3i Group – scripts for half-yearly results to 30 September 2009

MICHAEL QUEEN – CHIEF EXECUTIVE

Good morning everyone and welcome to our presentation

KEY THEMES

Our key themes today are - firstly we have transformed our financial position, secondly we remain cautious about the economy, thirdly we are confident in the strength of our portfolio and finally we have done a lot of work to make sure 3i is ready for the upturn.

AGENDA

I will start by providing a short update on the priorities we set out at the time of our final results in May. Stephen Halliwell will then go through the results for this six month period in detail. I will then take you through the current shape of the business, our future direction and share some thoughts on what will be the key elements that will generate performance at 3i in the future.

Firstly, let's go back to May and the priorities we set at the time.

PRIORITIES

We identified these four short term priorities.

Top of the list was a reduction in net debt as part of a move to a more conservative financial structure. We also said we would focus much of our efforts on working with investee companies to protect value and ensure where appropriate, businesses were strengthening their position in their own markets.

We were also determined to use this opportunity to change - looking to make sure we were ready for the upturn and finally to grow our external funds under management.

PROGRESS IN THE FIRST HALF

As you can see from this slide we have made a lot of progress. The result is that we have transformed our financial position and have a much strengthened balance sheet and substantial liquidity.

The reduction in net debt to £854 million was considerably assisted by the support from shareholders for our rights issue and realisations exceeding new investment by £317 million. Not only is the net debt lower, we have also improved the repayment profile.

We have been actively realising the non core portfolio selling 49% of those assets held at the year end.

We have continued to be conservative in our valuation approach anticipating further earnings falls where relevant but I am pleased to say that the portfolio is performing inline with our expectations and a good indicator of this strength is that we have only had to invest £47 million in equity cures and provisions remain very low.

We have also been focused on cost discipline within 3i and the absolute level of costs are down by 18% on the same period last year. As Stephen will discuss later on a like for like basis the reduction is closer to 30%.

The combination of these factors means we have available liquidity of £2 billion which allows us to invest when we see attractive opportunities. I will comment on the investment climate after Stephen has taken us through the results. Finally we have a positive total return and we will be paying an interim dividend of 1 pence per share.

I will now hand over to Stephen.

STEPHEN HALLIWELL
Thank you Michael and good morning.

KEY FINANCIALS
I will start by running through the key financials for the period.

As you will see on this slide and throughout the presentation, given the volatility over the last eighteen months, I have also provided additional comparatives for the most recent six months to March.

The Group generated a positive cash flow from investment activity achieving realisations of £507m with a low level of investment of £190m.

Moving to returns, we have generated a positive total return of £81m in the six months. This represented a 3.2% return on opening equity and is a significant improvement on the previous six months. The core business lines delivered a combined Gross Portfolio Return of 9.8%, but this was pegged back by the non-core portfolio to an overall return of 7.8%.

The increase in NAV per share since March reflects this positive total return performance, the comparative for March has been re-stated to include the impact of the Rights Issue and the QPE transaction.

Finally on this slide, as Michael has already mentioned, Net debt has reduced by over £1bn to £854m.

So moving to the detail. Looking firstly at realisations………

REALISATIONS £507M IN SIX MONTHS TO 30 SEPTEMBER 2009
Realisations of over half a billion in the six months, again demonstrated the strength and depth of the portfolio as well as our progress in realising the non-core portfolio.

The three most significant individual sales from the portfolio Venture Production, AWG and Salamander accounted for almost half of the total realisations in the period. Sales from the non-core Venture and SMI portfolios and assets previously held by 3i Quoted Private Equity accounted for a third of all realisations. And it is worth noting that the Venture sales only included £23m of the £128m portfolio sale we announced in September. The balance is being received in stages and almost all of it will be in before the financial year-end.

Overall the sales were achieved marginally ahead of their carrying value, and those from our core business lines were achieved at a solid uplift of 13%.

Moving then to investments……

INVESTMENT - £190M IN SIX MONTHS TO 30 SEPTEMBER 2009

Gross investment for the period was £190m and, as can be seen, a large proportion related to capitalised loan instruments (or Payment in Kind notes) so actual cash invested only amounted to £94m.

There were no new companies added to the portfolio so all investment was into the existing portfolio. Of this, £47m was for equity cures or rescue funding which was lower than anticipated. We also provided acquisition finance to 8 of our portfolio companies.

If I now move on to returns …..

TOTAL RETURN ANALYSIS

This slide sets out all the components of the newly named Statement of Comprehensive Income, which we will continue to refer to as Total Return. As you can see the overall return was a positive £81m.

Before I go into the detail of the Gross Portfolio Return, I wanted to draw out from this slide the Net Portfolio Return of £232m, which is a 5.8% return for the half year.

GROSS PORTFOLIO RETURN

The key driver of Gross Portfolio Return in the period was unrealised profits of £227m. In summary, increases in the value of the quoted portfolio and in the earnings multiples applied to those companies valued on an earnings basis in the unquoted portfolio have had a positive effect. However, this has been partially offset by lower earnings in the portfolio.

Realised profits, as I have already covered, **<u>were</u>** at an uplift to carrying value. Portfolio income at £76m continues to be lower than historic levels as we do not recognise accrued income on any loans with value impairments. The majority of income continues to be from capitalised interest and dividends.

The bottom half of this slide contains the detail by business line which I covered earlier.

MOVEMENT IN PORTFOLIO VALUE

So moving into the detail of the unrealised value growth.

Firstly, I wanted to put the value movement in the context of the overall stable portfolio value and the investment activity over the period. As you can see from the slide the portfolio is now valued at £3.8bn.

Tracking across the movements, you can see the new investment and realisations and the unrealised value uplift, which is shown here in three core components. Firstly, the market driven movement from our quoted portfolio, increases from changes in earnings multiples and the recovery in value of the Debt Warehouse. Next the more investment specific performance driven movements – which includes changes in earnings and any provisions. And finally a small amount “other” which includes 3i specific factors mainly where a marketability discount has been applied for the first time.

The final red block of other movements is mainly the foreign exchange impact as Sterling has strengthened in the period, especially against the US dollar.

I will now focus on the two main elements within the value movement, which are the movement in earnings multiples which has a value uplift of £464m and the change in earnings which led to a value reduction of £322m.

EARNINGS MULTIPLES - £464M VALUE MOVEMENT

As 71% of our unquoted portfolio is now valued on an earnings basis, this is an increasingly influential area for our overall return.

Within our valuation process, we identify a best-fit set of comparable quoted companies and sectors to derive the multiple to apply to the company's earnings. As quoted markets have risen, the earnings multiples applied to 3i's portfolio have increased by 21% from March to September. Several market indices and implied multiples have certainly seen higher increases than this, but the nature of our portfolio, the process of deriving comparator groups, the influence that the larger assets have on the overall movement and the balance of sectors we invest in, will generally explain this divergence.

Certainly over the recent volatile times, our higher-value, stronger performing assets have seen a lower degree of volatility in their multiples.

Once the appropriate multiple has been selected this is applied to the company's earnings.

VALUATION EARNINGS - £(322)M VALUE IMPACT

There are essentially three ways of measuring earnings. The audited accounts, which are historic, the latest management accounts from which we derive the latest twelve months earnings and finally an earnings forecast.

We base valuations on latest management earnings of the past 12 months unless the forecast is lower or we believe a lower figure from the last audited earnings provides a more reliable picture of performance. As you can see from the slide the pattern over the last three six month periods has reflected the general macroeconomic environment. So at 30 September this year only 22% of earnings have been taken from audited accounts with 39% forecast earnings being used.

This bias towards the lowest of three measures means we use forecasts only where they suggest a future fall in earnings but don't use them where they suggest a rise in future earnings.

So while earnings in this substantial part of the portfolio fell only 6% during the period, the figures we use for valuations are down by 13%.

The key point here then is that our conservative approach means that our valuations tend to lag performance as the economy bottoms out.

The impact to valuations from earnings is a fall of £322m, however this is concentrated in a small number of assets in sectors and geographies that have been particularly affected by the economic downturn.

UNREALISED PROFITS / (LOSSES) ON REVALUATION OF INVESTMENTS

This final slide on valuation brings together all the valuation bases which combine to make the £227m value uplift. There are 4 key movements that I have not already mentioned that I wanted to cover.

Firstly the market adjustment basis, which is a £40m negative movement in the period and relates to 5 assets which have moved from a market adjustment basis and where we have applied a marketability discount for the first time.

Secondly, Impairments which are covered in two lines on the slide and total a net gain of £54m in the period, which is mainly due to the value increase of the Debt Warehouse. This is a significant reversal from last year when you may recall, this was a key feature of the value falls, where impairment losses of £848m were recognised.

Next is provisions, which are relatively low at £27m. I should also note that around 5% of previously impaired loans were also moved to provision status. Although there is no impact on value as they were already carried at nil value. And lastly the quoted portfolio, which has a value gain of £108m, is largely due to share price increases for 3i Infrastructure plc and Telecity plc.

TOTAL RETURN ANALYSIS

Returning to the other elements of total return, operating expenses at £108m are 18% down on the equivalent period last year and 9% down on the last 6 months.

Net interest payable is higher than in recent periods as the interest earned on cash balances has fallen more steeply than the more fixed levels on interest paid on our borrowings.

There is a net foreign exchange loss of £66m. We continue to hedge our foreign exchange exposure only through the use of matched currency borrowings where possible. We are currently 67% hedged on the European and Nordic portfolios but only 14% hedged on our US and Asian, dollar-denominated portfolios. The strengthening of sterling in the period, most notably against the US dollar, has driven this loss.

We have also recognised an accounting pension charge of £36m in the period. Whilst rising equity markets have increased the value of the pension plan assets, a fall in corporate bond yields used to discount the value of the plan liabilities, more than offsets the asset increase resulting in a net charge.

The final total return of £81m is a 3.2% return on average shareholders equity. This average includes the £732m of equity raised through the Rights Issue in June.

FURTHER REDUCTION IN OPERATING COSTS

Looking then in more detail at operating costs, this slide shows the ongoing downward trend in these costs. This is a result of the headcount reduction to 537 at 30 September, down from 731 this time last year, and other cost saving initiatives.

Operating costs include the cost of redundancy, and restructuring as well as staff bonuses. Excluding these items, the underlying like for like cost reduction is 29% from the same period last year.

We will continue our focus on cost discipline in the second half of the year.

STRONG CASH FLOW GENERATION

Before I get to the balance sheet, I have included this slide from our March 2009 presentation and updated it for the latest 6 months, as it captures quite clearly how we have returned to being net divestors of assets and the impact that this, and the Rights Issue (which is shown in the final column in yellow), has had on gearing levels.

This demonstrates our continued ability to generate cash through economic cycles and periods of market volatility.

BALANCE SHEET

The significant reduction in gearing to 31% from 103% at March 2009 is demonstrated through the balance sheet and comparatives. The Rights Issue proceeds have bolstered equity and reduced net borrowings and coupled with the continued focus on cash generation in the business, this has delivered net debt of £854m at 30 September 2009.

The increase in NAV since March reflects the total return profit in the period as the March NAV shown here is adjusted for the Rights Issue and the QPE transaction.

CHANGES TO MATURITY PROFILE OF DEBT

In addition to the reduction in net debt, we have also been able to extend the maturity profile of our debt through 3 new or extended facilities, the most recent of which, a £200m 5 year multicurrency facility, has been signed since the half year end and we are announcing today. This has significantly reduced the imminent maturities of the debt. The repayment profile on £300m drawn under committed long term facilities, previously due within one year from 30 September 2009, has been extended by three years. As a consequence, including the repayment of £50m of debt, long term debt repayable within one year has been reduced from £456m to only £106m.

Our new facilities also boost our liquidity position, which today is now over £2bn in cash or undrawn facilities.

The new facilities are accompanied by a covenant, being an Asset Cover Ratio of total assets to gross debt of 1.45x. We are operating significantly above the required ratio.

FINANCIAL SUMMARY

So to summarise ….

We have a significantly improved financial position and achieved a positive return for the first half driven by a 10% portfolio return from our core business lines.

A cautious approach to investment and a good level of realisations combined with the Rights Issue underpinned the reduction in net debt, gearing, and the significant improvement in liquidity.

Our focus on cost efficiency is also now benefitting returns.

I will now hand back to Michael.

MICHAEL QUEEN – CHIEF EXECUTIVE

Thank you Stephen.

KEY THEMES

Over the next few minutes I want to focus on the economic outlook and the market in which we operate. I will then move onto our business, our strategic focus and the steps we have taken to position 3i for the future. Finally I will update you on what will be the key drivers of performance over the next few years.

Let me start by saying a few words about the economies in which we operate.

Asia – especially China and India is showing good growth and this is creating investment opportunities although pricing is high for good assets reflecting underlying growth. In the US and Europe we still see challenges ahead despite a return to growth in most countries; public sector deficits, the unwinding of quantitative easing and continuing difficulties in the banking sector could all lead to significant volatility and a wide range of economic outcomes. We will continue to take a measured approach in this environment with prudent gearing. However our high liquidity enables us to take advantage of the investment opportunities that this market creates.

INDUSTRY AND MARKET

The European Private Equity market has seen a significant fall off in activity. As you can see from this chart this is mainly in the buyout area and large cap deals in particular. On this chart most of the green segment relates to growth capital which didn't reach the scale of buyout investment at the height of the market and is showing faster signs of a return in activity. While there are also signs of increased buyout activity I think that the lack of debt, overhang of unspent capital and uncertain economic prospects will continue to result in activity at a level closer to the early 2000s rather than the 2005-2007 period for a number of years.

As economies return to growth and companies require working capital we expect banks will be constrained in their ability to lend. This could lead to a pronounced equity gap and significant demand for growth capital. 3i is probably the best placed Private Equity firm to take advantage of this.

Infrastructure activity has largely followed the same pattern as the Private Equity industry. A number of funds have suffered losses as a result of taking inappropriate levels of risk. 3i Infrastructure plc and the 3i India Infrastructure Fund have both invested carefully and are well capitalised and ready to take advantage of an increased deal flow as Government decisions to invest in projects result in new opportunities both in Europe and India.

3i TODAY

This slide is a reminder of the shape of 3i following the closure and disposal of QPE and our Venture Capital business. We have reduced our remaining non core portfolio which is now less than 8% of total portfolio value allowing greater focus on the core assets. In each of our core businesses our target market is unchanged and in addition we will be looking to work with portfolio companies to help them grow.

In tough markets it is easy to overlook companies that are thriving despite the conditions. Here are four examples:

GROWTH COMPANIES – EXAMPLES FROM THE PORTFOLIO
2 from our Growth portfolio, 1 Buyout and 1 Infrastructure asset.

Enterprise provides outsourced services to utilities and the public sector. It is a real UK success story; having grown 29% in the last year from a combination of new contract wins and the acquisition of a small competitor.

Quintiles – a leading US outsourced testing company serving the international pharma industry is also showing growth of 20% pa and has increased its order book by over 23%.

Labco – a French laboratory company has made 14 acquisitions since we invested in 2008, 13 of them in the last 12 months taking advantage of the economic conditions to consolidate a highly fragmented sector.

Indian based power group Adani was one of the world’s largest IPOs in 2009 as it raised further capital to finance a large expansion programme to become one of the leading power production groups in India.

Highlighting these companies leads me neatly on to the first element of 3i’s strategy.

STRATEGIC FOCUS

We are looking to invest in high return assets. By being selective, using our sector knowledge and International network we aim to find a relatively small number of great companies each year.

The other two elements of our strategy that I would like to highlight today are - we are looking to increase the assets on our balance sheet through growing the value of our existing portfolio and increasing assets we manage on behalf of others. I will talk about growing value in a few moments but I would like to reinforce a point I made back in May and that is that all our business lines will ultimately manage third party capital. Guy Zarzavatdjian has been ensuring our Growth Capital business is ready to raise third party funds at the right time.

The final point is an important priority. 3i's culture has always been strong but the number of business lines, geographies and sectors has sometimes diluted our overall impact in the market. Having simplified the business, created greater cross team working we now present a single more disciplined face to the market.

A key part of our utility to both shareholders and investors in our funds is how we generate value and this is particularly important given a key part of our returns will come from how we generate value from the £7.2 billion of assets we manage.

VALUE CREATION STRATEGY

This next slide sets out the core components of value generation through combining our premium market access with an excellent execution model and then following through with active asset management.

The combination of our international network, sector knowledge and brand enables us to see a very significant proportion of actual and potential transactions across all our business.
In the last six months we have been refining our approach and getting ready to invest. All aspects of our execution approach have been reviewed as we have sought to learn lessons both positive and negative from the last few years. The tough economic climate has reinforced the need to actively manage assets. We are making good progress and every asset in our core portfolio has been the subject of a detailed review in the last six months identifying opportunities for value enhancement as well as ensuring that companies facing difficulties have appropriate support.

While we have made a number of changes and developments in our approach – the core business model is unchanged – driving value through company performance has always been key to our success.

VALUE CREATION

As you can see from this next slide the value we have created has been mainly due to earnings growth. In Buyouts 58% and in Growth 60%. Going forward we expect to have an even greater impact on performance through our Active Partnership programme.

ACTIVE PARTNERSHIP DRIVING VALUE THROUGH PERFORMANCE IMPROVEMENT

Active Partnership is a fundamental step change in our valuation creation strategy. Essentially we have created a unique resource for our portfolio providing access to knowledge, network and experienced specialists. We are looking to do two things – firstly to identify and deliver value in key functional areas of a business through improvements and secondly to create an environment for portfolio companies to share experiences and learn from others. We are essentially asking ourselves what is the best this business could be and in essence we are taking best practice in key functional areas and delivering this across the portfolio.

There are many functional areas that we could target – so far we have focussed on: working capital management, pricing, sales force effectiveness, procurement and lean manufacturing as our key targets.

To achieve this it’s been important to engage the portfolio. We are doing this through events, in-house specialists and 3i Net a portal for our portfolio. We have already seen major benefits in individual companies but the real impact will come as economies start to recover.

POSITIONING 3i FOR THE UPTURN

This next slide sets out what we have been doing as preparation for the upturn.

We have reviewed all our recent investments to understand what worked well and where we could improve. Ian Nolan our CIO has updated and refined our investment process as a result.

We have also looked at our key portfolio companies with fresh eyes and effectively gone through a re-buying process testing whether the original investment thesis is still valid and where change is needed putting, this in place.

Equally importantly as I have already mentioned we are delivering a more consistent culture across the business – which we call one 3i.

As Stephen noted earlier costs have been reduced and we will continue to exercise discipline on costs while ensuring we have the right skills and capabilities to move forward.

We continue to emphasise our Corporate Responsibility agenda not as a token but as a way of recognising our broader social responsibility and creating an environment where our people feel proud to work for 3i. We have been working with our portfolio to ensure that they are also adopting best practice and recognise the importance of Corporate Responsibility in their long term success.

DRIVERS OF FUTURE PERFORMANCE

All of the changes we have made will strengthen the market position of 3i and improve our long term value.

In the short term however the key things that will create value are set out on this slide.

Our existing portfolio performance is key to our success – we are very pleased with the underlying market position of these companies and we expect a steady flow of realisations as well as value growth over the next few years.

If our analysis of the economic landscape is correct the next few years could offer great investment opportunities particularly in growth capital. We are ready to take advantage of this.

Portfolio growth and new investment will increase our assets under management. We will also be alert to the possibility of accelerating this but not at the expense of careful investment judgement or adding inappropriate risk to the balance sheet. We shall of course continue to keep a tight rein on costs.

CLOSING REMARKS

In closing I would like to highlight a few points. We have a strong market position and benefit from our international reach and diversity of investment style within our business lines. With our shareholders support we have transformed our financial position. We remain cautious about the economy however we are confident in the strength of our portfolio and business model 3i is ready for the upturn.

We'd now be happy to take your questions.