

Chief Executive's statement

"Continued broadening of our investment activities by geography and asset class, and a focus on delivering real value within each specific opportunity, remain critical components of our strategy."

This was a further year of good progress for the Group. The Group's financial performance was very strong, in terms of new investment and divestment activity, as well as the high level of returns achieved. At the same time we are able to report further significant progress in our strategic development, most notably in the scale up of our Infrastructure business and the launch of our QPE business line.

Further significant progress in our strategic development

The first element of our strategy is to invest in high-return assets. In this regard, total return was notable at 26.8%, a figure that was beyond our expectations at the start of the year, not least because divestment conditions remained attractive throughout the period due to favourable economic conditions and the buoyancy of debt financing markets. This figure was well ahead of last year's return of 22.5%, principally as a result of both our Buyouts and Growth Capital businesses delivering exceptional gross portfolio returns on a one year basis at 53.8% and 47.7% respectively, well ahead of our through the cycle targets and last year's equivalent figures of 29.4% and 26.4%.

These results were underpinned by a high proportion of realised profits, a consequence of a record level of realisations, which at £2.4 billion for the Group, was an improvement on last year's previous record figure of £2.2 billion. Our Venture Capital business line improved its performance in the second half, reducing its negative return to (5.6)% for the full year compared to (8.4)% for the first six months.

The next elements of our strategy are to grow our assets and those we manage on behalf of third parties, as well as to extend our international reach both directly and through investing in other funds. The amount of 3i's own investment rose from £1.1 billion to £1.6 billion, an increase of 42% on last year. This rise in new investment reflects the strategic changes of the last few years, with the most significant increases coming in Growth Capital and Infrastructure on a business line basis, and within Growth Capital in Asia on a regional basis.

Asia represented 9% of the Group's portfolio value at the end of the year, an increase over last year's 4%. Assuming no change to financial markets, we are targeting a further increase in investment levels over the new financial year, with a contribution from our QPE business line and further progress in Buyouts and Growth Capital.

As a key element of our strategy is to grow the level of third-party funds under management, it is pleasing to report that these rose by 76% last year, increasing from £1,573 million to £2,772 million. This figure includes the third-party element of our most recent buyout fund, Eurofund V, which in total closed at €5 billion, a significant increase on the €3 billion raised for Eurofund IV.

Further growth in assets under management came from the launch of 3i Infrastructure Limited, a £700 million Jersey-based listed infrastructure fund to which the Group contributed assets and cash of £325 million and third-party shareholders contributed the balance of £375 million.

The Group's strategy is to raise third-party money where structurally it is necessary to do so as in the case of Buyouts, or where it optimises our shareholders' exposure to a particular asset due to the nature of the returns, such as Infrastructure. These activities can be attractive due to the opportunity to earn management, advisory and performance fees that enhance the overall level of shareholder return. Since the end of the year we have announced the signing of a Memorandum of Understanding with IIFCL, a debt financing institution set up by the Indian Government, which will pave the way for 3i to raise a further infrastructure fund dedicated to the Indian market.

These developments are also excellent examples of the fourth part of our strategy, which is to use our balance sheet and resources to develop both existing and new business lines.

With unprecedented liquidity in financing markets, as well as continued significant change in the shape of the Group's business, **the last element of our strategy, to continue to build our strong culture of operating as one company across business lines, geographies and sectors, is critical.**

All of our senior management, and in particular our Group Partners, have made it their priority to ensure that this unique 3i culture is nurtured and strengthened, through informal and formal channels. We measure our colleagues' level of engagement on an annual basis, and the 2007 figure of 87%, together with other key performance measures, is reported on page 11 of this report to shareholders.



At a time when there is increasing debate about private equity as an asset class, with concerns being raised with respect to its stewardship, its transparency and the sources of and sustainability of returns, we have chosen to increase yet again 3i's own level of disclosure in this report to shareholders. In addition to the point by point disclosure of progress against our strategy mentioned above, we are also giving greater disclosure of the financial and business progress of key investments for each of our major business lines.

We have chosen, yet again, to increase 3i's level of disclosure

Twelve months ago we announced the intention to return some £700 million to shareholders. At the time we wanted to retain sufficient resources to grow our near-term investment levels whilst maintaining strategic flexibility as we considered the development of the Infrastructure and QPE business lines. With these two initiatives now launched, and on the back of the excellent rate of realisations over the year, it is possible to recommend a further return of cash without compromising our ambition to grow assets.

Markets remain fast-changing. On the one hand the drive by major firms to increase their deal size is expanding the definition of the mid-market, which given the international spread of 3i's network is to our advantage. On the other hand, there is an increase in the number of firms contemplating investing in the growth capital market on a trans-national basis.

Prices are generally high, and so our teams remain selective in their choice of targets, focused on identifying and then driving, with management, the underlying value of each investment in order to deliver or exceed our return targets. It is important to keep the organisation of our business flexible in order to face these markets. The formation of distinct Infrastructure and QPE business lines was consistent with our policy of building internal capabilities before building assets.

We welcome the announced and actual listings of other private equity firms, whether as management companies, or funds under management. We believe that this can only be beneficial to stock markets' understanding of both the sector generally, and their appreciation of the 3i business model in particular. Just as within the public markets there are different companies with different models, so too within private equity will the market grow to understand better that various firms have different strategies, some differentiated and others less so.

An explicit choice to work in the mid-market

3i is defined by an explicit choice to work predominantly in the mid-market, by our spread of assets over 14 countries and five different asset classes, and our desire to ensure that all of our teams nurture and value our relationships with those outside the Group in a way that delivers real benefits to the companies in which we invest.

We continue to see good investment opportunities in our chosen areas, albeit that pricing remains high. Continued broadening of our investment activities by geography and asset class, and a focus on delivering real value within each specific opportunity, remain critical components of our strategy. Although levels of realisations are expected to slow, we remain confident of reporting further good progress in the delivery of our strategy over the year ahead.

Philip Yea Chief Executive
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