Chief Executive's statement

My role as Chief Executive is to deliver performance from the present business while building for the future.

I am pleased to report a strong set of results and good progress in the acceleration of 3i's development as a truly international private equity firm. Total return for the year was 15.9% on restated opening shareholders' funds. Both Buyouts and Growth Capital performed well, with gross portfolio returns of 22% and 24% respectively, and Venture Capital showed an improved performance with a gross return for the year of 11%.

Although, during the year, investment conditions were competitive for Buyouts, with increased funds flowing into European private equity and the high availability of debt, our teams invested £532 million, of which £338 million was from 3i's own resources. Growth Capital had a slower year in terms of the amount of investment (£263 million) but the pipeline going forward is encouraging. Our Venture Capital business continues to be selective and disciplined in its investment approach and invested £143 million.

Realisation proceeds were £1.3 billion and these were generated at good uplifts to carrying value. The portfolio performed well and health remains sound, reflecting both improved investment processes and the relatively benign economic backdrop.

To assist understanding of our current business model, we have decided to report separately the returns from our SMI portfolio which, in fact, has been run by a dedicated team since 2001. This team continues to make excellent progress in realising value from this part of the portfolio.

At the time of our interims in November, I spoke of the opportunities I saw for the Group to continue to improve our returns but also to increase the level of our investment. In view of the opportunities within our Growth Capital business to invest at a larger deal size, which quite often involves investing in companies with cross-border ambitions, we have decided to operate this business line on a more integrated international basis.

We are accelerating the development of our Asian business by opening an office in Shanghai and starting the recruitment of a high quality team to develop a business in India. We are also actively building relationships to access the market for infrastructure investment in the UK and the rest of Europe. These steps are the prelude to achieving a higher level of investment over the next few years without diluting our returns.

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Our vision:
to be the private equity firm of choice

Over the following pages we explain how we are working to achieve this.

In his new role as Head of Group Markets, Chris Rowlands has taken a number of important steps to improve the agility with which we bring our resources to bear in the market.

Our central sector group of industrialists has been strengthened to support the greater emphasis being given to sector specialisation in the origination of investments. We have also taken specific opportunities to add to the quality of our existing teams by bringing in fresh, relevant experience from outside, including Managing Directors for our German speaking and Indian businesses and our Group Marketing Director.

The creation of partnership style structures within each of our business lines has been supported in recent years by the introduction of carried interest schemes. These reward our teams for successful realisations. The continued success of our business line model within our international network is critically dependent upon the quality of our people and how well we deliver partnership models across the Group as a whole. Denise Collis, who joined our Executive Committee as Group Human Resources Director in November, is having a major impact on how we further improve our employment proposition and progress the development of our people to deliver a true culture of partnership across the Group as a whole.

As we develop our resources in new markets, we anticipate a modest increase in our cost base but, over the medium term, would expect our costs as a proportion of our gross returns to decline.

Following Michael Queen's move from Finance Director to head up our Growth Capital business, and the appointment of Simon Ball as his successor, the announcement in January that Jo Taylor would succeed Rod Perry in heading our Venture business has completed the series of changes required to implement our immediate plans. Rod has made a major contribution to the Group in this and other roles and I have asked him to continue his association with us by heading up an international advisory board for our Venture business.

At the interims, we took the step of making public the gross cash to cash returns that we are targeting for each of our business lines, as well as the volatilities that we expect to experience over given time periods (page 78). At the mid-point of these ranges and with an appropriate level of leverage to our equity base, we would expect to achieve an average return on equity of 20%.

The good returns we are achieving, and particularly the high level of realisation proceeds we have generated over the past two years, have given rise to a higher level of financial resources than we can profitably reinvest in the near term. By reference to the level of gearing we believe is appropriate for the business and, having reviewed our medium-term projections of cash flows, we have decided to take immediate steps to return capital to shareholders.

Although we intend to increase the amounts we invest, particularly through accelerating investment in growth capital opportunities and expanding our business lines and geographic footprint, we are committed to maintaining financial efficiency by returning cash when it is surplus to our investment needs.

Our strategic opportunities are clear and much change is under way to accelerate their delivery. At the same time, our teams are maintaining their focus on continuing to deliver high quality investment opportunities. Despite the hesitancy apparent in the financial markets, I intend to report further good progress towards our performance and strategic goals in the year ahead.

Philip Yea
Chief Executive
11 May 2005