



terra firma

ANNUAL REVIEW 2008

A UNIQUE PERSPECTIVE

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TERRA FIRMA AIMS TO BE THE LEADING CONTRARIAN  
INVESTMENT FIRM – RESPONSIBLY DELIVERING SUPERIOR  
RETURNS OVER THE LONG TERM







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# 1 Executive Summary



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## LETTER FROM THE CEO

I hope you will agree that our portfolio businesses have, to date, weathered the financial storm and are being managed to deliver lasting value to our investors and our key stakeholders



31 December 2008

I am delighted to present the second Annual Review of Terra Firma and its portfolio businesses.

In the time since our last Annual Review, the financial world has changed beyond recognition. Governments now own, or effectively control, many of the biggest financial institutions on the planet. Some financial groups are breaking apart, others are merging, and a few have simply ceased to exist. The dramatic worldwide decline in stock market values has destroyed more than five years of growth in the value of listed investments. Nominal stock market valuations in the UK are effectively back to those last seen in 1997, while real share values have retreated to 1993 levels. Most Western countries are now in recession, and the key question is whether this will develop into a global depression.

Over the last four years, I have expressed great concern about the state of Western economies, how leveraged they were, and about our financial systems. However, I did not foresee either the speed with which recent events would unfold or how systemic and deep the collapse would be.

During the last 10 years, unfortunately, virtually all governments, banks, consumers, commentators, economists and investors in the West adopted the same thesis justifying a belief in perpetual economic growth. There was a widespread conviction that the economic cycle had been tamed and that diversification and syndication could somehow eliminate the risk of economic bust. Meanwhile, if the West did need money, the new emerging economies of Asia and the oil rich economies of the Middle East would provide a bottomless pit which would bail the West out.

Much has been, and undoubtedly will be, written about the driving forces behind the resulting extraordinary bubble, the subsequent implosion in the financial sector, and its effect on the real economy. One of the key questions is: what were the causes behind the unprecedented levels of leverage that were allowed to build up? For Western economies, the period from 2002 through to 2008 saw many developed nations abandon sustainable fiscal rectitude for uninhibited, short-term prosperity. In the UK, regulators and shareholders acquiesced while six major banks increased their aggregate reliance on wholesale, unsecured funding from £38 billion in 2003 to £498 billion in 2008 in order to finance increasingly speculative lending.



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In retrospect, it is almost beyond belief that sophisticated, developed nations put themselves in a position where they were so dependent on foreign funding. The easing of monetary policy clearly played a major role in encouraging banks, individuals and companies to borrow as debt became cheaper than ever before. However there were, I believe, two equally important contributory factors: first, a lack of transparency; and second, inappropriate incentive schemes at many financial institutions. Leverage is particularly dangerous when it is masked in opaque structures, and many people simply did not know how dependent the Western banking systems had become upon short-term foreign funding. This danger was further compounded as many key market players had powerful incentives to keep the illusion of perpetual motion going. Across the G-7 countries, senior bank executives, economists, regulators and politicians not only loudly claimed credit for the 'new economic paradigm' but also benefited substantially from it. In reality, the 'Great Moderation' was merely a very large bubble waiting to burst.

Eighteen months ago, in order to be more like public companies, private equity in the United Kingdom was enjoined to become more open and to explain to stakeholders at large its activities and why it was beneficial to the overall economy. This initiative was entirely appropriate given that private equity firms purchase and control businesses that affect the lives of a wide range of stakeholders. Terra Firma and other private equity groups continue to work hard to improve on this front, and I hope you find this Annual Review informative. However, it is now clear that the same task should have been given to a much wider group of companies in the financial world – including those with public filing requirements. The truth is that banks and their activities, which most thought were of little interest to those outside the financial community, have been shown to be of critical importance to all.

At the very least, the boards of directors and auditors of public companies should have ensured that appropriate disclosure was provided to stakeholders. The boards of private equity-owned businesses are typically made up of people who have relevant sector expertise and therefore understand the business they are overseeing. The same cannot be said of some public companies – particularly banks – where the members of the boards uniformly have impeccable reputations and world-class connections, but often lack the expertise to oversee complex financial operations. Furthermore, going forward, we must surely increase the overall degree and clarity of information that public audited accounts provide.





I also believe we have to return to a banking system where there is a division between commercial lending banks, which take deposits and are effectively back-stopped by the Government, and investment banks, which take a variety of significant risks in pursuit of fees and quick gains. The Glass-Steagall Act was a sensible reaction to the 1930s depression, and it is a tragedy that the hubris of bankers, regulators and politicians resulted in its repeal. It needs to be reinstated globally as soon as possible, and backed by real regulatory teeth. Commercial banks must get back to what they are meant to do, while those investment banks who are entrepreneurial and inventive should continue to operate, but without a taxpayer-backed safety-net. We cannot afford a financial system where heads the investment bankers win and tails everybody loses.

Turning to compensation, better, longer-term structures, such as those that are found in private equity, would also have helped to prevent recent events. The short-term bonus culture of most financial groups meant that many senior executives were incentivised to ignore or avoid longer-term risks, whilst enjoying extraordinary short-term gains. Simple share schemes are just as dangerous as yearly cash bonuses and have, perhaps, even greater dangers as they push management teams to grow their business, year on year, regardless of the risks. In this race for wealth, again, all too many parties became complicit. Over the past several decades, government budgets – and in the US, political campaigns – have been major beneficiaries of the short-term bonus culture. As income tax revenues soared, politicians were able to fund pet projects without concern for the longer-term fiscal consequences. Now rueing their unsustainable largesse, they have become finance's harshest critics.

As I have argued publicly for several years, to be effective, incentive structures must be long term in nature, and by long term I mean at least 5-10 years. Moreover, I am a strong proponent of clear, simple, fully-understood tax and regulatory rules that encourage such forms of remuneration. In my opinion, there is no better way to nurture a good, sustainable entrepreneurial environment for business. Unfortunately, this is not what has been happening in certain Western countries, in particular the UK, where the ever-increasing complexity and level of tax has resulted in non-economic actions and inefficiencies.

All of the employees of Terra Firma know that their rewards depend on the longer-term performance that our portfolio businesses deliver to our investors. The operational performance of our portfolio has been strong,





but the investment climate has been harsh on the valuations of our businesses. As a result, Terra Firma will in March distribute back to investors the carried interest (payments for strong investment performance) that had previously been earned (accrued in escrow, but not paid) and which would have formed the bulk of the reward for Terra Firma's senior team's hard work since 2004. This is absolutely right; our investors have suffered and therefore our rewards should suffer at the same time. Such longer-term rewards throughout the entire financial system would have led to a very different world to the one we find ourselves in today.

In the current climate, private equity groups must focus more than ever on ensuring their businesses are operationally robust in order to generate returns for their investors. This emphasis on operations will mean that private equity will continue to help the economy and will be one of the forces that help us recover from the current troubles. At Terra Firma, we have always considered this one of our key strengths and, as you review the performance of our portfolio companies, I hope you will agree that they have, to date, weathered the financial storm, and are being managed to deliver lasting value to our investors and our key stakeholders. We are exceedingly fortunate in having approximately 50% of TFCP III still to invest and investing over the next two years will, I believe, provide some quite incredible opportunities for success and enable TFCP III to return a substantial profit to our investors.

Finally, as someone who believes that there is virtually nothing new in human behaviour, the following quote by Abraham Lincoln seems rather poignant:

**"As an individual who undertakes to live by borrowing, soon finds his original means devoured by interest, and next, no one left to borrow from, so must it be with a government."**

Abraham Lincoln

Best wishes

Guy Hands

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## ABOUT TERRA FIRMA<sup>1,2</sup>

TERRA FIRMA INVESTS IN LARGE, ASSET-BACKED AND COMPLEX BUSINESSES THAT HAVE BEEN OVERLOOKED, UNDER-VALUED OR MISUNDERSTOOD BY THE FINANCIAL COMMUNITY

**These portfolio businesses are then nurtured to a higher level of performance through a combination of strategic change, sustained investment and improved management. In the current environment, we also seek to help companies with some of their funding and liquidity issues.**

We add value through involving ourselves directly in the companies we buy. Working alongside management, we overhaul the business both strategically and operationally. This often involves introducing new initiatives, processes and procedures in order to change the behaviour and culture of a company. This type of change takes time, but a long-term approach to investment is vital in

order to create successful, sustainable businesses. These revitalised companies are later sold to realise a return for the investors in Terra Firma's funds.

Since its launch in 1994, Terra Firma has invested approximately €11 billion of equity capital and has completed investments with an aggregate transaction value of €42 billion.

<sup>1</sup> A reference to 'Terra Firma' means, prior to 27 March 2002, the Principal Finance Group of Nomura International plc and post 27 March 2002, as the context requires, TFCP Holdings Limited, Terra Firma Capital Partners Limited, Annington Management Services (Guernsey) Limited and any of their affiliates.

<sup>2</sup> The information contained in this Annual Review is as of 31 December, 2008





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**€16 billion**  
of equity raised

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**€11 billion**  
invested

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**€42 billion**  
enterprise value of  
investments made

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## ABOUT TERRA FIRMA

An opportunity for our stakeholders to understand our intentions, plans and results

### OUR INVESTORS

We invest on behalf of pension funds, insurance companies, sovereign wealth funds and endowments from around the world. Our largest investors are pension funds – investing on behalf of today's pensioners and the pensioners of the future. The success of Terra Firma's businesses helps to provide improved and more secure retirement income for pensioners and our other investors. Clearly, the current decline in asset values is greatly troubling to all investors and Terra Firma is committed to delivering as strong a performance as possible.

### OUR STRUCTURE

Terra Firma's funds are typically Guernsey Limited Partnerships. Its active funds are Terra Firma Capital Partners II (TFCP II), Terra Firma Capital Partners III (TFCP III) and Terra Firma Deutsche Annington (TFDA). Terra Firma's investors invest as Limited Partners and the day-to-day affairs of each partnership are managed by its General Partner in Guernsey. The General Partners make all investment decisions on behalf of the funds.

Terra Firma Capital Partners Ltd (TFCPL) in the UK, with support from terrafirma GmbH in Germany, provides investment advice to the General

Partners, including sourcing and advising on investment opportunities and realisation strategies.

Terra Firma's funds make investments in selected businesses across the world, but with a particular focus on Europe. These portfolio businesses currently operate in over 60 countries globally.

### OUR PEOPLE

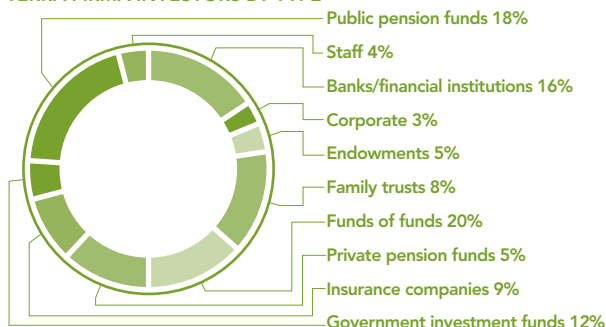
Terra Firma has developed the full range of financial skills, strategic insights and operational expertise to pursue a differentiated investment strategy. The highly diverse knowledge base of the group allows Terra Firma to spot opportunities that are missed by others and to carry out many different types of investment.

Operational expertise is fundamental to enhancing value within our

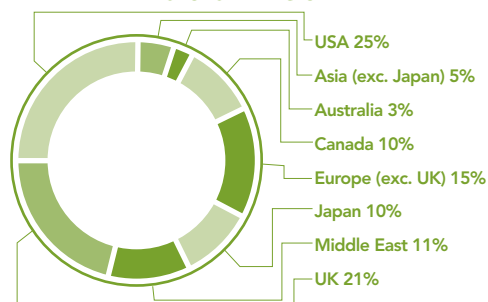
portfolio businesses and in the current economic climate such skills are more important than ever. Our operational team has many years' experience in running and improving performance in numerous businesses and has strong strategic, operational and managerial expertise. Financial expertise is also of huge importance at the current time and Terra Firma's personnel have a wealth of these skills, particularly with regards to helping companies with some of their funding and liquidity issues.

The Terra Firma advisory team is made up of around 100 people in London and Frankfurt, drawn from 20 countries and speaking 28 languages. They come from a wide variety of backgrounds, including industry, finance, consultancy, private equity, law and accountancy.

#### TERRA FIRMA INVESTORS BY TYPE



#### TERRA FIRMA INVESTORS BY REGION



A LONG-TERM APPROACH TO INVESTMENT IS VITAL IN ORDER TO CREATE SUCCESSFUL, SUSTAINABLE BUSINESSES



## SINCE 1994:

- €16 BILLION OF EQUITY FUNDS HAVE BEEN RAISED TO IMPLEMENT TERRA FIRMA'S INVESTMENT STRATEGY
- €11 BILLION OF EQUITY CAPITAL HAS BEEN INVESTED IN OUT-OF-FAVOUR BUSINESSES ACROSS A VARIETY OF SECTORS AROUND THE WORLD
- €42 BILLION IS THE TOTAL ENTERPRISE VALUE OF INVESTMENTS MADE
- OUR FUNDS HAVE DOUBLED THE MONEY THEY HAVE INVESTED. IN OUR VIEW, IT IS THIS LONG-TERM GENERATION OF PROFIT FOR OUR INVESTORS WHICH IS KEY, NOT THE ANNUAL MARKING TO MARKET OF OUR INVESTMENT HOLDINGS
- TERRA FIRMA HAS HELD ITS INVESTMENTS FOR ALMOST FIVE YEARS ON AVERAGE, WHICH IS FAR LONGER THAN THE AVERAGE HOLD PERIOD FOR PUBLIC COMPANY STOCK HELD BY UK INSTITUTIONAL INVESTORS. GOING FORWARD, TERRA FIRMA WOULD EXPECT THIS HOLDING PERIOD TO INCREASE AS IT SUPPORTS ITS PORTFOLIO BUSINESSES IN THE DIFFICULT PREVAILING ECONOMIC CLIMATE

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## REVIEW AND HIGHLIGHTS OF 2008

Despite tough conditions, Terra Firma's businesses continued to perform well in 2008 and have clear plans to sustain their performance in 2009

**The last year has been a difficult one for private equity. Obtaining third party debt to finance new investments has been virtually impossible, valuations have fallen and the returns on many of the investments that were made in 2006 and 2007 – the top of the market – will be much lower than the historical norms for private equity.**

We chose not to invest in any new businesses in 2008 and feel that 2009 will present better opportunities for investing. We have not been idle, however. This year, our focus has been on protecting the value in our existing portfolio and ensuring that

our portfolio businesses are resilient and robust enough to survive the current downturn and handle the more difficult operating environment which now exists.

The recent challenging conditions have taught us numerous lessons and forced us to create new solutions. As a business, we are extremely self-critical and we are not afraid to take difficult decisions.

### EBITDA BY PORTFOLIO BUSINESS

	Currency	2007	2008	Change %
Annington <sup>1</sup>	£m	145	99	-32%
AWAS <sup>2</sup>	\$m	523	698	n/a
DAIG	€m	435	466	7%
EMI <sup>1</sup>	£m	90	221	146%
Infinis	£m	53	54	3%
Odeon/UCI	£m	73	72	-1%
PNG	£m	29	30	3%
Tank & Rast	€m	180	188	4%

<sup>1</sup> Based on 9 months to December 07 and December 08

<sup>2</sup> Pegasus Aviation's results are included in 2007 from 14 June 2007





## OPERATING PERFORMANCE

Despite tough conditions, Terra Firma's businesses continued to perform well in 2008. They undertook approximately €540 million of capital expenditure during the year and have clear plans to sustain their performance in 2009:

### ANNINGTON

Annington reported higher rental revenue in year-to-date December 2008 compared with the same period the previous year. While rents make up approximately two thirds of business revenue, development sales which make up the remainder, have fallen substantially. This is reflected in a decline in EBITDA. As expected, sales volumes were behind comparable volumes in 2007, reflecting the prevailing UK housing market conditions. Sales, however, are not a critical component of Annington's revenue stream as its rental income is sufficient to cover its debt obligations and to enable Annington to take advantage of any future acquisition opportunities.

### AWAS

AWAS concluded a very challenging year with earnings broadly in line with budget. The business was able to avoid major customer defaults by proactively managing high-risk customers and will continue to do so going forward. Despite lower jet fuel costs, 2009 is likely to be a difficult trading environment for airlines as passenger traffic slows due to reduced GDP growth. However, AWAS sees a number of opportunities to take advantage of the soft market to grow the business through accretive acquisitions which will develop the business strategically.

### DEUTSCHE ANNINGTON

Earnings from both Deutsche Annington's rental and sales businesses were ahead of those from 2007. Furthermore, the overall vacancy rate showed a marked improvement, ending the year at 3.9% compared with 4.2% at the end of 2007. DAIG stepped up its expenditure on maintenance and modernisation in 2008 and as a result, €185 million has been earmarked to improve and maintain the homes in its portfolio.

### EMI

EMI has seen improved results at both its Recorded Music and Music Publishing businesses. In the year-to-date, earnings of Recorded Music have improved on the prior year due to the significant progress that has been made in cutting costs and introducing a new, more commercial culture to the business. Music Publishing delivered solid results as it pursues its long-term strategy of actively developing new markets and licence types for the commercial usage of music.

### INFINIS

Infinis recorded year-end earnings in excess of budget and prior year. The outlook for 2009 is positive, with additional generating capacity expected to be installed during the year. The company is substantially contracted for power sales in 2009 which were agreed at a healthy level – and it has a strong contract position with regard to prices for 2010 and 2011.

### ODEON/UCI

Odeon/UCI has continued to open and acquire new sites and roll-out 3D screens in order to benefit from the attractive 3D film slate. It continues to invest in successful retail initiatives and premium seating both in the UK and Europe. Overall, the business had a slightly softer year in 2008, primarily due to the need to change its screen advertising arrangements in the UK and the deferral of a major blockbuster film until 2009; but on a like-for-like basis, film revenue and EBITDA in 2008 were ahead of prior year. The business expects a stronger year in 2009 as a result of a good film slate, the contribution from further new cinemas and retail improvements.

### PNG

PNG also performed well in 2008, with results ahead of budget and prior year. In March 2008, PNG sold its transmission business to Northern Ireland Energy Holdings Ltd, using the proceeds of £99 million to pay down debt. PNG continued to grow its gas network and customer base during the year.

### TANK & RAST

In a challenging economic environment, Tank & Rast outperformed 2007's results. Despite high fuel prices for most of 2008 and the German economic downturn, revenue and earnings grew, driven by the performance of capital investment projects. The business expects some further improvements heading into 2009 generated by the implementation of its key growth initiatives including the roll-out of its fast food and other consumer-driven projects. ➤

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THE BUSINESSES  
ARE WELL-  
SUPPORTED WITH  
LONG-TERM  
FINANCING IN  
PLACE AND ARE  
WELL-POSITIONED  
TO CONTINUE  
TO OPERATE IN  
THE CURRENT  
ENVIRONMENT

14,000  
people employed in our portfolio businesses

€540m  
capital investment undertaken by our portfolio businesses



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### FINANCIAL POSITION

In what remains a liquidity-constrained environment, the Terra Firma portfolio businesses do not have significant refinancing needs in 2009. The businesses are well-supported with long-term financing in place and are well positioned to continue to operate in the current environment.

### VALUATIONS

We believe private equity firms must be realistic and transparent about valuing their businesses, even though some may argue that the only important valuation is the one attained when a business is ultimately sold. Terra Firma was therefore one of the first private equity firms to significantly revise its valuations to reflect this new market. We engaged in a thorough and detailed review of the valuations of Terra Firma's portfolio businesses and had those processes audited by KPMG.



Private equity valuations have two major elements: the operating performance of the portfolio business itself and the application of some multiple or discount rate from listed comparable companies or recent transactions to value that operating performance. As we have seen, the performance of Terra Firma's portfolio businesses in 2008 has continued to be strong with most showing year-on-year improvement. However, the valuations of public companies across all sectors have plummeted and, for private equity, this decline is magnified by the higher levels of leverage. Furthermore, in some of Terra Firma's businesses the continuing decline of Sterling against the Euro has reduced valuations in Euro terms, especially at EMI. While we are all working hard to ensure that the final performances of these investments are positive ones, we must be open and realistic about where the markets stand today and not take credit now for potential future improvements in earnings or market conditions.

Therefore, the General Partners have taken the view that if current market conditions were to continue, the funds may not recover the full value of their 2007 investments, and have therefore taken a provision for impairment in their results for 2008. Whilst indeed they could make a partial or indeed a full recovery in the future, the Directors of the General Partners believe that given the current world economic situation, this is a prudent position to take in terms of the long-term view of market recovery (see Profit and Loss Statement on page 103).



## PLAYING OUR PART IN THE ECONOMIC RECOVERY

**As long-term investors, private equity can help to restore economic health through improved operations and enhanced productivity**

**If private equity firms focus on investing where they can deliver fundamental change to businesses and improve their operations, then they can play a key role in helping to kick-start economic recovery.**

The rapid deterioration of the economic climate has forced companies, large and small, to re-examine their business models. Optimistic, sometimes aggressive, assumptions about consumer demand and credit availability are yielding to tougher realities. In such an environment, experienced management, committed owners and access to new capital are critical. Fundamentally, this is what private equity provides.

Terra Firma adds value through involving ourselves directly in the companies we buy. Working alongside management, we overhaul the business both strategically and operationally. This often involves introducing new initiatives, processes and procedures in order to change the behaviour and culture of a company. This type of change takes time, but a long-term approach to investment is vital in

order to create successful, sustainable businesses. Furthermore, we have the financial expertise to help companies with some of their funding and liquidity issues. All our management teams' incentives are contingent on the delivery of long-term, sustainable growth, in contrast to the focus on short-term rewards that have contributed to the economic crisis. As long-term investors, private equity can help to restore economic health through improved operations and enhanced productivity.

There are now specific proposals for European legislation which covers both disclosure and regulatory elements for hedge funds and private equity firms. The European Venture Capital Association estimates that in Europe alone, private equity firms still have over €75 billion to invest – capital that will rescue the fortunes of thousands of businesses across the continent. We trust that the urgent and necessary reforms needed to regulate and demystify banks, hedge funds and other complex institutions will not inadvertently stifle private equity firms' ability to invest this much-needed capital in Europe's economy.

**WORKING  
ALONGSIDE  
MANAGEMENT,  
WE OVERHAUL THE  
BUSINESS BOTH  
STRATEGICALLY AND  
OPERATIONALLY**

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## LONG-TERM ALIGNMENT

To be effective, incentive structures must be long term in nature

**The long-term nature of private equity is reflected in its reward structure. The long-term alignment of interest between investor and employee is of the utmost importance not only for private equity, but also for the stability of world financial markets.**

Whilst not perfect, private equity reward structures mean that value must be delivered over a long-term period and are far superior to the ritualised culture of annual bonuses. By way of example, in March, Terra Firma will distribute back to investors the carried interest (payments for strong investment performance) that had previously been earned (accrued in escrow, but not paid) and which would have formed the bulk of the reward for Terra Firma's senior team. If our investors suffer, then it is only right that the Terra Firma team's rewards should suffer at the same time. The future stability of the financial markets would be enhanced if other parts of the financial community adopted such long-term incentive practices.

Carried interest is performance-based and only results in enhanced returns for the Terra Firma team if investors receive a return in excess of 8% per annum over the life of the fund. A fund typically has a 10-14 year life and carried interest is typically paid in the later years when the majority of a fund's investments have been realised and investors have received back their investment plus the majority of their profits.



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## TRANSPARENCY AND DISCLOSURE

**Broadening the understanding of who we are and what we do is even more important in the current climate**

**Information is vital, particularly in times of economic strife, so broadening the understanding of who we are and what we do is even more important in the current climate.**

The businesses Terra Firma invests in touch the lives of many people and we are mindful of the social responsibilities that our work brings with it. It is essential that all our stakeholders – customers, employees, investors, suppliers, unions, governments and trade bodies – understand our intentions, plans and results, and how our activities and portfolio businesses contribute to the wider community.

We welcomed the publication of the Walker Report in the UK in November 2007 and are very positive about both the initial public response to our efforts, and the ongoing work to make

private equity even better understood by its stakeholders.

We remain committed to following – and in many areas, exceeding – the Walker guidelines. All our portfolio businesses have produced Annual and Interim Reports, even though the only one that was required to do so was Odeon/UCI. Our Irish and German portfolio businesses, AWAS, Tank & Rast and Deutsche Annington, also produced Annual Reports last year and Germany has since followed suit with its own voluntary disclosure code. Deutsche Annington and Tank & Rast are also fully compliant with these new German guidelines.

However, our approach to transparency is not entirely altruistic. We take the view that a progressive approach to transparency gives us a competitive advantage by making us more attractive to potential staff, to



**THE BUSINESSES  
TERRA FIRMA  
INVESTS IN TOUCH  
THE LIVES OF MANY  
PEOPLE AND WE  
ARE MINDFUL  
OF THE SOCIAL  
RESPONSIBILITIES  
THAT OUR WORK  
BRINGS WITH IT**



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companies that we wish to invest in, and to governments and unions with whom we co-operate. Of course, our investors, importantly, provide the capital that we invest in businesses, and the financial workings of our businesses have always been entirely visible to them. However, even this group is beginning to use broader transparency as a benchmark for whether or not they invest with a given private equity firm.

There is a real debate in Brussels as to whether private equity disclosures should be regulated at European level. Our concern is that attempts to regulate public disclosures for private equity investment will stifle this competitive tension if disclosure requirements are based on mandatory and rigid rules designed for complex financial institutions like hedge funds. For evidence of this, one only has to look at public company

reporting, which is so rule-driven and bureaucratic that it has been rendered meaningless and as a consequence is increasingly mistrusted. In the case of banks, all of the largest of which are publicly-listed, this has had catastrophic consequences.

There is a template for success. The Walker initiative in the UK has been very well received and the German and Scandinavian initiatives have been great steps forward. The support of European governments, the European Commission and the European Parliament would be welcomed to see this approach succeed throughout Europe.



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## OUTLOOK FOR 2009

**We believe that we will start to enter an environment which will offer value that has not been seen in the private equity arena in years**

**As the world struggles through the most challenging economic crisis in over 70 years, private equity faces severely challenging times. The current lack of finance for any investing means that the absolute amounts allocated to private equity will decline considerably for the next few years. Combined with the lack of debt for private equity-backed companies, this will mean that both the scale of private equity investments and the industry itself will shrink materially.**

However, for long-term investors with a secure capital base, we believe significant opportunities do exist. After a long pause throughout 2008, sellers are beginning to become more realistic and pricing now increasingly reflects the liquidity needs of vendors. Almost no business is 'recession proof', but those businesses which cater to basic

needs and are underpinned by real assets are, in our view, at the lower end of the risk spectrum. All businesses will face operational difficulties in the upcoming years and how management deals with these challenges will be fundamental to generating or maintaining value within portfolio businesses.

We are seeing opportunities to invest in businesses that are operationally sound, but which have financial challenges due to their level of debt. Terra Firma has a great deal of experience in dealing with such difficulties and therefore many of these businesses represent attractive investment opportunities.

In addition, given the huge mark-downs in valuations that are occurring, it is more likely that Terra Firma can find opportunities where the



**BOTH THE SCALE  
OF PRIVATE EQUITY  
INVESTMENTS AND  
THE INDUSTRY  
ITSELF WILL SHRINK  
MATERIALLY**



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true valuation and potential of the businesses are being overlooked. In these situations, Terra Firma's contrarian investment approach and ability to utilise its skills and resources to build value in businesses over the long term can potentially deliver strong results.

We believe that the number of investment opportunities in 2009 and 2010 will continue to be low and that the number of investments completed will be small. Holding periods for investments made during this period are also likely to be longer than in recent years. During the course of 2010, we expect the market to improve and become more predictable and that we will start to enter an environment which will offer value that has not been seen in the private equity arena in years.



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## 2 Portfolio Business Review

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## INTRODUCTION

TERRA FIRMA'S INVESTORS PROVIDE CAPITAL WHICH IS USED TO ACQUIRE AND INVEST IN UNDERPERFORMING BUSINESSES. YET CREATING VALUE IN THOSE BUSINESSES REQUIRES MUCH MORE THAN CASH; IT DEMANDS ENERGY, STRATEGY AND LONG-TERM COMMITMENT

**While shareholders in public companies can sell their shares on a daily basis and rarely hold them longer than several months, Terra Firma's investors commit their capital for over 10 years. Every business we invest in has this stable, ongoing backing. We work this way because we recognise that both time and commitment are vital to deliver fundamental change and long-term success in the kind of out-of-favour companies we acquire.**

## STRATEGIC CHANGE

Once acquired, Terra Firma's portfolio businesses are nurtured to a higher level of performance through a combination of strategic change, improved management and sustained investment. This transition requires an intense, ongoing and long-term partnership between Terra Firma and the management of each

portfolio business. As part of that, all Terra Firma's employees invest their own money in each fund, so their personal, professional and financial success is tied to the success of our portfolio businesses. Similarly, the management of our businesses, often selected from different industries to bring fresh thinking to a sector, is motivated to succeed and is compensated based on the long-term success of each business. This alignment of interest is fundamental to the way Terra Firma does business.

It is perhaps no surprise that Terra Firma people and our management teams are passionate – even a little obsessive – about our businesses. The next few pages give an overview of our portfolio businesses and how we are working together to create a successful, sustainable future.

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## PORTFOLIO BUSINESSES



UK residential housing  
sales & rental



UK renewable  
energy



Worldwide aircraft  
leasing



Pan-European cinema  
operator



German residential  
housing sales & rental



Northern Ireland natural  
gas distribution and supply



Global music publishing  
and recorded music



German autobahn services

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Photo: Jeff Brantner



## ANNINGTON



# ANNINGTON IS A HOUSING BUSINESS THAT ACQUIRED AROUND 57,600 HOMES IN ENGLAND AND WALES FROM THE UK'S MINISTRY OF DEFENCE

Annington rents the majority of its properties to the Ministry of Defence (MoD) to provide family accommodation for married service personnel. The MoD has the responsibility for maintenance and upkeep of the properties it leases. As and when the MoD determines that vacant properties are surplus to requirements, given the constraints of planning for future troop redeployments, it returns surplus properties to Annington. Annington then renovates and sells these houses to the public, including current and ex-service personnel, at competitive prices. Annington also privately rents a number of properties and occasionally redevelops sites or builds new homes

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**60%** of total homes sold have been to first-time buyers

**35%** of total homes sold have been to key workers

**£164,053** average sales price in 2008



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## ANNINGTON



## ANNINGTON'S HOMES HAVE PROVED POPULAR WITH THE PUBLIC BECAUSE IT HAS FOCUSED ON CREATING ENVIRONMENTS WHERE PEOPLE WANT TO LIVE

### INVESTMENT RATIONALE

Following detailed due diligence of the UK residential housing market, Terra Firma believed that rent and house price increases would substantially exceed the forecasts at the time of the acquisition. Based on detailed analysis of demographic, military and political trends, it looked likely that the MoD would release surplus properties for redevelopment and sale earlier than it had agreed at the time of acquisition.

Predicting that more cash would be generated more quickly than many other bidders were expecting, Terra Firma ensured this was reflected in the price it paid to the MoD. It was also clear that the rental cash flow from the estate, along with proceeds from the future sale of properties, could be securitised to help fund the initial investment in the portfolio.

### CHALLENGES FACED

The biggest single challenge facing Annington at the moment is clearly the housing market. Operating predominantly at the first-time buyer end of the market, the company saw sales all but evaporate during 2008 as mortgage availability dried up. House

prices in the United Kingdom fell by an average of more than 16% in 2008 with forecasts of a further 10%–15% decline through 2009 and into 2010. Sales, however, are not a critical component of Annington's revenue stream as its rental income is sufficient to cover its debt obligations and to enable it to take advantage of any future acquisition opportunities.

Another challenge facing Annington relates to the release of surplus properties from the MoD. Annington has no control over the timing of the release of properties as the MoD's housing requirement is dependent on the long-term defence strategy which dictates troop movements and deployments. With the wars in Iraq, Afghanistan and a number of other commitments abroad, management of housing requirements has become even more complicated for the MoD. Once Annington is notified of the release of surplus properties, it has to respond quickly so that sites are not left vacant or unoccupied and they can be prepared for sale.

Historically, Annington's primary business has been the refurbishment and sale of previously-owned homes. ➤

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YEAR END: 31 MARCH	YTD Dec 07	YTD Dec 08
Rental business revenue	£116m	£123m
Sales business revenue	£68m	£20m
Income from investments	£44m	£1m
Costs	(£83m)	(£45m)
<b>EBITDA</b>	<b>£145m</b>	<b>£99m</b>
Bank interest	(£116m)	(£112m)
<b>Earnings/(loss) before depreciation and tax</b>	<b>£29m</b>	<b>(£13m)</b>
Capital expenditure	(£74m)	(£37m)
Private units sold	299	110
Development sales units sold	225	0
Average sales price per unit	£129,624	£167,317

The significant deterioration in the UK housing market, both in terms of volumes and prices, has been mitigated by the stable rental income the business receives matched to its long-term financing structure. Annington remains well positioned with a flexible business model that has allowed it to minimise the impact of the current market difficulties.

### ACHIEVEMENTS

One of Annington's key strengths has been the efficiency of its sales operation. Since 1996, the MoD has returned 16,397 units to Annington, of which more than 15,600 have now been sold to the public. In normal market conditions, Annington attracts first-time buyers with pricing that makes mortgage payments comparable to rental payments. Together with the use of various financial incentives, it aims to make home-buying a realistic option for those who have previously been priced out of the UK's property market. On average, more than 60% of those buying an Annington home have been first-time buyers and 30% have been sold to Service or ex-Service personnel. On average, 35% of properties have been sold

to people who the UK Government classifies as 'key workers'.

Another reason Annington's homes have proved so popular with the public is that it has also focused on creating environments where people will want to live. Wherever possible, the 'street scene' is improved, from planting new landscaping to changing the external appearance of a property.

Annington had predicted the end of the housing boom for some time and has spent the past three years rationalising the business in readiness for falling release numbers and the anticipated decline in sales levels. Annington's operating model was based on a small core team using outsourcing as a major tool so a major restructuring exercise has not been necessary, although some level of downsizing has occurred. Staff numbers and operating structures have been reduced over the last three to four years through gradual cuts and natural wastage. These combined actions meant that adapting to the current environment has been a lot less painful for Annington than for many in the property sector.

Given the turmoil in the housing market in recent months and the downturn in house sales across the UK, Annington is expected to weather the storm better than its peers. From January 2008, Annington had reached a point where it was no longer reliant on house sales for cash flow to service its loans.

### CURRENT FINANCIALS

For the 9 months to December 2008, Annington reported rental revenue of £123 million and sold 110 units which generated a further £20 million of sales revenue. Sales volumes were below budget and behind comparable volumes in 2007, reflecting the prevailing UK housing market conditions. However, sales stocks did not rise significantly due to continued low levels of releases from the MoD.

The business continues with a strong balance sheet which should enable it to take advantage of selective opportunities in the current market. Current debt servicing obligations can now be met by rental cash flows so the business is not dependent on sales volumes. With its long-term financing structure in place, the business has no new near-term funding requirements. ➤

## DEVELOPMENT PLAN

In the current climate, Annington will continue to manage its business tightly. Stock levels are low, but it will continue to refurbish and sell available properties to reduce its debt levels as appropriate.

The robustness of its rental income will enable Annington to adapt to the new economic environment, which itself may afford the business some future opportunities allowing complementary investments at attractive valuations. The business continues to selectively build its investment portfolio of residential rental units acquiring properties that exceed threshold return criteria. Annington is also keen to work with the MoD to find creative solutions to its housing challenges.

## COMPANY STRUCTURE

Annington Homes manages the core business of renting 41,000 properties to the MoD and the refurbishment and sale of homes on the open market. Since 1996, Annington has sold more than 15,600 properties to the public. Annington Rental Holdings owns 1,404 flats and houses let on individual and bulk leases on the open market. It manages a further 359 properties on behalf of other Group companies. Annington Developments seeks opportunities for infill or wholesale re-development on all Annington sites. The business's priority is to maximise added value through obtaining planning consent and then either to sell the land, carry out infrastructure works, carry out construction or partner with developers.

## MANAGEMENT

### James Hopkins, Chief Executive Officer

James joined Annington Homes Ltd as Chief Executive in 1998. Prior to joining Annington, James was Managing Director of Hanson Land Ltd, a property development and management company established to undertake the £1 billion Hampton 'new town' development south of Peterborough. James was previously at Hanson plc, where he performed a number of roles involving asset management and property development, including directorships of both subsidiary and joint venture companies.

### Barry Chambers, Finance Director

Barry was appointed Finance Director of Annington Holdings plc and other Annington group companies in 1998. His responsibilities span all financial matters, liaising with shareholders, IT systems development, administration and rent reviews. Barry joined Annington from Rouse Kent Ltd, a special purpose vehicle established to construct a large mixed-use development on 650 acres at Kings Hill, Kent. Prior to that, he was Group Financial Controller at Rosehaugh plc.

### Nick Vaughan, Commercial Director

Nick joined Annington Property Ltd as Commercial Director in January 2001 and was appointed to the Annington Holdings plc Board in April 2001. Previously, Nick was Financial Analyst and Programme Manager at Annington Management Ltd. He joined from Rosehaugh plc, where he was Finance Director of a number of group companies.

## FORWARD THINKING IN THE OFFICE AND IN THE COMMUNITY

**As long ago as 2005, Annington was predicting that the housing boom would turn into a housing bust. Through the rising market, Annington was able to structure its finances for the long term. Despite the weakening market, the business is now in a robust position as it no longer needs to rely on sales of houses to service its debt and has cash on its balance sheet.**

This action meant that the company was positioned not just to weather a widespread economic downturn, but to seize the opportunities that come with a falling market. With the recession continuing to deepen, Annington has costs under control. It is forecasting cash surpluses in every financial quarter over the next five years, which will help to significantly repay current debt still further.

Some moderate diversification has also been a factor in Annington's continuing success, with selective investment in its rental portfolio. The business has taken advantage of strong running yields that have been underpinned in an area of the property market where demand is outstripping supply.

The plan for the future is equally measured. The next year will be a time to focus on managing costs, continually reviewing the business and taking advantage of the opportunities to purchase properties for rental.

Against the backdrop of a turbulent marketplace, Annington has also kept up its good work outside the office. The business remains committed to being as much a part of the local



community as the properties it owns. The Annington Trust was set up in 1996 to support projects benefiting Service families. Grants range from a few hundred pounds to a few thousand and can be used to fund anything from toddler groups to summer youth camps or welfare staff training. An example in 2008 was a grant of £2,500 in support of 'Storybook Soldiers', an innovative project allowing Service personnel to record stories for their children before being deployed abroad on active service.

Annington, as a company, also supports the local communities in which it is working. One of 2008's grants, for example, was used to help Hemswell Cliff Pre-School move to a new site from the former RAF community centre. A £2,000 donation paid for a much-needed new cabin where the pre-school equipment could be stored.

Whether in the business world or in its community work, Annington is an organisation with a clear vision of what it wants to achieve. Forward-planning and the energy of its people have ensured that, whatever it sets out to do and whatever the challenges along the way, it is getting results.



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## AWAS



# AWAS IS ONE OF THE WORLD'S LEADING AIRCRAFT LEASING COMPANIES

AWAS was acquired by Terra Firma in 2006 and followed by the 2007 acquisition of Pegasus Aircraft Finance Company. Following last year's order of new aircraft, the combined business now has over 210 owned aircraft and a delivery pipeline of more than 130 aircraft

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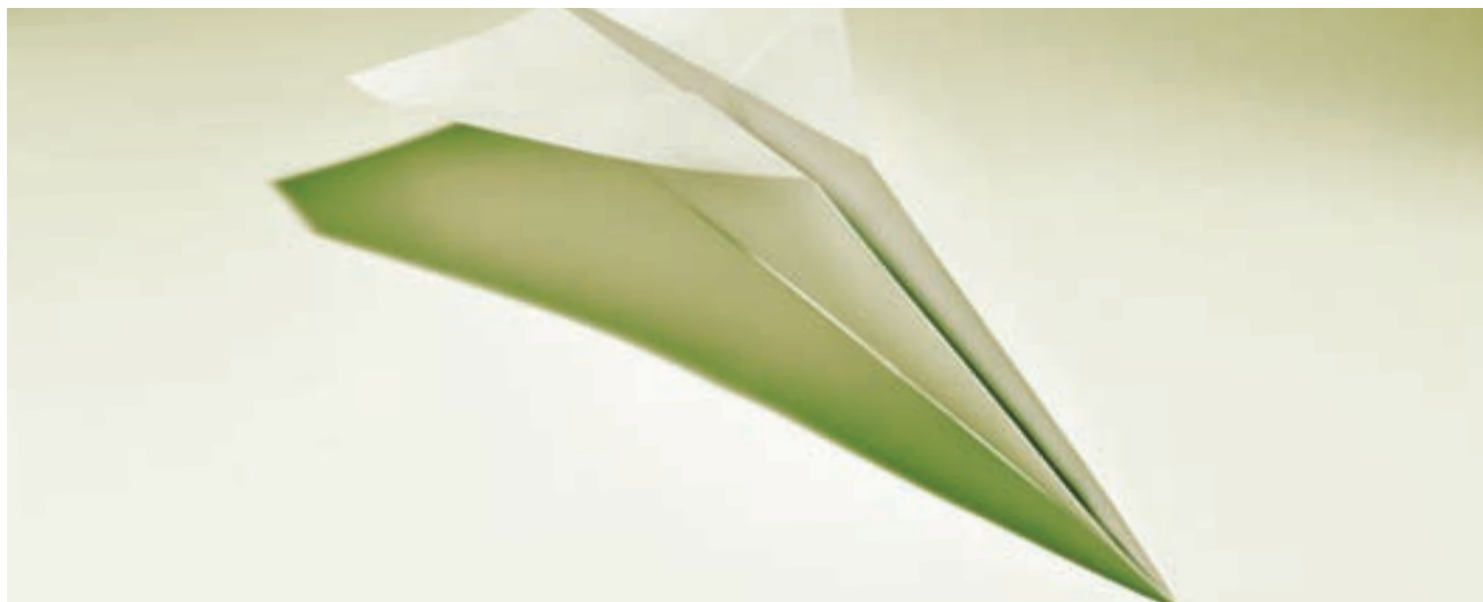


**\$5 billion** owned aircraft asset value

**8 years** average age of the fleet

**4.4 years** average lease expiry

## AWAS



## AWAS HAS BEEN REPOSITIONED TO FOCUS ON MAXIMISING RETURNS AND MANAGING RISK THROUGH A COMBINATION OF BOTH AIRCRAFT LEASING AND TRADING

### INVESTMENT RATIONALE & REDEFINITION OF STRATEGY

The combination of AWAS and Pegasus created a market leader with a highly distinctive strategy. That strategy is to drive superior rental yields on an aircraft portfolio that is highly diversified by vintage, aircraft type and lessor quality, and to maximise residual asset value through a leading asset trading capability.

AWAS has been repositioned to pursue a differentiated strategy within the aircraft leasing market, focusing on maximising returns and managing risk through a combination of both aircraft leasing and trading. This strategy is highly distinctive as it places a heavy emphasis on a rigorous, investment-led approach to all leasing and asset trading decisions with an emphasis on return on invested capital. This is complemented by proactive asset trading based on a proprietary and differentiated view of prospective movements in the aircraft cycle and also on the credit and equity capital markets. AWAS takes a measured approach to risk-taking and prices each transaction at a level which offers an appropriate balance between risk and return.

The investments in AWAS and Pegasus involved a high degree of operational change. With AWAS, that change was heavily focused on centralising the business in Dublin and significantly increasing the operational efficiency of the business. The acquisition of Pegasus posed the different, but equally challenging, operational task of integrating a business of equivalent size and taking advantage of the synergies to reduce costs in as short a timescale as possible.

### ACHIEVEMENTS

From an operational perspective, the rationalisation of the AWAS business was completed within 12 months of acquisition. The subsequent merger with Pegasus released significant synergies and the integration was managed to ensure that the 'best of both' businesses was retained within the combined entity. As a consequence of the improved operational efficiencies in the business, it has been possible to materially increase assets under management. The integration of AWAS and Pegasus was completed early in 2008 ahead of budget and has generated cost savings ahead of plan.

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YEAR END: 30 NOVEMBER	2007 <sup>1</sup>	2008 <sup>2</sup>
Revenue	\$591m	\$781m
Costs	(\$68m)	(\$83m)
<b>EBITDA</b>	<b>\$523m</b>	<b>\$698m</b>
Bank interest	(\$240m)	(\$287m)
<b>Earnings before depreciation and tax</b>	<b>\$283m</b>	<b>\$411m</b>

1 Pegasus Aviation's results are included in 2007 from 14 June  
2 2008 results are subject to final audit approval

Terra Firma has focused on improving the overall quality of the management of the business. Under Terra Firma's ownership, there have been new appointments to the position of CEO, CFO and Head of Sales, as well as the creation of new positions and functions reflecting the dramatically increased emphasis placed on investment analysis and the management of credit risk. As the business gears up for the next phase of development and management in the context of dramatically changed financial and asset markets, there will be continued emphasis placed on ongoing improvement of the management team and business processes.

AWAS has successfully sold a high number of assets at favourable prices and used the proceeds to repay debt. The merger of AWAS and Pegasus has diversified the portfolio and made it more defensive ahead of the downward cyclical adjustment that the industry is currently experiencing.

### CURRENT FINANCIALS

In the face of current market conditions, AWAS has continued to develop the business with a particular emphasis on protecting value through

proactive management of the overall fleet mix alongside protecting income through re-marketing and credit management activities.

In a year that saw record oil prices, a general economic downturn and turmoil in the credit markets, and a consequently high rate of airline bankruptcies, the business performed well ending the year in line with budget at the EBITDA level and ahead of budget at the PBT level.

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## DEVELOPMENT PLAN

2009 is likely to present a difficult trading environment as passenger traffic slows due to reduced GDP growth. This, in turn, is likely to result in a soft market for lease rates and asset values, as well as increased credit defaults by weak airlines. The price of jet fuel has declined significantly in line with the decline of oil prices. However, for some of the larger and financially stronger airlines, the benefit of this is not likely to feed through until the second part of the year as a number of them bought hedges during last year at record high oil prices.

The business's development plan is therefore very focused on protecting value through active management of credit risks, rapid redeployment of assets after repossession or scheduled lease expiry and using in-house technical expertise to maximise residual values of assets at the end of their useful life. Alongside this, the business sees a number of opportunities to take advantage of the soft market to grow the business through acquisition and which develop the business strategically.

Aside from opportunistic acquisitions, AWAS will take delivery of three new A330-300s aircraft under lease contracts to Singapore Airlines in the first half of 2009. In the second half of 2009, two A330-200s are due for delivery to Oman Air.

Given the turmoil in financing markets seen over the course of 2008 and particularly the second half of the year, the business's liquidity and funding requirements remain under ongoing review by AWAS management and Terra Firma.

## MANAGEMENT

### Frank Pray, Chief Executive Officer

Frank joined AWAS as its Chief Executive and President in September 2006. Frank was previously Managing Director of CIT Aerospace International, where he managed CIT's international aircraft portfolio. Frank joined CIT in 1997 as Vice President of Marketing. In 1998, he formed CIT Aerospace's New Aircraft Programs Group and took the position of Senior Vice President of Marketing and Sales.

### Michael Howard, Chief Financial Officer

Michael Howard was appointed as AWAS's Chief Financial Officer in March 2007. Michael joined AWAS from Statoil Topaz, where he also held the position of Chief Financial Officer. Prior to that, he was with Irish Distillers Group, originally as Treasury and Projects Manager before becoming Group Finance Director in 2000. Michael is due to leave AWAS in April 2009, his successor is Alan Stewart.

### Alan Stewart, Chief Financial Officer

Alan will replace Michael Howard as CFO. Previously, Alan was Group Finance Director at WHSmith plc, a role he had held for 5 years. Prior to that, Alan was Chief Executive at Thomas Cook UK Ltd and sat on the Thomas Cook AG Board.

### Peter Ellison, Head of Sales

In early 2008, AWAS appointed Peter Ellison as Head of Sales for worldwide operations. Peter has almost 25 years' experience in aviation and joined AWAS from easyJet, where he was Technical Director and responsible for restructuring the airline's engineering

organisation in preparation for growth plans. He was previously at Lufthansa Technik Budapest, where he was Managing Director responsible for the start-up of operations.

### John Nozell, Chief Investment Officer

John Nozell joined AWAS in October 2007 as Chief Investment Officer. Previous to this, John was a Senior Finance lecturer at Cornell University. John has 25 years' experience in senior finance positions, primarily with Chase Manhattan where he was the Managing Director Global Investment Banking, Regional Head: Airlines & Aerospace Group.

### Angus Williamson, Head of Risk Management

Angus Williamson joined AWAS in April 2007 as Head of Risk Management. Angus has over 18 years' experience in aviation having worked for the International Bureau of Aviation and most recently as Head of Investment & Business Development at AerCap.

## MAKING A DIFFERENCE TO CHILDREN AROUND THE WORLD

**Following a review of the AWAS Corporate Social Responsibility policy during 2008, the company has made a commitment to funding organisations involved in educating and supporting children in need. That commitment has already reaped big benefits for a number of good causes from Dublin to the USA and Ethiopia.**

One of the recent fund-raising highlights has been the 'AWAS Mission for Vision Ball' in aid of the sight-saving charity, Orbis. Orbis Ireland specifically fundraises to support a project to eradicate blinding trachoma in the Gama Gofu region of Ethiopia by 2012. This is vital work in an area where around a third of one to nine years olds have their lives blighted by this disease.

The theme for the night was 'World Cultures', reflecting the global nature of the aviation industry and the ambition of a charity that is working to eliminate blindness in some of the world's poorest countries. Orbis International has long-established ties with the industry as it also operates a McDonnell Douglas DC-10 flying eye hospital equipped with an operating theatre and teaching hospital. The impressive support on the night helped the final fund-raising total to more than €95,000, adding to the €25,000 raised in 2008 at a smaller event.

In addition to its work with Orbis, AWAS has also developed a global relationship with Childfund Alliance, a worldwide organisation whose members provide assistance to more than 5.5 million impoverished children and families in over 50 countries.

The charity helps its member organisations to apply consistent quality standards to child development programmes and to work efficiently and effectively.

On a local level, AWAS's larger offices in Dublin and Miami have set up partnerships with good causes based in their communities. In Dublin, they include St. Joseph's School for the Visually Impaired and the John Street West Transitional Care Unit which provides support to young people who have been in care. In Miami, the team is supporting the work of United Way, a charity that helps children succeed at school, and Hands on Miami, an organisation that puts volunteers in touch with local schools and public agencies.

These are just some of the charitable projects AWAS is supporting around the world. With such strong partnerships in place, the organisation will now be able to help even more children and young people in the future.



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## DEUTSCHE ANNINGTON



# DEUTSCHE ANNINGTON IS GERMANY'S LEADING HOUSING COMPANY

Deutsche Annington Immobilien GmbH (DAIG) was created in 2001 when Terra Firma acquired 64,000 apartments from the German Federal Railways. Through add-on acquisitions, the company has more than tripled in size. DAIG's investment model and philosophy centres on providing socially responsible, tenant-focused property management and widening the opportunities for people to buy their own homes. One of the most efficient operators in the industry, DAIG has also successfully applied its management approach to newly-acquired portfolios of residential property

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**No.1** residential landlord in Germany  
by number of units

**50,000** homes sold

**€185** million modernisation and maintenance  
programme started in 2008

**12,000** tonne reduction in CO<sub>2</sub> emissions



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## DEUTSCHE ANNINGTON



**IN 2008, DAIG  
ANNOUNCED A  
COMPREHENSIVE  
STRATEGIC INITIATIVE  
TO FURTHER  
RAISE THE LEVEL  
OF CUSTOMER  
SATISFACTION  
ACROSS THE GROUP**

**INVESTMENT RATIONALE**

DAIG's original housing portfolio was occupied mainly by existing or retired railway workers and their families who were entitled to stay in the housing as part of their contractual employment rights. This ongoing rental stream gave the business a strong and predictable source of cash flow. Furthermore, rents were substantially below market levels and could be modestly increased to improve cash flow. The apartments were owned and managed by 10 regional housing companies which had historically operated independently on a not-for-profit basis. As such, there was enormous scope for the portfolio to be run more efficiently by integrating the companies into one platform and introducing market-based processes and strategy. German residential real estate is an intrinsically low-risk asset class and the business also benefited from strong asset backing with a geographically diversified portfolio. The original portfolio was supplemented by the acquisition of Viterro in 2005 (which owned or managed approximately 150,000 apartments) creating a total of over 12 million square metres of rented space.

Today, DAIG is the largest residential housing management company in Germany and has proven its ability to acquire new portfolios and successfully integrate them into its operations. The company relies on a value enhancement strategy based on three core elements: efficient long-term management of the housing portfolio, selective sales to tenants and portfolio growth through strategic acquisitions.

**STRATEGY**

DAIG has a clearly defined strategy which enables it to generate long-term profitable growth. This strategy has proven to be successful in different market conditions and has solidified the market leadership of DAIG over the past years. The business model is focusing on three core elements:

**Long-term, value-enhancing property management:** As a responsible landlord, DAIG offers its customers a competitive range of properties with excellent service. The group has implemented a benchmark platform for the management of its portfolio and is constantly striving to further improve service quality, customer focus and efficiency.

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YEAR END: 31 DECEMBER	2007	2008 <sup>1</sup>
Rental business gross rents	€710m	€751m
Rental business costs	(€275m)	(€290m)
Sales business revenue	€236m	€137m
Sales business costs	(€240m)	(€132m)
Other	€4m	€0m
<b>Operational EBITDA</b>	<b>€435m</b>	<b>€466m</b>
Bank interest	(€248m)	(€255m)
<b>Earnings before depreciation and tax</b>	<b>€187m</b>	<b>€211m</b>
Overall vacancy rate	4.2%	3.9%
Acquisitions signed	8,834	763

<sup>1</sup> 2008 results are subject to final audit approval

**Strategic acquisitions of residential housing portfolios:** DAIG aims to further expand its portfolio through the purchase of suitable residential properties. The company therefore continuously pursues opportunities for further acquisitions on the basis of a disciplined approach to valuation.

**Selective and socially responsible sales of units primarily to tenants:** DAIG offers property ownership at affordable prices. DAIG only sells carefully selected units, primarily to its tenants, but also to investors. DAIG involves tenants and local authorities in this process at an early stage.

### ACHIEVEMENTS

DAIG's strategy has been highly successful even in the recent more challenging environment and the group has proven its ability to create sustainable growth in the German property market. It is now the prime consolidator of housing portfolios in the German market, with the company's acquisition platform sustaining year-on-year returns by continually replenishing the portfolio and building an ever-growing rental asset base that provides stable, recurring cash flows.

Over the past two years, DAIG has pursued a very careful acquisition strategy due to generally unfavourable conditions in the wholesale housing market. Some investors acquired portfolios of property at unsustainable valuations with heavy debt burdens in the hope that property prices would rise. We believe that this inflated market has now come to an end and that DAIG is well-positioned to acquire portfolios opportunistically as speculative buyers experience a more difficult market.

DAIG has also successfully improved the quality and reduced the cost of maintaining and servicing the homes it rents to its customers. It also has invested in improving the quality and value of the properties with DAIG tenants enjoying a whole host of benefits. For example, the company negotiates special deals for its tenants with companies with relevant products and services. These include special discounts for cinemas, a telephone service provider, an online pharmacy and a removal firm. Additionally, together with the German railway, Deutsche Bahn, DAIG is now helping its tenants to become more mobile. In an initial pilot project, tenants in Cologne can use a car-sharing offer from

Deutsche Bahn at special rates. DAIG also provides a consultancy service, Annington Wohnen Plus, for older tenants, which is designed to help elderly people live independently in their own homes for as long as possible.

Furthermore, the tenant privatisation programme created by DAIG has given thousands of German citizens the opportunity to own their own homes for the first time, and the company has now sold more than 50,000 homes since its inception.

### SETTING NEW STANDARDS IN THE INDUSTRY

In 2008, DAIG announced a comprehensive strategic initiative to further raise the level of customer satisfaction across the whole group. It will invest approximately €70 million to reshape the company to better meet the needs of the customer and to improve efficiency. These plans, which DAIG believes will set new standards within the German residential housing industry, will be implemented in 2009.





The plan provides for a complete overhaul of the group's structure and organisation. The core features of the new organisation will be a tenant centre, a nationwide hotline for all tenant questions, a service centre for handling standard procedures such as utility charges and a new, powerful mobile service organisation employing state-of-the-art communication technology that will focus on providing tenants with fast and flexible on-site service. The new organisation will enable DAIG to streamline processes as well as accelerate and simplify response procedures.

### CURRENT FINANCIALS

The financial performance of DAIG has further improved in 2008. Based on preliminary results, DAIG again increased its profitability. Compared with the prior year, EBITDA increased by 7.1% to €466 million.

DAIG's rental business concluded 2008 on a positive note with a rental vacancy rate of 3.2% at the end of the year. During the year, vacancies had been slightly higher than expected, a trend which has now been reversed. Due to this effect as well as higher rents and lower costs, full year rental business earnings were 6.0% ahead of 2007. The overall vacancy rate, which includes sales-related vacancies, showed a marked improvement to 3.9% compared with 4.2% at the end of 2007.

Within the sales business, the year-end earnings result of €4.8 million marked a significant improvement over the prior year. Earnings were

higher due to a reduction in sales costs and the successful conclusion of unbudgeted high margin land sales.

### DEVELOPMENT PLAN

DAIG stepped up its expenditure on maintenance and modernisation in 2008, further enhancing the attractiveness of its properties to tenants. As a result of a €185 million investment programme, the business has been able to cut the CO<sub>2</sub> emissions of its properties by 12,000 tonnes in 2008 alone.

With a letting rate of over 95%, the business generates a steady cash flow and, having reduced the selling programme in 2008, the business will again be selling fewer units in the coming months.

DAIG has access to significant committed capital funding and Terra Firma believes the business is in a strong position to make the most of the continued disruption in the capital markets by selectively acquiring residential property portfolios.

### MANAGEMENT

#### Wijnand Donkers, Chairman of the Management Board

Wijnand was appointed Chairman of the Deutsche Annington Management Board in May 2007. Before joining DAIG, Wijnand spent over 20 years with BP plc gaining extensive international experience. He ran several large businesses in the foodstuffs, petrochemicals and gas sectors where customer orientation was the priority and has worked and lived in Europe, the USA and Asia.

He was a member of BP Chemical's Germany supervisory board from 2001 to 2005. Wijnand is Vice Chairman of the GDW, the association of residential housing companies in Germany.

#### Dr. Manfred Püschel, Member of the Management Board

In 1998, Manfred Püschel was appointed Chief Financial Officer of Viterra AG. After DAIG acquired Viterra in 2005, Manfred became a member of the Deutsche Annington Management Board. Manfred's professional career started at VEBA as a member of the planning staff, from which he moved to management positions as board member and Chief Executive at Raab Karcher, as well as at several Stinnes group companies.

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YOU CAN HAVE  
ANY COLOUR YOU  
WANT AS LONG  
AS IT'S GREEN

**Underlining DAIG's long-term commitment to its residents, the company launched a €185 million programme in 2008 to modernise and maintain its housing stock. The focus of that investment has been on environmental and energy saving measures (such as using green materials or upgrading insulation) and on improving the quality of life for those living in the properties.**

In a modernisation project in Barsinghausen, for example, DAIG has opted to use a new type of roof tile which breaks down air borne pollutants. The make-up of the tile allows daylight to convert harmful nitrogen oxides into harmless substances which are washed away by the rain. Matthias Stock, Managing Director of DAIG Nord, sees active environmental protection as a key issue for DAIG. "As the largest provider of homes for rent in Germany, we can make a direct contribution to cleaner air in our cities and towns with this new roof tile technology," he says. Following the success of early trials, the company is planning to renew more than 10,000 square metres of roofing with the new tiles.

As well as delivering environmental benefits, the modernisation programme is also improving the quality of life for residents. 72-year old Inge Hanke is a DAIG tenant who has been living in a development at Knauer-und Karbonweg in Dortmund for more than 40 years. Following an extensive €1.5 million renovation programme of her building she commented, "The hallways have now been freshly painted and brightly lit. Following our balcony's renovation and the installation of new railings, it is now quite attractive and also easy to keep clean. And the new front door with its intercom is a great convenience for day-to-day living." Other improvements have included renovating and installing insulation throughout, upgrading the electrical systems and installing communal laundry rooms.

Some 700 kilometres to the south, in Traunstein, DAIG has invested approximately €240,000 in modernising buildings in Permanederstraße. These buildings, dating from the 1930s, now feature new entrance doorways with intercoms as well as new windows. The attics and cellar ceilings were insulated, as were some of the exterior walls. DAIG tenant Otto Diener is impressed. "I'm happy to have a landlord who's investing in the building," says the 47-year old technical employee. "Good insulation is really important, especially in view of exploding energy prices."



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## EMI GROUP



# EMI IS ONE OF THE WORLD'S LARGEST MUSIC COMPANIES

It operates directly in 50 countries, has licensees in a further 20 countries and employs over 3,150 people. The business is made up of two divisions: EMI Music Publishing and EMI Recorded Music

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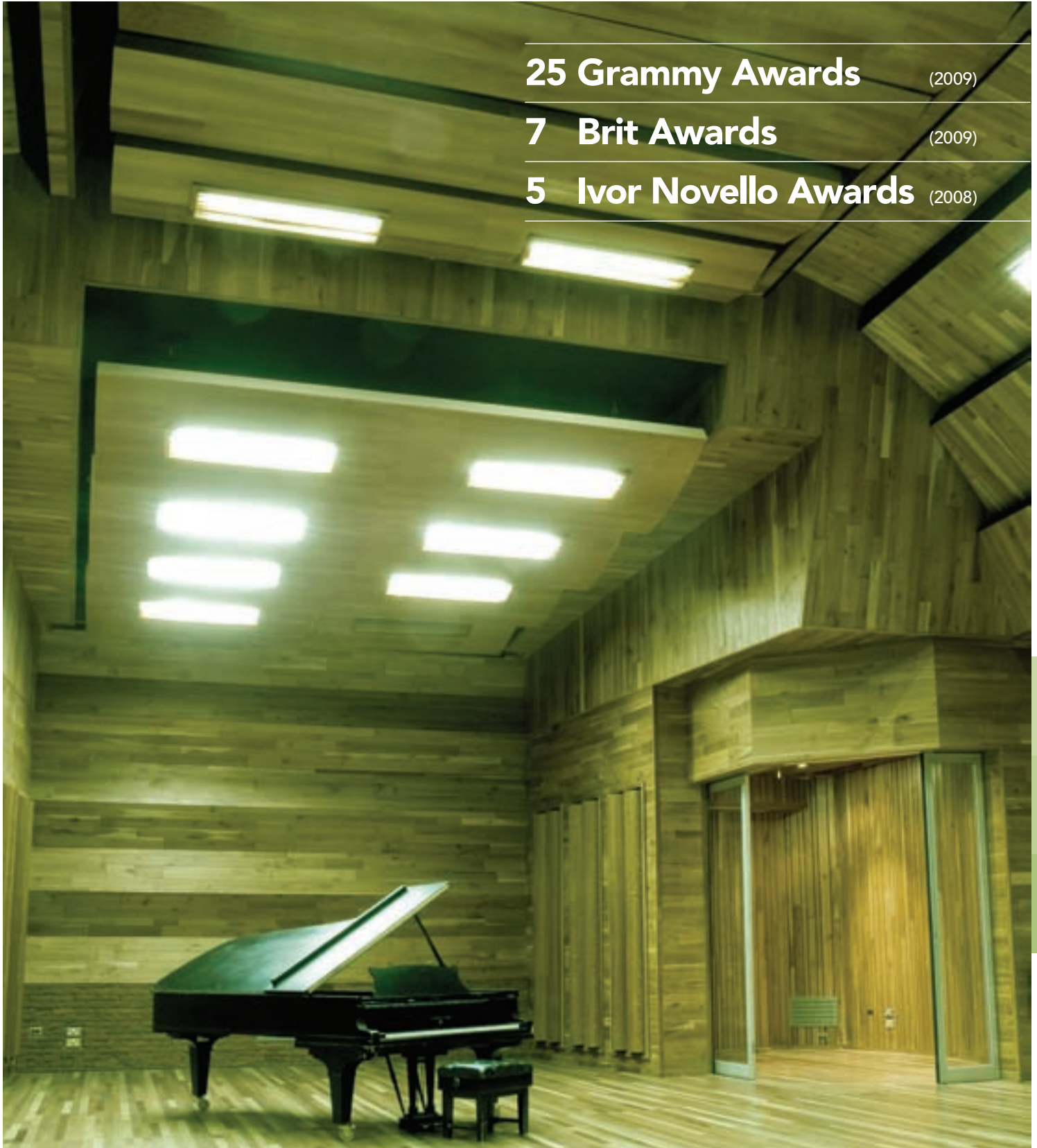
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**25 Grammy Awards** (2009)

**7 Brit Awards** (2009)

**5 Ivor Novello Awards** (2008)



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## EMI



## THE GOAL IS FOR EMI TO BECOME THE MOST INNOVATIVE, ARTIST-FRIENDLY AND CONSUMER-FOCUSED MUSIC COMPANY IN THE WORLD

### INVESTMENT RATIONALE

EMI draws on Terra Firma's experience in strategically transforming businesses, repositioning assets, driving operational change and enhancing cash flows. It is an asset-rich business with exceptional publishing and recorded music catalogues. However, EMI's revenue had been declining due to the structural shift in the consumer music market and to a slow response, both by the industry and the company, to the move towards digital consumption and falling retail space for music. This shift has been particularly detrimental to the consumer-facing Recorded Music business.

Terra Firma recognised the potential to develop the publishing catalogue while streamlining the recorded music business and repositioning it to capitalise on the opportunities offered by the booming digital market and by re-engaging with consumers and new generation retailers.

### REDEFINITION OF STRATEGY & DEVELOPMENT PLAN

Since acquiring EMI in August 2007, Terra Firma has embarked on a major restructuring of the business which

will transform not only EMI, but potentially the entire music industry. The goal is for EMI to become the most innovative, artist-friendly and consumer-focused music company in the world, while delivering the financial performance needed to build a sustainable business. EMI Recorded Music, like the other major music companies, has traditionally been focused on producing successful albums. This has led to a policy of making large advances to artists to secure recording contracts, followed by a number of album releases that are supported by significant up-front marketing spend.

The reality was that a small number of very successful albums compensated financially for the losses incurred on the majority of artists and for a general lack of cost discipline within the industry.

Under Terra Firma ownership, EMI will aim to provide the best service to artists while maintaining the company's cost base at a level that can ensure profitable growth. To achieve this, Terra Firma is radically changing EMI Recorded Music's existing organisation. This will involve

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YEAR END: 31 MARCH	YTD Dec 07	YTD Dec 08
<b>Recorded Music</b>		
Gross margin – net domestic sales	£192m	£250m
Gross margin – licence income and neighbouring rights	£69m	£70m
Overheads and miscellaneous <sup>1</sup>	(£249m)	(£216m)
<b>EBITDA</b>	<b>£12m</b>	<b>£104m</b>
<b>Music Publishing</b>		
Net revenue	£306m	£307m
Royalty costs, overheads and associates	(£225m)	(£216m)
<b>EBITDA</b>	<b>£81m</b>	<b>£91m</b>
<b>Group EBITDA<sup>2</sup></b>	<b>£90m</b>	<b>£221m</b>
Bank interest	(£139m)	(£147m)

1 Includes corporate overhead allocation and share of associates

2 Includes income at Group level

moving from standalone labels to a streamlined structure where the labels are solely focused on A&R (Artists and Repertoire). The key label support activities, such as marketing, will be brought together under a unified, global leadership. EMI labels in the future will work closely with their artists on the creative process and on developing their long-term music careers. The support functions will assist the labels, ensuring that both EMI and its artists extract the full value from their work. The resulting re-shaped organisation will simplify what EMI does and help creative development while also speeding up decision-making.

By avoiding duplication, these changes and other restructuring efforts will enable Terra Firma to reduce headcount by 1,500-2,000 people, rationalise existing artist rosters and streamline the international market 'footprint'. Cost savings are predicted to be in the region of £200 million per annum.

A key area of focus will be EMI Recorded Music's artist roster. Currently, EMI has more than 14,000 artists on its roster, of which just 200

account for half of revenues. It is actively working with 1,300 artists, but only a small number of these relationships are profitable. In the future, EMI will be more selective in its artist relationships. It will also develop a broader relationship with its new artists. EMI is financing the building of the artist 'brand' – the return on this investment will come through not only the sale of recorded music, but also from touring, licensing and other revenue streams.

### CURRENT FINANCIALS

#### Recorded Music

In the year-to-date, EMI's Recorded Music business realised a net domestic sales gross margin of £250.4 million, which was a 30.5% improvement compared with prior year. This positive variance arose from the combination of higher digital sales and lower physical returns. Coupled with lower costs, this meant that earnings in the year-to-date were £92 million better than prior year.

#### Music Publishing

The Music Publishing business recorded year-to-date revenue which was 1.6% below budget, but 0.4% better than prior year.

The favourable variance to prior year was due to strong results in the US, UK, Latin America and Spain. Digital sales at £21 million were 13.3% better than prior year.

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## MANAGEMENT

### Lord Birt, Chairman, Maltby Ltd

In addition to his function as a member of EMI's Supervisory Board, Lord Birt has acted as an adviser to Terra Firma since 2005. Prior to that, he was Chairman of Infinis Ltd and between 2000 and 2005, his activities included memberships of the Cabinet Office Strategy Board and the Civil Service Reform Programme Board as well as Strategy Adviser to the Prime Minister, an adviser to McKinsey's Global Media Practice and the Chairmanship at Lynx Capital Ventures. Lord Birt started his career with LWT where he became a Director of Programmes before moving in 1987 to the BBC where he was Deputy Director-General before becoming Director-General.

Lord Birt holds a degree from St. Catherine's College, Oxford.

### Roger Faxon, Chairman and Chief Executive of EMI Music Publishing

Roger took up his current role as Chairman and Chief Executive of EMI Music Publishing in March 2007. He was previously President and Co-Chief Executive of EMI Music Publishing. Roger has held a number of senior roles at EMI including President and Chief Operating Officer of EMI Music Publishing, Chief Financial Officer of EMI Group and Executive Vice President and Chief Financial Officer of EMI Music Publishing. Roger joined EMI from Sotheby's, where he was Chief Executive of Sotheby's Europe and previously Chief Operating Officer of Sotheby's North and South American operations.

### Elio Leoni-Sceti, Chief Executive of EMI Music, President of New Music

Elio joined EMI as CEO of EMI Music in September 2008. Prior to that he had spent 16 years at Reckitt Benckiser where he started as a category manager before being appointed Executive Vice President. From 2001 to 2005, he was Head of Category Development, leading the company's innovation, product pipeline, global marketing and media, and from 2005 to 2008, he was Executive Vice President Europe.

### Charles Allen, Non Executive Chairman

Charles joined EMI as Chairman of EMI Music in January 2009. In 2006, Charles was appointed Chief Adviser to The Home Office, providing advice and support to the Home Secretary and the Permanent Secretary. Charles served as CEO of ITV plc from 2004 to 2006, having previously served as Executive Chairman of Granada plc, which he led through the merger with Carlton Communications to form ITV.

### Stephen Alexander, Deputy Chairman of Maltby Capital, Senior Non-Executive Director of EMI Music Publishing

Stephen was appointed Deputy Chairman of Maltby Capital, the holding company of EMI, in January 2009; he was previously President of EMI Recorded Music Catalogue since March 2008. From 2002, Stephen was an Operational Managing Director with Terra Firma where his roles included Chairman of AWAS, interim CEO of Odeon, Chairman of Odeon/UCI and Chairman of the Thresher Group. Previously, Stephen was CEO of Hicks, Muse, Tate and Furst's European food businesses and had enjoyed a 17-year career with Allied Domecq PLC.

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## CHARTING THE RISE OF KATY PERRY



**2008 was Katy Perry's year. After moving to EMI from another label, she became the company's biggest breakthrough artist of 2008, her catchy brand of pop selling over 2 million albums and 11 million tracks and ringtones worldwide.**

Katy is the first big new artist for the new EMI and her meteoric rise has been helped along by some of the radical changes that have already taken place at the company. By getting closer to its artists, finding new ways to connect with consumers and taking a global approach to marketing, today's EMI is giving stars like Katy Perry every chance to shine.

Katy came to EMI with talent and a very specific vision. EMI's A&R and marketing teams worked collaboratively, building a close relationship with Katy that would enable her to realise her vision and take her music to fans around the world.

Making Katy Perry an international hit depended on giving her the kind of credibility that can only come from fans discovering an artist themselves. Delivering that would depend on flawless coordination between EMI's teams in the US and the rest of the world. Nine months before the album's US launch date, an aggressive marketing plan began with extensive use of the internet, the medium that would introduce Katy to fans, key taste-makers and the media. With her name out there and momentum building, the commercial radio plan could roll out.

The finished album included tracks from previously unreleased albums that Katy had produced with other record labels plus two collaborations with producer Dr. Luke – 'I Kissed a Girl' and 'Hot N Cold'. This material was the basis for the biggest multi-format assault ever seen for a new female pop artist. With marketing going into overdrive, her music and her face was all over the press, TV, video and online, first in the US and then feeding into the rest of the world.

After the initial word-of-mouth build up, this accelerated marketing plan kept up the momentum and Katy went on to have two number one hits that turned her into a US and worldwide recording sensation. It wasn't quite overnight success, but it was pretty close.

Katy Perry's rise is a template for the future success of EMI. The business has showed what it can achieve when it works together, gets closer to its artists and thinks globally. It's a powerful formula that's proved to be a big hit for the business and taken one talented newcomer to the very top of the charts.

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## INFINIS



# INFINIS IS THE UK'S LARGEST PURELY RENEWABLE ENERGY GENERATOR

In 2008, it produced 1.556 terawatt hours (TWh), approximately 10% of the UK's renewable power. The company's portfolio includes 101 generating sites across the UK and its total installed capacity amounts to 305 MW

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**360,000** the equivalent no. of UK homes  
powered by energy from Infinis

**9.3m** tonnes of CO<sub>2</sub> prevented from release into  
the atmosphere



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## INFINIS



## INFINIS IS FOCUSED ON DEVELOPING FROM A LANDFILL GAS BUSINESS TO A BROAD-BASED RENEWABLE ENERGY BUSINESS, MOVING DECISIVELY INTO ONSHORE WIND OVER THE NEXT FIVE YEARS

### INVESTMENT RATIONALE

Infinis was previously the waste-to-energy division of the Waste Recycling Group (WRG). Terra Firma acquired WRG in July 2003 and later merged it with Shanks' UK landfill waste business, which it acquired in 2004. A leading waste management company, WRG held approximately 30% of the UK land space that had been granted planning consent for use as landfill and also owned a renewable energy business.

In a market experiencing increasing regulatory pressure and a growing focus on alternative energy sources, Terra Firma identified the potential for WRG's fledgling waste-to-energy operations to be a significant development area and margin driver for the business.

Growth in the sector is underpinned by the numerous targets that have been set for the reduction in greenhouse gas emissions:

- Under the Kyoto Protocol, developed countries have committed to a 5% reduction in 1990 greenhouse gas emissions during the period 2008-2012.
- The EU has announced a policy of generating 20% of primary energy from renewable sources by 2020.
- The UK's Renewables Obligation sets increasing targets for the percentage share of renewable energy in the UK power sector.

Terra Firma de-merged the waste-to-energy business from WRG in May 2006. The business was renamed

Infinis and a new management team was appointed. WRG's landfill and incineration business was sold by Terra Firma in September 2006.

### GENERATING POWER FROM LANDFILL GAS

Landfill gas is one of the naturally occurring products of decomposing organic matter in landfill sites. Around 60% of landfill gas is methane, which is one of a number of gases known to be a cause of global warming. A highly potent greenhouse gas, its contribution to climate change is over 20 times greater than that of carbon dioxide. The generation of power from landfill gas helps to reduce the global warming impact of the methane emissions as well as providing an efficient and secure source of local power generation.

### A CLEAR STRATEGY

Since its acquisition by Terra Firma, the business has been transformed from a small landfill gas division into a strong stand-alone renewable energy generator. Its strategy is to further strengthen its leading position in the landfill gas industry through investment in additional capacity on existing sites and by playing an active

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YEAR END: 31 DECEMBER	2007	2008 <sup>1</sup>
Revenue	£101m	£113m
Costs	(£48m)	(£59m)
<b>EBITDA</b>	<b>£53m</b>	<b>£54m</b>
Bank interest	(£5m)	(£6m)
<b>Earnings before depreciation and tax</b>	<b>£48m</b>	<b>£48m</b>
Capital expenditure	(£22m)	(£24m)
Average megawatts	182.6	185.8

<sup>1</sup> 2008 results are subject to final audit approval

role in the industry's consolidation. At the same time, it is developing a strong onshore wind farm pipeline aiming for 500-800 MW of installed capacity in the medium term. The result will be a well-diversified renewable energy operator poised for strong growth.

### ACHIEVEMENTS

Infinis is the UK's largest purely renewable energy generator thanks to its market-leading position in the UK landfill gas industry.

Infinis' generation capacity has grown from 57 MW in 2003 to 305 MW in 2008. The company has also increased the power produced from 0.3 TWh to 1.556 TWh in the same period. This strong track record demonstrates the company's ability to grow the business successfully through operational optimisation, organic growth and acquisitions:

- In January 2007, Infinis acquired the shares of Summerleaze Re-Generation Limited and ENnate Technology Limited from their parent company, Summerleaze Limited, adding 42 (now 47) MW of operational capacity.

- In September 2007, Infinis acquired the renewable energy development assets of Scottish Resources Group (SRG) and its related company Scottish Biopower Limited, a renewable energy development portfolio with both biomass and wind projects. These projects include a 125 MW onshore wind portfolio and development rights to a 125 MW biomass portfolio.

- In 2008, Infinis acquired 29.9% of a UK-based renewable energy generator.

Infinis has established the industry's most advanced central logistics centre at its headquarters in Northampton which monitors the environmental and operational performance of its 247 gas engines across the UK on a 24/7 basis. The latter offers remote diagnostic and start-up capabilities to ensure maximum regulatory compliance and output.

### CURRENT FINANCIALS

Infinis reported strong results for 2008 with EBITDA 3% ahead of prior year. Good operating conditions across the sites, new working practices that optimise productivity

and a reduction in unscheduled maintenance hours all contributed to the strong operational performance.

The outlook for 2009 is positive with an improved contractual position for the company contributing to an expected increase in revenue and EBITDA.

In addition, an extra 20 MW of landfill gas capacity is to be installed in 2009. Whilst electricity prices are currently at a two-year low in the UK, the majority of the output for 2009 and 2010 was contracted out in the summer of 2008 when electricity prices were higher.

## DEVELOPMENT PLAN

Infinis is focused on developing from a landfill gas business to a broad-based renewable energy business, moving decisively into onshore wind over the next five years.

Infinis currently has 20 MW of new landfill gas developments in the pipeline for 2009. The recommendation to grant planning permission for a 16–27 MW wind farm adjacent to the landfill site of Greengairs in Scotland was confirmed by the Scottish Government in November 2008. In addition, the business is progressing four further projects, totalling up to 130 MW, on sites secured from SRG in September 2007 and plans to submit at least three for planning permission by the end of 2009.

## MANAGEMENT

### Phil Nolan, Chairman

Phil was appointed to the Infinis Board in January 2007. Prior to joining Infinis, Phil was Chief Executive of Eircom, the Irish national telecoms operator, after its acquisition by a private equity consortium. He led Eircom back to the public market in 2004 and stepped down after the sale of the company in 2006. Previously, Phil joined the board of BG Group in 1998 and led the demerger of Transco, becoming Chief Executive of the Lattice Group in 2000.

### Alan Lovell, Chief Executive

Infinis appointed Alan as Chief Executive in July 2006. In his previous role, he was Chief Executive of Jarvis plc and was responsible for the financial and operational turnaround

of the business. Alan's earlier roles include Chief Executive and Finance Director at Dunlop Slazenger and Costain Group plc.

### Stewart Gibbins, Operations Director

Stewart joined WRG as Director of Operations in 2005, moving to Infinis in May 2006. Stewart has over 12 years of senior management experience in power generation including managing a fleet of 50 MW gas-fired power stations for Rolls Royce in the UK, Europe and North America. Prior to that, Stewart was Engineering Director of Huwood Controls at Babcock Group.

### Jane Aikman, Finance Director

Jane joined Infinis in July 2007. Prior to this, Jane was Group Finance Director at Wilson Bowden plc, the major house building and property development group, where she was part of the team instrumental in the sale of the group to Barratt Developments plc. Jane previously held Finance Director roles at Amey plc and later at Pressac plc.

### Steven Hardman, Commercial Director

Steven joined Infinis in May 2008 to lead its commercial and legal activities. Steven was previously Group Legal Director for WRG where he was responsible for the entirety of the group's legal affairs. A qualified solicitor, Steven's early career was as a corporate lawyer in the City of London prior to a period with Hanson plc.

## SMALL STEPS TO MAKE A BIG DIFFERENCE

**As the UK's largest purely renewable energy generator, Infinis knows more than most about how modern lifestyles are impacting on our environment. The company also recognises that, when it comes to making a difference on an individual level, it's the small steps that count.**

This was the inspiration behind the Smallsteps scheme which was set up to help Infinis employees find new ways to make life greener. This education and incentives programme features an accompanying website full of hints and tips plus details of how Infinis can help employees to become more environmentally aware.

The scheme is focused on the three major energy-consuming areas of our lives – travel, home and work – and gives advice on how small behaviour changes can add up to a major difference.

It's well known that our travel habits, whether we're commuting to work or driving to the shops, are having a big impact on our environment. Infinis is putting its money where its mouth is and giving employees two incentives to encourage greener travel. The first relates to cars, with any employee purchasing a lower emission car receiving a cash bonus of up to £1,500. The greener the car, the bigger the bonus. The company is also encouraging its employees to get on their bikes, with a saving of up to 40% on a new bike as part of its cycle-to-work scheme.

For the home, the website has advice ranging from switching off lights when you leave the room and saving

up washing for a full load through to fitting green technology such as solar panels or a wind turbine. To help pay for the more expensive improvements, Infinis is offering a green loan of up to £5,000, £1,500 of which doesn't need to be paid back. Discounts have been negotiated with suppliers of microgeneration technology, and employees are also advised on how to apply for householder grants through the government-sponsored Low Carbon Buildings Programme.

At work, Infinis is definitely practising what it preaches, turning millions of tonnes of rubbish each year into energy. The company estimates that its work prevents over nine million tonnes of carbon dioxide from being released into the atmosphere each year. To use the company's own words, its environmental impact is 'not so much a carbon footprint as a carbon toeprint'.

Infinis as a company is already carbon positive (better than carbon neutral) and the Smallsteps programme is helping each employee across its 81 sites to reduce their own impact on the environment. The workforce has really got behind the idea and interest levels continue to increase – it is adding up to a lot of small but positive changes being made every day across the UK.



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## ODEON/UCI



# ODEON/UCI IS THE NO.1 PAN-EUROPEAN CINEMA OPERATOR

Odeon & UCI Cinemas Group is the market leader in the UK – where it has an approximate 27% market share by box office value – and also in Spain and Italy, making it the number one pan-European cinema operator. The group has a total of 1,802 screens in 200 cinema sites, in a combination of freehold, long leasehold and short leasehold sites. The business operates under the name of Odeon in the UK and retains the UCI and Cinesa national brand identities outside the UK

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**1,802** cinema screens

**71** million attendance in 2008

**27%** box market share, making it No.1 in the UK



## ODEON/UCI



## ODEON/UCI HAS CONTINUED TO OPEN AND ACQUIRE NEW SITES AND ROLL OUT 3D SCREENS IN ORDER TO BENEFIT FROM THE ATTRACTIVE 3D FILM SLATE

### INVESTMENT RATIONALE

Prior to its acquisition by Terra Firma, Odeon had no clear strategic direction. It was managed by a collection of shareholders with different plans for the business and this non-alignment of interest meant the company was not operating to its full potential. United Cinemas International (UCI), meanwhile, was considered a non-core asset by its two previous shareholders and had gone through a period of under-investment.

Terra Firma acquired Odeon in September 2004 and UCI in October 2004. Both acquisitions were independently attractive, but there were clearly even greater benefits flowing from a merger. The purchase and merger of the two distinct companies offered an exceptional chance to unlock value through integration savings. Also, further consolidation was expected within the European cinema industry, so establishing and adding to a European-wide company would enable significant operational improvements. With a stable cash flow stream due to its affordable ticket price in the leisure sector, Odeon/UCI offered a number of areas for earnings improvement including ticket pricing, food and beverage retail sales and alternative revenue streams such as advertising. In addition, further opportunities were identified to selectively unlock value from the property owned by the company.

### REDEFINITION OF STRATEGY

The strategy focused on realising savings from merging Odeon and UCI in the UK and on continuing to look for acquisitions in the key

markets that would offer benefits from economies of scale. The strategy for the combined Odeon/UCI business was to enhance revenue through increasing admissions, improving the customer retail offering, greater capacity utilisation and investment in future technology developments such as digital and 3D. There was also an opportunity to dispose of any cinema assets and property that would achieve a significant premium.

### ACHIEVEMENTS

The organisation was restructured to capture synergies and establish clear lines of accountability. The subsequent integration of both businesses delivered synergy savings and other cost improvements totalling more than £10 million per annum.

The acquisition of individual cinemas and cinema chains has always been part of the strategic development of the business. As part of that policy, Odeon/UCI has successfully integrated Warner Lusomundo Sogecable (11 cinemas/109 screens) and the Iberian assets of AMC (5 cinemas/106 screens) with its existing Spanish business. These

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YEAR END: 31 DECEMBER	2007 <sup>1</sup>	2008 <sup>2</sup>
Revenue	£556m	£549m
Costs	(£483m)	(£477m)
<b>EBITDA</b>	<b>£73m</b>	<b>£72m</b>
Bank interest	(£18m)	(£22m)
<b>Earnings before depreciation and tax</b>	<b>£55m</b>	<b>£50m</b>
Capital expenditure	(£31m)	(£43m)
Attendance	75m	71m

1 2007 was a 53-week year. On a comparable 52-week basis, revenue was £539 million, EBITDA was £68 million and attendance was 73 million

2 2008 results are subject to final audit approval

acquisitions strengthened its market leadership in the region and also offered the opportunity to eliminate overheads. Two further acquisitions in Italy (Europlex and Cinestar) have enabled UCI to take the position of number one cinema operator in that market. In 2008, Odeon/UCI also completed the acquisition of four sites from Hoyts in Germany for a nominal consideration.

Odeon/UCI has successfully opened new cinemas in the past year in Alessandria in Northern Italy, in Belfast and in Liverpool. Towards the end of the year, Odeon purchased two IMAX MPX digital systems for two major sites in the UK.

The business has invested heavily in the roll-out of improved/premium seating, retail food and beverage offerings in the cinemas both in the UK and Europe; broadening the range of ice creams and coffees, and introducing pizza. It has also invested in switching from self-service areas to assisted service, which has both improved the customer experience and helped to grow retail sales. The business has focused on further diversifying revenue sources,

including increasing admissions through the use of alternative content and improving capacity utilisation. Odeon/UCI is continuing its roll-out of 500 3D screens across the group along with the introduction of digital projectors. The use of digital technology offers long-term print cost savings to the distributors, an improved advertising platform, alternative content capability, such as live opera from the New York Opera House, and greater flexibility in programming.

Odeon has now rolled out, a new ticketing system across the UK and Germany, which contains major operational and customer-friendly improvements.

The business has also significantly increased its customer database, improving contact with cinema goers and driving growth in advance bookings.

In 2008, a new screen advertising joint venture, Digital Cinema Media, was formed with Cineworld, from the acquisition of assets of Carlton Screen Advertising, the existing supplier in the UK. The joint venture

is now fully operational and has got off to a strong start, ahead of the acquisition plan.

### CURRENT FINANCIALS

Odeon/UCI reported EBITDA slightly below 2007, but ahead on a comparable 52 week period. This was in spite of the adverse impact of the collapse of Carlton Screen Advertising, the company's supplier in the UK, and the resultant loss of circa £3 million of revenue from previously-agreed guaranteed contracts.

The postponement of Harry Potter 6 from Christmas 2008 to July 2009 resulted in the deferral of significant anticipated earnings. However, this was partially mitigated by the surprise hit of the year, Mamma Mia, which set new box office records to become the highest grossing film in the UK.

Looking ahead to 2009, the film slate looks promising with a strong opening of multi-Oscar winner, Slumdog Millionaire, and with Ice Age 3D, Harry Potter 6, Monsters vs Aliens 3D, The Boat that Rocked, Bruno, and Angels and Demons all expected to perform well.



## DEVELOPMENT PLAN

The business will continue to focus on improving its customer product offering and on enhancing its customer experience. The successful retail initiatives and improved seating will continue to be rolled out at additional sites. The customer loyalty programme will be further developed and the business will drive further benefit from its growing customer relationship information. The programme of new cinemas sites will continue with new cinemas opening in all major territories in 2009.

Progress has been made with the major studios to conclude a potential large-scale deployment of digital and roll-out of 3D. The business has begun a roll-out of 3D screens in the UK and continental Europe during 2009 to benefit from the attractive 3D film slate. This is part of the Real Deal agreement for 500 3D cinemas across Europe. An agreement with the major film studios was reached for these 3D-enabled screens to secure appropriate print fees (per film) that would justify the investment.

The business continues to review further opportunities for growth in existing markets, both organically through opening new sites and via acquisitions. Odeon/UCI is also looking at taking advantage of opportunities to take over management contracts for selected sites/small circuits should the opportunity arise.

## MANAGEMENT

### Rupert Gavin, Chief Executive Officer

Rupert was appointed as Chief Executive of Odeon/UCI in 2005. Prior to joining the business, he was a member of the BBC's Executive Committee and Chief Executive of BBC Worldwide, which he led through a period of rapid expansion. His earlier roles included Managing Director at BT, where he was responsible for the UK consumer business with total revenue of £6 billion and a team of 30,000.

### Jonny Mason, Chief Financial Officer

Jonny joined Odeon/UCI in March 2006 from Sainsbury's where he was Finance Director and a member of the Operating Board. Sainsbury's had sales of £17 billion, 750 locations and 150,000 employees. Jonny's previous roles included CFO of a private equity-backed fitness chain and financial management in Hanson and Shell.

### Roger Harris, Chief Operating Officer, UK and Ireland

Roger joined UCI in 2002 and, following the merger with Odeon, has been working with the UK Senior Management Team to develop and execute a five-year plan for the business. Roger has been in the cinema business for 20 years. He held a number of positions at Famous Players prior to 2002 including Senior Executive Vice President and General Manager.

### Jose Batlle, Chief Operating Officer, Continental Europe

Jose joined the cinema industry in 1986 as Chief Executive of Cinesa, Spain. He was appointed Vice President of UCI when Cinesa was sold to UCI in 1991 and later established UCI Brazil, started operations in Italy and Portugal and continued the rapid expansion in Spain. In 2003, he was appointed Senior V.P. Continental Europe and made additional acquisitions in Germany and Austria.

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## WHEN THE GOING GETS TOUGH, WE GO TO THE MOVIES

**Cinemas have generally fared well in times of recession and Odeon/UCI has seen this in most of its markets in 2008.**

When the public mood is gloomy and money is scarce, a trip to the cinema offers excellent value-for-money escapism. In 2008, the sector again lived up to its counter-cyclical reputation: in the UK market, cinema-going attendance remained steady on prior year at 162.5 million, with box office takings up 3.5% on 2007.

As nights out at the cinema continue to be a popular leisure pursuit, Odeon is making sure its consumers have more reasons to choose one of its many screens.

Odeon/UCI sees digital technology as a key selling point for the business and the continuing roll-out of digital screens is one of the ways the company is making sure it stands out in the market. Odeon/UCI is dedicated to installing the latest technology across its cinemas, so that film fanatics are able to enjoy tomorrow's blockbusters in the highest quality possible.

Odeon/UCI has plans to extend its network of DCI-compliant screens to some 110 cinema locations



across the UK, Spain, Portugal, Italy, Germany and Austria. As part of the roll-out, Odeon/UCI is opening new IMAX screens and tripling its coverage of 3D digital screens, capitalising on the pipeline of 3D blockbusters slated for release in 2009. Disney Studios alone has six major Digital 3D releases set for 2009 and 17 over the next few years.

These new innovations are building on the digital foundation laid in 2006 and 2007 when Odeon/UCI launched Europe's first 'digiplexes' at two sites in the UK. The digital launch has been a real success and by the end of 2009, there will be a digital screen with 3D capacity within a half hour's drive of over 70% of Odeon/UCI's local population base throughout Europe.

Rupert Gavin, Odeon's Chief Executive, is confident that Odeon/UCI will be one of the few businesses able to view the months ahead with some level of optimism. "People want to get out of their homes and enter a fantasy, escapist world," he says. "And that's exactly what we offer."



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## PNG



# PNG SUPPLIES NATURAL GAS TO THE GREATER BELFAST AREA

PNG supplies 123,000 properties with natural gas in the region and is continuing to invest in its network to offer natural gas to the significant majority of Greater Belfast's homes and businesses

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**7,900** new connections in 2008

**60km** of gas mains laid in 2008

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## PNG



**THE PNG NETWORK IS NOW CONSIDERED A WORLD CLASS INDUSTRY BENCHMARK FOR DEVELOPMENT BEST PRACTICE AND THE LESSONS LEARNED IN NORTHERN IRELAND ARE INFLUENCING NATURAL GAS DEVELOPMENT AROUND THE WORLD**

**INVESTMENT RATIONALE**

When Terra Firma acquired ESH, a portfolio of regulated utility businesses, it recognised the good growth prospects of PNG, the gas business in Northern Ireland. The strong management team was delivering far greater operational and capital investment efficiencies than were being achieved in the mainland businesses.

While the opportunities for natural gas in the Greater Belfast area were attractive at the time of the acquisition, the comparative instability of the regulatory framework – combined with the relative immaturity of the network – demanded a new owner with a strong vision. Terra Firma has invested significant time working with PNG management and the regulatory authorities to agree a mutually-satisfactory regulatory framework to allow PNG to develop its business and to benefit its customers.

**REDEFINITION OF STRATEGY**

The acquisition of ESH was, in reality, the acquisition of three separate utility businesses with very different profiles. Sutton and East Surrey Water was a monopoly supplier to 250,000 households in the south of

England. Terra Firma identified it as an ex-growth, non-core asset and decided to sell the business shortly after acquisition for £191 million. East Surrey Pipelines (ESP), a UK gas connections and gas transportation business, was viewed as a potential consolidation opportunity in a buoyant new housing market. Terra Firma initially grew ESP by acquiring and successfully integrating BGCL, a connection business owned by British Gas. This made ESP the third largest independent gas connections business in the UK. Further consolidation followed in the sector and the subsequent increase in the value of ESP led to its sale by Terra Firma, leaving Terra Firma with PNG, the business with the most development potential.

Natural gas is a relatively new fuel in Belfast, having been first introduced in 1996. With more than 90% of new homes choosing natural gas, PNG is well placed to serve the region's rapid growth in housing construction. In Belfast, only 37% of the energy market is now connected to gas. As a result, there is a potential for a further 180,000 homes to convert from coal, heating oil and electricity to gas. ➤

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YEAR END: 31 DECEMBER	2007	2008 <sup>2</sup>
Revenue	£99m	£125m
Costs <sup>1</sup>	(£70m)	(£94m)
<b>EBITDA</b>	<b>£29m</b>	<b>£30m</b>
Bank interest	(£21m)	(£19m)
<b>Earnings before depreciation and tax</b>	<b>£9m</b>	<b>£12m</b>
Capital expenditure	(£12m)	(£11m)
Customers	113,000	123,000

<sup>1</sup> Excludes exceptional costs

<sup>2</sup> 2008 results are subject to final audit approval

## ACHIEVEMENTS

When PNG was set up in 1996, the core objective was to build and operate one of the most modern and environmentally friendly natural gas networks in Western Europe. PNG has made gas available to more than 267,000 properties, with 123,000 already connected to natural gas in the Greater Belfast area, and is investing in further new network to connect a further 75,000 homes and businesses in the next 10 years.

The PNG network is now considered a world-class benchmark for development best practice in the industry and the lessons learned in Northern Ireland are influencing natural gas development around the world.

Through continual innovation, implementation of ground-breaking technologies and dedication to its customer service, PNG's aim is to help keep Northern Ireland's businesses competitive globally and help in significantly reducing its carbon footprint (given that natural gas produces at least 25% less carbon dioxide emissions than other fossil fuels).

The development of the natural gas market to maturity throughout Northern Ireland over the coming decades should deliver significant carbon emission reductions, bringing it in line with the rest of the UK and many European countries.

In January 2008, the group separated its distribution business from its transmission assets.

Following negotiations with PNG's regulator, a regulatory framework governing: the business's connection incentives, permitted market development costs, and other operating costs is now in place.

## CURRENT FINANCIALS

PNG outperformed prior year in 2008 with revenues up 25% and EBITDA slightly higher. This was primarily driven by tariff increases to consumers as a result of higher wholesale gas costs, as well as an increased demand for gas as Northern Ireland experienced its coldest year for five years. Earnings will be reduced in 2009, however, as in practice, actual gas costs did not rise as forecast. As a result, more than £5 million of gas cost savings accumulated at the end of

2008 are being returned to customers through reduced tariff prices during the year, thereby impacting 2009 earnings.

PNG also installed more connections than budgeted and continued to develop its distribution network during the year.

PNG sold its transmission business to Northern Ireland Energy Holdings Ltd in March 2008, using the £99 million proceeds to pay down debt.



### DEVELOPMENT PLAN

Unlike the UK mainland where about 90% of consumers use gas, in Belfast only about 37% of the market is currently connected to gas. As a result, there is potential for a further 180,000 homes to convert from coal, heating oil and electric to gas. PNG is committed to investing in its distribution infrastructure and increasing the number of users connected to its network.

### MANAGEMENT

#### Sir Gerry Loughran KCB, Group Non-Executive Chairman

Sir Gerry's role as the Non-Executive Chairman of the PNG Group is a continuation of his work championing economic development in Northern Ireland. Gerry retired from his post as Head of Northern Ireland's Civil Service in 2002, ending a Civil Service career that spanned 36 years. Gerry previously held the post of Permanent Secretary, Department of Economic Development.

#### Peter Dixon, Group Chief Executive

Peter was appointed to the PNG board as Chief Executive in 2000 and joined the East Surrey Holdings board in November 2003 as an Executive Director. Peter has always worked in the gas industry, starting as an engineer in 1976 with North West Gas in Liverpool. Peter then moved on to play a key role in the break-up of British Gas into separate standalone businesses, before joining PNG as Commercial Director in 1997.

#### Michael McKinstry, Group Finance Director

Michael joined PNG in 1996 and was appointed to the group board in 2006. His responsibilities include finance, business planning, human resources, systems and contracts and procurement. Michael's extensive management experience prior to joining PNG includes roles in heavy engineering with GEC, in the textiles industry with Ulster Weavers and in the energy industry with Premier Power after its purchase by British Gas.

### COMPANY STRUCTURE

#### Phoenix Natural Gas Ltd

Phoenix Natural Gas builds, owns and operates the business's gas system, making sure gas gets from A to B. The Phoenix network currently extends to 2,900 kilometres, distributing natural gas throughout the licence area, representing around 50% of the population of Northern Ireland. The company's aim is to make natural gas available to 90% of Greater Belfast and connect over 60% of available properties by 2016.

#### Phoenix Supply Ltd

Phoenix Supply was formed in January 2007 as a result of EU Directive (EC55), which requires PNG to separate certain business functions when there are over 100,000 customers using natural gas. The core responsibility of Phoenix Supply is the supply of natural gas – this includes the purchasing of gas, customer service provision, customer billing, customer contact centre and credit control operations. In addition, Phoenix Supply trades gas on the wholesale market.

#### Phoenix Energy Services Ltd

Established in 2001, Phoenix Energy Services provides meter reading, servicing and maintenance activities as well as 24/7 emergency services. Since then, the company has grown from a start-up to a business with 54 skilled staff carrying out around 35,000 jobs per year. With a turnover of £2.8 million and 10% growth year-on-year, Phoenix Energy Services is now a significant service provider in the Northern Ireland home heating and energy services market.

## PUTTING ENERGY INTO A GREATER BELFAST

**Greater Belfast has changed dramatically in recent years, evolving to become a city that can offer a better quality of life on many fronts to its thousands of residents. PNG is proud to have played a part in that transformation, both through its day-to-day business and through its charitable work.**

When the company arrived in Belfast more than 12 years ago, PNG worked with the wider local natural gas industry to build one of the largest and most innovative private sector infrastructure projects the region had seen.

The result is a gas transportation and metering system that helped to underpin the city's subsequent regeneration. Having created an infrastructure that is recognised globally as a model of best practice and the latest technology, the company will now be supplying natural gas to the latest phase of the city's redevelopment – the Titanic Quarter, the famous shipyard and docklands area in the east of the city. It is estimated that when this 185-acre development is completed, over 20,000 people will live and work in what will be an entirely new urban community.

PNG is also making a difference through its charity work. In 2005, the company set up The Energy for Children Charitable Trust with the aim of reaching out to disadvantaged children throughout the Greater Belfast area and improving their lives.

The Trust's aim is to identify those causes that slip through the net provided by other charities and to

help disadvantaged children who might otherwise be forgotten. It is run on the principle that all money raised goes directly to projects benefiting children and young people. Helping to keep the overheads to zero, PNG provides all the administrative back-up the Trust needs.

Although the Trust was originally founded by PNG with the help of the local natural gas industry, it also looks for support from the wider commercial sector. George Best Belfast City Airport is just one of the prominent local businesses that have pledged to raise money for the charity.

Since being set up, Energy for Children has helped more than 3,000 disadvantaged children through a variety of projects, and that number is growing every month.



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## TANK &amp; RAST



# TANK & RAST HOLDS 90% OF GERMAN MOTORWAY CONCESSIONS FOR PETROL STATIONS, SHOPS, RESTAURANTS AND MOTELS

This includes approximately 370 restaurants, 340 petrol stations and around 50 hotels. The company's key revenue streams are lease income from tenants, fuel supply commissions from the oil companies and income from self-operated sites

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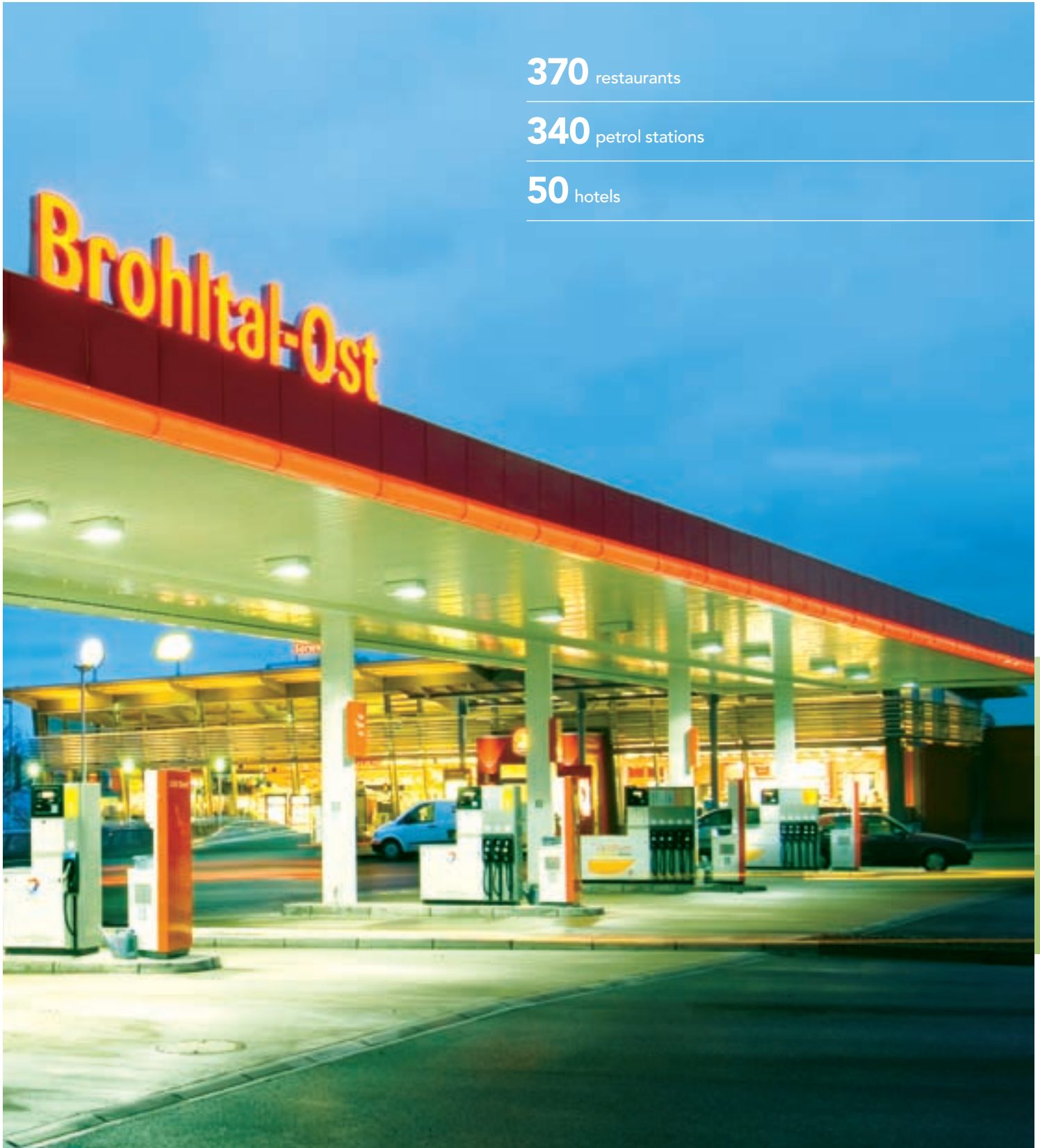
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**370** restaurants

**340** petrol stations

**50** hotels



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## TANK &amp; RAST



## TANK & RAST'S EFFORTS TO MODERNISE AUTOBAHN SERVICES AND INTRODUCE HIGH QUALITY AND PERFORMANCE STANDARDS HAVE WON IT INDEPENDENT ACCLAIM

### INVESTMENT RATIONALE

Tank & Rast had a strong position on the German Autobahn, underpinned by long-term concessions granted by the government. The company's stable cash flows were supported by a significant fixed lease component of income and the large number of independent sites represented a highly diversified low-risk portfolio. These high quality assets also came with the benefit of a major investment

programme. Furthermore, Tank & Rast's complex operational and contractual structure offered significant opportunities for improved asset yield management, cash generation and potential for evolution of its business model.

In addition to these more defensive qualities, Terra Firma believed there were further opportunities to achieve superior returns through operational development, particularly through highly selective capital investment in customer-focused initiatives. Further changes would be focused on the business operating model, with the priority of creating an environment for the most entrepreneurial tenants to flourish.

### OPERATING ENVIRONMENT

Tank & Rast operates long-term concessions granted by Germany's government along Europe's busiest motorway network. The service operations on the sites are sub-leased by Tank & Rast to around 150 tenants. Tank & Rast is responsible for the planning, construction, financing, maintenance and the leasing-out of the site facilities.

In addition to the government, Tank & Rast's main business partners are the oil companies – who supply branding and fuel but do not operate the fuel stations – and the tenants, who run the petrol stations, shops, restaurants and hotels. The oil companies are a mix of global oil companies and 'Mittelstand' German oil companies, whilst the tenants are typically local individuals or small companies complemented by a small number of corporate tenants.

### REDEFINITION OF STRATEGY

Following Terra Firma's acquisition, the business was refocused strategically in three main areas:

**The Consumer:** international benchmarking showed that Tank & Rast was lagging behind comparable European networks in terms of penetration, conversion and customer expenditure.

Tank & Rast's response was threefold: it worked to improve the food offering by signing development agreements with major international fast food players such as Burger King; it initiated a massive washroom refurbishment programme under the brand 'Sanifair'; ➤

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YEAR END: 31 DECEMBER	2007	2008 <sup>1</sup>
Revenue	€272m	€285m
Costs	(€92m)	(€97m)
Bank interest	(€83m)	(€133m)
<b>Earnings before depreciation and tax</b>	<b>€97m</b>	<b>€55m</b>
Capital expenditure	€68m	€76m

1 2008 results are subject to final audit approval

and it transformed the visibility of the service stations by gaining agreement from the German regional and federal governments to allow up to four brands to be signposted on the autobahn. This was combined with a newly created brand, 'Serways'.

**The Tenant:** Tank & Rast has consolidated the operation of its 400 individual sites under around 150 of its most effective tenants. They were given the opportunity to operate extra sites offering certain local economies of scale and were supported by further investment from Tank & Rast that would help them to improve their business performance.

**Capital Investment:** in 2005, Tank & Rast launched a €500 million investment programme to finance the construction of new sites, the refurbishment of older sites and the introduction of capex-driven strategic and consumer-focused initiatives (outlined previously) over the medium to long term.

### ACHIEVEMENTS

The refocus in strategy has resulted in a service station network that is comparable to the best international

benchmarks. Consumer choice has significantly increased and research has shown a jump in customer satisfaction levels. Almost all of Tank & Rast's sites now have motorway signage, the development agreement with Burger King is proceeding well and the Serways brand is being rolled out across the network.

The Sanifair washroom concept, which introduced permanent manning and a revolutionary voucher system, has been an enormous success and has been rolled out across nearly all of Tank & Rast's sites. Customer satisfaction now exceeds 95%.

In the most European-wide ADAC Autobahn Services Tests of the last five years, a Tank & Rast network facility came first and was recognised as offering service levels among the best in Europe. In 2008, Tank & Rast was voted as the most family friendly service network in Europe.

In 2008, the Serways brand was officially launched with a big consumer campaign, combining marketing and PR measures. It included surveys, press conferences, a TV campaign and special consumer events. The campaign

supported a significant increase of the Serways brand awareness. In addition, general customer satisfaction reached a new high in all disciplines: overall satisfaction increased to 95%.

### CURRENT FINANCIALS

Tank & Rast reported lower than budgeted results for 2008. Exceptionally high oil prices during the second and third fiscal quarter reduced traffic volumes and fuel sales and the business was impacted by the deteriorating economic environment and consumer confidence in Germany with regards to discretionary spending towards the end of the financial year.

Despite these unfavourable market conditions, Tank & Rast outperformed 2007 results largely as a result of successful capex-driven retail and catering initiatives – including the opening of new branded fast food offerings and the completion of signing and branding projects which together contributed to revenues and EBITDA growth year-on-year.



## TANK & RAST

### DEVELOPMENT PLAN

During 2009, Tank & Rast will continue to implement its key capex-driven growth initiatives including the roll-out of its proven branded fast food and other consumer-focused projects. In a more difficult current market environment, Tank & Rast is focused on prioritising available capital on its most lucrative and deliverable projects.

The agreement with B&B Hotels is progressing well with five projects currently under construction and a further one due to commence shortly. Tank & Rast is also working closely with its tenants on a major investment programme to develop and implement an EPOS and cash desk system, which should drive cost and working capital efficiencies in the network.

Tank & Rast's capital investment programme will continue over the long term, with several new sites planned every year (subject to success in winning tenders) and an ongoing refurbishment programme to keep all sites up to date.

The revolutionary Sanifair washroom concept, which has now been rolled out across the network, has attracted enquiries from a number of different sectors in both Germany and other countries. Pilots are underway to test its application in other high-volume retail environments and these are expected to lead to investment in washrooms off the autobahn.

### MANAGEMENT

#### **Dr Karl-H. Rolfes, Group Chief Executive Officer**

Karl was appointed as Chief Executive of Tank & Rast in 2001. His previous role was Director for Motorway Operations and Major Filling Stations with Elf France (TotalFinaElf). Karl started his career at the University of Münster working in the energy sector. After joining Elf Germany, he held a variety of positions including Head of Legal Affairs and Strategy before being named Head of Retail and Restaurant Operations and attending Elf's Ecole Supérieur des Cadres in Paris.

#### **Michel Marlière, Chief Operating Officer**

Michel joined Tank & Rast in 2001 as Head of Marketing and Sales and, since 2005, has been the business's Chief Operating Officer. Michel's previous roles include Managing Partner at Evologic GmbH and Senior Investment Manager for Information Technologies & Key Account Equity at DEG Deutsche Investitions- und Entwicklungsgesellschaft mbH, as well as several leading positions in the oil industry (Fuel Pricing, Controlling, Fleet Card Business and Sales).

#### **Bernhard Spetsmann, Chief Financial Officer**

Bernhard has been Tank & Rast's Chief Financial Officer since 2005. Before joining the business, he worked independently as a business consultant for various private equity-owned companies, including Tank & Rast. Bernhard's previous roles include a number of positions at Schmalbach-Lubeca AG including Head of Mergers & Acquisitions, Chief Financial Officer White Cap Europe/Asia and Head of Corporate Audit.

#### **Peter Markus Löw, Managing Director and Chief Representative Governmental Affairs, Concessions & Communication**

Peter joined Tank & Rast in 2001 with responsibility for the management of concessions and public relations as well as relationships with the federal and state governments. Since June 2008, he has held the position of Managing Director. Before he joined Tank & Rast, Peter held various positions in politics. These included Personal Assistant to the Prime Minister of the state of Saarland and working for two Federal Ministers (Personal Assistant and Head of Communication) within the German Ministry of Transport and Housing.

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## WHERE BUSINESS MEETS SCHOOL

**In an effort to build stronger links between German businesses and schools, Tank & Rast has taken part in a recent placement programme launched by business magazine Focus-Money.**

The programme gives a handful of youngsters each year the chance to shadow a CEO and see what it's like to be the boss of a big company. With few children in Germany being given a taste of the business world before embarking on their careers, the programme has proved extremely popular.

In 2008, more than 6,600 students applied for just 10 available places. This mountain of applications was whittled down to a final shortlist of applicants who were invited to a 'casting weekend' at a hotel near Frankfurt. Isabel Ruckelshauß, a 17-year-old from a grammar school near Bonn, was one of those who made it through the selection process and her prize was to spend a day behind the scenes at Tank & Rast.

She started off at Tank & Rast headquarters, shadowing CEO Karl-H. Rolfes and finding out what a busy executive's diary looks like. The morning was spent sitting in on his meetings with senior managers and being introduced to the company's key projects. Having had a front row seat on the workings of Head Office, she set off with Karl to the Siegburg-Ost service station near Bonn. After meeting the management team, Isabel was given a full tour and found out a little about how a large, busy service station works.



Having had a whirlwind introduction to Tank & Rast business, Isabel was keen to come back and learn more. In her meeting with the Human Resources team the following day, she took up the offer of an internship that will see her returning to the business for a longer visit during 2009.

Following on from Isabel's day at Tank & Rast, Karl visited her school to speak to her classmates and answer their questions about what life's like in today's fast-moving business world. He feels that encouraging young people to think about where their future might lie is an extremely useful process, and not just for the children. "When school meets business, it's meeting reality – for both sides," he says. "And this is very interesting and most inspiring for everyone involved."



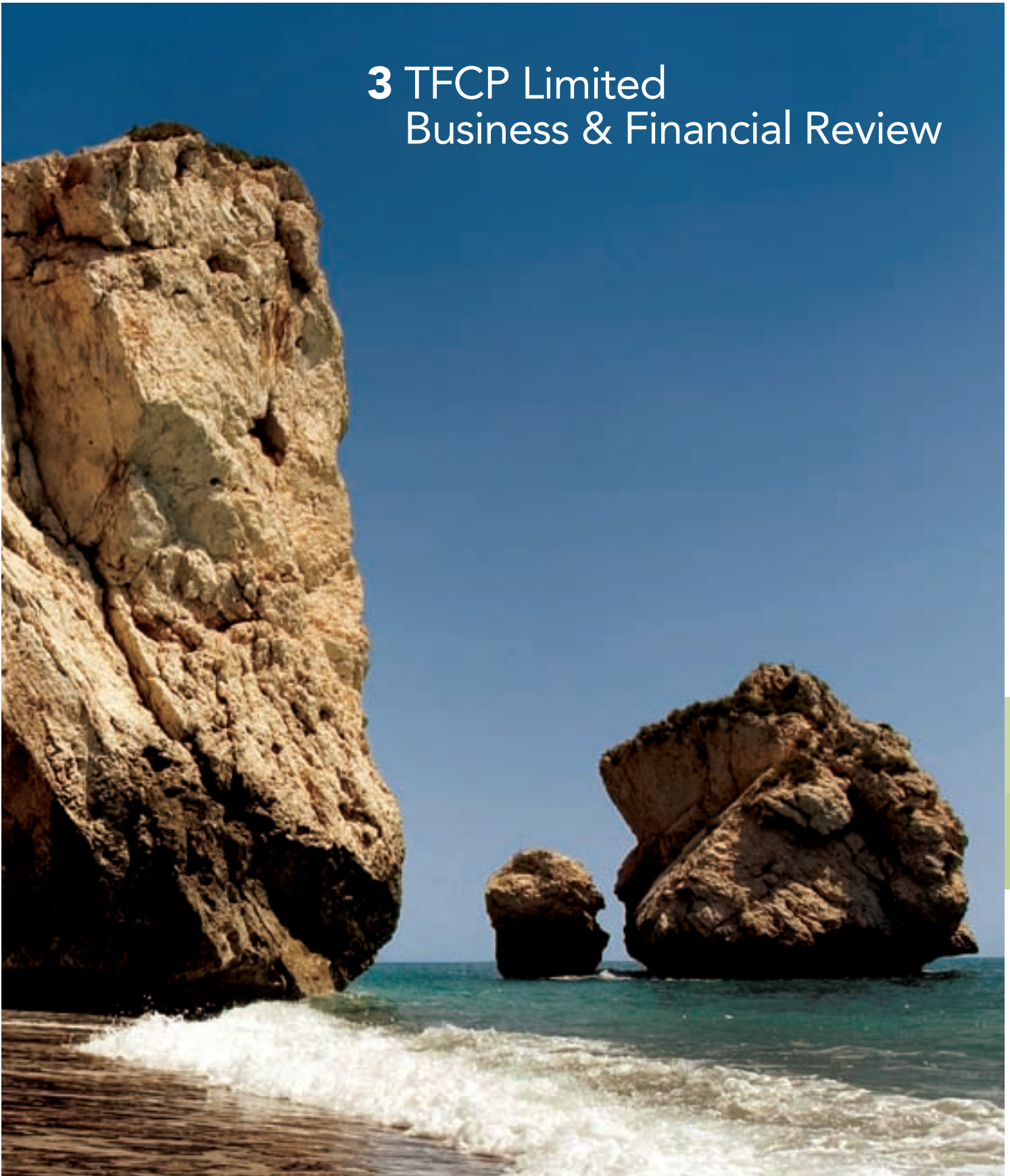
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# 3 TFCP Limited Business & Financial Review



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## INTRODUCTION

TFCPL IN THE UK PROVIDES INVESTMENT ADVICE TO THE GUERNSEY BASED TERRA FIRMA FUND MANAGERS, WHICH INVEST CAPITAL PROVIDED BY INVESTORS FROM AROUND THE WORLD. THIS INVESTMENT ADVICE INCLUDES SOURCING AND ADVISING ON INVESTMENT OPPORTUNITIES AND REALISATION STRATEGIES

**The businesses in which the fund managers invest differ in size, in sector and in geographical location. However, they are all typically in out-of-favour sectors that have been overlooked or misunderstood by the financial community.**

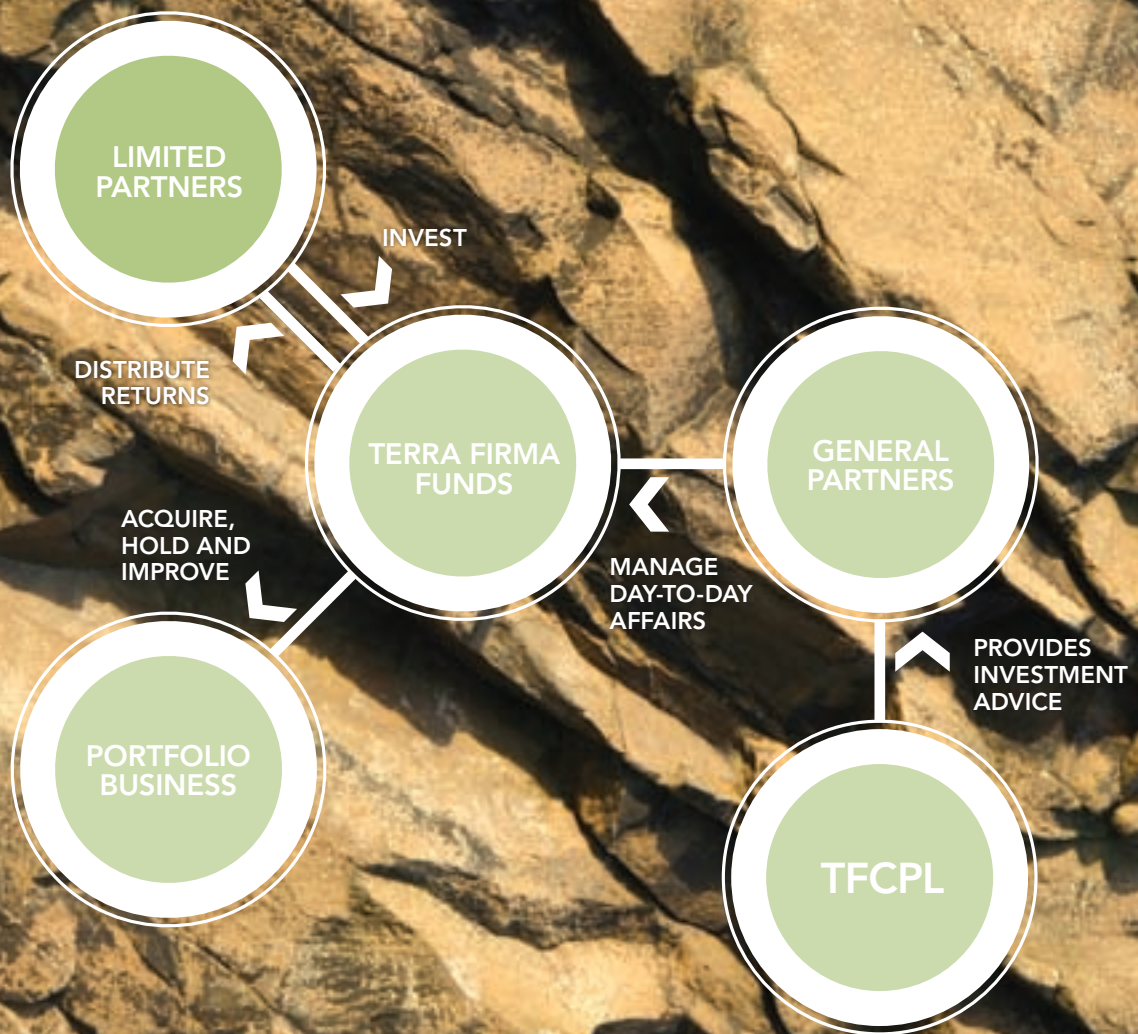
Since 1994, TFCPL has advised on investments amounting to approximately €11 billion of equity with an aggregate enterprise value of €42 billion.

This business and financial review is based on the principles and guidelines for Operating and Financial Reviews published by the Accounting Standards Board, which is best practice and voluntary.

The review contains forward-looking statements and information which:

- a. have been made available by the Directors in good faith based on the information available to them up to the time of their approval of this report; and
- b. should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information.







## STRATEGY

**We focus on businesses that will benefit from strategic, operational or management change**

### BUSINESS OBJECTIVE

Terra Firma raises long-term capital from investors such as public and private pension funds, insurance companies, endowments and charitable foundations. The funds raised by Terra Firma are used to acquire businesses that are underperforming in some way, with these portfolio businesses then being held by the funds. Terra Firma's objective is to maximise investor returns by unlocking the underlying potential in the businesses it acquires. Through a combination of strategic change, improved management and sustained investment, the portfolio businesses are nurtured to a higher level of performance.

Later, often after many years, these revitalised companies are sold to realise a return for the investors in Terra Firma's funds.

### INVESTMENT APPROACH

Since 1994, Terra Firma has consistently applied an investment strategy that focuses on identifying and capturing value in businesses from sectors that are often overlooked, undervalued or misunderstood by the financial community. Terra Firma favours large, asset-backed businesses that have complex structures or regulatory issues and which will benefit from strategic, operational or management change. In the current environment, we also seek to help companies with some of their funding and liquidity issues.

We seek businesses that have a market leading position – or provide a platform for add-on acquisitions that will create a market-leading position – as this allows Terra Firma's portfolio companies to drive change in a sector. It is these attributes, rather than any specific sector or country, that determine where Terra Firma invests.



## VALUE CREATION

There are a number of factors that give Terra Firma a sustainable competitive advantage when it comes to creating value:

**TERRA FIRMA  
FUNDAMENTALLY  
REVISES BOTH  
STRATEGY AND  
OPERATIONS WITHIN  
ITS BUSINESSES TO  
CREATE SIGNIFICANT  
IMPROVEMENTS IN  
PERFORMANCE. THIS  
IS NOT ALWAYS EASY  
OR WELCOME, BUT  
IT IS NECESSARY IN  
ORDER TO CREATE  
A SUCCESSFUL  
BUSINESS THAT IS  
SUSTAINABLE OVER  
THE LONG TERM**

**DIFFERENTIATED STRATEGY**

We focus on businesses where our views differ from the market consensus and where we can exploit our capacity to implement strategic and operational change. This approach is even more important in the current economic climate where we need to protect the value of our businesses and ensure that they can handle the more difficult operating environment which now exists. Terra Firma fundamentally revises both strategy and operations within its businesses to create significant improvements in performance. This is not always easy or welcome, but it is necessary in order to create a successful business that is sustainable over the long term.

**TAILORED ORGANISATION**

Since its inception, Terra Firma has evolved and has developed the full range of financial skills, strategic insight and operational expertise to pursue a differentiated investment strategy. The highly diverse knowledge base of the group allows Terra Firma to spot opportunities that are missed by others and to carry out many different types of transaction. Furthermore, we have the financial expertise to help companies with some of their funding and liquidity difficulties.

Our culture is an open one that demands debate and discussion across every level of our organisation and this is an approach that has consistently delivered excellent results.

Our people are encouraged to be as creative as possible and to challenge the conventional view. Our teams also have the advantage of being able to draw on the range of skills and experience of members across the group, enabling them to identify the most suitable solution for each transaction.

The investment teams co-ordinate the transaction process, which includes evaluating potential acquisition opportunities, overseeing the due diligence process, making price recommendations and recommending debt financing arrangements.

Our operational team has many years' experience in running and improving performance in numerous businesses and has strong strategic, operational and managerial expertise.

We are flexible in the way in which we use our operational experts, whether it is through involvement in deal due diligence, developing and overseeing the implementation of the strategic plan or acting as interim senior management within the newly acquired business.

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#### OPERATIONAL EXPERTISE COMBINED WITH ACTIVE MANAGEMENT

Operational expertise is fundamental to enhancing value and in the current economic climate, such skills are more important than ever. Our in-house operational team is closely involved with every Terra Firma portfolio business. The period immediately after the completion of an acquisition is particularly important to the success of that investment. This is when it is vital to make sure momentum is created and that management and staff are motivated and incentivised to work with Terra Firma to maximise the value of the business. Working in the business alongside management, our operational team refines the strategic and operational plan that we developed pre-acquisition and helps with its implementation. Our breadth of in-house operational expertise means we are able to address any short-term management changes or gaps whilst the business is in transition.

On an ongoing basis, staying in close and constant contact with the portfolio

company at many different levels enables us to actively influence and monitor business performance. This ensures that the long-term value of the business is being maximised and means we can assist on significant 'value shifting' opportunities and respond to any special circumstances.

This hands-on approach allows us to be closely involved in day-by-day development and implementation of performance initiatives in each of Terra Firma's portfolio businesses.

#### BUSINESS MODEL REDEFINITION & PERFORMANCE IMPROVEMENT

We always invest considerable time in exploring the basic, but vital, issues relating to a potential acquisition's strategy and operations. This process enables us to identify fundamental weaknesses in existing business models and opportunities to significantly improve performance. As well as transforming the business, the intensive overhaul of a company's strategic and operational direction often places it at the forefront of



#### WE ALWAYS INVEST CONSIDERABLE TIME IN EXPLORING THE BASIC, BUT VITAL, ISSUES RELATING TO A POTENTIAL ACQUISITION'S STRATEGY AND OPERATIONS

developments in its industry. Playing such an active role in industry change leadership differentiates Terra Firma from other private equity firms.

EMI provides a good example of how Terra Firma has embarked on the major restructuring of a business which will transform EMI and in the process have repercussions across the entire music industry (see feature overleaf).

## LIFE CYCLE OF A TERRA FIRMA FUND





## The EMI Story, Changing the music



Above: the prestigious  
Abbey Road Studios in  
London

**Terra Firma has become known not just for turning around ailing businesses, but for transforming companies that go on to lead and shape their industries. With the acquisition of EMI in 2007, Terra Firma's goals were not just to return an under-performing business to profitability, but to take the company back to a leadership position in an evolving music business.**

Terra Firma's trademark approach to achieving those objectives can be broken down into three broad phases: the quick wins of operational change such as cost-saving measures, the medium-term goal of restructuring to create an organisation that is fit for purpose, and the long-term drive to deliver a business model that will be an example for others to follow.

At the acquisition stage, Terra Firma had identified many of EMI's problems as originating from EMI Music, the division of the business responsible for sourcing and promoting recording artists. EMI's other division, EMI

Music Publishing, was in fact generating significant returns from maintenance and development of the the company's world-leading music publishing catalogue. As a result, EMI Music has been the focus of much of Terra Firma's strategic and operational decision-making.

### PHASE ONE – OPERATIONAL

In the first phase after any acquisition, Terra Firma takes a hands-on approach, focusing on key operational, day-to-day issues that need swift and radical change.

#### Controlling costs and improving transparency

In common with the music industry as a whole, EMI Music was hamstrung by a money-no-object spending culture. During the acquisition process, Terra Firma had identified significant cost saving opportunities and set a target of £200 million overall, with £100 million to be achieved in the first period.





THE KEY TO THE  
COMPANY'S LONG  
TERM SUCCESS  
LIES IN THE WAY  
IT EMBRACES  
CHANGES IN THE  
MARKETPLACE AND  
TECHNOLOGY

Much of the planned cost cuts related to a salary bill which was so high as to be seriously eroding profits. Music industry salaries have traditionally exceeded norms in the wider media, telecoms and entertainment industry and EMI Music was no exception, with many individuals paid at the very top of their peer group. Compounding this problem, contracts were often fixed over unusually long periods and guaranteed executives generous benefits. While excess salaries were concentrated mainly at the senior level, there was also overstaffing lower down in the organisation.

Cutting headcount and changing policies on recruitment and pay have been key priorities in this first period, with a figure of 1,500 job losses being identified during the acquisition. This has been achieved through natural wastage, redundancies and, where appropriate, outsourcing. At a senior level, replacing some senior executives has not only reduced the salary bill, but also brought in a fresh perspective from outside the music business.

It was also important to create a controlled, disciplined corporate environment. Areas such as management information were in desperate need of updating if they were to support true strategic analysis and help the business to identify risks and opportunities. Reporting practices were also inadequate, making it difficult to assess underlying trends in the business, particularly in the areas of artists' advances and physical returns.

Underpinning the initial cost-cutting phase, Terra Firma also carried out a benchmarking review, comparing EMI Music's expenditure to others in the industry.

#### **Control of expenditure**

The drive to control investment-related expenditure has been led by Julie Williamson, a Terra Firma Financial Managing Director. Her appointment as Chief Investment Officer supported by a team of Terra Firma investment professionals has ensured a new emphasis on return on capital. As part of the new

corporate governance structure, an Investment Committee has been created to evaluate expenditure and review major deals. During the initial analytical phase, it was found that there was little correlation between sales and expenditure on marketing, promotion and repertoire creation costs.

Day-to-day expenditure is also now much more closely monitored. Instead of an unpoliced expenses system, all expenses and invoices must now be signed off by management.



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#### A new team refocusing the business

Terra Firma is unique among private equity firms in putting substantially new leadership in place when turning a business around. At EMI Music, the process of selecting the right senior team was led by Terra Firma's Pat O'Driscoll.

In her search, she looked beyond the confines of the music industry to find individuals with the experience and ideas to create a new model for the industry to follow. New hires have included a CEO, Chairman, Digital President and Catalogue President, and Terra Firma also seconded around 30 people into the business at the height of the change programme. A smaller team remains and is now working with longstanding and valued EMI Music

executives who have been providing vital continuity during the turnaround.

With the right team at the helm, the refocusing could get underway. The focus has been on taking EMI Music back to business basics: understanding customers, sourcing an excellent product, finding the right channels to market and packaging and marketing music in an appealing way.

Changing the corporate culture has also been key; creating a business that could be much more self-critical and benchmark itself against the best practices and standards of its competitors and leading businesses outside the music industry.

The structure of EMI Music has also been changed to allow greater control and accountability. It now has three distinct business units – New Music, Catalogue and Music Services. In each unit, strategy and performance targets are being set globally, with offices in the regions providing local intelligence and delivery.

This international approach is a move away from the inefficient territorial structure of EMI Music before the acquisition, with scores of labels around the world failing to share resources and even competing with each other.

#### PHASE TWO – STRATEGIC

With fresh leadership and a new structure in place at EMI Music, the focus shifted to the changes that needed to be made if the business was to keep up with the evolving music industry. To guide that process, Terra Firma worked closely with the

senior management team and carried out a substantial strategic review to identify where efforts should be concentrated.

#### Closer relationships

EMI Music has had to respond to a fundamental shift in the nature of the relationship between the consumer and music. Focusing purely on selling physical or digital music is no longer enough in an industry where new methods of accessing music are constantly emerging. Digital downloads from websites and bundled music subscriptions are replacing the CD and music is increasingly being delivered through relationships with third parties such as mobile phone companies or games manufacturers.

For EMI Music, this means that brand partnerships, licensing agreements and other new income streams are becoming increasingly important. Agreements with Nokia and Sony Ericsson to supply music to their customers and with consumer brands to feature EMI Music and artists in their advertising or to sponsor their tours are increasingly typical of this new direction.

#### Better integrated global and local marketing

To help deliver EMI Music's planned strategic changes, the marketing organisation has been overhauled and substantially strengthened. As well as providing global leadership, the new structure has improved understanding of consumers and encouraged a more creative approach to marketing music. A major project to segment consumers has been a key platform of the new

EMI MUSIC IS NOW GEARED TO ADDRESS THE NEED FOR A FUNDAMENTALLY DIFFERENT RELATIONSHIP WITH CONSUMERS AND MOVE FROM BEING A PURE CONTENT PROVIDER TO DELIVERING A MUCH BROADER SERVICE

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marketing approach and allows the business to target people according to their music tastes and purchasing habits. This knowledge is also feeding into decisions such as where an artist should tour and how their promotional budget should be spent.

#### Expansion of non-recorded services

Diversification is critical and EMI Music is moving away from seeing itself as purely a maker and marketer of physical and digital albums, and focusing more on ways it can bring music to a global audience. Areas such as merchandising, ticketing and touring are substantial revenue generators and EMI Music is extending its involvement with artists into all of these areas. The company is also working with its artists to maximise the potential of their websites, the shop window to so many of today's music consumers.

#### PHASE THREE – THE FUTURE

By the end of 2008, EMI Music had done a significant amount of work to make sure the right people, structure and strategy were in place. The new EMI Music is now geared to address the need for a fundamentally different relationship with consumers and move from being a pure content provider to delivering a much broader service.

EMI Music's bold vision for the future is to build a number one, consumer-led, global music company. The company has set itself the goal of being the best in the industry at understanding consumers, what they want from music and how they want to access it. Achieving this depends on working closely with artists to help them use that understanding to bring

their music to the widest audience and realise its full commercial potential.

The newly global focus of the business is vital in both operational and commercial terms as EMI Music aims to become a truly worldwide marketing organisation for its artists. Instead of regions acting independently, there will be a more coherent approach that will help to bring music to fans wherever they are in the world.

The changes being made throughout the organisation have created a radically different business in terms of method and outlook and the effect is being felt well beyond the corridors of EMI Music.

In the act of redefining a business, Terra Firma has again created an example for others within its industry to follow.

It will take time and further investment to build a new EMI Music that is in a position to take full advantage of the opportunities of the new music marketplace. New people, processes and a leaner culture are now in place and the early results show that EMI Music has begun its journey to recovery. At the same time, the already profitable Music Publishing business is gaining fresh momentum; it is continuing to drive growth from its widely diversified revenue streams whilst continually improving its operational efficiency. As the music business continues to evolve, the new EMI is well-placed to capitalise on the opportunities and regain its position as a pioneer within the industry.





## OUTLOOK

### Looking ahead



**The global economic outlook has severely worsened in the last 12 months. Despite vast provisions of liquidity from central banks and unprecedented deficit-financed stimulus spending, Western economies are in the grip of the worst recession since the Second World War. Equity valuations have returned to mid 1990s levels. Policy responses to date have been muddled and discouraging – government deficits are rising dramatically, demand has failed to respond to any stimuli, inflationary pressures are building and protectionism is re-emerging in political discourse.**

These developments will have significant consequences for private equity. Liquidity will remain constrained for the foreseeable future and the scale of private equity transactions will shrink as a result.

However, significant opportunities do exist for long-term investors that have a secure capital base. After a long pause throughout 2008, sellers are beginning to become more realistic and pricing now increasingly reflects the liquidity needs of vendors. Concurrently,

businesses are having to re-examine long-cherished business models and strategic approaches to realign them with the new economic reality. However, with increased government involvement in the economy, the political implications of investments will need to be thoroughly examined and understood.

Terra Firma is well-placed to capitalise on these opportunities given its historic focus on businesses backed with real assets and its expertise in operational and strategic change. In managing its portfolio businesses, the firm has adopted a holistic approach, focusing on business fundamentals and engaging all stakeholders from governments and unions to employees, suppliers and capital providers. This broad approach to managing businesses will provide significant added value in this challenging economic and political environment. In looking at new opportunities, Terra Firma's track-record of identifying unloved, misunderstood businesses will serve it well. By investing in, re-orienting and rejuvenating such companies, Terra Firma will make its own contribution to the recovery from this economic downturn.

**BY INVESTING IN, RE-ORIENTING AND REJUVENATING SUCH COMPANIES, TERRA FIRMA WILL MAKE ITS OWN CONTRIBUTION TO THE RECOVERY FROM THIS ECONOMIC DOWNTURN**

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## RESOURCES

Our senior  
management team**Guy Hands**

Chief Executive Officer &  
Member of the Investment  
Advisory Committee

Guy Hands is Terra Firma Capital Partner's Chief Executive Officer and Founder. Guy sits on the Investment Advisory Committee and General Partners' boards.

Guy started his career with Goldman Sachs International where he went on to become Head of Eurobond Trading and then Head of Goldman Sachs' Global Asset Structuring Group. Guy left Goldman's in 1994 to establish the Principal Finance Group (PFG) at Nomura International plc which acquired 15 businesses with an aggregate enterprise value of €20 billion. Guy led the spin out of PFG to form Terra Firma in 2002.

Guy has an MA in Politics, Philosophy and Economics from Mansfield College, Oxford University. He was elected a Global Leader of Tomorrow of the World Economic Forum in 2000 in recognition of his achievements. Guy is also the President of 'Access for Excellence', a campaign based

at Mansfield College, Oxford, which promotes the broadest possible access to higher education in the UK. He is a Bancroft Fellow of Mansfield College, Oxford and a member of the University of Oxford Chancellor's Court of Benefactors. Additionally, Guy is a Fellow of the Duke of Edinburgh's Award Scheme.

Guy is married with four children. His interests include photography, gardens and his family.

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**Phillip Burns**  
Financial Managing Director

Phillip was involved in the acquisitions of WRG and Shanks and was responsible for Deutsche Annington's acquisition and financing of Viterra.

Prior to joining Terra Firma in 2002, Phillip was a Vice President in Investment Banking with Goldman Sachs.

Phillip graduated from the University of Michigan with a BSc in Aerospace Engineering before graduating from Syracuse University College of Law with a Juris Doctor, summa cum laude.

Phillip enjoys skiing, sailing, running and cycling.



**Pat O'Driscoll**  
Operational Managing Director

Pat joined Terra Firma in January 2009 direct from her role as Chief Restructuring Officer in EMI where she led the reorganisation of the Recorded Music business and worked with the team on developing the business's strategic direction. Her new role will continue to focus on both EMI Music Publishing and Recorded Music.

Prior to joining EMI in 2007, Pat was the Chief Executive of Northern Foods plc where she led the restructuring of the portfolio. She is also a non-executive director on the board of Xchanging plc.

Pat holds a degree in Sociology from Exeter University and is a Fellow of the Royal Society of Arts. Pat is a Trustee of the Cherie Blair Foundation for Women, a member of Forum UK and acts as a mentor to a number of younger women in business.

Pat lives with her partner and they enjoy cycling, walking their dogs, good food and wine.



**Peter Cornell**  
Managing Director,  
Stakeholder Relations

Peter focuses on Terra Firma's relationships with investors, regulators, government, banks and media. The role also includes product and business development. Prior to joining Terra Firma in 2007, Peter was Global Managing Partner of Clifford Chance, one of the world's leading international law firms with over 3,500 lawyers in 30 offices. In his career at Clifford Chance, Peter managed offices in Asia, the UK, the US and continental Europe.

Peter has an honours degree in Economics & History from the University of Exeter. He is on the Board of Directors and is a Teaching Professor at IESE Business School, Madrid. Peter was elected 'Lawyer of the Year' by Legal Business in 2007.

Peter is married with four children. His interests include skiing, surfing, golf and tennis.



**Fraser Duncan**  
Managing Director, Portfolio  
Businesses & Member of the  
Investment Advisory Committee

Fraser's role is primarily focused on the Portfolio Businesses and his responsibilities include pre- and post-acquisition operational change planning and implementation, performance monitoring and governance processes. Fraser has a board seat on a number of the portfolio companies, providing him with an overview of operational matters. He has a team of operational finance and change management professionals which enables hands-on involvement in specific areas. Fraser is also a member of the General Partners' boards.

Prior to joining the group in 1997, Fraser held positions within Rentokil Initial, Cameron Consultants and Unilever.

Fraser is a Chartered Management Accountant and holds a degree in Economics and Statistics from York University.

Fraser enjoys cooking, travel and photography.

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#### Tim Pryce

General Counsel &  
Member of the Investment  
Advisory Committee

Tim is responsible for the legal, structuring, tax and compliance teams. Prior to joining the group in 2002, Tim worked for Nomura heading the legal team that provided legal support for the group.

Tim previously practised law at Slaughter and May in London and Paris and was General Counsel for GE Capital (AFS Europe) and Transamerica (TDF Europe).

Tim is a solicitor and has an LLB (English law) and an Associateship from King's College, London and a Maîtrise (French law) from the Sorbonne, Paris.

Tim's interests include travel, skiing and scuba diving.



#### Cormac O'Haire

Finance Director & Member  
of the Investment Advisory  
Committee

Cormac is responsible for investor reporting, fund accounting and transaction equity funding. He is also responsible for the internal finance support within Terra Firma.

Prior to joining the group in 2002, Cormac was CFO and member of the Dresdner Kleinwort Capital Executive Committee.

Cormac is a Fellow of the Institute of Chartered Accountants in Ireland and studied Accounting at the College of Industrial Relations.

Cormac is married with three children and takes a keen interest in music and Gaelic football.



#### Mayamiko Kachingwe

Financial Managing Director

Mayamiko was closely involved in the simultaneous acquisitions of Odeon and UCI, and he led both the AWAS and the Pegasus Aviation Finance Company investments.

Prior to joining the group in 2001, Mayamiko worked in the London office of the Boston Consulting Group where he focused on strategy development in the financial services and industrial goods sectors.

Mayamiko holds a BA in Politics, Philosophy and Economics from Oxford University. After being awarded a Rhodes Scholarship, he went on to complete an M.Phil. and D.Phil. in Economics at Oxford and subsequently won a Prize Research Fellowship in Economics.

Mayamiko lives with his partner and their three children. His interests include football and golf.



#### Mike Kinski

Operational Managing Director

Mike has been involved in a number of the group's investments including some of the pub companies, WRG and Shanks and East Surrey Holdings. He is currently the Chairman of the Odeon/UCI Cinema Operating Company and his other portfolio responsibilities also include Infinis.

Prior to joining the group in 2000, Mike was Group Chief Executive Officer of Stagecoach Holdings Plc, and Chief Executive Officer of Power Distribution and Water Operations for Scottish Power Plc. This included the position of Chairman and Chief Executive Officer of Manweb Electricity Plc and Chairman and Chief Executive Officer of Southern Water plc. He was also a government appointed non-executive director of the UK Post Office from 1998 to 2002.

Mike has an HNC in electrical and electronic engineering from Lanchester Polytechnic (Coventry) and an MBA (with distinction) from Warwick University. He is a visiting professor and honorary doctor at Middlesex University and a visiting professor at both Brunel and Reading Universities.

Mike is married with two children. When not spending time with his family, he enjoys gardening and has a particular interest in football.







#### Quentin Stewart

Financial Managing Director

Quentin has specific expertise in the waste management and utilities sector, having originated the investments in WRG, Shanks and East Surrey Holdings. He subsequently oversaw the sale of WRG and various disposals from East Surrey Holdings. Quentin was also involved in the William Hill and Thorn transactions.

Prior to joining the group in 1997, Quentin worked for Arthur Andersen specialising in structured products.

Quentin is a Chartered Accountant and holds a degree in Business from De Montfort University.

Quentin enjoys watching and playing sport, film, music and art.



#### Julie Williamson

Financial Managing Director

Julie led the team advising on the investment in Tank & Rast and was responsible for its refinancing in 2006 and the partial exit in 2007. Julie was also heavily involved in the group's pub businesses. Since September 2007, Julie has been seconded on a full-time basis into the EMI business as Group Chief Investment Officer.

Prior to joining the group in 1998, Julie worked for Nomura heading the legal team that provided legal risk analysis and transaction execution support for the group. Prior to that, she was a partner in the Banking department with the law firm of Winthrop & Weinstine.

Julie has a Bachelor of Business Administration, majoring in Finance from the University of Iowa and has a Juris Doctor also from the University of Iowa. She is a member of the Minnesota State Bar Association.

Julie is married with one son and enjoys skiing and mountain hiking.



## RESOURCES

Broad-based  
expertise

## OUR REPUTATION

Since 1994, Terra Firma has developed a strong reputation in the investment community for being able to execute large, complex transactions. This has resulted in a robust and high quality pipeline of deals, with Terra Firma being actively sought out by strategic sellers, government institutions, advisers, investment banks and other intermediaries and service providers.

## OUR PEOPLE

We believe that what sets us apart is the commitment of our staff and the breadth of experience and skills they can offer. The Terra Firma team is made up of around 100 people based in London and Frankfurt, from 20 countries and speaking 28 languages. Our team of approximately 70 investment professionals is drawn from a wide variety of backgrounds and gives us the diverse expertise we need to analyse each opportunity in minute detail.

Our operational team has many years' experience in running and improving performance in numerous businesses and has strong strategic, operational and managerial expertise. This broad pool of in-house talent has helped to generate proprietary ideas and repeatedly enabled us to identify potential operational improvements. Financial expertise is also of huge

importance at the current time and Terra Firma's personnel have a wealth of such experience, particularly with regards to helping companies which have funding and liquidity issues.

EMPLOYEE TRAINING  
AND DEVELOPMENT

Our training and development programme is designed to ensure that our people have the skills they need to help our business achieve its strategic goals. As part of their induction programme, all new staff meet senior executives to ensure they have a broad understanding of Terra Firma and how it operates.

Throughout our business, we encourage our people to take responsibility for their own personal and professional development. That development can take many forms such as on-the-job coaching and counselling, job enrichment as well as formal training programmes, courses and professional qualifications identified by the individual, their Line Manager or Human Resources.

Our sponsorship programme helps those wishing to gain recognised professional qualifications and Terra Firma has a policy of encouraging employees to pursue relevant qualifications that will help their work and career development.



Photo: Colin Campbell

WHAT SETS US  
APART IS THE  
COMMITMENT OF  
OUR STAFF AND  
THE BREADTH OF  
EXPERIENCE AND  
SKILLS THEY CAN  
OFFER

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All professional staff have access to training either in interview skills, performance review skills, language training, executive coaching or study courses that will support their development.

Each year, Terra Firma also offers internship opportunities to undergraduate and postgraduate students, allowing individuals to gain an insight into life at work. In 2008, Terra Firma made ten internships available.

#### TERRA INCOGNITA AND TERRA CONSILIA

Terra Firma is also advised by an array of distinguished professionals from the realms of international politics, economics and business. The advisers form two groups: Terra Incognita, a political and macro-economic advisory group, and Terra Consilia, an advisory council of highly experienced senior business people.

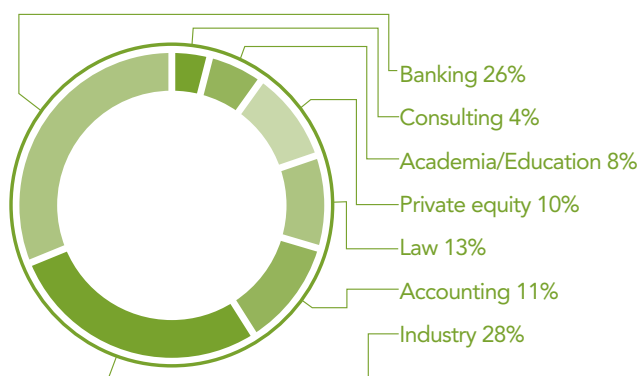
These two groups provide Terra Firma with the collective experience of renowned figures who lead their respective fields. The groups also provide independent views on the portfolio businesses' performance as well as insight into specific business sectors and how changing political landscapes might affect potential investments and opportunities in new markets.

#### SPECIALIST ADVISERS

The fund managers, which are based in Guernsey and make all the investment decisions in relation to Terra Firma's funds, are advised by many professional firms, of which TFCPL in London is one.

The Terra Firma team is complemented by the best specialist expertise available. This includes lawyers and accountants to help carry out due diligence, structure and execute transactions; investment banks to provide market advice; tax specialists to ensure compliance with worldwide tax rules; environmental consultants; industry specialists; and business change consultants to assist on strategic change programmes within the portfolio businesses.

#### BACKGROUND OF TFCPL EMPLOYEES



## BUSINESS DESCRIPTION & ENVIRONMENT

Private equity has a major role to play in improving the quality and efficiency of businesses

### OUR MARKETS

From our offices in London and Frankfurt, TFCPL and terrafirma GmbH advise the Terra Firma fund managers on investments in developed markets across the globe, with a particular emphasis on Europe.

While the geographical headquarters of these portfolio businesses vary, many of them, such as AWAS, the aircraft leasing business, have truly global activities. In fact, in 2008, only 18% of the combined revenue of Terra Firma's portfolio businesses came from the UK.

### TERRA FIRMA'S DIFFERENCE

Terra Firma's competitive difference lies in its focus on the businesses that most other private equity firms tend to avoid. We seek companies where our views are different to the market consensus. Such businesses are frequently in out-of-favour sectors, are usually complex or subject to regulatory regimes, and are in need of strategic, operational or managerial change. In the current environment, we also seek to help companies which have funding and liquidity issues.

### THE PRIVATE EQUITY ENVIRONMENT

As the world struggles through the most challenging economic crisis in over 70 years, private equity faces difficult times. The lack of liquidity for any investing at this time means that the absolute amounts allocated to private equity will decline considerably for the next few years. This combined with the lack of debt for private equity-backed companies

will mean that both the scale of private equity transactions and the industry itself will shrink materially.

However, significant opportunities do exist for long-term investors that have a secure capital base. After a long pause throughout 2008, sellers are beginning to become more realistic and pricing now increasingly reflects the liquidity needs of vendors. Almost no business is 'recession proof', but those businesses which cater to basic needs and are underpinned by real assets are, in our view, at the lower end of the risk spectrum. All businesses will face operational difficulties in the upcoming years and how management deal with these challenges will be fundamental to generating or maintaining value within portfolio businesses.

We are seeing a number of opportunities to invest in businesses that are operationally sound, but which have financial challenges due to their level of debt. Terra Firma has a great deal of experience in helping with funding and liquidity issues and therefore many of these businesses represent attractive investment opportunities.

In addition, given the huge mark-downs in valuations that are occurring, it is more likely that Terra Firma can find opportunities where the true valuation and potential of the businesses are being overlooked. In these situations, Terra Firma's contrarian investment approach and ability to utilise its skills and resources

to build value in businesses over the long term can potentially deliver strong results.

We believe that the number of investment opportunities in 2009 and 2010 will continue to be low and that the number of investments completed will be small. Holding periods for investments made in 2009 and 2010 are also likely to be longer than in recent years. During the course of 2010, we expect the market to improve and become more predictable and we believe that we will start to enter an environment which will offer value that has not been seen in the private equity arena in years.





## ECONOMIC IMPACT OF TERRA FIRMA'S ACTIVITIES

### Global Investment Activities

Terra Firma's investment activities, although based in Guernsey, are global.

- **The funds have approximately 180 investors from nearly 30 countries around the world**
- **Terra Firma's portfolio businesses operate in over 60 countries and 82% of the combined revenue of the portfolio businesses comes from outside the UK**

### UK Investment Activities

While 21% of the funds raised by Terra Firma are from the UK, over 70% of the funds' private equity investments are made within the UK.

- **A total of €8 billion of equity has been invested in the UK by Terra Firma since 1994**

This investment benefits not only Terra Firma's UK portfolio businesses, but also their suppliers, employees and business partners.

### UK-Based Advisory Services

Although based in the UK, TFCPL provides advice on investments that have operations all over the world. Its revenues consist of advisory fees from the Terra Firma fund managers. In 2008:

- **TFCPL generated £46 million of earned income and £4 million of profit**
- **£14.6 million of corporation tax, income tax and national insurance was paid to the UK Treasury by TFCPL and its employees**

Terra Firma's funds complement TFCPL's investment advice by drawing on the expertise of a broad group of other professional experts, including lawyers, accountants, investment banks, tax specialists, environmental consultants and industry specialists.

# £136m

paid for services in the UK in 2008

## CORPORATE SOCIAL RESPONSIBILITY

**Our social responsibility extends to our employees, the portfolio businesses we advise and the communities in which we work**

**At Terra Firma, we take our responsibility to the wider community very seriously. We recognise that the businesses we invest in touch the lives of many people and we are mindful of the social responsibilities that our investments bring. Our social responsibility extends to our employees, the portfolio businesses we advise and the communities in which we work. This approach is key to creating long-term, sustainable relationships that will enable us to better serve our employees, investors and stakeholders.**

### EQUAL OPPORTUNITIES

As an employer, Terra Firma is committed to maintaining an inclusive, productive work environment in which all workers are treated with respect and dignity. We want each employee to work in a professional atmosphere that promotes equal opportunity and prevents discriminatory practices based upon gender, age, religion, race, disability, sexual orientation or any other form of discrimination that affects work performance or creates an uncomfortable working environment. Terra Firma adheres to strict equal opportunities policies and strives to develop a culturally diverse and inclusive team.

### INVESTMENT CRITERIA

When advising on potential investments, we take account of social, environmental and ethical issues. Terra Firma invests in companies that respect human rights and comply

with industry standards and local regulations and which act in a socially responsible manner.

### COMMUNITY SUPPORT

From 2006 to 2008, TFCPL donated 10% of its net annual profits to the Terra Firma Charitable Trust. This enabled the Trust to make commitments of over £700,000 to charitable organisations working in our local community. We aim to fund charities on a three-year basis so that they can confidently plan and undertake long-term projects.

In late 2008, Terra Firma also sent over 1,000 copies of J K Galbraith's 'The Great Crash' to schools, universities and libraries throughout the UK.

Terra Firma is a founding member of the Private Equity Foundation, an organisation which aims to invest the capital and expertise of the private equity community into charities to help them achieve a step-change in their impact. Two Terra Firma professionals have been working in a PEF deal team since June 2008.

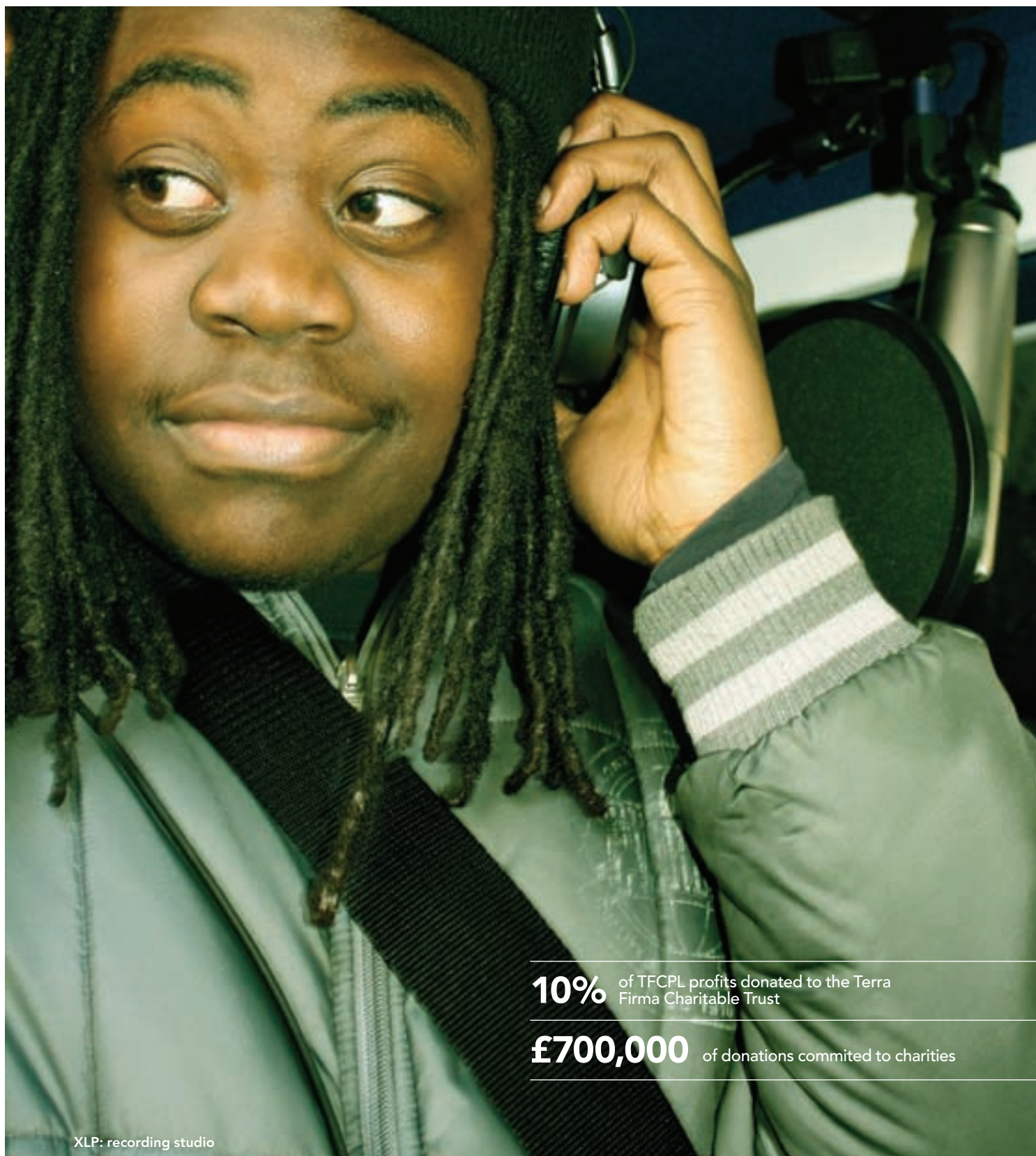
### TERRA FIRMA CHARITABLE TRUST

The mission of the Charity Committee of the Terra Firma Charitable Trust, a non-profit charitable fund formed and funded by TFCPL and its employees, is to make charitable investments which will directly benefit our local community in the borough of Southwark.

We aim to act as a good neighbour and help develop a sense of pride within our community through donations to locally based charities that support programmes in Southwark. We also support non-locally based charities which have programmes that focus on Southwark to which we can specifically earmark our donation.

We will support programmes that put an emphasis on aiding and educating children and helping the elderly, but will consider proposals outside of this scope if they meet our community focus mission.





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**10%** of TFCPL profits donated to the Terra Firma Charitable Trust

**£700,000** of donations committed to charities

XLP: recording studio

## The Terra Firma Charitable Trust is proud to support the following charities and initiatives:

### AGE CONCERN

#### 3-YEAR FUNDING (2007–9)

Age Concern is dedicated to the promotion of the well-being of all older people and to help make later life a fulfilling and enjoyable experience. It supports people over 50 in the UK, ensuring that they get the most from life as well as providing essential services such as day care and information.

### BLOOMFIELD LEARNING CENTRE

#### 2-YEAR FUNDING (2007–8)

The Bloomfield Learning Centre is a charity that offers diagnostic assessment and tuition for children aged between six and sixteen years of age who have specific learning difficulties such as dyslexia. The Centre operates with the Department of Child Psychology at Guy's Hospital, London.

### CHILDREN'S COUNTRY HOLIDAY FUND

#### 2-YEAR FUNDING (2009–10)

The Children's Country Holidays Fund was established in 1884. The charity offers severely disadvantaged children and young people a range of residential activity and respite breaks. It also provides on-going support to help improve the quality of their lives, recognise their potential and achieve their goals in the safest possible environment.

### CREATE ARTS

#### 3-YEAR FUNDING (2008–10)

Create Arts uses creative arts to help transform the lives of the most disadvantaged and vulnerable people in our society. Using leading professional artists, Create develops and delivers an extensive, UK-wide programme of education and community activities across all art forms. Since its foundation, Create

has run more than 1,950 workshops, mainly as part of sustained, life-changing programmes, for over 13,900 participants.

### KIDS COMPANY

#### 3-YEAR FUNDING (2007–9)

Kids Company was founded in 1996 to provide practical, emotional and educational support to vulnerable inner-city children and young people. Terra Firma funding helped set up the Kids Company's Urban Academy, a post-14 educational and life skills academy. It is specifically designed to meet the needs of young people who reject or have been rejected from other educational facilities. The Academy provides a balance of courses to help with their life management, along with study and business skills.

### PRINCES TRUST

#### 4-YEAR FUNDING (2006–9)

The Prince's Trust is a UK charity that helps young people overcome barriers and get their lives on track. Through practical support including training, mentoring and financial assistance, it helps 14–30 year olds realise their potential and transform their lives.

### ST CHRISTOPHER'S HOSPICE

#### 3-YEAR FUNDING (2008–10)

St Christopher's has been caring for people in the final stage of their life since 1967. The hospice cares for around 2,000 people a year, including around 500 people who are looked after at home daily. St Christopher's has inspired innovation in 110 countries and continues to provide world-leading training via courses and clinical placements to 4,000 health professionals annually.

### TOMORROW'S PEOPLE

#### 3-YEAR FUNDING (2008–10)

Founded by Grand Met (Diageo) in 1984, Tomorrow's People has been running as an independent charity since early 2005. In that time, it has helped change the lives of over 400,000 people across the UK who had been resigned to long-term unemployment and welfare dependency. On average, 90% of people helped by its specialist employment advisers are still in work after three months and 76% still in work 12 months later.

### UNICORN THEATRE

#### 3-YEAR FUNDING (2008–10)

The Unicorn Theatre is one of the leading producers of professional theatre for children in Britain. Founded in 1947, its mission is to create amazing shows for children which are fun, challenging and exciting – shows which rise to the challenge of a child's imagination.

### XLP

#### 3-YEAR FUNDING (2008–10)

XLP aims to provide support to young people and encourage wise lifestyle choices. Since 1996, XLP has grown from working in a single school to operating in over 30 schools and communities across Southwark, Lewisham, Greenwich, Bexley, Tower Hamlets and Newham.



**In recent years, the Terra Firma Charitable Trust has chosen to focus on charities that work with children and old people. Here are some specific examples of what our funding has provided:**

#### **AGE CONCERN LEWISHAM AND SOUTHWARK**

Age Concern Lewisham and Southwark (ACLS), is an independent charity empowering older people to live full and active lives. The only organisation working across the boroughs of Lewisham and Southwark specifically for older people, ACLS helps people often living in poverty and isolation and suffering from related health problems such as heart disease, high blood pressure and mental health conditions.

Terra Firma is supporting the work of Age Concern's North Southwark Healthy Living Centre in Bermondsey. The Centre provides a warm welcome to older people who might want a hot meal, a game of bingo or simply a cup of tea and some companionship. Terra Firma's contribution of £20,000 in 2008 will meet around half of the charity's funding gap for the year. The money will be used in all areas of the charity's work, from funding activity expenses and weekly health and exercise tutors through to paying for the Centre's popular day trips.

#### **ST CHRISTOPHER'S HOSPICE**

St Christopher's Hospice is a south east London-based charity that is affectionately known as 'The Mecca of Palliative Care'. Founded by Dame Cecily Saunders, St Christopher's provides high quality care to dying people and much needed support for their families and friends. The charity was a pioneer in the arena of palliative

care and the first to combine pain and symptom control with emotional, spiritual and practical support.

Starting in 2008, Terra Firma will contribute £21,000 a year for three years. This funding will be focused on the in-patient department where the charity has 48 beds on four wards and cares for more than 1,000 people a year. It costs around £500 a day to care for someone at St Christopher's, so each year the Terra Firma donation will pay for someone to benefit from St Christopher's 24-hour care for six weeks.

#### **XLP**

XLP is a Southwark-based charity dedicated to tackling social violence, poverty and educational failure among young people across seven of London's most deprived boroughs. XLP works with around 10,000 students a year, running arts, drama, music and video workshops that inspire them to stay on at school and stay away from gangs. Their projects range from running a homework club on a London bus that visits London estates through to teaming up with MTV and EMI to film a programme for the popular series 'Pimp my Ride'.

Terra Firma began working with XLP in mid-2008 and has committed £20,000 a year until 2011. This money will be used to pay salaries and cover expenses so that around 450 young people 'at risk' or excluded from school have access to the one-to-one support they need. XLP find this kind of general funding the hardest to attract, so Terra Firma's contribution will enable the charity to focus on working with young people without having to worry that the bills are being paid.



**Above: St Christopher's Hospice  
Below: Age Concern**

**OUR DONATIONS  
DIRECTLY BENEFIT  
OUR LOCAL  
COMMUNITY**

## CORPORATE GOVERNANCE

**TFCPL has a well-established and highly effective corporate governance framework**

### FRAMEWORK

TFCPL has a well-established and highly effective corporate governance framework which has been developed to meet the needs of a small investment advisory business. The bodies and processes in place are more immediate and focused than those often seen in large public companies and enable the business to develop flexibly and securely.

### THE BOARD OF DIRECTORS

TFCPL is managed and controlled in the UK. It has a board of UK-based directors comprising three Executive Directors – Guy Hands, Cormac O’Haire and Fraser Duncan – and one Non-Executive Director – Deborah Pluck.

Robert Felton, the previous Non-Executive Director, resigned from the board on 9 September 2008.

Deborah Pluck is an independent non-executive director and is a Fellow of the Institute of Chartered Accountants in England and Wales. Deborah started her training with a national audit firm in Bristol before moving back to Oxford where she qualified and subsequently became a partner in Oxford’s longest established accountancy practice. She holds a number of director and trustee roles outside the practice including Chairman of the Governors of an independent school in Oxford. She is a founder member of The Oxfordshire Women’s Forum which champions the role of women in local business.

The Board meets at least quarterly, but in practice more often. The Board’s responsibilities include the direction and control of strategy, approval of the annual budget, approval of the

Financial Statements, review of Annual Money Laundering and Compliance Reports and appointment of members of subcommittees of the Board. These include the Investment Advisory Committee, Remuneration Committee and Portfolio Operating Committee.

Tim Pryce is Company Secretary.

### COMMITTEES

#### Investment Advisory Committee

The Investment Advisory Committee (the IAC) consists of Guy Hands, Fraser Duncan, Cormac O’Haire and Tim Pryce. The IAC meets weekly or more often if business activity requires the consideration of investment-related matters. Its role is to recommend potential transactions to the fund managers in Guernsey. This includes assessment of potential new investments, refinancings or disposals, as well as follow-on fund financing for the portfolio businesses and post-investment appraisals. The IAC will review progress and make recommendations at all stages of a transaction.

The members of the IAC have the specialist skills to support the investment teams whilst bringing objectivity and consistency to the review of each of Terra Firma’s investment opportunities. The fact that the IAC members are not members of any particular transaction team increases the objectivity the IAC brings to its vital role.

#### Remuneration Committee

The Remuneration Committee consists of Peter Cornell, Guy Hands, Cormac O’Haire, Tim Pryce and Mel Willshire (Head of Human Resources) and meets twice a month or as otherwise required.

It is responsible for all compensation and benefits issues, including Terra Firma’s broad policies and principles and the individual remuneration packages for all TFCPL’s employees.

#### Portfolio Operating Committee

The Portfolio Operating Committee (the POC) consists of Guy Hands, Fraser Duncan and the relevant senior Terra Firma employees assigned to a particular portfolio business. The POC usually meets on a weekly basis and its role is to review Terra Firma’s management of its portfolio businesses. The POC is a forum for the relevant Terra Firma team to raise any opportunities, issues and concerns. This allows appropriate resources to be deployed and critical decisions to be made in a timely and focused manner.

### CONFLICTS OF INTEREST

TFCPL has a Conflicts Policy addressing both personal and corporate conflicts of interest. Most procedures for dealing with conflict involve, in the first instance, disclosure of the relevant conflict to the affected parties and then either (i) seeking such third parties’ consent or (ii) refraining from taking the conflicting action. Detailed provisions are in place to regulate, amongst others, business or other activities outside TFCPL, entertainment and gifts, personal account dealing and directorships in portfolio companies. In addition, each of the Terra Firma funds has an Advisory Board composed of representatives of a selection of each fund’s investors.

The principal purpose of each Advisory Board is to consider and, if thought appropriate, consent to arrangements



being entered into when there is a possibility of conflicts arising.

#### PROFESSIONAL DEVELOPMENT

The nature of the professional training within TFCPL is broad, depends on the development needs of the individual and can include both technical and soft skill based training.

All TFCPL investment professionals are required to complete Part 1 of the Investment Management Certificate. This course and exam focuses on the financial markets and the UK Regulatory Environment and is classified as a Financial Services Authority (FSA) approved threshold competency examination.

#### GENERAL ACCOUNTABILITY Authorised Status

TFCPL is authorised and regulated by the UK FSA to provide investment advice to, and arrange deals for, the funds.

#### Compliance Officer

Tim Pryce, the General Counsel, is also the Compliance Officer of TFCPL. The Compliance Officer's function is to ensure that our directors and employees comply with the FSA Rules and any other rules and regulations governing the conduct of designated investment business made under the Financial Services and Markets Act 2000.

#### Financial Statements

TFCPL prepares annual audited Financial Statements. These accounts which are prepared following United Kingdom company law give a true and fair view of the state of affairs of TFCPL and its group. TFCPL's year-end is March and the accounts are filed every

year at Companies House in London. TFCPL's auditor is Deloitte.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of TFCPL and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

#### Contingencies – Litigation

TFCPL is not currently involved in, and has no knowledge of, any threatened litigation which would have a material adverse impact on its results of operations or financial conditions.

#### Ownership

Guy Hands is the ultimate beneficial owner of the share capital of TFCPL.

## SENIOR MANAGEMENT REMUNERATION

A high quality management team is essential to maintain our position as one of the leading contrarian investment advisory firms

### REMUNERATION POLICY

The remuneration of Senior Management is designed to attract, motivate and retain staff of the highest calibre. A high quality management team is essential to maintain our position as one of the leading contrarian investment advisory firms.

### REMUNERATION PACKAGE

The main elements of the remuneration package for Senior Management are as follows:

#### ANNUAL SALARY

In 2008, the total cash compensation paid to Senior Management was £10,538,945 and the average for these 16 individuals was £679,931. Salaries are reviewed annually by the Remuneration Committee and are set in relation to an individual's performance and market comparator groups. Senior Management is not eligible for bonuses. Terra Firma employees who are appointed to the boards of Terra Firma portfolio businesses do not receive Directors' fees.

#### Benefits in Kind

##### Medical Insurance

All members of the Senior Management team are eligible to join the Group Medical Insurance scheme which is provided by BUPA. TFCPL pays the premium and the respective employee pays tax at source for this benefit via the monthly payroll.

##### Permanent Health Insurance

All members of Senior Management are provided with insurance under the company's Permanent Health

Insurance Scheme. This policy provides 75% of pre-disability income (pensionable salary) once an individual exceeds six months' continuous sickness absence.

### Pension Arrangements

Senior Management is all eligible to be members of the company's group personal pension scheme which is provided by Legal & General. A range of benefits are provided in the event of death whilst employed by the company:

(i) a lump sum payment equal to four times Pensionable Earnings at the date of death.

(ii) a pension will be provided to an individual's spouse at the date of death, equivalent to 25% of Final Pensionable Earnings, together with pensions for each of up to three children under the age of 18 (or 23 if in full time education) of 10% of Final Pensionable Earnings.

(iii) In the event of an employee's death whilst a member of the Plan, the full value of the accumulated fund will be paid to their dependants.

For 2008–09, Pensionable Earnings was linked to a salary cap of £110,000.

### SENIOR MANAGEMENT CONTRACTS

It is the company's policy that Senior Management has contracts with an indefinite term which provide for six months' notice to be given by either party. Guy Hands' contract provides

for six months' notice to be given by him and 12 months' notice to be given by the company.

In addition to the notice period, each contract for Senior Management contains restrictive covenants that prohibit the individual from: taking up employment with any business that is (or is about to be) in competition with Terra Firma, soliciting or canvassing customers or clients of Terra Firma; and enticing or trying to entice away any member of staff – for a period of up to six months following the termination of their employment.

**SALARIES ARE SET  
IN RELATION TO  
AN INDIVIDUAL'S  
PERFORMANCE  
AND MARKET  
COMPARATOR  
GROUPS**



## ALIGNMENT OF INTEREST

## Alignment of interest is fundamental to the way Terra Firma does business

As well as investing capital on behalf of others, Terra Firma and its team have committed a total of more than €400 million to the Terra Firma funds. As one of the largest investors, it prospers along with its investors by developing and growing successful businesses.

This alignment of interest is fundamental to the way Terra Firma does business. 'Carried interest' is performance-based and only results in Terra Firma's team participating in enhanced returns if a fund generates a return to investors in excess of 8% per annum over its life. A fund typically has a 10-year life and carried interest is typically paid in the later years when the majority of a fund's investments have been realised and investors have received back their investment plus the majority of their profits. This type of structure aligns interest to help create value in businesses over the long term and, while not perfect, is far superior to the focus on annual results and bonuses that exists in public companies and investment banks.

By way of example, in March, Terra Firma will distribute back to investors the carried interest (payments for strong investment performance) that had previously been earned (accrued in escrow, but not paid) and which would have formed the bulk of the reward for Terra Firma's senior team. If our investors suffer, then it is only right that the Terra Firma team's reward should suffer at the same time.

€400m  
committed to Terra Firma Funds

## RISK AND UNCERTAINTIES<sup>1</sup>

Investment-related risks are taken into account by the IAC

### RISK AND UNCERTAINTIES

As an investment adviser, TFCPL must provide high-quality investment advice to the fund managers. This advice necessarily provides views on uncertain future conditions and events which may not turn out as expected. TFCPL has the appropriate skilled investment professionals, organisational structure and processes to manage the risk inherent in this activity. Where risks are relevant to investment recommendations, they are taken into account by the IAC in its risk and return assessment of a potential investment.

### RISK MANAGEMENT Framework and the role of the IAC

It is the role of the IAC to make investment and divestment recommendations to the fund managers. Part of this role is to ensure that all recommendations adhere to the fund managers' strategy and to assess the risk and return profile of an investment opportunity. We believe that this consistent approach, and the resulting build-up of knowledge, enhances Terra Firma's ability to extract additional value in transactions and generates higher returns with less risk.

The IAC brings objective discipline to the review of each investment opportunity. The ongoing dialogue

between the IAC and the team working on a particular transaction results in the sharing of best practices across all Terra Firma transactions as well as identifying additional risks and opportunities that might otherwise have gone unnoticed. It also increases pricing discipline and generally acts as a constructive check for the investment team.

The advice that TFCPL provides aims to take account of potential market risks related to economic and political events and trends. In order to stay apprised of current events and future financial trends and help form its view, TFCPL constantly reviews advice from economic, political, legal, financial, tax and accounting advisory firms.

TFCPL is advised by two independent advisory councils – Terra Incognita and Terra Consilia – which each meet regularly with senior TFCPL team members. The groups provide independent insight and ideas on specific business sectors, and advise on how current and changing political landscapes might affect investment activity. Several of these advisers also participate on the boards of Terra Firma's portfolio businesses as Non-Executive Chairmen or Non-Executive Directors.

**TFCPL HAS THE APPROPRIATE SKILLED INVESTMENT PROFESSIONALS, ORGANISATIONAL STRUCTURE AND PROCESSES TO MANAGE THE RISK INHERENT IN PROVIDING ADVICE TO THE FUND MANAGERS**

<sup>1</sup> The risks outlined here represent those faced by TFCPL. The risks faced by the Terra Firma funds are set out in the Notes to the Accounts in Section 4. The portfolio businesses will face risks in their normal course of business and will be set out in their respective accounts.

#### CORPORATE RISK

TFCPL has in place policies and procedures to appropriately consider and manage its risks as set out below:

#### Liquidity Risk

TFCPL has a financial reporting and budgeting process which incorporates regular cash flow forecasts of advisory fee income and overheads. Given the predictable nature of its cash flows, liquidity risk is remote.

#### Leverage Risk

TFCPL has no current borrowings.

#### Interest Rate Risk

TFCPL has no interest rate exposure as it has no current borrowings.

#### Currency Risk

TFCPL is exposed to currency risk to the extent that, while its income is predominantly in £ Sterling, some of its costs are in € Euros. These costs relate to the fees paid to its German subsidiary, terrafirma GmbH. While this mismatch is not hedged, management believes it does not represent a material risk to the business.

#### Competitor Risk

Given the success of the strategy to date and the strength of the advisory team, the Board considers it unlikely that the fund managers might seek alternative investment advisers.

#### Key Man Risk

The reputation of TFCPL is highly correlated to the ability of Guy Hands and other members of the Senior Management team. TFCPL has considered the risk of the resignation, incapacity or death of these individuals and has put in place appropriate plans to manage this risk, including the purchase of key man insurance.

#### TREASURY POLICIES

TFCPL generally receives its advisory fees from its clients in advance. Costs are budgeted and forecasts updated regularly. Cash flows are monitored to ensure reserves are adequate.



## 4 Terra Firma's Funds TFCP II, TFCP III, TFDA

Photo: Nigel Flory

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4



## FINANCIAL INFORMATION

BALANCE SHEET	Note	Aggregate 2008 €'000	Aggregate 2007 €'000
<b>FIXED ASSETS</b>			
Investments	3(b), 6	4,598,641	5,514,289
<b>CURRENT ASSETS</b>			
Cash at bank		58,979	64,085
Accounts receivable	7	3,517	5,234
<b>CURRENT LIABILITIES</b>			
Loans and advances	8	0	(145,505)
Accounts payable	9	1,496	(6,846)
<b>NET ASSETS</b>		<b>4,659,641</b>	<b>5,431,257</b>
<b>PARTNER'S CAPITAL ACCOUNTS</b>		<b>4,659,641</b>	<b>5,431,257</b>

PROFIT AND LOSS STATEMENT	Note	Aggregate 2008 €'000	Aggregate 2007 €'000
<b>INCOME AND EXPENDITURE</b>			
Bank interest	3(d)	980	3,015
Foreign exchange	3(e)	(9,142)	8,137
Interest on investments	3(d)	0	48,281
Partnership expenses		(13,655)	(30,191)
Auditor's remuneration		(189)	(167)
Bank charges		(17)	(42)
<b>Net Income</b>		<b>(22,023)</b>	<b>29,033</b>
Provision for impairment <sup>1</sup>		(1,365,396)	0
Capital gain on investments	3(d)	0	1,039,417
<b>NET RESULT FOR THE YEAR</b>		<b>(1,387,419)</b>	<b>1,068,450</b>

<sup>1</sup> While we anticipate that over the long term our businesses will achieve capital gains as in the past, given the current world economic turmoil, the directors have taken the prudent decision to take a provision for impairment on two of the investments in the funds.

CASH FLOW STATEMENT	Aggregate 2008 €'000	Aggregate 2007 €'000
<b>RECONCILIATION OF NET RESULT TO NET CASH</b>		
<b>OUTFLOW FROM OPERATING ACTIVITIES</b>		
Net result for the financial year	(1,387,419)	1,068,450
Add back impairment loss on investments	1,365,396	0
Increase in receivables	1,824	124
Decrease in payables	(5,332)	(9,206)
Income and gain on investments	0	(1,087,698)
<b>Net Cash Outflow from Operating Activities</b>	<b>(25,531)</b>	<b>(28,330)</b>
<b>CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT</b>		
Proceeds from sale of investments	0	1,289,590
Purchase of fixed asset investments	(454,689)	(3,195,716)
<b>Net Cash Outflow from Investment Activities</b>	<b>(454,689)</b>	<b>(1,906,126)</b>
<b>FINANCING</b>		
Drawdowns on partners' commitments	729,550	3,157,152
(Decrease)/increase in loans and advances	(145,505)	145,505
Advance of General Partners' shares	(105,396)	(129,852)
Returns during the year	(4,233)	(1,223,443)
<b>Net Cash Inflow from Financing Activities</b>	<b>474,416</b>	<b>1,949,362</b>
Foreign exchange translation	(698)	0
<b>NET (DECREASE)/INCREASE IN CASH</b>	<b>(5,106)</b>	<b>14,906</b>

## NOTES TO THE ACCOUNTS

### 1. ORGANISATION AND PURPOSE

The financial information presented represents the aggregated financial position and financial performance of the Terra Firma Limited Partnerships described in the following table ('the Partnerships'). The financial information has not been consolidated. The Partnerships aggregated in the financial information are:

Partnership	Establishment Date	General Partner
Terra Firma Capital Partners II, L.P.-A *	21 June 2002	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners II, L.P.-B *	21 June 2002	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners II, L.P.-C *	2 July 2002	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners II, L.P.-D *	2 July 2002	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners II, L.P.-E *	22 August 2002	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners II, L.P.-F *	25 October 2002	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners II, L.P.-H *	1 October 2003	Terra Firma Investments (GP) 2 Ltd
TFCP II Co-Investment 1 LP #	24 November 2003	Terra Firma Investments (GP) 2 Ltd
TFCP II Co-Investment 2 LP #	25 November 2004	Terra Firma Investments (GP) 2 Ltd
TFCP II Co-Investment 3 LP #	23 March 2005	Terra Firma Investments (GP) 2 Ltd
TFCP II Co-Investment 2a LP #	29 April 2005	Terra Firma Investments (GP) 2 Ltd
Terra Firma Capital Partners III*	19 December 2005	Terra Firma Investments (GP) 3 Ltd
Terra Firma Deutsche Annington L.P. +	3 March 2006	Terra Firma Investments (DA) Limited
Terra Firma Deutsche Annington-II L.P. +	19 May 2006	Terra Firma Investments (DA) II Limited
Terra Firma Deutsche Annington-III L.P. +	19 May 2006	Terra Firma Investments (DA) Limited
TFCP II Co-Investment 4 LP #	23 August 2006	Terra Firma Investments (GP) 2 Ltd
TFCP III Co-Investment LP #	4 September 2007	Terra Firma Investments (GP) 3 Ltd
TFCP II Co-Investment 4a LP #	17 September 2007	Terra Firma Investments (GP) 2 Ltd
TFCP III Co-Investment 2 LP #	29 November 2007	Terra Firma Investments (GP) 3 Ltd
Terra Firma Deutsche Annington-IV L.P. +	19 December 2007	Terra Firma Investments (DA) Limited
Terra Firma Deutsche Annington-V L.P. +	19 December 2007	Terra Firma Investments (DA) Limited
TFCP II Co-Investment 4b LP #	4 August 2008	Terra Firma Investments (GP) 2 Ltd
TFCP III Co-Investment A LP #	4 August 2008	Terra Firma Investments (GP) 3 Ltd

The principal place of business of the Partnerships is Guernsey. Their day-to-day activities are carried out by the General Partners of the Partnerships on behalf of the Limited Partners.

The main purpose of the Partnerships is to provide partners with long-term capital appreciation through the acquisition of equity and equity-related investments predominantly in unquoted companies in Western Europe and by making other selective equity and equity-related investments.

## 2. GENERAL PARTNERS' SHARES

The General Partner of the Partnerships marked \* receives a profit share of 1.5 per cent of committed capital per annum (1.0 per cent of aggregate total contributions for Terra Firma Capital Partners II, L.P.-H) payable semi-annually in advance. Where a Limited Partnership does not yet have sufficient profits any shortfall is funded by payment of an interest-free loan from the Limited Partnership. Such a loan is repayable only out of future allocations of net income or capital gains, but not otherwise.

The General Partner of the Partnerships marked # are allocated a percentage of net profits to a maximum of €1,000 if any.

	Aggregate 2008 €'000	Aggregate 2007 €'000
Advance of General Partners' share at 1 January	140,839	39,331
General Partners' shares for the year	105,396	129,852
Allocation of current year profit	0	(28,344)
	<b>246,235</b>	<b>140,839</b>

The General Partners of the Partnerships marked + are allocated a proportion of all amounts of principal, net income, net income losses, capital gains and capital losses, which would otherwise be allocated and distributed to non-executive Limited Partners, as defined in the Limited Partnership Agreements of these Partnerships. The General Partners' share is included within the Partners' Capital Accounts.



### 3. PRINCIPAL ACCOUNTING POLICIES

The following accounting policies have been used consistently in dealing with items which are considered material in relation to the Partnerships' financial statements:

#### (a) Basis of Accounting

The aggregated financial statements have been prepared in Euros (€) since this is the functional currency of the Partnerships (except for TFCP II Co-investment 1 LP) under the historical cost convention and in accordance with the Limited Partnership Agreements.

#### (b) Investments

Those investments that are associates or are subsidiary undertakings are carried at the lower of cost or the General Partners' valuations in accordance with the Partnerships' normal policies and Limited Partnership Agreements and are neither equity-accounted nor consolidated.

The General Partners consider that investments in subsidiaries are held as part of an investment portfolio with a view to the ultimate realisation of capital gains and hence, in accordance with the Limited Partnership Agreements, fully consolidated financial statements are not required.

#### (c) Valuation of Investments

Investments are valued at the lower of cost or General Partners' valuations at the balance sheet date. The Limited Partnership Agreements require the General Partners to prepare such valuations in accordance with International Private Equity Valuation Principles. Provisions for diminution in value are recognised where the General Partners consider there has been a permanent impairment in value.

#### (d) Income

Bank interest is accounted for on an accruals basis. Due to the nature of investments in the Partnerships, whereby they are deemed to be equity or equity-related, investment income receivable and foreign exchange gains and losses on investments are accounted for when the receipt of income is reasonably certain. Where taxes on income received by the Partnerships have been deducted at source, these have been allocated to individual Partners in accordance with the Limited Partnership Agreements.

#### (e) Foreign Exchange

Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are reported at the rates of exchange prevailing at that date. All amounts for reporting purposes are shown in Euros (€). Investment transactions and income and expenditure items are translated at the rate of exchange achieved in the transaction. The assets and liabilities of TFCP II Co-investment 1 LP have been translated into Euros at the reporting date. Income and expenses have been translated at exchange rates as at the dates of the transactions.

### 4. Allocation of Partnerships Profits and Losses

The profits and losses of the Partnerships are allocated between the Partners pursuant to the Limited Partnership Agreements.

### 5. Material Agreements

Under the terms of the Limited Partnership Agreements, the General Partners are responsible for the management of the Limited Partnerships. Under the terms of the Investment Advisory Agreements, Terra Firma Capital Partners Limited (TFCPL) was appointed to advise the General Partners as to the acquisition, monitoring and realisation of the investments of the Limited Partnerships.

6. INVESTMENTS	Aggregate 2008 €'000	Aggregate 2007 €'000
<b>EQUITY AND EQUITY-RELATED INSTRUMENTS</b>		
As at 1 January	5,514,289	2,520,465
Additions during the year	454,469	3,195,716
Disposals during the year	0	(201,892)
Provision for impairment of investments	(1,365,396)	0
Foreign exchange translation	(4,721)	0
<b>COST OF INVESTMENTS AT 31 DECEMBER</b>	<b>4,598,641</b>	<b>5,514,289</b>
Estimate of fair value	4,489,826	7,794,426

7. ACCOUNTS RECEIVABLE	Aggregate 2008 €'000	Aggregate 2007 €'000
Drawdowns receivable	755	4,296
Divestment proceeds receivable	469	458
Deal costs	0	460
Recoverable costs receivable	2,293	0
Other debtor	0	20
<b>TOTAL</b>	<b>3,517</b>	<b>5,234</b>

8. LOANS AND ADVANCES	Aggregate 2008 €'000	Aggregate 2007 €'000
Bridging loan for acquisition (repayable January 2008)	0	103,381
Bridging loan for acquisition (repayable June 2008)	0	42,124
<b>TOTAL</b>	<b>0</b>	<b>145,505</b>

9. ACCOUNTS PAYABLE	Aggregate 2008 €'000	Aggregate 2007 €'000
Accrued expenses	467	6,138
Recoverable costs payable	603	0
Other creditor	129	393
Limited Partner contributions	297	315
<b>TOTAL</b>	<b>1,496</b>	<b>6,846</b>

## 10. RISK MANAGEMENT

### Government regulation

The Guernsey Limited Partnerships are regulated by the Guernsey Financial Services Commission. The operations of the Terra Firma portfolio companies are regulated by local authorities where the companies operate. Changes to the regulatory frameworks under which the companies operate are monitored.

The Partnerships operate complex legal and corporate structures across a number of legal jurisdictions. The General Partners of the Partnerships take appropriate professional advice on the suitability of these structures.

### Macroeconomic risks

The Terra Firma Partnerships invest mainly in European companies. The performance of their investment portfolios is influenced by economic growth, interest rates, foreign exchange rates, and commodity and energy prices in these countries. This risk is mitigated by the geographically diversified operations of the Terra Firma portfolio companies, which cover over 60 countries.

### Investment decisions

The Partnerships operate in a competitive market. Changes in the number of market participants, the availability of debt financing within the market and the pricing of assets may have an effect on the Partnerships' financial position, financial returns and ability to bid successfully for potential acquisitions. The General Partners of the Partnerships appraise potential investments in a rigorous manner, taking advice from a range of advisers, including TFCPL.

### Valuations and exits

The unrealised valuations of the Partnerships' investments in portfolio companies and opportunities to realise the value in these investments is affected by market conditions, including the availability of debt finance and the level activity in the buyouts market. The timing of opportunities for the Partnerships' to exit their investments is also dependent on market conditions.

The Partnerships do not hedge the market risk inherent in their portfolios, but continually monitor current conditions by taking advice from a range of advisers, including TFCPL.

### Liquidity risk

By giving appropriate notice, the Partnerships may call on their Limited Partners to fund calls for investment and partnership expenses. The Partnerships do not commit to investment decisions beyond their ability to draw funds from investors.

### Currency risk

The Partnerships generally report in Euros and distribute profits to investors in Euros. The Partnerships invest in portfolio companies denominated in Euros, US dollars and Sterling and pay expenses in a range of foreign currencies and hence have an exposure to currency movements. The Partnerships hedge foreign exchange exposures in the completion of investment acquisitions and realisations.

### Interest rate risk

Some Terra Firma Partnerships bear short-term borrowings with floating-rate interest and are subject to risk of arising from changes in interest rates.

### Operational and credit risks

The Partnerships are exposed to a range of operational risks inherent in their portfolio companies, including business disruptions, legal and regulatory changes and human resources risk. The General Partners mitigate these risks by taking advice from TFCPL, which maintains operational oversight of portfolio business companies supported by a reporting framework and controls. The maximum credit risk of the Partnerships with regard to an individual portfolio company is their carrying value of their investment in the company.

## CONTACT INFORMATION

### TERRA FIRMA'S FUNDS

#### General Partners

Terra Firma Investments (GP) 2 Ltd  
Terra Firma Investments (GP) 3 Ltd  
Terra Firma Investments (DA) Limited  
Terra Firma Investments (DA) II Limited  
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#### Boards of Directors of the General Partners

Nigel Carey  
Fraser Duncan  
Guy Hands  
John Loveridge  
John Stares  
Iain Stokes

#### Administrator

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#### Funds' Auditor

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## TERRA FIRMA'S BUSINESSES

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