derived by using a rating system. DAIG regularly compares its valuations to actual market data as well as to actual transactions.

Furthermore, in preparing consolidated financial statements, DAIG needs to estimate its income tax obligations. This involves estimating the actual tax exposure as well as assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. Judgments are required in determining the consolidated provision for income taxes. During the ordinary course of business, there are transactions and calculations for which the ultimate tax determination is uncertain.

Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each balance-sheet date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Judgment is required in determining the amounts of deferred tax assets and whether those assets can be utilised.

At the time when the consolidated financial statements were prepared, there was no reason to assume that the assumptions and best possible estimates made on the basis of the circumstances at the balance-sheet date would change materially.

Other judgments that DAIG's management has made in the process of applying the entity's accounting policies and that may have a significant effect on the amounts recognised in the financial statements include the following:

- Upon initial recognition, the management must determine whether real estate properties are classified as investment properties, trading properties or owner-occupied properties. The classification determines the subsequent measurement of those assets.

- DAIG measures investment properties at fair value. If management had opted to use the cost model as permitted under IAS 40, the carrying values of the investment properties as well as the corresponding figures in the income statement would differ significantly.

- DAIG recognises actuarial gains and losses according to the corridor method. The application of a different option to recognise actuarial gains and losses as permitted under IAS 19 would lead to a significantly different carrying value of the recognised provision for pensions and would also have a significant effect on the income statement.

- IFRSs do not regulate the accounting treatment for further share purchases after control has been obtained, e.g. the acquisition of minority interests. In accordance with IAS 8 para. 10, management has decided to treat such purchases as equity transactions. Increases or decreases in the ownership interest in subsidiaries without a change in control as well as any premiums or discounts are recognised directly in the parent shareholders' equity.

(s) Changes in accounting policies due to new standards and interpretations

The application of numerous new standards, interpretations and amendments to existing standards became mandatory for the 2006 financial year.

The following amendment was adopted by DAIG for the 2006 financial year:

IAS 19 "Employee Benefits"

The amendment to IAS 19 introduces another recognition option for actuarial gains and losses. There are additional recognition requirements for multi-employer plans where insufficient information is available. Furthermore, new disclosure requirements were added.

DAIG continues to recognise actuarial gains and losses according to the corridor method and does not participate in multi-employer plans. Therefore, the adoption of the amendment only has an impact on the format and extent of disclosures presented for defined benefit plans.

The following standards, amendments and interpretations became effective for the 2006 financial year but are not relevant to DAIG's operations:

- IFRS 6 "Exploration for and Evaluation of Mineral Resources"
- IFRIC 4 "Determining Whether an Arrangement Contains a Lease"
- IFRIC 5 "Rights to Interests Arising from Decommissioning, Restoration and Environmental Funds"
- IFRIC 6 "Liabilities Arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment"
- Amendment to IAS 21 "The Effects of Changes in Foreign Exchange Rates" – Net Investment in a Foreign Business Operation
- Amendment to IAS 39 "Financial Instruments: Recognition and Measurement" – Cash-flow Hedge Accounting of Forecast Intra-group Transactions

- Amendment to IAS 39 "Financial Instruments: Recognition and Measurement" – Regulations on the Use of the Fair Value Option
- Amendment to IAS 39 "Financial Instruments: Recognition and Measurement" and IFRS 4 "Insurance Contracts" – Financial Guarantee Contracts
- Amendment to IFRS 1 "First-time Adoption of the International Financial Reporting Standards" and the Basis for the Conclusions on IFRS 6 "Exploration for and Evaluation of Mineral Resources"

(t) New standards and interpretations not yet adopted

Application of the following standards, interpretations and amendments to existing standards was not yet mandatory for the 2006 financial year. DAIG did not choose to apply them in advance, either. Their application will be mandatory for the financial years following the dates stated in the following table:

New Standards, Interpretations and Amendments to Existing Standards		Effective date
IFRS 7	"Financial Instruments: Disclosures"	Jan. 1, 2007
IFRS 8	"Operating Segments"	Jan. 1, 2009
IFRIC 7	"Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies"	March 1, 2006
IFRIC 8	"Scope of IFRS 2 Share-based Payment"	May 1, 2006
IFRIC 9	"Reassessment of Embedded Derivatives"	June 1, 2006
IFRIC 10	"Interim Financial Reporting and Impairment"	Nov. 1, 2006
IFRIC 11	"Group and Treasury Share Transactions"	March 1, 2007
IFRIC 12	"Service Concession Arrangements"	Jan. 1, 2008
Amendment to IAS 1 "Presentation of Financial Statements" – Capital Disclosures		Jan. 1, 2007

IFRS 7 "Financial Instruments: Disclosures" and Amendment to IAS 1 "Presentation of Financial Statements" – Capital Disclosures

These standards require extensive disclosures about the significance of financial instruments for an entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. IFRS 7 and amended IAS 1 will require additional disclosures with respect to DAIG's financial instruments.

IFRS 8 "Operating Segments"

IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of SFAS 131. The standard requires an entity to adopt the "management approach" to reporting on the financial performance of its operating segments. Operating segments are defined by the standard as components of an entity whose operating results are regularly reviewed by the entity's chief operating decision-maker to make decisions about resources to be allocated to the segment and assess its performance and for which discrete financial information is available. DAIG is currently reviewing the potential effect of the standard.

IFRIC 7 "Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies"

This interpretation addresses the application of IAS 29 when an economy first becomes hyperinflationary and in particular the accounting for deferred tax. IFRIC 7 is not expected to have any impact on the consolidated financial statements.

IFRIC 8 "Scope of IFRS 2 Share-based Payment"

IFRIC 8 addresses the accounting for share-based payment transactions in which some or all of goods or services received cannot be specifically identified. IFRIC 8 is not expected to have any impact on the consolidated financial statements.

IFRIC 9 "Reassessment of Embedded Derivatives"

This interpretation requires that a reassessment of whether an embedded derivative should be separated from the underlying host contract should be made only when there are changes to the contract. IFRIC 9 is not expected to have any impact on the consolidated financial statements.

IFRIC 10 "Interim Financial Reporting and Impairment"

IFRIC 10 prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, an investment in an equity instrument or a financial asset carried at cost. As DAIG is currently not required to prepare interim financial statements, IFRIC 10 does not have any impact on the consolidated financial statements.

IFRIC 11 "IFRS 2 Share-based Payment – Group and Treasury Share Transactions"

IFRIC 11 requires a share-based payment arrangement in which an entity receives goods or services as consideration for its own equity instruments to be accounted for as an equity-settled share-based payment transaction, regardless of how the equity instruments are obtained. The interpretation also provides guidance on whether share-based payment arrangements in which suppliers of goods or services of an entity are provided with equity instruments of the entity's parent should be accounted for as cash-settled or equity-settled in the entity's financial statements. IFRIC 11 is not expected to have any impact on the consolidated financial statements.

IFRIC 12 "Service Concession Arrangements"

Service concessions are arrangements whereby a government or public sector entity grants contracts for the supply of public services to private sector operators. IFRIC 12 specifies how service concession operators should apply existing IFRSs to account for the obligations they undertake and rights they receive under those service concession arrangements. IFRIC 12 is not expected to have any impact on the consolidated financial statements.

Notes to the Consolidated Income Statement

6 Income from property management

The income from property management breaks down as follows:

€ million	2006	2005
Rental income	670.1	425.0
Ancillary costs (charged)	201.0	241.0
Gross rental income	**871.1**	**666.0**
Other income from property management	27.7	15.7
Income from property management	**898.8**	**681.7**

7 Profit on disposal of properties

In the year under review, a book gain of € 123.5 million (2005: € 147.4 million) was recorded from the sale of trading properties.

A book gain of € 7.8 million (2005: € 36.0 million) was realised from the disposal of investment properties.

8 Net valuation gains on investment property

Investment properties are measured according to the fair value model. That means that the carrying amount of investment properties is the fair value of those properties. Any gains or losses from a change in fair value are recognised in the income statement. In the financial year, a net valuation gain of € 360.7 million (2005: € 26.1 million) was recognised.

9 Impairment losses on trading properties

Properties that are held for sale in the ordinary course of business are classified as trading properties and are shown within inventories. If the carrying amount exceeds the net realisable value, trading properties are written down to net realisable value item by item. In the financial year, for several properties impairment losses of € 2.8 million (2005: € 0.0 million) were recognised as an expense.

However, the overall fair value of trading properties has increased.

10 Cost of materials

€ million	2006	2005
Increase (-)/decrease (+) in inventories of finished goods and ancillary costs	–60.2	21.5
Cost of purchased goods and services	481.6	416.4
	421.4	**437.9**

The increase in finished goods and ancillary costs mainly relates to changes in inventories in connection with the billing of ancillary costs. The cost of purchased goods and services relates in particular to ancillary cost expenses and maintenance expenses.

11 Personnel expenses

€ million	2006	2005
Wages and salaries	108.0	94.1
Social security, pension and support contributions	20.2	15.9
	128.2	**110.0**

Personnel expenses contain costs for restructuring measures, partial retirement schemes and other severance payments totalling € 15.8 million.

In the year under review, employers' contributions to the statutory pension insurances totalling € 7.5 million (2005: € 5.3 million) were paid.

As at December 31, 2006, 1,385 people (2005: 1,889) were employed in the Deutsche Annington Real Estate Group. On an annual average, 1,481 people (2005: 1,036) were employed. The figures do not include trainees. The average figure for 2005 only contains the employees of Viterra, which was acquired in 2005, proportionately for the period in 2005 in which Viterra belonged to DAIG.

12 Depreciation and amortisation

Amortisation of intangible assets totalled € 2.5 million (2005: € 2.0 million). Of this figure, customer bases accounted for € 1.6 million (2005: € 1.6 million). Depreciation of property, plant and equipment amounted to € 1.5 million (2005: € 1.9 million).

13 Other operating income

€ million	2006	2005
Income from the reversal of provisions	27.9	7.9
Book gain from the disposal of investments	24.4	–
Income from the reversal of impairment losses	6.6	1.3
Income from compensation paid and cost reimbursements	4.0	3.3
Recognition of negative goodwill	–	109.5
Other	13.0	8.8
	75.9	**130.8**

Of the total income from the reversal of provisions, € 10.7 million results from a reversal following the settlement of arbitration proceedings concerning various guarantees given in connection with the sale of Viterra Contracting GmbH in 2003.

DAIG realised a book gain of € 24.4 million from the divestment of the financial investment in Rhein Lippe Wohnen GmbH, Duisburg. The financial investment was measured at amortised cost. The carrying amount was € 0.6 million.

In 2005, the other operating income included € 109.5 million, which was attributable to the immediate recognition of the negative goodwill from the first-time consolidation of the Viterra Group and MIRA Grundstücksgesellschaft mbH & Co. KG, Grünwald (after change of company name: MIRA Grundstücksgesellschaft mbH, Düsseldorf), as income.

14 Other operating expenses

The other operating expenses break down as follows:

€ million	2006	2005
Impairment losses on receivables	21.4	9.5
Additions to provisions	20.2	9.6
Auditors' and consultants' fees	18.4	15.1
Legal and notary costs	17.1	1.1
Rents, leases, ground rents	12.6	12.2
IT and administrative services	11.2	11.3
Sale preparation costs	8.2	6.7
Real estate transfer tax	3.9	81.0
Adjustment to sales of past periods	2.9	1.1
Surveying costs	2.4	2.5
Advertising costs	2.1	1.7
Sales incidentals	2.0	0.9
Analysis and remediation costs	1.4	2.6
Other	26.6	8.2
	150.4	**163.5**

The legal and notary costs include costs for entering transfers of title of € 13.4 million connected with the restructuring and refinancing measures.

In 2005, the real estate transfer tax paid was a result of intra-Group restructuring following the Viterra acquisition.

15 Financial income

€ million	2006	2005
Income from other investments	2.0	0.7
Income from non-current securities and non-current loans	1.9	0.8
Other interest and similar income	21.1	16.4
	25.0	**17.9**

16 Financial expenses

€ million	2006	2005
Interest and similar expenses	356.2	266.3
(thereof from affiliated companies)	(28.2)	(27.0)
	356.2	**266.3**

The financial expenses mainly relate to interest expense on financial liabilities measured at amortised cost.

Interest expense contains interest accretion to provisions, thereof € 11.1 million (2005: € 5.8 million) relating to provisions for pensions and € 1.0 million (2005: € 0.7 million) relating to other provisions.

17 Income tax

€ million	2006	2005
Current income tax	24.5	26.8
Aperiodical current income tax	–9.7	–1.2
Deferred income tax	182.8	–121.8
	197.6	**–96.2**

The current tax expense is determined on the basis of the taxable income for the assessment period. For the assessment period 2006, the combined tax rate of corporate income tax and solidarity surcharge is 26.4% of earnings. Including German municipal trade tax at nearly 13.6% (in consideration of deductibility for corporate income tax purposes), the combined tax rate is 40% (rounded) in 2006.

Deferred taxes are the expected tax charges or benefits arising from the difference between the carrying amounts of assets and liabilities in the consolidated financial statements and the valuation amounts used to calculate the taxable income (tax balance sheet).

Deferred tax liabilities are generally recorded for all taxable temporary differences. Deferred tax assets are recognised only to the extent that the realisation of the respective benefit is probable. Based on the profits of the past and the expected profits in the foreseeable future, allowances are only accounted for if this criterion is not fulfilled.

Therefore, no deferred tax assets were recognised in the balance sheet for deductible temporary differences (excluding loss carryforwards) totalling € 66.5 million (2005: € 213.8 million) plus € 46.8 million only for trade tax purposes as their future utilisation is unlikely.

Such deferred tax assets and liabilities are not recognised where the temporary difference arises from goodwill in connection with a business combination or the initial recognition (other than a business combination) of other assets and liabilities in a transaction which neither affects taxable income nor net income.

Deferred taxes were determined using the combined tax rate of corporate income tax and trade tax of approx. 40%. The effects of the extended trade tax exemption ("erweiterte Grundstückskürzung") in accordance with the German Trade Tax Act were taken into consideration in the measurement of deferred taxes.

Deferred taxes on loss carryforwards are recognised provided that it is likely that there will be sufficient income in the following years for these loss carryforwards to be utilised. Under German tax law, tax loss carryforwards for corporate income and trade tax purposes may only offset taxable income of € 1.0 million plus 60% of taxable income exceeding € 1.0 million (so-called "minimum taxation"). These restrictions were taken into consideration in the measurement of the deferred tax assets on loss carryforwards.

As at December 31, 2006, the unutilised corporate income tax loss carryforwards totalled € 897.1 million (2005: € 842.9 million) and the unutilised trade tax loss carryforwards amounted to € 432.0 million (2005: € 356.0 million), for which deferred tax assets have been established where their realisation is probable. Of these figures, discontinued operations account for corporate income tax loss carryforwards of € 0.0 million (2005: € 16.6 million) and unutilised trade tax loss carryforwards of € 0.0 million (2005: € 8.1 million).

The measurement of deferred tax assets on tax loss carryforwards in 2006 led to tax expense of € 21.3 million (2005: tax income of € 107.7 million).

Tax reductions due to the utilisation of tax loss carryforwards for which no deferred tax assets existed led in the financial year 2006 to a reduction in the tax burden of € 1.8 million (2005: € 2.9 million).

No deferred taxes were recognised in the balance sheet for unutilised corporate income tax loss carryforwards of € 413.9 million (2005: € 318.6 million).

Expiry dates of the unrecognised corporate income tax loss carryforwards:

€ million	Dec. 31, 2006	Dec. 31, 2005
Expiry date		
within 1 year	–	–
within 2 years	–	–
within 3 years	–	–
after 3 years	–	2.6
Unlimited carryforward	413.9	316.0
	413.9	**318.6**

Of the aforementioned, no corporate income tax loss carryforwards (2005: € 2.6 million) are attributable to foreign companies. In addition, there are further trade tax loss carryforwards of € 360.2 million (2005: € 155.0 million) which have an unlimited carryforward and which have not led to deferred tax assets.

A reconciliation between actual income taxes and expected tax expense which is the product of the accounting profit from continuing operations multiplied by the average tax rate applicable in Germany is shown in the table below. The applicable tax rate of 40% results from the corporate income tax of 25% plus a solidarity surcharge of 5.5% and the average trade tax.

€ million	2006	2005
Operating profit before income taxes	**428.7**	**58.3**
Income tax rate of the company in %	40.0	40.0
Expected tax expense	**171.5**	**23.3**
Trade tax effects	–5.0	4.2
Non-deductible operating expenses	12.9	2.7
Tax-free income	–10.2	–20.1
Tax rate differences at foreign Group companies	0.0	0.3
Effect arising from Section 6b of the German Income Tax Act (EStG)	0.0	8.4
Change in the deferred tax assets on loss carryforwards	21.3	–107.7
Additional losses for which no deferred tax asset is recognised	10.0	0.0
Utilisation of loss carryforwards without deferred tax assets	–1.8	–2.9
Effects of taxes from prior years	–1.0	–1.2
Other (net)	–0.1	–3.2
Actual income taxes	**197.6**	**–96.2**
Actual tax rate in %	**46.1**	**–165.0**

The deferred taxes refer to temporary differences in balance sheet items and unused tax losses as follows:

€ million	Dec. 31, 2006	Dec. 31, 2005
Investment properties	13.9	7.3
Plant and equipment	7.4	9.3
Inventories	52.3	29.1
Financial investments	2.9	3.6
Receivables	6.0	–
Prepaid expenses	23.0	6.2
Provisions for pensions	31.2	32.0
Other provisions	23.3	–
Liabilities	0.5	–
Unutilised tax losses	137.2	165.7
Deferred tax assets	**297.7**	**253.2**

€ million	Dec. 31, 2006	Dec. 31, 2005
Intangible assets	5.1	3.8
Investment properties	509.3	315.0
Plant and equipment	2.6	–
Inventories	144.0	106.5
Receivables	0.0	8.1
Other provisions	2.3	12.4
Liabilities	149.0	110.8
Deferred income	2.7	–
Untaxed income (Section 6b EStG)	52.4	89.7
Deferred tax liabilities	**867.4**	**646.3**
Net deferred tax liabilities	**569.7**	**393.1**

Deferred tax assets and liabilities are only netted against each other when the same tax authority is involved and the realisation period is the same. As a result, the following deferred tax assets and liabilities are stated in the balance sheet as at December 31, 2006:

€ million	Dec. 31, 2006	Dec. 31, 2005
Deferred tax assets	53.1	50.9
Deferred tax liabilities	622.8	444.0
Net deferred tax liabilities	**569.7**	**393.1**

Deferred tax assets and liabilities in connection with the discontinued operation in 2006 are part of the assets/liabilities classified as held for sale. In 2005, a net liability of € 8.6 million is contained in the aforementioned net deferred tax liabilities.

The change in deferred taxes recognised directly in equity in 2006 amounts to - € 18.0 million (2005: € 28.0 million).

Deferred tax liabilities for unremitted earnings of subsidiaries are recognised to the extent that they are expected to be permanently invested. These earnings, the amount of which cannot be reliably calculated, might be subject to additional tax if they were remitted as dividends or if the sharehold-ings in the subsidiaries were sold.

Notes to the Consolidated Balance Sheet

18 Intangible assets

€ million	Concessions, industrial rights, licences and similar rights	Customer bases	Total
Cost			
Balance on Jan. 1, 2006	8.3	15.8	**24.1**
Additions	2.0	–	**2.0**
Disposals	1.4	–	**1.4**
Transfer to assets classified as held for sale	0.5	–	**0.5**
Other transfers	–0.9	–	**–0.9**
Balance on Dec. 31, 2006	7.5	15.8	**23.3**
Accumulated amortisation			
Balance on Jan. 1, 2006	7.4	1.6	**9.0**
Amortisation in 2006	0.9	1.6	**2.5**
Disposals	1.4	–	**1.4**
Transfer to assets classified as held for sale	0.4	–	**0.4**
Other transfers	–0.9	–	**–0.9**
Balance on Dec. 31, 2006	5.6	3.2	**8.8**
Carrying amounts			
Balance on Dec. 31, 2006	1.9	12.6	**14.5**
Cost			
Balance on Jan. 1, 2005	1.5	–	**1.5**
Change in scope of consolidation	6.8	15.8	**22.6**
Additions	0.1	–	**0.1**
Disposals	0.1	–	**0.1**
Balance on Dec. 31, 2005	8.3	15.8	**24.1**
Accumulated amortisation			
Balance on Jan. 1, 2005	1.3	–	**1.3**
Change in scope of consolidation	5.8	–	**5.8**
Amortisation in 2005	0.4	1.6	**2.0**
Disposals	0.1	–	**0.1**
Balance on Dec. 31, 2005	7.4	1.6	**9.0**
Carrying amounts			
Balance on Dec. 31, 2005	0.9	14.2	**15.1**

In the year under review, scheduled amortisation of € 2.5 million (2005: € 2.0 million) was performed on the intangible assets.

No impairment of intangible assets was identified at the balance-sheet date.

19 Property, plant and equipment

€ million	Land and buildings	Technical equipment, plant and machinery	Other equipment, fixtures, furniture and office equipment	Construction in progress, pre-construction expenses	Total
Cost					
Balance on Jan. 1, 2006	–	1.6	41.2	1.2	**44.0**
Additions	–	–	1.4	0.3	**1.7**
Disposals	–	0.2	9.4	0.3	**9.9**
Transfer to assets classified as held for sale	–	–	2.3	–	**2.3**
Other transfers	13.5	–0.6	–5.1	–0.1	**7.7**
Balance on Dec. 31, 2006	13.5	0.8	25.8	1.1	**41.2**
Accumulated depreciation					
Balance on Jan. 1, 2006	–	1.4	33.8	0.9	**36.1**
Depreciation in 2006	0.2	0.1	1.3	–	**1.6**
Disposals	–	0.2	9.1	0.1	**9.4**
Transfer to assets classified as held for sale	–	–	1.9	–	**1.9**
Other transfers	–	–0.6	–3.7	–	**–4.3**
Balance on Dec. 31, 2006	0.2	0.7	20.4	0.8	**22.1**
Carrying amounts					
Balance on Dec. 31, 2006	13.3	0.1	5.4	0.3	**19.1**
Cost					
Balance on Jan. 1, 2005	–	0.1	8.5	0.1	**8.7**
Change in scope of consolidation	–	1.7	36.5	1.8	**40.0**
Additions	–	–	1.1	1.1	**2.2**
Transfers	–	–	–	–1.7	**–1.7**
Disposals	–	0.2	4.9	0.1	**5.2**
Balance on Dec. 31, 2005	–	1.6	41.2	1.2	**44.0**
Accumulated depreciation					
Balance on Jan. 1, 2005	–	0.1	5.2	–	**5.3**
Change in scope of consolidation	–	1.5	31.2	0.9	**33.6**
Depreciation in 2005	–	0.1	1.9	–	**2.0**
Disposals	–	0.3	4.5	–	**4.8**
Balance on Dec. 31, 2005	–	1.4	33.8	0.9	**36.1**
Carrying amounts					
Balance on Dec. 31, 2005	–	0.2	7.4	0.3	**7.9**

The item land and buildings contains transfers from investment properties of € 13.5 million relating to real estate used by the company itself which under IFRS must be shown under other property, plant and equipment.

Scheduled depreciation of € 1.6 million (2005: € 2.0 million) was performed on property, plant and equipment in the year under review.

No impairment of property, plant and equipment was identified at the balance-sheet date.

20 Investment properties

€ million	
Balance on Jan. 1, 2006	**6,561.9**
Additions	133.8
Capitalised modernisation costs	1.7
Transfer to trading properties	23.0
Transfer from trading properties	81.4
Transfer to assets classified as held for sale	204.7
Other transfers	23.6
Disposals	39.8
Fair value adjustment	360.7
Fair value adjustment on investment properties transferred to assets classified as held for sale	13.0
Balance on Dec. 31, 2006	**6,908.6**
Balance on Jan. 1, 2005 as previously reported	**1,601.8**
Change in accounting policy	454.9
Balance on Jan. 1, 2005	**2,056.7**
Change in scope of consolidation	4,873.9
Additions	8.1
Transfer to trading properties	281.5
Transfer from trading properties	–
Other transfers	76.1
Disposals	197.5
Fair value adjustment	26.1
Balance on Dec. 31, 2005	**6,561.9**

Due to a change in the assessment of their marketability, properties totalling € 81.4 million (2005: € 0.0 million) were transferred from trading properties to investment properties.

The transfer to assets classified as held for sale comprises the investment properties from Viterra Development, Viterra Baupartner and Viterra Logistikimmobilien. The other transfers include other assets totalling € 35.3 million (2005: € 74.3 million), which were transferred to investment properties. They were the housing stock of Wilhelm Sander-Stiftung, Neustadt an der Donau, acquired the previous year. In 2005, they were shown in current other assets under advance payments as benefits and burdens had yet to be transferred. The other transfers also comprise owner-occupied property of - € 13.5 million, which was transferred to property, plant and equipment. Transfers from property, plant and equipment to investment properties totalled € 1.8 million (2005: € 1.8 million). The disposals contain carrying value disposals of € 2.8 million from the sale of the materials handling division of Viterra Logistikimmobilien, which were not shown in the income statement as selling expenses but as discontinued operation.

The investment properties include leased assets which are defined as finance leases according to IAS 17 and are treated as if they were the Group's economic property. They amount to € 31.7 million (2005: € 48.7 million) and relate to the Spree-Bellevue (Spree-Schlange) property in Berlin. The property has been leased from DB Immobilienfonds 11 Spree Schlange von Quistorp KG until 2044. The leasing agreement includes an obligation to pay compensation for loss of use as agreed by contract. At the end of 2028, each fund subscriber is entitled to return his share to the property fund at a fixed redemption price. If all of the fund investors make use of this option, DAIG is obliged to acquire the property at a fixed purchase price after deduction of borrowings. If more than 75% of the shares are returned in this way, DAIG has a call option for the purchase of all fund shares. Details of minimum lease payments are given in the notes on financial liabilities.

The carrying amount of the investment properties is predominantly encumbered with land charges in favour of different lenders; see note (29) Financial liabilities.

Long-term leases

The long-term leases on commercial properties are non-cancellable operating leases. The minimum future leasing receipts from these leases are due as follows:

€ million	2006	2005
Total minimum lease payments	**43.5**	**154.0**
due within one year	26.3	28.9
due within 1 to 5 years	10.0	89.2
due after 5 years	7.2	35.9

As of 2008, the minimum lease payments to Viterra Logistikimmobilien are not included because of the agreement to sell Viterra Logistikimmobilien in December 2007.

The fair values of the real estate portfolios were determined in accordance with IAS 40.

Fair values

In 2006, we performed an internal valuation to determine the fair values of the DAIG's entire stock of residential buildings, small commercial units, garages/parking spaces and undeveloped land. The following criteria were applied in the valuation of the different segments of real estate:

Residential real estate

The value of the entire portfolio of residential properties was determined on the basis of the International Valuation Standard Committee's definition of market value. It is not permitted to take into account either portfolio premiums and discounts which can be observed when portfolios are sold in market transactions or time restrictions in the marketing of individual properties. The determination of fair values performed by DAIG thus complies with the IFRS standards.

In line with our business model, a distinction was made between apartments which are being sold individually or which, in our opinion, are basically suitable for being sold individually (privatisation portfolio) and the buildings which are to be considered properties to be managed.

First, all buildings were valued according to a rating system with regard to their quality, their market attractiveness and their macro-location. The aspects considered in assessing the quality of the buildings included particularly their age, the standard of their heating systems, the quality of the windows and heat insulation and an assessment of the technical condition of the building. The assessment of their market attractiveness was based on factors including the micro-location of the buildings, how built-up the area is, the average size of the apartments and the number of rooms. The quality of the macro-location was derived from the purchasing power index in the particular postal code district.

The property management portfolio was valued using the income capitalisation approach. The basis of the valuation is the net annual income per building which results from the annual net rent minus non-allocable ancillary costs, maintenance expenses and administrative expenses following the II. BV (German Regulation on Calculations for Residential Buildings in Accordance with the Second Housing Construction Law). With properties on land with inheritable building rights, the annual ground rent was also deducted. Vacant properties were taken into consideration on the basis of future anticipated rental income from assumed re-letting scenarios. In order to determine the capitalised value of potential yield returns, the annual net yield at building level was capitalised using capitalised interest rates which were derived from the current German real estate market and allocated to the buildings with the aid of the previously determined ratings.

For the privatisation portfolio, it was assumed that, apart from the apartments in a building which can be sold directly to tenants, owner-occupiers and capital investors (privatisation share), there are a certain number of apartments which, depending on the attractiveness, quality and macro-location, can only be sold at a discounted price to capital investors (remainder share).

The value of the privatisation share per building was determined using the comparable method. In principle, the remainder share was valued in the same way as the properties in the property management portfolio.

A residential real estate portfolio acquired at the end of the year was not re-valued but recognised at cost as this was, in our opinion, the fair value of the portfolio.

Commercial properties

The commercial properties in the portfolio were measured on the basis of individual experts' opinions, offers made in the course of sales activities or appraisals of internal experts.

Undeveloped land

Undeveloped plots of land were measured according to their state of development, the likelihood of development and the local market situation on the basis of derived land guide prices.

Results of the valuation

The fair value of the stocks of residential units, commercial units, garages and undeveloped land of the Deutsche Annington Real Estate Group as at December 31, 2006 was approx. € 9.9 billion (2005: € 9.4 billion).

The fair value of the real estate portfolio by region is as follows:

	Residential units		Other rental units		Fair values in € million	
	2006	2005	2006	2005	2006	2005
Deutsche Annington Nord GmbH	18,370	18,731	4,232	4,497	823.8	848.6
Deutsche Annington Ost GmbH	18,073	20,707	2,803	3,355	733.3	727.0
Deutsche Annington Rheinland GmbH	19,920	18,805	6,315	5,339	1,270.6	1,061.5
Deutsche Annington Ruhr GmbH	36,991	37,249	6,296	7,230	1,684.9	1,667.9
Deutsche Annington Süd GmbH	16,966	18,190	8,285	7,948	1,164.1	1,127.8
Deutsche Annington Süd-West GmbH	31,658	32,430	7,313	7,367	1,940.9	1,781.8
Deutsche Annington Westfalen GmbH	43,460	43,774	6,477	6,590	1,984.5	1,825.3
Commercial units					207.5	234.0
Undeveloped land					80.5	76.7
	185,438	**189,886**	**41,721**	**42,326**	**9,890.1**	**9,350.6**
of which						
Investment properties					6,908.6	6,561.9
Inventories					2,793.5	2,788.7
Assets classified as held for sale					174.5	
Owner-occupied assets					13.5	

Restraints on disposal

The 38,000 DEUTSCHBAU Wohnungsgesellschaft mbH apartments acquired from the German federal government in 1997 are subject to restrictions on sale until December 31, 2007. The restrictions specify that apartments may only be sold to capital investors if, in blocks with more than 10 apartments, 60 % of the tenants (or owner-occupiers if apartments are vacant) and, in blocks with up to 10 apartments, 50 % of the tenants have already purchased their apartments. Tenants who were 65 or over at the time of sale cannot be served regular notice to vacate or notice to vacate for personal use. The sale of entire blocks is ruled out as a matter of principle until December 31, 2007.

When acquiring 13,895 WohnBau Rhein-Main AG apartments in 1999 a number of commitments to Deutsche Post and Deutsche Post Wohnen were made, including an undertaking by DAIG that it would serve no notice to vacate for personal use until 2009. Tenants and their spouses may not be served notice to vacate for personal use if they are aged 60 or over. Furthermore, when residential units are converted into owner-occupier apartments, there is an obligation to give tenants first right of refusal.

The 63,626 residential units which DAIG acquired from Bundeseisenbahnvermögen in 2000 are subject to the following restrictions on sale: not more than 50 % may be sold within the first 10 years with the exception of housing stock in eastern Germany. If residential units in eastern Germany are sold, 25 % of the proceeds must be paid to Deutsche Bundesbahn and a further 25 % (less sales costs) must be invested in the modernisation and maintenance of the remaining housing stocks in eastern Germany. Furthermore, residential property used as such by a specified category of people may only be sold to them or to people named by them. Multi-family houses and owner-occupier apartments may only be sold to parties other than the specified category of people if more than half of the apartments in a block are already rented by tenants who do not fall under the specified category. At least € 12.78 per square meter per year must be invested in maintenance and modernisation in the first five years after acquisition. The obligation only applies to residential units which DAIG does not intend to sell and which are occupied by tenants who belong to the specified category of people.

The 10,413 Frankfurter Siedlungsgesellschaft mbH residential units acquired from the German federal government in 2001 and 2002 are subject to the restriction on sale that an annual sales programme must be agreed with the government. In addition, until November 2011, residential units must first be offered for sale to the tenant. Residential units may only be sold to persons other than the tenant if 50 % of the residential units in a building have previously been sold to tenants or owner-occupiers (vacant residential units). Tenants aged 65 or over whose residential unit is sold have a right to live in it for life. Furthermore, no residential units in the Rhine-Main region for which the federal government is entitled to name tenants may be sold before December 31, 2006.

In December 2006, DAIG acquired various housing stocks (1,623 residential units) from Corpus Immobiliengruppe and entered into the following social obligations: Tenants and their spouses who have rented an apartment at various contractually stipulated times in the past may not be served notice to vacate for personal use if they are aged 60 or over. No notice may be served to other tenants until after certain contractually fixed dates. Furthermore, DAIG undertakes not to perform any luxurious modernisation work for a certain period defined for each group of properties which would lead to rents above usual rents for the locality. If the apartments are sold, the tenants are to be given first right of refusal until after certain contractually fixed dates. For housing stocks which were formerly owned by Stadtsparkasse Düsseldorf, there are special agreements regarding rent increases for tenants who are employees of Stadtsparkasse Düsseldorf. Furthermore, DAIG has undertaken to offer certain apartments of Deutsche Post AG as well as other legal successors of Deutsche Bundespost and Bundesanstalt für Post und Telekommunikation for rent to their employees.

Under the GRAND documentation, DAIG is obliged to use a certain portion of the disposal proceeds for the repayment of the REF Notes. Overall, DAIG has to ensure that the aggregated disposal proceeds less any sales costs cover these fixed repayments. If DAIG does not meet this requirement, it will have to fund the difference out of own cash. If DAIG is not able to fund this shortfall, it will not be allowed to sell any properties.

21 Financial assets

	Dec. 31, 2006		Dec. 31, 2005	
€ million	non-current	current	non-current	current
Non-consolidated companies	0.8	–	1.0	–
Other investments	1.7	–	3.5	–
Loans to related companies	34.0	–	34.0	–
Long-term securities	2.3	–	2.3	–
Other long-term loans	0.9	–	1.2	–
Derivatives	–	–	48.3	–
Restricted cash	3.0	–	12.2	–
Dividends from other investments	–	1.7	–	0.0
	42.7	**1.7**	**102.5**	**0.0**

The loans to related companies relate to a loan to the property fund DB Immobilienfonds 11 Spree Schlange von Quistorp KG.

As part of the refinancing measure, the amortising interest-rate hedging agreements were transferred to German Residential Asset Note Distributor P.L.C. (GRAND) (2005: € 48.3 million).

As part of financing, cash restrictions were imposed on the company in respect of credit balances with banks totalling € 3.0 million (2005: € 12.2 million). Bank deposits to which cash restrictions apply for at least 12 months after the balance-sheet date are stated as non-current financial assets.

22 Other assets

	Dec. 31, 2006		Dec. 31, 2005	
€ million	non-current	current	non-current	current
Advance payments	–	0.0	–	36.3
Insurance claims	6.9	0.9	2.8	1.4
Miscellaneous other assets	13.8	26.0	14.7	28.2
Prepaid expenses	1.2	1.6	1.3	2.7
	21.9	**28.5**	**18.8**	**68.6**

As part of the transfer of the rewards and burdens from the acquisition of housing stock of Wilhelm Sander-Stiftung, Neustadt an der Donau in 2006, most of the advance payments made in the previous year were transferred to investment properties.

While the indirect obligation arising from pension obligations transferred to former affiliated companies of the Viterra Group is shown under provisions for pensions, a corresponding asset of € 13.7 million (2005: € 14.4 million) arising from the right to reimbursement is shown under non-current miscellaneous other assets.

23 Inventories

€ million	Dec. 31, 2006	Dec. 31, 2005
Trading properties	2,270.5	2,557.3
Land and equivalent rights excluding buildings	3.3	59.0
Pre-construction expenses	–	7.8
Land and equivalent rights including finished/unfinished buildings	1.9	27.3
Ancillary costs	355.0	296.4
Other inventories	–	0.5
	2,630.7	**2,948.3**

The carrying amount of the trading properties is predominantly encumbered with land charges in favour of different lenders; see note (29) Financial liabilities.

For information on disposal restrictions on trading properties, see note (20) Investment properties.

24 Trade and other receivables

€ million	Dec. 31, 2006 current	Dec. 31, 2005 current
Trade receivables		
from the sale of properties	248.9	444.1
from letting	8.9	9.1
from property management	0.5	0.4
from other supplies and services	0.0	2.6
Gross amount due from customers for contract work	–	36.3
	258.3	**492.5**

The carrying amounts of current trade receivables correspond to their fair values.

Following the divestment of Viterra Development and Viterra Baupartner, DAIG does not engage in construction contracts anymore.

25 Cash and cash equivalents

Cash and cash equivalents include cash on hand, cheques and deposits at Deutsche Bundesbank as well as at other banking institutions with an original term of up to three months totalling € 703.1 million (2005: € 481.5 million). Furthermore, the item contains marketable securities of € 3.3 million (2005: € 3.2 million).

The deposits at banking institutions include an amount of € 194.8 million (2005: € 117.6 million), which was pledged in connection with borrowings. Of these accounts, € 120.7 million (2005: € 55.0 million) are restricted. The marketable securities are also restricted with regard to their use.

Bank deposits to which cash restrictions apply for at least twelve months after the balance-sheet date are stated as non-current financial assets.

26 Equity

The subscribed capital of DAIG mbH is unchanged at € 75,000, split into shares in the nominal amounts of € 25,000, € 26,000, € 23,250 and € 750 respectively.

The previous shareholder, Monterey, established Deutsche Annington S.A., Luxembourg, on December 29, 2006. The capital was paid in by contributing all shares in DAIG mbH. Thus Deutsche Annington S.A., Luxembourg, has been the sole shareholder of DAIG mbH since December 29, 2006.

The capital reserve amounts to € 682.2 million (2005: € 202.7 million). In the course of the reporting year, Monterey made a contribution of € 214.6 million to the capital reserve (2005: € 1.0 million). At the end of December 2006, Monterey irrevocably waived its right to repayment of a shareholder loan granted to DAIG mbH for a nominal amount of € 209.7 million plus accrued interest of € 55.2 million. Accordingly, € 264.9 million was added to the capital reserve. The financial liabilities were reduced by € 209.7 million and the other liabilities were reduced by € 55.2 million.

The development of the Group's equity is shown in the consolidated statement of changes in equity.

The difference of € 6.2 million (2005: € 2.0 million) resulting from acquisitions and disposals of minority interests was transferred to retained earnings.

The other reserves contain cumulative changes in equity not affecting income. Those changes arise from foreign currency differences arising from the translation of the financial statements of foreign operations. Furthermore, the effective portion of the cumulative net change in the fair value of cash flow hedging instruments is shown within this reserve until the underlying hedged item affects net income as well as the cumulative net change in the fair value of available-for-sale financial assets until the asset is derecognised.

As part of the sale of the Development division, all foreign subsidiaries have been disposed of and therefore all cumulative changes in equity not affecting income arising from the translation of the financial statements of those subsidiaries have been transferred to profit or loss.

The cumulative changes in equity not affecting net income from cash flow hedges are as follows:

€ million	2006	2005
January 1	27.0	–14.9
Fair value gains in the period	96.1	45.0
Taxes on fair value gains	–38.4	–18.0
Transfer to profit/loss	–141.1	24.8
Taxes on transfer to profit/loss	56.4	–9.9
December 31	**0.0**	**27.0**

In the reporting period, € 57.7 million in changes in the fair values of cash flow hedges (2005: € 27.0 million) were recognised within the cumulative changes in equity not affecting net income. € 84.7 million were realised as income (2005: expenses of € 14.9 million). In connection with a comprehensive re-capitalisation programme during the reporting period (see note [29] Financial liabilities), all interest rate hedging agreements were transferred to a third party. The impact resulting from this is shown under financial expenses.

Shares of third parties in Group companies are shown under minority interests.

The cumulative changes not affecting net income of € 8.1 million result from acquisitions and disposals of minority interests.

27 Provisions

€ million	Dec. 31, 2006 non-current	Dec. 31, 2006 current	Dec. 31, 2005 non-current	Dec. 31, 2005 current
Provisions for pensions and similar obligations	**272.0**	**–**	**285.6**	**–**
Provisions for taxes (current income taxes excl. deferred taxes)	**–**	**129.1**	**–**	**170.3**
Other provisions				
Environmental remediation	32.9	2.3	36.0	2.7
Personnel costs (excluding restructuring)	22.7	30.5	14.5	28.3
Restructuring	–	6.9	–	22.5
Contractually agreed guarantees	3.6	16.3	8.2	21.6
Outstanding trade invoices	–	30.9	–	35.7
Follow-up costs from property sales	–	3.5	0.2	4.0
Miscellaneous other provisions	45.5	85.3	31.4	104.7
	104.7	**175.7**	**90.3**	**219.5**
	376.7	**304.8**	**375.9**	**389.8**

Development of other provisions

€ million	Jan. 1, 2006	Additions	Reversals	Change in scope of consolidation	Transfers	Interest portion	Utilisation	Dec. 31, 2006
Other provisions								
Environmental remediation	38.7	4.9	–3.9	–	–	–	–4.5	35.2
Personnel costs (excluding restructuring)	42.8	33.5	–3.6	–1.4	1.8	–	–19.9	53.2
Restructuring	22.5	3.2	–2.5	–	0.0	–	–16.3	6.9
Contractually agreed guarantees	29.8	13.7	–12.0	–6.5	0.0	–	–5.1	19.9
Outstanding trade invoices	35.7	24.8	–5.2	–8.8	6.5	–	–22.1	30.9
Follow-up costs from property sales	4.2	1.9	–0.2	–0.5	0.1	–	–2.0	3.5
Miscellaneous other provisions	136.1	38.3	–13.9	–3.4	–8.4	1.0	–18.9	130.8
	309.8	**120.3**	**–41.3**	**–20.6**	**0.0**	**1.0**	**–88.8**	**280.4**

Provisions for pensions and similar obligations

DAIG has pension obligations towards various employees which are based on the length of service. Defined benefit obligations – for which the company guarantees a certain level of benefit – are provided for through provisions for pensions. DAIG has taken out reinsurance contracts for individual people.

Pension plan obligations and the expenses necessary to cover these obligations are determined using the projected unit credit method prescribed by IAS 19, whereby current pensions and vested rights as well as expected future increases in salaries and pensions are included in the measurement. The following actuarial assumptions were made at the reporting date:

in %	2006	2005
Discount rate	4.25	4.00
Projected salary increases	2.75	2.75
Projected pension payment increases	1.75	1.75
Expected return on plan assets	3.25	3.25

Plan assets comprise solely of reinsurance contracts and the expected return on plan assets is based on the interest rate guaranteed in those contracts.

The defined benefit obligation (DBO) has developed as follows:

€ million	2006	2005
Defined benefit obligation as at Jan. 1	**309.9**	**37.8**
Interest cost	11.6	5.8
Current service cost	3.4	2.3
Actuarial gains/losses	–6.1	5.5
Past service cost	0.3	–
Benefits paid	–18.3	–8.5
Liabilities acquired in business combinations	–	267.2
Liabilities transferred in sale of subsidiaries	–9.6	–
Other transfers	–0.1	–0.2
Defined benefit obligation as at Dec. 31	**291.1**	**309.9**

The following table shows a reconciliation of the defined benefit obligation to the provision for pensions recognised in the balance sheet:

€ million	Dec. 31, 2006	Dec. 31, 2005
Present value of funded obligations	21.2	20.5
Present value of unfunded obligations	269.9	289.4
Total present value of obligations (DBO)	**291.1**	**309.9**
Fair value of plan assets	–17.6	–17.1
Unrecognised actuarial losses	–1.5	–7.2
Net liability in the balance sheet	**272.0**	**285.6**

The total net periodic pension cost comprises the following:

€ million	2006	2005
Interest cost	11.6	5.8
Current service cost	3.4	2.3
Actuarial gains recognised during the year	0.0	–
Expected return on plan assets	–0.5	–0.2
Past service cost	0.3	–
	14.8	**7.9**

The expected return on plan assets is only included to the extent that is necessary to cover the periodic cost from the corresponding obligation; i.e. the obligation for whose coverage those plan assets have been established.

The change in the fair value of plan assets is as follows:

€ million	2006	2005
Fair value of reinsurance contracts as at Jan. 1	**17.8**	**0.0**
Expected return on reinsurance contracts	0.7	0.2
Actuarial gains/losses	0.1	0.2
Benefits paid	–0.5	–0.2
Reinsurance contracts acquired in business combinations	–	17.6
Fair value of reinsurance contracts as at Dec. 31	**18.1**	**17.8**
Reimbursement rights (adjustment for the amount by which the fair value of reinsurance contracts exceeds the corresponding obligation)	–0.5	–0.7
Fair value of plan assets as at Dec. 31	**17.6**	**17.1**
Actual return on reinsurance contracts	**0.8**	**0.4**

As at December 31, 2006, € 17.6 million (2005: € 17.1 million) was offset against the corresponding provision for pensions. The amount by which the fair value of the reinsurance contracts exceeds the corresponding benefit obligations is shown under other assets.

The present value of the defined benefit obligation, the fair value of plan assets and the corresponding funded status developed in the past three years as follows:

€ million	2006	2005	2004
Present value of the defined benefit obligation	291.1	309.9	37.8
Fair value of plan assets	–17.6	–17.1	0.0
Deficit in the plan	**273.5**	**292.8**	**37.8**

The following table shows the experience adjustments arising on the plan liability during the respective period and the difference between the actual and expected return on the reinsurance contracts.

	2006	2005
Experience adjustments arising on plan liability (in %)	–2.9	–2.8
Difference between actual and expected return on reinsurance contracts (in € million)	0.1	0.2

The provisions for pensions contain liabilities of € 13.7 million (2005: € 14.4 million) for pension obligations transferred to former affiliated companies of the Viterra Group relating to vested rights and the payment of current pensions. A corresponding non-current receivable is shown under miscellaneous other assets.

Other provisions

Reversals of provisions are generally offset against the expense items for which they were originally established.

The provisions for environmental remediation refer to site remediation of locations of the former Raab Karcher companies. Remediation has either already begun or an agreement has been reached with the authorities as to how the damage is to be remedied. The cost estimates are based on expert opinions detailing the anticipated duration of the remediation work and the anticipated cost.

The personnel obligations are provisions for pre-retirement part-time work arrangements, bonuses, severance payment beyond restructuring and other personnel expenses.

During the normal course of business, DAIG and its subsidiaries give product warranties to the buyers of owner-occupier houses and apartments, commercial buildings and land. As at December 31, 2006, provisions of € 6.0 million (2005: € 14.0 million) had been recognised for these product warranties in the DAIG consolidated financial statements. The provisions for contractually agreed guarantees have been established for debt assumptions signed with buyers relating to tax, legal and other risks as part of the divestment of companies.

Outstanding trade invoices and follow-up costs from property sales relate to unbilled goods and services as well as contractually agreed completion work.

The restructuring provisions relate to personnel expenses.

The miscellaneous other provisions consist mainly of a conditional purchase price commitment, past and future compensation with reference to heat contracting, costs of changes in land register entries and costs of the vacant Grugaplatz premises in Essen.

28 Trade and other payables

€ million	Dec. 31, 2006 non-current	Dec. 31, 2006 current	Dec. 31, 2005 non-current	Dec. 31, 2005 current
Liabilities				
from property letting	–	16.0	–	11.0
from other goods and services	0.4	16.0	1.3	33.2
	0.4	**32.0**	**1.3**	**44.2**

29 Financial liabilities

€ million	Dec. 31, 2006 non-current	Dec. 31, 2006 current	Dec. 31, 2005 non-current	Dec. 31, 2005 current
Financial liabilities				
Banks	864.1	273.2	7,114.8	110.8
Other creditors	5,891.0	222.9	555.7	32.1
Related companies	–	0.1	209.7	0.1
Miscellaneous other financial liabilities	–	5.3	–	14.6
	6,755.1	**501.5**	**7,880.2**	**157.6**

Maturity of the nominal value of the financial liabilities is as follows:

€ million	total	2007	2008	2009	2010	2011	from 2012	thereof secured
Financial liabilities	7,568.8	527.6	367.6	361.1	519.7	549.4	5,243.4	7,433.7

The nominal obligations towards creditors are mainly secured by land charges and other collateral amounting to € 7,433.7 million.

At the end of December 2006, Monterey irrevocably waived its right to repayment of a shareholder loan granted to DAIG mbH for a nominal amount of € 209.7 million plus accrued interest of € 55.2 million. This waiver reduced the financial liabilities by € 209.7 million and the other liabilities by € 55.2 million.

Loans bearing no interest or interest below market rates in return for occupancy rights at rents below the prevailing market rates are stated at their present values in the balance sheet.

The nominal interest rates on the financial liabilities towards banks and other creditors are between 0.0% and 8.0% (average weighted approx. 3.4%).

In the reporting year, syndicated loans totalling € 5,898.5 million were repaid in full. Of this amount, € 1,570.9 million was used for repaying a recapitalisation measure performed by DAIG in 2005, which was used to repay company borrowings and also partly to fund the Viterra acquisition. The remainder was used for repaying a syndicated loan of € 4,327.6 million taken out by subsidiaries the previous year for the Viterra acquisition (€ 3,562.5 million), the repayment of financial debt in connection with the Viterra acquisition (€ 715.1 million) and as well as for market adjustment resulting from the transfer of interest rate swaps (€ 50.0 million).

€ 482.5 million of the company's own funds were used for the repayment of these loans. € 5,416.0 million was refinanced by securitisation through the issuing of bearer bonds (REF Notes) to German Residential Asset Note Distributor P.L.C. (GRAND). In connection with this comprehensive recapitalisation, the amortising interest rate hedging agreements of originally € 5,876.0 million were also transferred to GRAND. The REF Notes bear an average interest rate of 3.29% until July 2010. After July 2010, the average interest rate will increase to 4.68%. The REF Notes will mature in July 2013.

As part of a further securitisation measure, liabilities of € 393.5 million were entered into with GRAND. These REF Notes bear an average interest rate of 4.38% until the final maturity in July 2013. These funds were used to repay company borrowings of € 170.0 million. The rest of the cash inflow remained in the Group companies.

A loan agreement for a total of € 200.0 million was signed with Barclays Capital in December 2006. This loan was taken out to fund portfolio acquisitions. As at December 31, 2006, a total of € 130.2 million of the loan had been utilised. This financing is of short-term character and will mature in February 2007. The agreed interest rate for this loan is 4.17%.

Liabilities to other lenders include as at December 31, 2006 a liability of € 87.5 million from a finance lease (2005: € 87.0 million) (Spree-Bellevue property). The following table shows the total minimum lease payments and reconciliation to their present value.

	Dec. 31, 2006			Dec. 31, 2005		
€ million	Total minimum lease payments	Interest	Present value	Total minimum lease payments	Interest	Present value
Due within one year	4.5	0.2	4.3	4.4	0.2	4.2
Due in 1 to 5 years	17.4	3.0	14.4	17.5	3.0	14.5
Due after 5 years	257.3	188.5	68.8	261.7	193.4	68.3
	279.2	**191.7**	**87.5**	**283.6**	**196.6**	**87.0**

30 Other liabilities

	Dec. 31, 2006		Dec. 31, 2005	
€ million	non-current	current	non-current	current
Advance payments	–	386.8	–	307.9
Liabilities from deferred interest	–	43.4	–	123.4
Miscellaneous other liabilities	3.4	30.9	3.5	29.5
Deferred income	0.5	0.9	2.4	15.6
	3.9	**462.0**	**5.9**	**476.4**

The advance payments are mainly payments made in instalments by tenants for ancillary costs.

Of the liabilities from deferred interest, € 0.0 million (2005: € 27.0 million) are for liabilities towards the shareholder. At the end of December 2006, Monterey irrevocably waived its right to repayment of a shareholder loan plus accrued interest. The corresponding amounts were added to the capital reserve.

The miscellaneous other liabilities include other tax liabilities of € 3.7 million (2005: € 6.0 million), liabilities for social insurance contributions of € 0.0 million (2005: € 1.9 million) and € 14.4 million from a subsequent adjustment of the acquisition cost of Viterra.

31 Assets and disposal groups held for sale and discontinued operation

DAIG has decided to focus on its core business, the letting, buying and selling of housing units and to sell the Development division. The Development division mainly comprises Viterra Development, Viterra Baupartner and Viterra Logistikimmobilien. During the reporting year, several subsidiaries and business units of that division were already sold. DAIG agreed to sell the remaining parts of the division by December 2007. Therefore, those remaining parts have been classified as a disposal group held for sale and the entire Development division has been classified as a discontinued operation.

The Development division was not a discontinued operation or classified as held for sale as at December 31, 2005, however, the comparative income statement has been restated in accordance with IFRS 5 as if the discontinued operation had been discontinued from the start of the comparative period.

The results of the discontinued operation are as follows:

€ million	2006	2005
Income	74.5	126.6
Expenses	–63.8	–99.7
Results from operating activities	**10.7**	**26.9**
Income tax expense	–10.2	–10.8
Results from operating activities, net of income tax	**0.5**	**16.1**
Loss on sale of discontinued operation	–19.1	–
Income tax on loss on sale of discontinued operation	–5.4	–
Loss on sale of discontinued operation	**–24.5**	**–**
Loss/profit for the period	**–24.0**	**16.1**

The loss from discontinued operation in 2006 is increased by a subsequent adjustment of the acquisition cost of Viterra amounting to - € 14.4 million relating to the Deutsche Post settlement agreement described under note (38) Litigation and claims.

The tax on discontinued operation income before tax differs as follows from the hypothetical amount arrived at by applying a tax rate of 40% to net income before tax:

€ million	2006	2005
Loss/profit before income taxes	**–8.4**	**26.9**
Income tax rate of the company in %	40.0	40.0
Expected tax expense	**–3.4**	**10.8**
Trade tax effects	0.6	0.6
Non-deductible operating costs	13.1	1.1
Tax-free income	–	–1.8
Tax-free effects from deconsolidation	3.8	–
Effects of taxes from prior years	1.9	–
Other (net)	–0.4	0.1
Actual income taxes	**15.6**	**10.8**
Actual tax rate in %	**–185.7**	**40.1**

The cash flows from discontinued operation are as follows:

€ million	2006	2005
Net cash from (used in) operating activities	52.4	–38.8
Net cash from investing activities	64.1	37.5
Net cash used in financing activities	–16.1	–4.0
Net cash from (used in) discontinued operation	**100.4**	**–5.3**

The disposal of subsidiaries and other business units of the Development division during the period had the following effect on the financial position of DAIG:

€ million	2006
Property, plant and equipment	0.4
Investment property	37.1
Financial assets	1.3
Inventories	72.2
Trade and other receivables	84.2
Other assets	0.1
Cash and cash equivalents	23.3
Deferred tax assets	17.0
Provisions	–31.3
Trade and other payables	–61.7
Financial liabilities	–15.3
Other liabilities	–19.6
Deferred tax liabilities	–10.1
Net identifiable assets and liabilities	**97.6**
Consideration received, satisfied in cash	93.0
Costs to sell (cash) attributable to discontinued operation	–9.7
Cash disposed of	–23.3
Net cash inflow	**60.0**

The remaining parts of the Development division have been classified as a disposal group held for sale and are subdivided as follows:

€ million	2006
Assets classified as held for sale:	
Investment properties	174.5
Deferred tax assets	2.5
	177.0
Liabilities classified as held for sale:	
Financial liabilities	174.3
	174.3

Other explanations and information

32 Risk management

In the course of its business activities, DAIG is exposed to various financial risks. The Group-wide risk management system focuses on the unpredictability of developments on the financial markets and its aim is to minimise the potentially negative impact on the financial position of the Group. Derivative financial instruments are used for hedging risks connected with operational business and never for speculative purposes.

Interest rate risks

DAIG is exposed to interest rate risks in the course of normal business. Floating-rate debt exposes DAIG to a cash flow interest rate risk. DAIG uses derivative financial instruments to limit or eliminate these risks.

DAIG's policies permit the use of derivatives if they are associated with underlying assets or liabilities, contractual rights or obligations and planned operating transactions.

Due to the fact that DAIG refinanced short-term interest-bearing facilities totalling € 5,898.5 million in 2006 and has transferred the corresponding interest rate swaps to German Residential Asset Note Distributor P.L.C. (GRAND), DAIG currently does not have any derivatives. The majority of the remaining part of the financial debt bears long-term interest rates so that DAIG currently does not have any significant interest rate risks. However, the interest-rate risk is monitored on a monthly basis so derivatives can be entered into when required.

DAIG has no significant interest-bearing assets.

Credit risks

In the Deutsche Annington Real Estate Group, there are no significant concentrations of potential credit risks. Contracts for derivative financial instruments and financial transactions are only concluded with first-rate banks. DAIG has a Group-wide policy to ensure that rental contracts are only made with tenants with a good credit history. Valuation allowances are provided for the risk of loss of financial assets.

The carrying amount of the financial assets is the maximum risk of loss.

In the acquisition financing agreements, DAIG committed itself to fulfilling certain covenants. Based on the current corporate planning, we believe that these covenants can be fulfilled.

Market risks

(a) Currency risks
Owing to the limited internationality of DAIG's business, there are no substantive currency risks.
(b) Price risks
DAIG is exposed to property price and market rental risks.

Liquidity risks

DAIG uses a liquidity forecast and a liquidity plan to manage the liquidity risks. In addition, DAIG has certain credit lines in place which enable DAIG to meet short-term liquidity requirements.

33 Derivative financial instruments

From 2005, ten interest rate swaps were used in the Deutsche Annington Real Estate Group to limit the interest rate risk from floating-rate debt. The nominal volume of these ten swaps was € 5,876.0 million. As at December 31, 2005, the stripped present value of € 48.3 million was shown under other financial assets.

These ten interest rate swaps were transferred to German Residential Asset Note Distributor P.L.C. (GRAND) in August 2006 as part of the securitisation transaction performed with GRAND. At the time of their transfer, the interest rate swaps had a stripped present value of € 151.6 million. In addition to these ten interest rate swaps, DAIG has entered into two further swap agreements. The reason for entering into these swaps was to extend the swap period to seven years and to bring the existing ten interest rate swaps in line with the requirements of the securitisation transaction. These additional swaps were also transferred to GRAND in August 2006. Together with other transaction costs, this stripped present value was deducted from the funds granted by GRAND. The amount is released over time using the effective interest method.

In addition to the transactions mentioned above, DAIG has entered into one additional interest rate swap. This interest rate swap was transferred to GRAND in October 2006 within the tab issue of the MIRA portfolio into the securitisation transaction.

As at December 31, 2006, DAIG had no derivative financial instruments.

34 Non-derivative financial instruments

The carrying amount of financial liabilities as at December 31, 2006 was € 7,256.6 million (2005: € 8,037.8 million). The fair value of the financial liabilities amounted to € 7,349.9 million (2005: € 8,094.6 million) at the balance-sheet date and was determined on the basis of financial calculations using the market information available on the balance-sheet date. The figure shown is not necessarily the figure which DAIG could achieve under current market conditions.

35 Information on the consolidated cash flow statement

When determining the cash flow from operating activities using the indirect method, the profit for the period was adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, as well as items of income or expense associated with investing or financing cash flows. Therefore, direct comparison with the corresponding changes in the published consolidated balance sheets is not possible.

The income from the sale of trading properties is shown in cash flow from operating activities, the proceeds from the disposal of investment properties, intangible assets and property, plant and equipment are shown in cash flow from investing activities.

Exercising the IAS 7 option, interest received is shown under cash flow from investing activities and interest paid is shown under cash flow used in/from financing activities.

The application of the fair value model in accordance with IAS 40 from January 1, 2006 leads to changes in the figures of various items in the cash flow from operating activities. The profit for the period, depreciation of fixed assets and the results from disposals of investment properties are for example affected. The pre-year figures have been adjusted accordingly, but overall the cash flow from operating activities for 2005 remains unchanged.

The item “Disposal of discontinued operation” within the cash flow from/used in investing activities contains the purchase price obtained for the sold companies of the Development division classified as discontinued operation less attributable costs to sell less cash and cash equivalents disposed of.

The item “Proceeds received from disposals of financial investments” mainly relates to the disposal of the equity investment in Rhein Lippe Wohnen GmbH, Duisburg.

The item “Acquisition of intangible assets, property, plant and equipment, and investment properties” shows the investments adjusted for cash-neutral debt assumptions. As part of the acquisition of various housing stocks from Corpus Immobiliengruppe, debts amounting to € 5.7 million were assumed. The item “Cash proceeds from issuing loans and notes” has been adjusted accordingly.

The item "Cash repayments of financial liabilities" refers to the syndicated loans of € 5,898.5 million repaid by subsidiaries in full in 2006. The corresponding recapitalisation of € 5,416.0 million by the issuing of bearer bonds is reflected in the item "Cash proceeds from issuing loans and notes".

The item "Capital contributions from the shareholder" shows the cash-effective part of the capital increase described under note (26) Equity.

Of the cash and cash equivalents, restraints on disposal applied to € 124.0 million (2005: € 58.2 million). These were mainly pledged bank deposits (restricted cash).

36 Contingent liabilities

Contingent liabilities exist for cases in which DAIG mbH and its subsidiaries give guarantees to various contractual counterparts.

Contingent liabilities towards third parties are mainly letters of comfort and guarantees for warranty claims. The terms of the guarantees and letters of comfort are mainly limited to an agreed time or depend on the term of the loan to which they apply. In some cases, the term is unlimited.

As part of the divestment of companies, the vendor subsidiary, Viterra GmbH, signed letters of indemnity with the buyers relating to tax, legal and other risks. The assurances agreed were normal for commitments given in such transactions. The terms of the agreements are generally two to three years, in a few cases also 10, 15 or max. 30 years.

During the reporting year, several subsidiaries and business units of the Development division were sold. As part of the agreement for sale, DAIG signed letters of indemnity with the buyers relating to tax, legal and other risks. The assurances agreed were normal for commitments given in such transactions. The terms of the agreements are generally effective until December 31, 2007, respectively until April 13, 2014.

37 Other financial obligations

The future minimum payment obligations arising from such agreements as a result of the fact that they are non-cancellable operating leases are due as follows:

€ million	Dec. 31, 2006	Dec. 31, 2005
Total minimum lease payments	299.2	352.3
Due within one year	16.5	13.7
Due in 1 to 5 years	40.0	42.0
Due after 5 years	242.7	296.6

Payments of € 18.0 million (2005: € 6.5 million) under rental, tenancy and leasing agreements were recognised as expenses in 2006.

The expected total future minimum payments from non-cancellable subleases are € 0.0 million (2005: € 0.3 million).

The lease payments relate particularly to rented real estate and ground rent.

Furthermore, there are financial obligations from the commissioning of future services of € 97.2 million (2005: € 96.3 million).

38 Litigation and claims

DAIG is involved in litigation resulting from operating activities, both as the plaintiff and the defendant. These legal disputes and claims for damages are routine resulting from the normal course of business. They are in particular disputes under the Law of Tenancy and claims for damages/contract penalty claims in the Development division.

Where claims are made against DAIG, it has a right of recourse against general contractors or subcontractors which is secured by amounts retained as collateral or guarantees. Should, in isolated cases, recourse not be possible, the provision for guarantees calculated on the basis of historical values is utilised. None of these legal disputes and claims for damages will have a material effect on the balance sheet, profits or liquidity of DAIG.

In 2000, Viterra acquired eight logistics centres from Deutsche Post AG and at the same time leased them back to Deutsche Post. Deutsche Post subsequently failed to meet its contractual obligation to obtain legally valid building permits for all locations within two years from their handover. Therefore, on August 31, 2004, Viterra made use of its contractual right of rescission and demanded repayment of the original purchase price. After Deutsche Post disputed the legality of the rescission, Viterra filed an action against Deutsche Post. The Essen regional court (Landgericht) ruled in Viterra's favour on February 17, 2005. Deutsche Post AG appealed against this lower court ruling to the appellate court (Oberlandesgericht) in Hamm on April 22, 2005.

The appeal before the appellate court in Hamm was suspended as the parties were negotiating a settlement. On December 21, 2006, the parties signed a settlement recorded by a notary which among other things provides for Deutsche Post to repurchase the eight logistics centres from the buyer. The passing of economic ownership of the logistics centres will take place on December 31, 2007. Deutsche Post is also to pay the purchase price on this date provided the usual preconditions for payment are met. After all the obligations from the settlement agreement have been met in full, the parties will terminate the suspended proceedings before the appellate court in Hamm.

On February 22, 2006, the Federal Court of Justice (Bundesgerichtshof – BGH) gave another landmark ruling on the subject of contracting in a Viterra case. In the BGH's opinion, it is not possible to outsource the supply of heat to contractors (heat contracting) without a tenant's consent unless the tenancy agreement expressly provides for this. Accordingly, the change-over to contracting was not permitted under the term of any DAIG tenancy agreements which were entered into with tenants before 1999, as DAIG tenancy agreements have only contained a clause allowing contracting since 1999 and tenants' consent to heat contracting had not been obtained in any other way. In the meantime, DAIG has agreed with various tenants' associations and the German Tenants' Association (Deutscher Mieterbund) to settle the case by refunding about € 10 million to the affected tenants to compensate them for past heating expenses. As far as possible, the repayments are to be made in the first quarter of 2007. Furthermore, for the remaining term of the heat supply contracts, i.e. for about 10 years, DAIG will have to bear the difference between the invoiced heat supply costs and the costs which can be passed on to the tenants.

39 Related party transactions

The members of the management and the supervisory board and members of their immediate families do not personally have any business relations with DAIG companies other than in their capacity as members of the management or supervisory board.

There are also no business relations between DAIG companies and affiliated and associated DAIG companies or with members of the management or supervisory bodies of consolidated DAIG companies or members of their immediate families.

As at December 31, 2005, there was a shareholder loan of € 209.7 million granted by Monterey. At the end of December 2006, Monterey irrevocably waived its right to repayment of the loan (€ 209.7 million) and accrued interest (€ 55.2 million). € 264.9 million was added to the capital reserve. Financial liabilities were reduced by € 209.7 million; other liabilities were reduced by € 55.2 million.

In 2005, consultancy agreements were signed with Terra Firma Capital Partners Limited, London, and terrafirma GmbH, Frankfurt am Main. In 2006, services totalling € 0.9 million were provided (2005: € 2.5 million), of which € 0.6 million has already been paid (2005: € 2.2 million).

As at December 31, 2006, there is a loan with a nominal value of € 30.7 million granted to the property fund DB Immobilienfonds 11 Spree Schlange von Quistorp KG. The loan has a fixed term and runs until August 31, 2044. The interest rate is 6% p.a.

Citibank N.A.

In 2006, Citibank N.A. and its subsidiary, Citigroup Global Markets Limited, had the following business relations with DAIG:

As part of the refinancing of the acquisition financing for the railway workers' apartments, Citibank N.A. London Branch made funds of € 523.6 million available to DAIG in 2006 as part of a financing agreement signed in August 2005 with a total of three banks. The agreed loan volume in this syndicated agreement totalled € 1,610.0 million plus a credit line of € 60.0 million. This funding was refinanced in full on August 3, 2006 by a securitisation transaction.

For the interest hedging of this loan, DAIG contracted a fixed payer swap with Citibank N.A. London Branch with an initial amount of € 788.0 million. The fixed interest rate to be paid by DAIG was 2.8075%. Citibank N.A. paid the prevailing 3-month EURIBOR to DAIG in exchange for this fixed interest payment. This interest rate swap was transferred to German Residential Asset Note Distributor P.L.C. (GRAND) as part of the securitisation transaction.

In addition to the refinancing of the railway workers' apartments, Citibank N.A. London Branch provided part of the acquisition financing (€ 836.8 million) for the acquisition of Viterra AG by DAIG as part of a syndicated financing facility totalling € 4,327.6 million. The acquisition financing was utilised in full by DAIG. Furthermore, Citibank N.A. London Branch made credit lines of € 36.8 million available to DAIG as part of this syndicated financing facility. In total, the agreed credit lines under the syndicated financing facility amounted to € 180.0 million. In 2006, no funds were drawn under these credit lines. The syndicated financing facility was arranged in 2005 by Citigroup Global Markets Limited and five other banks. It was refinanced in full on August 3, 2006 by a securitisation transaction.

As part of the above-mentioned syndicated financing facility, Citibank N.A. London Branch provided DAIG with fixed payer swaps of initially € 3,225.0 million. The fixed interest rate to be paid by DAIG was 2.8075%. Citibank N.A. London Branch paid the prevailing 3-month EURIBOR to DAIG in exchange for this fixed interest payment. These interest rate swaps were transferred to GRAND as part of the securitisation transaction.

Within the transfer and the adjustments needed for the above-mentioned fixed payer swaps of initially € 788.0 million and € 3,225.0 million, DAIG paid a total of € 9.9 million to Citibank N.A. London Branch.

As part of the above-mentioned securitisation transaction, DAIG mandated Citigroup Global Markets Limited as arranger and lead manager together with another bank. Under this mandate, Citigroup Global Markets Limited received a fee of € 13.5 million. In addition, two interest rate swaps totalling € 3,049.8 million and an interest rate cap agreement of € 141.6 million were signed with Citibank N.A. London Branch in 2006. As part of the interest rate swap and the interest rate cap agreement, payments totalling € 16.6 million were made to Citibank N.A. London Branch. These interest rate swaps and the interest rate cap were transferred to GRAND on August 3, 2006 as part of the securitisation transaction.

In the reporting year, Citibank and DAIG signed cooperation agreements on future projects. The agreements end in September 2007 and March 2009.

40 Events after the balance-sheet date

On December 29, 2006, DAIG made a non-cancellable offer to Corpus Immobiliengruppe to purchase 1,164 residential units at a price of € 81.9 million.

Corpus Immobiliengruppe accepted the offer on January 2, 2007. The benefits and burdens are due to be transferred to DAIG at the end of March 2007.

41 Remunerations

The members of the supervisory board received € 40,000 for their work in 2006 (2005: € 0).

The total remuneration of the management amounted to € 4.5 million (2005: € 7.3 million). Of this figure, € 1.4 million (2005: € 1.6 million) was for fixed remuneration components including benefits in kind and other remunerations. The variable remuneration of € 3.1 million (2005: € 5.7 million) refers to bonuses, the exercise of virtual share options and other special payments. The share options result from the stock appreciation rights programme (SARs) of E.ON AG in which Viterra participated until leaving the E.ON Group in 2005. The variable remuneration includes bonus claims due in the long term of € 0.7 million.

The total remuneration of former managing directors amounted to € 6.7 million in 2006 (2005: € 1.4 million). Of this figure, € 1.1 million (2005: € 0.0 million) relates to long-term bonus claims.

Provisions of € 4.0 million (2005: € 2.7 million) have been provided for the pension obligations of former managing directors and their dependants and € 2.9 million (2005: € 2.7 million) for current managing directors and their dependants.

Supervisory Board

Guy Hands, Chairman,
Chief Executive Officer of Terra Firma Capital Partners Limited, London

David Pascall (until December 1, 2006),
Managing Director of Terra Firma Capital Partners Limited, London
Managing Director of terrafirma GmbH, Frankfurt am Main

Georg Kulenkampff (December 1, 2006 until December 18, 2006),
Managing Director of Terra Firma Capital Partners Limited, London
Managing Director of terrafirma GmbH, Frankfurt am Main

Fraser Duncan,
Executive Officer of Terra Firma Capital Partners Limited, London

Phillip Burns,
Managing Director of Terra Firma Capital Partners Limited, London

Joseph E. Azrack,
President & Chief Executive Officer of Citigroup Property Investors, New York

Sir Thomas Macpherson,
Chairman of Annington Holdings PLC, London

Wolfgang König (since July 6, 2006),
Corporate Consultant, Esslingen

The Supervisory Board does not have the rights and obligations provided for in the German Stock Corporation Law (Aktiengesetz).

Management

Georg Kulenkampff (since December 19, 2006), Chairman

Dr Volker Riebel (until December 19, 2006)

Dr Manfred Püschel

Jeff E. Kirchhoff (from September 28, 2006 until February 9, 2007)

Dr Ludwig Söhngen (until October 31, 2006)

Düsseldorf, March 26, 2007

Georg Kulenkampff

Dr Manfred Püschel

Auditors' Report

We have audited the consolidated financial statements prepared by Deutsche Annington Immobilien GmbH, Düsseldorf, comprising the balance sheet, the income statement, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year from 1 January to 31 December 2006. The preparation of the consolidated financial statements and the group management report in accordance with IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB are the responsibility of the parent company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB (Handelsgesetzbuch "German Commercial Code") and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with IFRSs, as adopted by the EU, the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB (and supplementary provisions of the shareholder agreement/articles of incorporation) and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Essen, 29 March 2007

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

signed
Beumer
Wirtschaftsprüfer

signed
Huperz
Wirtschaftsprüfer

List of Shareholdings

List of Shareholdings of the DAIG Group as at December 31, 2006

Company	Seat	Interest %	Equity € '000	Net income for the year € '000
Deutsche Annington Immobilien GmbH	Düsseldorf	100.00	827,733	–58,285
A. Consolidated companies				
Baugesellschaft Bayern mbH	Munich	94.90	122,712	169,773
Bundesbahn Wohnungsbaugesellschaft Kassel Gesellschaft mit beschränkter Haftung	Kassel	94.90	19,441	72,105
Bundesbahn-Wohnungsbaugesellschaft Regensburg mbH	Regensburg	94.90	53,277	69,994
BWG Frankfurt am Main Bundesbahn-Wohnungsgesellschaft mbH	Frankfurt am Main	94.90	86,007	190,813
Deutsche Annington Bestands GmbH & Co.KG	Düsseldorf	100.00	681,188	–742
Deutsche Annington Beteiligungsverwaltungs GmbH	Essen	100.00	493,572	–254,671
Deutsche Annington Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	401,662	7,021
Deutsche Annington DEWG GmbH & Co.KG	Düsseldorf	100.00	6,768	–511
Deutsche Annington DEWG Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington DID Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington Dienstleistungen Holding GmbH i.L.	Essen	100.00	18,563	12,007
Deutsche Annington Dritte Beteiligungsgesellschaft mbH	Essen	100.00	21	–4
Deutsche Annington EWG Augsburg GmbH & Co.KG	Düsseldorf	100.00	28,330	2,563
Deutsche Annington EWG Augsburg Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG Essen Bestands GmbH & Co.KG	Düsseldorf	100.00	91,736	7,817
Deutsche Annington EWG Essen Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	21,596	2,304
Deutsche Annington EWG Essen Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG Frankfurt Bestands GmbH & Co.KG	Düsseldorf	100.00	106,930	7,827
Deutsche Annington EWG Frankfurt Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	53,824	3,557
Deutsche Annington EWG Frankfurt Verwaltungs GmbH	Düsseldorf	99.60	20	–5
Deutsche Annington EWG Karlsruhe Bestands GmbH & Co.KG	Düsseldorf	100.00	75,274	6,208
Deutsche Annington EWG Karlsruhe Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	26,660	2,506
Deutsche Annington EWG Karlsruhe Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG Kassel Bestands GmbH & Co.KG	Düsseldorf	100.00	12,108	2,000
Deutsche Annington EWG Kassel Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	33,012	2,593
Deutsche Annington EWG Kassel Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG Köln Bestands GmbH & Co.KG	Düsseldorf	100.00	103,394	5,257
Deutsche Annington EWG Köln Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	103,517	4,875
Deutsche Annington EWG Köln Verwaltungs GmbH	Düsseldorf	99.60	22	–3
Deutsche Annington EWG Mainz GmbH & Co.KG	Düsseldorf	100.00	96,508	6,465
Deutsche Annington EWG Mainz Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG München Bestands GmbH & Co.KG	Düsseldorf	100.00	110,949	3,155
Deutsche Annington EWG München Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	81,312	2,985
Deutsche Annington EWG München Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG Nürnberg GmbH & Co.KG	Düsseldorf	100.00	67,145	15,365
Deutsche Annington EWG Nürnberg Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington EWG Regensburg GmbH & Co.KG	Düsseldorf	100.00	57,960	3,625
Deutsche Annington EWG Regensburg Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington Finance GmbH	Düsseldorf	100.00	405	374
Deutsche Annington Fundus Immobiliengesellschaft mbH	Cologne	100.00	2,505	967 [1]
Deutsche Annington Fünfte Beteiligungsgesellschaft mbH	Düsseldorf	100.00	1,708	–1
Deutsche Annington Haus GmbH	Kiel	100.00	2,045	–
Deutsche Annington Heimbau Bestands GmbH & Co.KG	Düsseldorf	100.00	221,522	13,393
Deutsche Annington Heimbau Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	70,466	3,929
Deutsche Annington Heimbau GmbH	Kiel	100.00	43,752	–10,728
Deutsche Annington Heimbau Verwaltungs GmbH	Düsseldorf	99.60	20	–5
Deutsche Annington Immobilien-Dienstleistungen Bestands GmbH & Co.KG	Düsseldorf	100.00	30,206	1,532
Deutsche Annington Immobilien-Dienstleistungen GmbH	Düsseldorf	100.00	7,771	–15,007 [1]
Deutsche Annington Informationssysteme GmbH	Essen	100.00	2,121	–111 [1]
Deutsche Annington Interim DAMIRA GmbH	Düsseldorf	100.00	22	–3
Deutsche Annington MIRA Bestands GmbH & Co.KG	Düsseldorf	100.00	89,547	–321
Deutsche Annington MIRA Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	71,349	45
Deutsche Annington MIRA Verwaltungs GmbH	Düsseldorf	99.60	24	–1
Deutsche Annington Nord GmbH	Kiel	100.00	25	–45 [1]

Company	Seat	Interest %	Equity € '000	Net income for the year € '000
Deutsche Annington Ost GmbH	Berlin	100.00	25	159 [1]
Deutsche Annington Rheinland GmbH	Düsseldorf	100.00	25	90 [1]
Deutsche Annington Rheinland Immobiliengesellschaft mbH	Cologne	100.00	11,926	2,617 [1]
Deutsche Annington Rhein-Ruhr GmbH & Co.KG	Essen	100.00	42,274	7,457
Deutsche Annington Ruhr GmbH	Essen	100.00	25	–22 [1]
Deutsche Annington Sechste Beteiligungsgesellschaft mbH	Düsseldorf	100.00	125,025	–
Deutsche Annington Service GmbH	Frankfurt am Main	100.00	50	–462 [1]
Deutsche Annington Süd GmbH	Munich	100.00	25	–14 [1]
Deutsche Annington Süd-West GmbH	Frankfurt am Main	100.00	100	467 [1]
Deutsche Annington Vermögensgesellschaft mbH & Co.KG	Essen	100.00	558,633	24,409
Deutsche Annington Vertriebs GmbH	Bochum	100.00	25	–2,338 [1]
Deutsche Annington Verwaltungs GmbH	Bochum	100.00	25	2,383 [1]
Deutsche Annington Vierte Beteiligungsgesellschaft mbH	Düsseldorf	99.60	21	–4
Deutsche Annington Westfalen GmbH	Dortmund	100.00	25	477 [1]
Deutsche Annington WOGE Vier Bestands GmbH & Co.KG	Düsseldorf	100.00	11,886	–161
Deutsche Annington WOGE Vier Bewirtschaftungs GmbH & Co.KG	Düsseldorf	100.00	10	–
Deutsche Annington WOGE Vier GmbH & Co.KG	Düsseldorf	100.00	32,397	–639
Deutsche Annington Wohnungsgesellschaft I Bestands GmbH & Co.KG	Düsseldorf	100.00	173,825	2,653
Deutsche Annington Wohnungsgesellschaft I mbH	Essen	100.00	28,816	154,071
Deutsche Annington WOGE Eins Verwaltungs GmbH	Düsseldorf	99.60	20	–5
Deutsche Annington Wohnungsgesellschaft III Bestands GmbH & Co.KG	Düsseldorf	100.00	21,974	2,929
Deutsche Annington Wohnungsgesellschaft III mbH	Recklinghausen	100.00	34,834	2,600
Deutsche Annington WOGE Drei Verwaltungs GmbH	Düsseldorf	99.60	21	–4
Deutsche Annington Zweite Beteiligungsgesellschaft mbH	Essen	100.00	–	–8
Deutsche Eisenbahn-Wohnungs-Gesellschaft mbH	Leipzig	100.00	10,251	605 [1]
Eisenbahn-Siedlungsgesellschaft Augsburg mbH (Siegau)	Augsburg	94.90	18,474	38,647
Eisenbahn-Wohnungsbau-Gesellschaft Karlsruhe GmbH	Karlsruhe	94.90	105,759	123,822
Eisenbahn-Wohnungsbaugesellschaft Köln mbH	Cologne	94.90	126,138	188,304
Eisenbahn-Wohnungsbaugesellschaft Nürnberg GmbH	Nuremberg	94.90	16,126	76,369
Frankfurter Siedlungsgesellschaft mbH	Essen	100.00	394,177	23,567
FSG Immobilien GmbH & Co.KG	Essen	100.00	198,735	16,424
FSG Immobilien Verwaltungs GmbH	Essen	99.60	23	–
FSG-Holding GmbH	Essen	94.80	15,154	–107
Grundstücksgesellschaft Eins Stauffenbergstraße mbH	Berlin	100.00	47	12
JAMUNA Grundstücksgesellschaft mbH & Co.KG i.L.	Grünwald	94.90	8	–3
JANANA Grundstücksgesellschaft mbH & Co.KG	Grünwald	94.90	6,008	–42
KADURA Grundstücksges. mbH & Co.KG	Grünwald	92.51	25,859	–185
LEMONDAS Grundstücksgesellschaft mbH & Co.KG	Grünwald	94.90	1,413	62
LEVON Grundstücksgesellschaft mbH & Co.KG	Grünwald	94.90	7,693	1,519
MANGANA Grundstücksgesellschaft mbH & Co.KG	Grünwald	94.90	1,540	–
MELCART Grundstücks-Verwaltungsgesellschaft mbH	Grünwald	94.80	637	–1
MIRA Grundstücksgesellschaft mbH (formerly: MIRA Grundstücksgesellschaft mbH & Co. KG)	Düsseldorf	94.90	167,890	171,110
Praetorium Sechsunddreißigste VV GmbH	Düsseldorf	100.00	24,937	–
"Siege" Siedlungsgesellschaft für das Verkehrspersonal mbH Mainz	Mainz	94.90	91,539	145,263
Viterra Holdings I GmbH	Düsseldorf	100.00	655,143	355
Viterra Holdings II GmbH	Düsseldorf	100.00	626,598	–6
Viterra Logistikimmobilien GmbH & Co. KG	Essen	99.96	11,463	50,644
Wohnungsgesellschaft Ruhr-Niederrhein mbH Essen	Essen	94.90	51,445	255,556
B. Subsidiaries not included in the consolidated financial statements				
Deutsche Annington Revisionsgesellschaft mbH	Essen	100.00	52	1
Immobilienfonds Koblenz-Karthause Wolfgang Hober KG	Düsseldorf	86.51	–3,548	198
VITERRA FRANCE SA i.L.	Paris	100.00	–324	–75 [2]
C. Other investments > 20 % interest				
FEA Verwaltungs GmbH	Bonn	25.00	23	–2 [2]

[1] Profit-and-loss transfer agreement
[2] Balance-sheet date: December 31, 2005

The Deutsche Annington Real Estate

DEUTSCHE ANNINGTON

REGIONAL SUBSIDIARIES

Deutsche Annington Nord
Sophienblatt 100
24114 Kiel
Phone +49 431 | 99074-0
Fax +49 431 | 99074-16
nord@deutsche-annington.com

Deutsche Annington Ost
Hannoversche Strasse 19
10115 Berlin
Phone +49 30 | 300093-0
Fax +49 30 | 300093-90
ost@deutsche-annington.com

Deutsche Annington Süd
Landsberger Strasse 308
80687 München
Phone +49 89 | 179109-0
Fax +49 89 | 179109-47 / -66
sued@deutsche-annington.com

Deutsche Annington Süd-West
Ludwigstrasse 43
60327 Frankfurt am Main
Phone +49 69 | 63301-0
Fax +49 69 | 631-4040
sued-west@deutsche-annington.com

Deutsche Annington Rheinland
Merowingerstrasse 150
40225 Düsseldorf
Phone +49 211 | 9333-01
Fax +49 211 | 9333-490
rheinland@deutsche-annington.com

Deutsche Annington Ruhr
Bonsiepen 9-12
45136 Essen
Phone +49 201 | 83711-0
Fax +49 201 | 83711-800
ruhr@deutsche-annington.com

Deutsche Annington Westfalen
Hülshof 24
44369 Dortmund
Phone +49 231 | 57704-0
Fax +49 231 | 57704-303
westfalen@deutsche-annington.com

Deutsche Annington Nord GmbH

Deutsche Annington Ost GmbH

Deutsche Annington Ruhr GmbH

Deutsche Annington Westfalen GmbH

Deutsche Annington Rheinland GmbH

Deutsche Annington Süd-West GmbH

Deutsche Annington Süd GmbH

Deutsche Annington Vertriebs GmbH

Deutsche Annington Vertriebs GmbH
Philippstrasse 3
44803 Bochum
Phone +49 234 | 314-1711
Fax +49 234 | 314-1812
info@deutsche-annington.com

Group

IMMOBILIEN GMBH

Deutsche Annington Immobilien GmbH
Philippstrasse 3
44803 Bochum
Phone +49 234 | 314-0
Fax +49 234 | 314-1314
info@deutsche-annington.com

Deutsche Annington Service GmbH

Deutsche Annington Service GmbH
Riedhofweg 23
60596 Frankfurt am Main
Phone +49 69 | 2411821-0
Fax +49 69 | 2411821-572
info@deutsche-annington.com

Deutsche Annington Verwaltungs GmbH

Deutsche Annington Verwaltungs GmbH
Philippstrasse 3
44803 Bochum
Phone +49 234 | 314-0
Fax +49 234 | 314-1314
info@deutsche-annington.com

The Deutsche Annington Real Estate Group (DAIG), Bochum, is one of Germany's leading residential property companies with some 221,000 residential units let and managed nationwide. As an integrated real estate company, DAIG pursues three core activities: the value-enhancing management of its nationwide residential real estate portfolio, the selective sale of residential units to tenants, owner-occupiers or capital investors and the acquisition of attractive housing stocks to achieve a sustained increase in the company's value. DAIG is a residential property company with a long-term view and a responsible, efficient lessor with a nationwide selection of residential property.

Deutsche Annington Immobilien GmbH
Philippstrasse 3
44803 Bochum
Phone +49 234 | 314-0
Fax +49 234 | 314-1314
info@deutsche-annington.com
www.deutsche-annington.com

Concept & Design
Berichtsmanufaktur GmbH, Hamburg

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