Reconstruction Capital II Ltd

Quarterly Report

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neweuropecapital

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Message from the Investment Manager and Advisers

Dear Shareholders

There was a large sell off of Romanian and Bulgarian stocks during the first quarter of 2008, with the Romanian BET EUR index and Bulgaria's SOFIX plunging 34% and 29%, respectively, over the quarter. The main reason behind the particularly heavy sell-off is a theory circulating in international investment circles that the countries of South East Europe are particularly vulnerable to the worldwide credit crunch due to their need to finance externally their high trade deficits. The lack of significant local institutional investors compounds the problem, by making SE European markets particularly vulnerable to international capital flows.

We believe that the fears of the international investment community are overdone. First of all, unlike many developed markets, growth remains strong. The consensus estimate for Romanian GDP growth over 2008 is 6%. Secondly, the trade deficit in these markets has traditionally been financed by a mixture of FDI, remittances from overseas workers, and, increasingly, EU accession funds. There is no indication that FDI has dried up, as highlighted by the recent acquisition by Ford of a Romanian car factory, and the much publicized relocation of Nokia's mobile phone production from Germany to Romania. Remittances remain strong and, if anything, EU funds are going up.

Another theory of the pessimists is that financing from Romanian banks, many of which are subsidiaries of international banks, will dry up as their parents withdraw loans made to their Romanian subsidiaries to strengthen their own battered balance sheets. However, this ignores the fact that many of the parents of Romanian banks are regional banking groups with little exposure to US sub prime. Furthermore, their Romanian operations continue to be very profitable, which means that they will be loath to reduce their Romanian activities.

The recently reported first quarter results of Erste Bank, which owns the largest Romanian bank, and of Banca Transilvania, show rising, not falling, profits over the period.

Due to the strong falls in the prices of shares on the local stock markets, and a 3.3% depreciation of the Romanian currency against the euro, RC2's NAV per share fell by 12.4% over the first quarter of 2008.

We remain confident in the ongoing growth of the SE Europe region. As such the fund has been active in seeking out and making new investments.

In March, RC2 acquired a 63% shareholding in Antares Hotels SRL, the owner of a 305 room beachside hotel at Mamaia, Romania's prime seaside resort, for a total consideration of EUR 8m. Because the bulk of the monies were used to repay bank debt, the hotel is now debt free. The fund has appointed a new management team to re-launch the hotel and is in negotiations to include the hotel in the Golden Tulip chain.

RC2 has also committed a further EUR 1m to its investment in healthcare provider Romar Holding Limited, increasing its participation in the company from 33% to 40%.

The fund is pleased to announce that it has now extended its operations to Serbia with the addition of Belgrade-based New Europe Capital DOO to its advisory team. We thank you for your continued interest and support.

Very Truly Yours,

New Europe Capital

Statistics

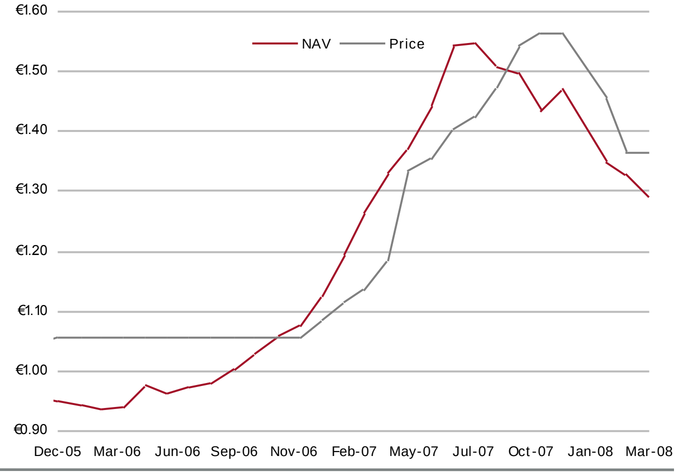
NAV per share (€)	1.2891
Share price (€)	1.3650
Total NAV (€ m)	145.3
Mk Cap (€ m)	153.8
# of shares (m)	112.7
Return since inception	34.77%
12-month CAGR	7.80%
Annualized Return*	14.18%
Annualized Volatility	12.15%
Best month	6.93%
Worst month	-8.27%
# of months up	17
# of months down	10

** since inception*

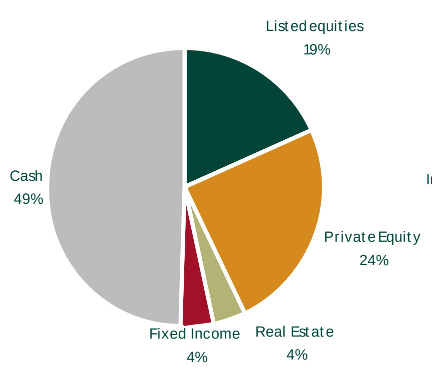
RC2 NAV returns

	2006	2007	2008
Jan	-0.61%	4.70%	-8.27%
Feb	-0.73%	6.17%	-1.48%
Mar	-0.87%	5.90%	-3.03%
Apr	0.44%	5.05%	-
May	3.73%	3.08%	-
Jun	-1.25%	5.19%	-
Jul	1.23%	6.93%	-
Aug	0.61%	0.22%	-
Sep	2.18%	-2.50%	-
Oct	2.74%	-0.69%	-
Nov	2.80%	-4.09%	-
Dec	1.70%	2.46%	-
YTD	12.47%	36.74%	-12.36%

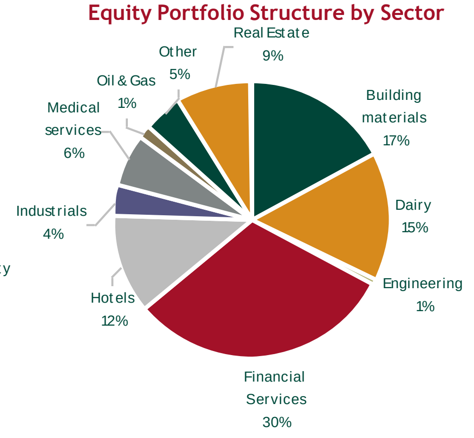
Share price / NAV per share (€)



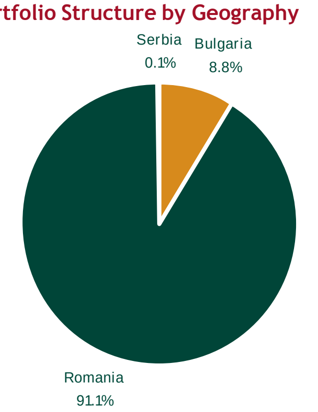
Portfolio Structure by Asset Class



Equity Portfolio Structure by Sector



Portfolio Structure by Geography



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Antares Hotels

Antares Hotels SRL is the owner and operator of the 305-room Fantasy Beach Hotel located in Mamaia, Romania's premium holiday resort on the Black Sea coast and in close vicinity to Constanta. In March 2008, RC2 acquired a 63% shareholding in Antares Hotels SRL from a distressed seller for a total consideration of EUR 8m.

Overview

Antares Hotels is the owner of the Fantasy Beach Hotel located in Mamaia, Romania's premium holiday resort on the Black Sea coast. The hotel is 6km from the centre of Constanta, Romania's 3rd largest city and Europe's 4th largest port. As part of the transaction, the funds invested in the Company were primarily used for the repayment of loans that were taken out for recent upgrades of the hotel rooms and its general facilities, and to provide working capital to the Company. The hotel, which overlooks the sea, occupies approximately half a hectare of owned land adjacent to Mamaia beach. The hotel's constructed area amounts to approximately 15,000 sqm. In addition, the Company owns a 2,257 sqm plot of land adjacent to it, also facing the beach, which is unused at present and which RC2 intends to be developed into "aparthotel" style holiday apartments.

Prospects

RC2 has appointed Peacock Hotels/Global Hotel Management, a professional local hotel management company with a strong track record, to run the hotel and intends to franchise the hotel as part of the international 'Golden Tulip Hotels, Inns & Resorts' chain. It is intended that the hotel will operate not only as a summer resort hotel (as is the case at present) but also as a business hotel for the city of Constanta with operations throughout the year.

RC2 is also in discussions with international and local developers to develop an "aparthotel" block of flats on the free land adjacent to the hotel.

Albalact

Albalact is a quoted Romanian dairy producer in which RC2 has acquired a significant stake under its Private Equity Programme. Following market purchases over the quarter, RC2 now holds a 12.2% shareholding, compared to 9.8% at the end of last year. Based on month-end prices, RC2's shareholding in Albalact had a market value of EUR 10.2m compared to a cost of EUR 5.7m.

(EUR '000)	2006A	2007A	1Q08
Income Statement (according to RAS)			
Sales Revenues	**28,965**	**46,389**	**12,517**
Other operating revenues	1,466.8	4,182.8	246.3
Total Operating Revenues	**30,431.5**	**50,572.0**	**12,763.7**
Total Operating Expenses	28,633.7	47,794.9	12,397.0
Operating Profit	**1,797.8**	**2,777.1**	**366.7**
Operating margin	6.2%	6.0%	2.9%
EBITDA	**3,145.8**	**5,257.2**	**1,036.9**
EBITDA margin	*10.9%*	*11.3%*	*8.3%*
Financial Profit/(Loss)	279.5	(1,632.0)	(91.0)
Profit before Tax	**2,077.3**	**1,145.1**	**275.8**
Income Tax	368.3	174.4	49.0
Profit after Tax	**1,709.0**	**970.7**	**226.8**
Net margin	*5.9%*	*2.1%*	*1.8%*
Avg exchange rate (RON/EUR	*3.525*	*3.334*	*3.689*

Source: Albalact

Financial results

Albalact recorded strong sales growth of 60% in 2007. Whilst EBITDA increased by 67% year-on-year in 2007, net profit was impacted by the delayed commissioning of the new plant and a strong euro. Annual marketing expenses increased by EUR 1.1m to EUR 2.4m in order to build up Albalact's brands.

Albalact released its financial results for the first quarter of 2008: sales were only up 10% year-on-year from EUR 11m to EUR 13m mainly due to capacity constraints as it took longer than expected for the new factory to become fully operational.

Financial results (cont'd)

Because of this, the net profit was also impacted as both new and old factories had to be used in parallel, resulting in higher operating costs

Operations

In 2007, the total milk processed was approximately 51 million litres, up 58% from 2006. 93% of its raw material came from dairy farms and individual producers in Romania and Hungary, whilst 7% was covered by Albalact's own farm.

After a six month delay, the new EUR 11m production facility is now fully operational, allowing Albalact to almost double its processing capacity from 145,000 to 250,000 liters/day.

Prospects

In an effort to better control both the quality and the cost of its raw milk, Albalact intends to acquire new farms. Its target is to secure about 25% of its raw milk needs from its own farms, compared to 7% at present.

The company's 2008 budget targets an increase in sales of 29% to EUR 59.8m, an EBITDA increase of 21%, and an improvement in the net margin from 2.1% to 5.1%.

Albalact aims to widen its product offering to include cheese and baby foods in 2008.

In an effort to improve its distribution, Albalact is investing in a new logistics centre near Bucharest that should become fully operational by July 2008.

Policolor Group

The Policolor Group is the the leading producer of coatings in Romania and Bulgaria. The group comprises Policolor S.A., a Romanian company quoted on the Bucharest Stock Exchange, and Orgachim, its 64%-owned Bulgarian subsidiary which is quoted on the Bulgarian Stock Exchange. At the end of March, RC2 held a 8.6% shareholding in Policolor and a 2.4% shareholding in Orgachim, at a total cost of EUR 7.6m and a market value of EUR 6.8m.. Because both companies are part of the same group, they are treated together.

Financial results

Because Policolor's reported statutory results do not consolidate the investment in Orgachim, we present separately the results of both companies.

(EUR '000)	2006A		2007A	
Income Statement	**PCL**	**ORGH**	**PCL**	**ORGH**
Sales Revenues	**42,408**	**48,368**	**48,134**	**62,633**
Other operating revenues	0	1,592	-961	1,888
Total Operating Revenues	**42,408**	**49,959**	**47,173**	**64,521**
Total Operating Expenses	39,726	46,993	47,514	59,444
Operating Profit	**2,681**	**2,967**	**(341)**	**5,077**
Operating margin	*6.3%*	*6.1%*	*neg.*	*8.1%*
EBITDA	**3,664**	**3,905**	**1,254**	**7,268**
EBITDA margin	*8.6%*	*8.1%*	*2.6%*	*11.6%*
Financial Profit/(Loss)	216	1,714	(2,648)	340
Profit before Tax	**2,897**	**4,680**	**(2,989)**	**5,417**
Income Tax	477	541	0	1,958
Profit after Tax	**2,420**	**4,139**	**(2,989)**	**3,458**
Net margin	*5.7%*	*8.6%*	*neg.*	*5.5%*
Avg exchange rate	*3.525*	*1.956*	*3.337*	*1.956*

Source: Company data

Note: PCL according to RAS, ORGH according to IFRS

2007 was another year of strong sales growth for the group. PCL reported sales growth of 14% even though a number of its automotive products had to be discontinued due to new environmental regulations introduced since Romania's entry into the EU. Orgachim, which was not affected by this problem, experienced sales growth of 29%, although this is inflated by intra-group sales to Policolor.

Financial results (cont'd)

The combined EBITDA of the two companies increased from EUR 7.6m to EUR 8.5m (+12.5%), which is satisfactory if one takes into account the impact of the new environmental rules on Policolor.

Although both companies appear to have suffered a decline in their bottom lines, much of this was due to non-operating items. In particular, Policolor was badly affected by the 7.6% depreciation of the Romanian currency against the euro in the fourth quarter of 2007. In addition, one of its main distributors experienced severe financial difficulties forcing Policolor to book a provision for bad debts. Orgachim's bottom line was affected by an additional depreciation charge of EUR 1.2m and a deferred tax charge of EUR 1.6m, due to a mandatory revaluation of its assets.

Operations

Policolor has continued to move part of its production to Orgachim in Bulgaria due to lower production costs, but has launched the production of expanded polystyrene (EPS) which is part of Policolor's insulation system for building facades.

Prospects

For 2008, Policolor official budget targets sales of EUR 59m (up 23% year on year) and a net profit of EUR 2.2m. Orgachim has not yet released its budget for 2008.

Top Factoring

In May 2007, RC2 invested EUR 3m in new and existing Top Factoring shares, thereby acquiring a 92.3% shareholding in this receivables collection company. The remaining shares are owned by the CEO.

Financial results

(EUR '000)	2006A	2007A
Income Statement (according to IFRS)		
Total Operating Revenues	**23.1**	**693.6**
Total Operating Expenses	51.8	836.4
Operating Profit	**(28.6)**	**(142.8)**
EBITDA	**(28.6)**	**(136.2)**
Financial Profit/(Loss)	(0.2)	110.5
Profit before Tax	(28.8)	(32.3)
Income Tax	-	-
Profit after Tax	(28.8)	(32.3)
Avg exchange rate (RON/EUR)	*3.525*	*3.334*

Source: Top Factoring

The above results, which are unaudited for 2007, reflect the early phase of this investment. 2007 was the first full year of operations, and also the first year that Top Factoring started acquiring packages of receivables, as opposed to acting as an agent for its clients.

Operations

Top Factoring acquired a portfolio of 40,000 cases from Vodafone at the end of 2006 at a cost of EUR 561,855 and a nominal value of EUR 12m, including accrued penalties. By the end of 2007, Top Factoring had already managed to recover EUR 547,485 on this portfolio.

For its agency business, Top Factoring is offering services to the Romanian subsidiaries of Vodafone, GE Money, Volksbank and Orange as well as local mobile phone operator Zapp, and local oil firm Rompetrol.

Prospects

Top Factoring acquired a second package of 60,000 bad debts from Vodafone at the end of 2007 with a nominal value including penalties of EUR 15m at a cost of EUR 1.2m for which it started collection at the end of March 2008. Because of the improved quality of this portfolio, we expect improved recovery rates compared to the 2006 debt purchase.

Romar

Following an initial investment of EUR 3m last year in which the Fund acquired a 33.3% shareholding in Romar, one of the leading private healthcares groups in Romania, RC2 has committed an additional EUR 1m in March 2008, lifting its equity stake to 40%.

Financial results

In 2006, Romar started a demerger process which was completed in September of that year. Consequently, the company's 2007 results are not comparable with those of the previous year.

(EUR '000)	2006A	2007A	2008e
Combined Income Statement			
Total Operating Revenues	**8,848**	**7,901**	**10,630**
Total Operating Expenses	8,134	7,425	9,320
Operating Profit	**714**	**477**	**1,310**
Operating margin	*8.1%*	*6.0%*	*12.3%*
EBITDA	**1,087**	**853**	**1,633**
EBITDA margin	*12.3%*	*10.8%*	*15.4%*
Financial Profit/(Loss)	18	(72)	
Profit before Tax	**732**	**405**	**1,310**
Income Tax	186	86	210
Profit after Tax	**546**	**319**	**1,100**
Net margin	*6.2%*	*4.0%*	*10.3%*
Avg exchange rate (RON/EUR)	*3.525*	*3.334*	*3.500*

Source: Romar, according to RAS, except for 2006 financials which are under IFRS

Note: Excludes Evolution Med

Financials results (cont'd)

Summary "combined" accounts for Romar are presented to the left. The 2007 financials exclude Evolution Med, a smaller Romanian private medical services company that Romar acquired in June 2007 at a cost of EUR 1.9m. Evolution Med is a loss making business which owns a clinic and a hospital under construction in the northern part of Bucharest and was primarily acquired for its real estate assets.

Operations

In the first quarter of 2008, Romar opened four laboratories and six policlinics in order to strengthen its position on the Romanian market. By the end of this year, Romar intends to open two further policlinics.

Land in Bucharest

In October 2007, RC2 purchased a 36.5% share of a plot of land from a distressed seller at a price of EUR 1,300/sqm, or a total consideration of EUR 3.64m. A zoning permit was obtained for the land since RC2's investment . The land is in close proximity to one of the major parks of Bucharest and located on the more desirable northern side of town. So far a number of real estate developers have made offers for the entire plot of land at prices starting at EUR 2,300/sqm.

Bulgarian Stock Exchange

RC2 owns 1.82% of the company which operates the Bulgarian Stock Exchange (BSE). The shares are valued at cost in the Fund's accounts (EUR 0.5m), given the fact that shares in the BSE are not traded on an organized market. The BSE is 44% owned by the Bulgarian state, 35% owned by Bulgarian brokerage firms, and the balance is owned by a combination of institutions and private individuals.

Financial results

(EUR '000)	2006A	2007A
Income Statement (according to IFRS)		
Revenues	**2,474**	**4,886**
Total Operating Expenses	1,522	2,057
Operating Profit	**952**	**2,828**
Operating margin	*38.5%*	*57.9%*
EBITDA	**1,090**	**2,993**
EBITDA margin	*44.1%*	*61.3%*
Financial Profit/(Loss)	53	156
Profit before Tax	**1,005**	**2,984**
Income Tax	152	300
Profit after Tax	**852**	**2,685**
Net margin	*34.4%*	*54.9%*
Avg exchange rate (BGN/EUR)	*1.9558*	*1.9558*

Source: BSE

Financials results (cont'd)

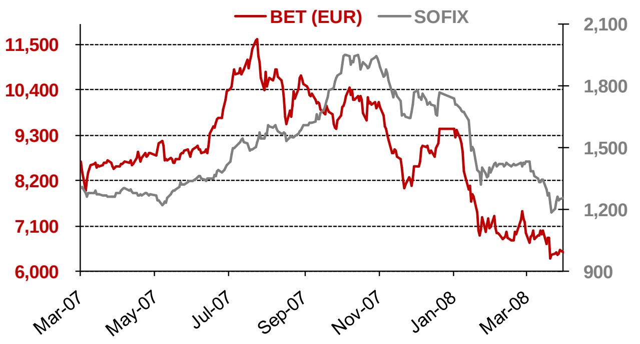
In 2007, BSE recorded operating revenues of EUR 4.9m, an impressive 97.5% increase compared to 2006, whilst the net profit more than tripled. This growth was mainly triggered by increased activity on the Official Market (up 50% year-on-year) and on the Unofficial Market (up 300% year-on-year).

Operations

By mid-2008, BSE plans to implement Xetra®, the platform used by the Deutsche Börse, as a basic trading system. This will require investments in new communications systems, technical equipment and training.

Capital Market Developments in Romania and Bulgaria

BET-EUR and SOFIX 1-year performance



Commentary

During the first quarter the Romanian and Bulgarian markets continued to lose ground, with the Bucharest Stock Exchange's EUR-denominated index (BET-EUR) falling 34% over the quarter and the Bulgarian Stock Exchange's SOFIX index decreasing by 29%. The first trading days of April saw recovery signs in both markets' evolution which suggest the markets may have turned. In terms of market capitalization, the Bucharest Stock Exchange was heavily influenced by Erste Bank's listing mid-February, which lifted total capitalization to EUR 31.6bn as opposed to EUR 24.6bn at the end of 2007. The Bulgarian Stock Exchange's capitalization decreased by 20% over the quarter, from EUR 14.8bn to EUR 11.9bn.

Macroeconomic Overview: Romania and Bulgaria

Overview

	RO	as of:	BG	as of:
GDP Growth*	6.0%	12M07	6.2%	12M07
Inflation*	8.6%	3M08	14.2%	3M08
Ind. prod. growth	7.7%	2M08	5.2%	2M08
Trade deficit (EUR bn)	2.9	2M08	1.2	2M08
y-o-y change	*3.2%*		*9.1%*	
FDI (EUR bn)	1.2	2M08	0.4	2M08
y-o-y change	*35.3%*		*15.3%*	

**y-o-y changes*

Commentary

Romania's consumer price index (CPI) was up 8.6% year-on-year in March 2008. The average monthly CPI growth over January - March 2008 was 0.7%, up from 0.1% over the same period last year. On a month-on-month basis, the CPI increase was 0.7% in March, basically maintaining the same pace as in January and February. Romania's central bank has recently revised its inflation target for 2008 from 3.8% +/- 1% to 5.9%.

Strong growth of 6.6% in 4Q-07 caused Romania's 07 GDP to grow by 6.0%, partially due to the booming construction sector which grew by 33.6% year-on-year.

Adverse weather conditions caused one of the worst draughts in the region making the agricultural sector contract by 16.9% over the year and fuelling food price inflation.

Romania's trade balance recorded a deficit of EUR 2.9bn over January-February 2008, slightly up from EUR 2.8bn over the same period last year. A very positive sign is the fact that February was the third consecutive month when export growth outpaced import growth: exports rose by 30.9% month-on-month compared to a 24.2% increase in imports.

Commentary (cont'd)

The EU was Romania's largest trading partner in this period: imports from EU-member states accounted for 70% of total imports, while the EU absorbed 71% of the country's exports. During the same period, Romania's current account deficit widened to EUR 2.2bn, a 5.6% increase year-on-year. FDI flow improved and covered 55.5% of the deficit at the end of February 2008 compared to 42.5% in the same period of last year.

In the last quarter of 2007, Bulgaria's GDP growth accelerated from 4.9% to 6.9%. As a consequence, full-year GDP growth stood at 6.2%. Despite a 29.7% year-on-year drop in the agricultural sector, GDP growth was fuelled by strong growth in the industry and construction sectors, which increased by 14.0% and 16.9% year-on-year, respectively.

Bulgarian CPI was up 14.2% year-on-year in March, the highest rate in ten years, driven by a 23.6% year-on-year increase in food prices. Nonetheless, the government's fiscal policy of pursuing budget surpluses will cap government spending and lessen inflationary pressures. Consequently, the Bulgarian Government has set a target inflation rate of 6.9% for 2008.

Bulgaria's trade deficit amounted to EUR 1.2bn over January-February 2008, a 9.1% increase year-on-year. The deterioration of the trade balance put the current account deficit over the same period at EUR 1.3bn compared to EUR 1.1bn in the same period of 2007. FDI covered 33.5% of the deficit at the end of February 2008. In 2007, the FDI level was an impressive EUR 6.1bn, covering 98.2% of the year's current account deficit.

In March, the Bulgarian unemployment rate reached 6.8%, down from 7.3% the previous month.

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