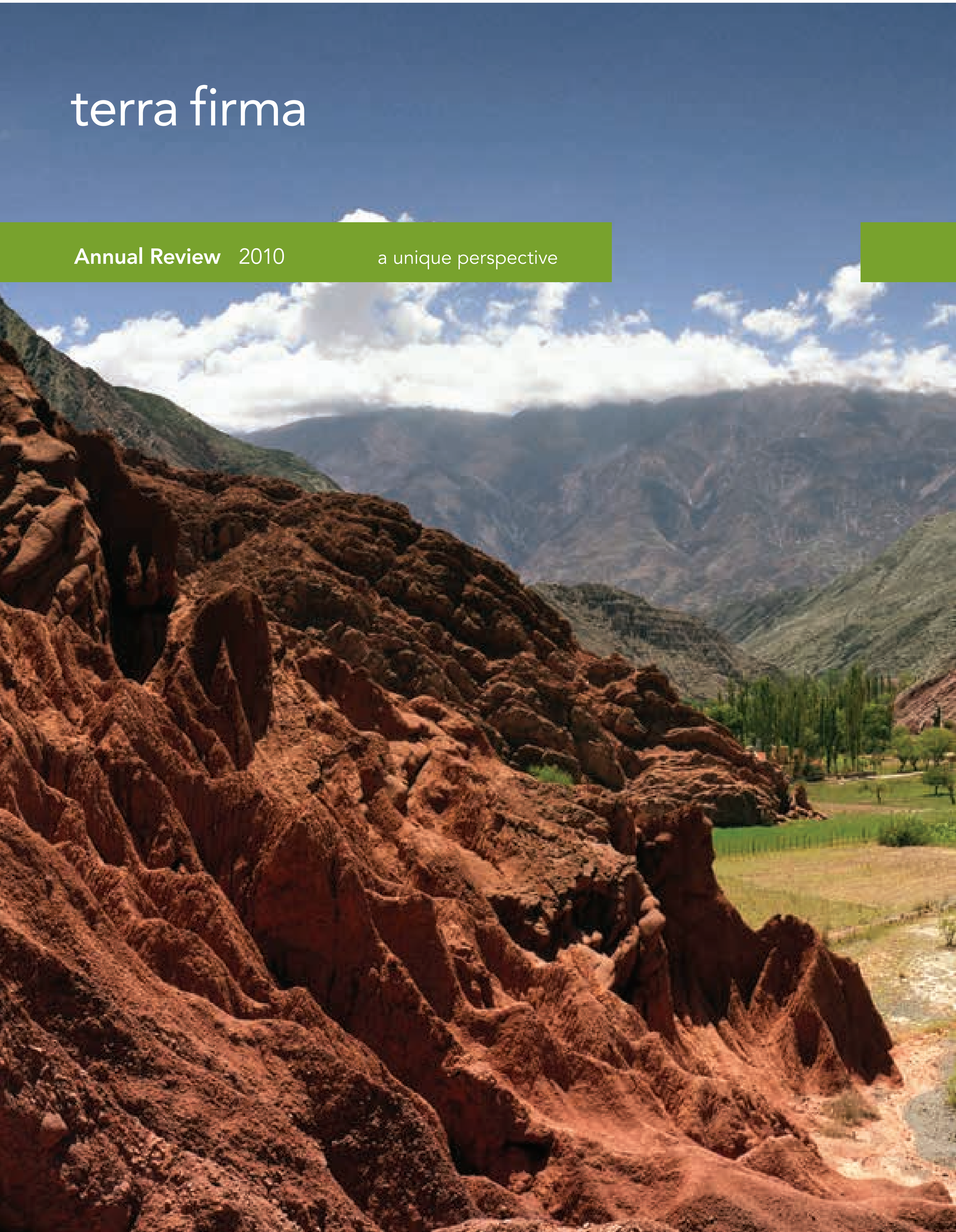
Contents



# terra firma

**Annual Review** 2010

a unique perspective



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

# 1 Executive Summary

## LETTER FROM THE CHAIRMAN

# OUR IMMEDIATE TASK IS TO CONTINUE TO ACHIEVE STRONG RETURNS FOR TFCP II AND TFDA AND TO RECOVER ALL OF THE CAPITAL FOR OUR INVESTORS IN TFCP III

**31 December 2010**

Welcome to the fourth Annual Review of Terra Firma in which we are pleased to present Terra Firma and our portfolio businesses.

Strategic change and operational improvement in our portfolio businesses are at the heart of what we do at Terra Firma. We strongly believe that, by focusing on these strengths, we will deliver the greatest value to all of our stakeholders as we build sustainable businesses. 2010 was a year of modest economic growth in the West and continued recovery in the financial markets. For Terra Firma, it was a year of significant achievements for our portfolio companies as we detail in this Annual Review.

Clearly, the big public issue for Terra Firma in 2010 was EMI and the associated litigation. Whilst EMI was operationally transformed by the Terra Firma team under our ownership (with a doubling of EMI's earnings), the relationship between Terra Firma and Citigroup during our ownership of EMI was not a happy one. This culminated in our court case about material misrepresentations made by Citigroup with regard to the auction for EMI in 2007. It was a difficult (and highly unusual) decision to sue one's bank, but the merits of the case and our strong belief that our first duty was to our investors caused us to proceed with the litigation.

The credit crunch created an untenable situation for deals done just prior to that time and hence the timing of our bid for EMI became a material factor in the success of the deal. That timing was determined by the apparent existence of a competitive auction – something that we believe Citigroup misled us about. Had we known there was no competitive auction we would not have bid and, had the bid deadline been pushed back, the imminent decline of markets for securitisations and leveraged loans would have become more apparent and the deal could never have been completed. Still, the outcome of the trial was not what we wanted or expected (and is currently being appealed). While EMI is now part of our history, we have learnt a lot from the experience, and included later in this Annual Review are some of the lessons learnt from what happened post the auction.

Turning back to our other portfolio companies, we worked hard on improving and growing our portfolio businesses throughout 2010, as well as sourcing and evaluating acquisition opportunities to complement and enhance them. Terra Firma continues to own businesses across a diverse number of sectors including: green energy; infrastructure; 'affordable' housing; agriculture; transportation leasing; and entertainment.

This year's Annual Review documents a year of solid results and steady improvement across the portfolio. For example, in the entertainment sector, Odeon & UCI reported 14% EBITDA growth year-on-year as audiences embraced the year's strong 3D film slate. Despite the difficult housing market in the UK, Annington achieved higher rental income in 2010, and is poised to do well in

2011 with the release of 175 new units by the Ministry of Defence in the first quarter. In Germany, Deutsche Annington generated over €500 million in EBITDA for the first time in its history. Meanwhile, AWAS, our aircraft leasing business, refinanced $530 million of its Jetstream/Jetbridge debt in June and negotiated a $600 million loan in the autumn. In renewable energy, Infinis demonstrated another strong performance as year-to-date EBITDA rose 52% to £75 million. In the US, EverPower continued to invest heavily in its wind farms, making excellent progress on its development pipeline. Phoenix Group exceeded its target for natural gas connections, despite challenging economic and weather conditions in Northern Ireland. Similarly, Tank and Rast overcame a soft consumer economy in Germany and severe weather to post an increase in year-on-year EBITDA. Finally, at CPC, our agricultural investment in Australia, we maintained a high level of investment in the business and made an acquisition to continue to build scale. All these successes are testimony to the dedication of the employees at our portfolio companies and the strength of the working relationship between Terra Firma and the management of our portfolio businesses.

2010 marked an important year for the private equity industry as a whole – and a year of consolidation at Terra Firma. The private equity industry entered the year still reeling from the bust that had followed the boom period of 2004 to 2007, but the private equity industry began to take measurable steps towards recovery. However, available capital for private equity worldwide ('dry powder') remained at an all time high, while the supply of investment opportunities offering attractive returns lingered at low levels, and hence investing for target returns was tough. Consequently, Terra Firma used 2010 to ensure that our investment strategy was firmly focused on our core thesis of investing in operating assets. We continued to scour the market seeking those investment opportunities that complement Terra Firma's existing portfolio and fit squarely within Terra Firma's investment model. We made bolt-on acquisitions that will improve the ultimate value of our portfolio companies such as at Odeon & UCI, where we acquired three key Italian sites. We also found new opportunities such as Rete Rinnovabile (RTR), a leading Italian solar generation business that will further solidify our market-leading position in the green energy industry.

Our investment activity in 2010 and the successes of our portfolio businesses meant that we moved from a feeling of gloom, which the credit crisis had cast upon us all, to one of measured optimism. Whilst not everything went our way in 2010, the year presented us with a unique opportunity to both build and reflect.

Having taken the time to look back on our experiences since the formation of Terra Firma in 2002, we have learnt from the pitfalls caused by the frenetic market activity that led to the 2007 bust. It is clear that all private equity firms in the period running up to 2007 maximised leverage to the greatest possible extent. In a stable economic environment, this was an entirely appropriate strategy. However, in a volatile economic environment, private equity firms must moderate their appetite for leverage in order to ensure the sustainability of their portfolio businesses even if it means sacrificing some

## LETTER FROM THE CHAIRMAN

potential return. In this way, the businesses become less vulnerable to a boom and bust cycle (as such a cycle will certainly re-occur). We have carefully analysed both the private equity industry and, within that industry, the particular business of Terra Firma, as we would any company we were looking to buy in order to determine what we did right and what may need to be changed.

Many private equity firms grew rapidly between 2002 and 2007, and Terra Firma was no exception. However, the private equity industry believed that its business model could defy the normal laws of rapid growth by capturing all the economic benefits of scale without suffering from the problems caused through strong growth. Terra Firma, in common with most of our competitors, expanded our business to take advantage of the market opportunity presented by the huge increase in the demand for private equity. We grew our fund size, our employee numbers and our geographical presence.

At Terra Firma, we saw the opportunity to apply our contrarian and interventionist investment approach on a much larger scale. We had invested successfully at Nomura from 1995 and formed a highly motivated team following our spin-out in 2002. We then had great success with TFCP II between 2003 and 2006 and were highly confident that we could manage a significantly larger fund, making much larger investments without compromising our investment success. From a core of about 60 employees, we began to hire in anticipation of having much more capital to invest. In a short period of time, we effectively doubled the size of our team and brought in new, high quality people on both the financial and operating sides of the organisation.

As we proceeded to raise TFCP III in the halcyon days of 2007, we recognised that we needed to do bigger deals. The €500 million to €1.5 billion deals that were the hallmark of TFCP II would not suffice in an investment environment built upon a €5 billion plus fund along with an enormous appetite among our investors for co-investment. In those days, Terra Firma was convinced that we could replicate our investment strategy on deals of €3 billion plus. Focusing on deals of this size meant that our universe of potential investments shrunk significantly, and a much larger proportion of our deals would now have to be sourced from public-to-private transactions. Our interest in 2007–2008 in Alliance Boots, Intercontinental Hotels and then EMI (to name but a few of the listed targets we looked at) was indicative of the size of companies that were required to make our fund size work. While these companies clearly met our investment objectives and disciplines, they required much larger teams than we had deployed historically, and much greater reliance on continued liquidity in the capital markets.

The investor demand for private equity was enormous in 2007, and we raised the soft cap on TFCP III from €3 billion to a hard cap of €5.4 billion: still not satisfying all investor interest. Indeed, we had over €3 billion of unsatisfied investor interest when we closed the fund in May 2007 after just over a year of fundraising. This investor demand was based on the performance of TFCP II, and the quantity of potential investment opportunities. This environment created a unique circumstance for us, one that was robustly debated both internally and externally: should we keep the fund open and raise several € billion more in investment capital or close it? Ironically, had we continued to market TFCP III and focused our investment activity on investing the over 30% of TFCP II that was still available, we would have avoided doing a huge deal near the top of the credit cycle. Indeed, if we had closed TFCP III sometime in late 2008, after fully investing TFCP II, then we would have had €7 – €10 billion of uninvested capital in the new fund at a more opportune point in the investment cycle. However, we chose to close TFCP III at €5.4 billion in May 2007, and focused on investing the new capital, whilst finding co-investment opportunities for our investors, and utilising the remainder of TFCP II's capital in cross-funded deals with TFCP III.

As we all now know, it did not turn out as we expected it would. We made two acquisitions before the financial crisis hit, one was EMI and the other was Pegasus (an add-on to AWAS). In the case of AWAS and its combination with Pegasus, the business has gone on to be operationally very successful and continues to grow having had the full support of its banks. Unfortunately in the case of EMI, despite the incredible effort of the Terra Firma team and the employees and artists in EMI, the loss of the business to Citigroup was a very disappointing outcome. What makes long-term success in business is having the ability to learn from such events and ensuring that history doesn't repeat itself.

In the process of analysing what happened with EMI, we also gained enormous insight into the steps needed to drive Terra Firma forward in today's private equity market. Our immediate task is to continue to achieve strong returns for TFCP II and TFDA and to recover all of the capital for our investors in TFCP III. We are hopeful that our green energy investments and our aircraft business will collectively make substantially more profit than we lost on EMI. While this will be a great recovery, we accept that when we seek to raise another fund it will be significantly smaller than TFCP III, probably in the range of €2 – €3 billion compared with the €7 – €10 billion that we could have raised back in 2008. However, a €2 – €3 billion fund will allow us to return to the €250 – €500 million initial equity investment size that is our hallmark. In the meantime, we have been restoring Terra Firma to a size where we all share a common DNA. In other words, we are going back to where we were in 2006 with approximately 60 professionals. We also intend to change the Limited Partnership Agreement for our next fund to prohibit cross-fund investments and restrict the maximum amount we can invest in any one transaction to 15% of the fund with a view to selling down 5% to co-investors, thus leaving our fund investors with an exposure to any one deal of 10%. This will limit the co-investment underwriting pool to 5% rather than 20%.

We deeply appreciate the support of all our stakeholders across our portfolio businesses throughout the past year during what has been a challenging time. In 2011, all of us at Terra Firma are highly motivated to build and recover value for our investors, particularly those investors in TFCP III. Obviously, we have a large financial incentive, as we are among the largest investors in all our funds and the largest in TFCP III. However, our strongest motivation is to do the right thing for all our investors and stakeholders: that is our mission.

**Best wishes**

**Guy Hands**

## LETTER FROM THE CEO

# WE FUNDAMENTALLY REDEFINE HOW OUR PORTFOLIO COMPANIES OPERATE

**31 December 2010**

Private equity has done an extraordinary job over the years of redefining and reinvigorating businesses that have experienced turbulent times and required new business models. Over the last 16 years in all of its 28 deals, Terra Firma has specialised in doing this and thereby fundamentally redefining how our portfolio companies operate.

The great credit crunch of 2007 has had a major effect on the private equity world and it was obvious from the end of 2008 that private equity needed to apply its skills to redefining and reinvigorating its own business model. Terra Firma was acutely aware of this, and therefore when I took over as CEO in April 2009, I set myself the objective of ensuring that Terra Firma, having survived the credit crunch, should become a much stronger organisation. I believe Terra Firma should have the resilience not just to endure such events, but also to thrive from the opportunities they create.

Almost two years on, as I look across the company, I believe our team is indeed more cohesive and capable than at any time in our history. Therefore, in the first part of my letter I want to highlight some of the key developments within Terra Firma, and then discuss a few of the key challenges facing the private equity industry, particularly in Europe.

**Building strength in Terra Firma in order to face the future with confidence**

In 2009, our organisation was not appropriately staffed to deal with the realities created by the credit crunch. Whilst our team of 112 people was appropriate in an environment where our €5.4 billion third fund would be followed by an expected €10 billion fund to be raised that year, this business plan was no longer realistic. Terra Firma needed to be revitalised and suitably-sized for the new business environment.

The overriding challenge was to reduce the team down to a level appropriate for the new reality (which I felt was about 85–90 people spread across professionals and support staff). It was a sensitive balancing act to keep a high level of experience in the organisation, and at the same time create opportunities for some of our up-and-coming professionals, whilst providing openings for fresh talent.

As a private equity firm that believes in making fundamental operational change in our portfolio businesses, Terra Firma also considers change within our own organisation to be a good thing. In the end, what is important, whether we are managing one of our businesses or Terra Firma, is that we have the team and resources necessary to operate effectively. In fact, we deem a certain level of staff turnover at all levels in Terra Firma essential in order to be able to advance people from within the organisation.

We have been able to promote (and therefore retain) key professionals at all levels of the organisation, despite experiencing some turnover. Notably, we have promoted five long-term Terra Firma employees to Managing Director in the past year. These promotions reflect Terra Firma's long-term goal of developing a top team from within its organisation, particularly on the investment side. We have kept the number of Financial Managing Directors and Operational Managing Directors at the same level as in 2007. In order to do this, we have made a number of hires, most notably recruiting operational experts. Overall, we now have around 90 people in the organisation and anticipate that this will rise to the mid-90s by year end. This plan brings us back to the level of staffing that we had at the beginning of 2007.

The enhanced capability of Terra Firma is reflected by the increased experience of our senior team. For example, the tenure of our Managing Director group now averages nine years compared with seven years back in 2007. Additionally, despite the changes in our organisation, the tenure of almost 70% of our Managing Director group pre-dates the creation of Terra Firma in 2002. In short, I firmly believe that we now have the right team to drive the performance of our existing portfolio businesses, successfully invest the remaining capital in the TFCP III and TFDA funds and meet the challenges of the emerging new environment for private equity.

The majority of Terra Firma's senior professionals have always spent a significant amount of time travelling, either visiting our portfolio businesses or looking at new opportunities. Indeed, time in the office is not time well spent, unless senior people are brain-storming with colleagues on either potential new deals or on strategies for portfolio businesses. The level of travel has intensified over the past two years with the addition of portfolio businesses in the US and Australia and the focus on our portfolio businesses interacting with Asian counterparties. Therefore, in order to maximise the value of the time we spend together, we have set aside a series of new deal and portfolio business days throughout the year in Guernsey which all Terra Firma professionals attend. In this way, we have increased our common understanding of the objectives of each portfolio business and the issues with regard to each new deal.

### Challenges facing the private equity industry

As a result of the recent financial crisis and associated scandals, regulators and politicians appear determined to make our industry subject to greater regulation. This is despite the fact that it is generally agreed that our industry was not a cause of the recent problems.

These regulatory initiatives may well result in significant changes to the way we do business. This is not a passing fad: private equity firms that want to survive and thrive in the future will have to adapt to this tougher environment.

## LETTER FROM THE CEO

Within Europe, the European Parliament is flexing its muscles in the financial services arena: both the Alternative Investment Fund Managers Directive ('AIFMD') and the Solvency II Directive are examples of this.

AIFMD, which is expected to come into effect across the EU in January 2013, has already been the subject of much commentary. It remains to be seen whether the AIFMD will reduce the scope and breadth of investment by European professional institutions (it may be that funds in non-EU jurisdictions have no interest in meeting the European criteria). Equally, it is not yet clear whether the AIFMD will increase or decrease the attractiveness of offshore financial centres. Due to the transparency and disclosure regulations it imposes on them, the AIFMD is likely to make European private equity investors less attractive to investees than other sources of funding.

Perhaps of even more concern is the Solvency II Directive. This directive is due to be implemented across the EU by 31 October 2012 and will make big changes to the regulation of insurers and reinsurers; in particular, introducing new requirements on the amount of capital firms must hold against various risks. Under Solvency II, investment in private equity is deemed to be high risk, meaning a high level of capital will have to be applied against private equity investments. Our concern is that the new requirements will dissuade insurance companies from investing in private equity.

In addition, there is an ongoing debate in Brussels about extending the Solvency II regime to pension funds. The European insurance industry is pressing for it on the grounds of creating a level playing field between insurance funds and pensions funds. As expected, representatives of the pension fund industry and governments of countries with developed defined benefit pension schemes are bitterly opposed to the move. While the European Commission is understood currently to have decided against extending Solvency II to pension funds, some of the proposals in its July 2010 Green Paper require pension funds to maintain minimum capital reserves related to risk levels and asset classes.

While the full impact of these regulatory initiatives is not yet known, it is undoubtedly the case that they will increase costs for fund managers, funds and investors and will make the private equity industry less agile due to the additional 'red tape'. More worryingly, it is perfectly possible that they will make private equity less attractive both to traditional private equity GPs and LPs. This potential result seems extraordinary when you consider private equity's role in driving companies forward and enabling them to compete, especially given the emergence of Asian businesses.

While it will take time to sort out the regulatory landscape in Europe, I am confident that Terra Firma will be able to continue to meet the needs of our investors, portfolio companies and stakeholders.

**Yours sincerely**

**Tim Pryce**

EMI

# THE EMI INVESTMENT: AN ANALYSIS

EMI

**On 1 February 2011, ownership of EMI was transferred to Citigroup, bringing to an end Terra Firma's ownership of the company. At the conclusion of a deal, we evaluate our investment decisions and strategies, in order to improve our future processes and investment results. Learning from what went right and what went wrong on every deal is the most effective way of improving a private equity firm's fund returns over the long term. Normally this is an internal process, but since EMI has been so highly visible, we have decided to share our analysis and the lessons we have learnt.**

## TERRA FIRMA'S INVESTMENT THESIS FOR EMI

EMI was the fourth largest record company and largest music publisher in the world when we committed to purchase it in May 2007. It was a business requiring strategic transformation, a repositioning of its assets, fundamental operational change and dramatic improvement in its cash flow. It was also an asset-rich business with market-leading publishing and recorded music catalogues. EMI was a company that fitted our investment strategy and we believed could benefit from ownership by Terra Firma; in particular, we felt that the business needed to switch from being primarily focused on 'music hits' to a business more broadly focused on rights management services.

EMI's overall revenue and profits had been declining for the better part of a decade. This was largely because it had responded slowly to the rapid structural shift in the consumer market for recorded music towards digital consumption. Within the company, the Music Publishing division's earnings were stable as it had already started to address the shift away from sales to consumers by increasing its business-to-business (B2B) transactions. Within the Recorded Music division, Terra Firma recognised the need to address the structural problems facing the division, whilst also reducing costs substantially. We saw the potential to increase the profitability of the Recorded Music catalogue considerably whilst also repositioning the division to capitalise on the opportunities offered by the digital market.

These opportunities meant that the EMI investment would fit neatly within Terra Firma's investment model.

## THE SIZE AND SCALE OF THE EMI INVESTMENT

EMI was a very large transaction for Terra Firma; it was over three times the size of the average deal we had done in the previous 12 years. Given where we were in our fundraising and investment cycles, we had made a strategic decision to consider larger deals, making EMI an attractive target. In 2006–2007, Terra Firma raised TFCP III (a €5.4 billion fund) and had approximately 40% of TFCP II (a €1.9 billion fund) left to invest. Despite much greater investor interest in TFCP III, we placed a hard cap on the fund in order to limit its size and maximise co-investment opportunities for our investors.

Terra Firma had approval through the Limited Partnership Agreements to invest up to 30% of each fund in any one investment with the intention of then selling down at least 10% to co-investors, particularly our LPs. This co-investment opportunity was a key selling point for attracting investors into Terra Firma's funds and one we have historically provided to our investors. Terra Firma also obtained approval from its Advisory Boards to cross-invest between funds.

## EMI

# THE SIX KEY FACTORS IMPACTING THE EMI INVESTMENT POST-COMMITMENT

**In examining the EMI investment, we have identified that, once we were committed to the investment, there were six primary factors (other than the EMI auction process) that impacted on the results of the EMI transaction. Four of these were market-related factors and two were judgment calls made by Terra Firma prior to, or during, the acquisition. These six factors emanated from our commitment to the EMI transaction which began with the auction process that we now know would have 'busted' had we not participated in it by the deadline. The six are briefly outlined below, along with our conclusions on each.**

## FACTORS

1

### COLLAPSE OF THE SECURITISATION MARKETS

The opportunity to securitise EMI's publishing assets was an important part of our financing strategy for the EMI transaction. The chance to lead the securitisation programme was also one of the main reasons that Citigroup and other banks were keen to provide financing. After the collapse of the sub-prime market in the US post-May 2007, the ability of banks to securitise any type of loan disappeared, along with their willingness to underwrite loans in the syndicated loan market. The effect on the EMI transaction was three-fold:

- The cost of debt became higher than we had expected and modeled;
- The financial covenants that Citigroup put in place in August 2007 became more onerous than originally envisaged. These covenants were designed as part of a debt package that both Terra Firma and Citigroup had intended to refinance in 2008 through a securitisation programme; and
- The loan made by Citigroup in advance of the expected securitisation was a lot smaller than the anticipated proceeds from that securitsation: Terra Firma therefore had to leave substantially more equity in the transaction to compensate.

2

### CITIGROUP'S INABILITY TO SYNDICATE THE LONG-TERM SENIOR BANK BRIDGE LOAN

With the securitisation market disappearing and collateralised bond obligations drying up, Citigroup could not syndicate its long-term senior bank bridge loan. Consequently, the entire loan package remained on Citigroup's books and Terra Firma faced a one-on-one negotiation with Citigroup over the necessary restructuring of the loan. Working with a syndicate of banks, each with a smaller individual exposure, would have been preferable for both EMI and Terra Firma.

## EMI

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### REDUCTION OF CO-INVESTMENT INTEREST

In May 2007, when Terra Firma committed to the EMI transaction, we had very substantial indications of co-investment interest from our fund investors, as expected. The co-investment interest that existed prior to the close of the deal was consistent with the level of interest we had seen from our fund investors in the past.

As the credit crisis developed in 2007, interest from our investors in co-investing in EMI waned and the opportunity to sell-down a portion of our funds' EMI investment disappeared. As a result, Terra Firma ended up with 30% of both TFCP II and TFCP III invested in EMI rather than the intended approximately 10%. The inability to execute our co-investment sell-down strategy also meant that Terra Firma had insufficient capital to consider a large consolidating acquisition, such as a merger of EMI with Warner Music (a similar-sized rival music business), or even an accretive acquisition in music publishing.

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### COLLAPSE OF INDUSTRY MULTIPLES

During the period 2008–2009, valuation multiples collapsed, particularly in the music industry. Aside from the general market pressure and the disruption that the internet was bringing to the music industry, there was additional pressure on multiples in music publishing brought on by a series of factors: first, speculation in the marketplace during 2007–2009 about a possible sale of EMI's Music Publishing division created the impression that Terra Firma and EMI were forced sellers; second, the markets correctly perceived that neither EMI nor Warner Music were in a position to buy the other; and finally, valuations were depressed by the possibility that Warner Music might, at some time in the future, dispose of its own publishing business. All of these factors combined to reduce multiples in the sector well beyond, and for a longer period than, the decline suffered in the general market.

The option to sell Music Publishing at a valuation based on the level of multiples prevailing in early 2007 was important in managing the downside risk in the EMI transaction for the lender, Citigroup, and the borrower. That option not only disappeared for the borrower, but, by mid-2010, the notional value of EMI's Music Publishing and Recorded Music divisions had gone down by more than 50% as multiples collapsed. The multiples for music companies, and therefore the valuation of the EMI business, did not start to recover until late 2010.

Today, Citigroup appears to be engaged in a process of selling EMI, and Warner Music has just been sold for a multiple that seems to indicate a blended forward multiple of 10.5 times EBITDA. Traditionally, EMI, based on its stronger publishing business and better music catalogue has been expected to trade higher. Therefore, an approximate blended rate for the valuation of EMI might be about 12 times today. Additionally, if the new owners of Warner Music were to be the purchasers then one would expect the seller of EMI to get 12x 50% of any expected synergies. Based on these numbers, EMI would once again be back to the levels at which it traded in May 2007 – particularly as the debt and securitisation markets have recently started to recover.

## Armed with these insights and lessons learnt, we will strive to ensure that history is not repeated

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### OPERATIONAL CHANGE STRATEGY

Prior to our acquisition of EMI, Terra Firma had devised a comprehensive operational change strategy to move EMI towards becoming a music rights management company. The new and the remaining members of the incumbent management team at EMI subsequently endorsed this strategy. Together, we worked hard to execute the operational transformation programme. Whilst we encountered strong resistance to our changes by some in the industry, and substantial noise in the media, the positive results are now clear: EMI's earnings have effectively doubled; the business's cash position has moved from very negative to highly positive; its margins now lead the industry; it has increased its market share; and EMI has garnered a disproportionate share of critical acclaim for its artists. In short, the Terra Firma team correctly spotted an opportunity ripe for operational transformation and executed it well.

Today, much of the music industry is being forced to make changes similar to those implemented by Terra Firma and EMI three years ago.

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### KEY MARKET ASSUMPTIONS

Terra Firma's post-acquisition strategy for EMI was built upon two market assumptions: a continued decline in physical sales of recorded music; and an increase in digital sales. Our thesis was therefore to increase earnings from B2B transactions and to restore the profitability of retail sales by shifting to digital platforms. Our team's forecast of the growing importance of B2B commerce to the music industry proved correct and we were able to exploit this successfully. Our thesis about the decline in physical sales of music to the consumer and its impact on EMI Recorded Music was also correct. However, the expected increase in digital sales to consumers did not materialise as we, and indeed the rest of the music industry, expected. Overall, the team's market assumptions, while more conservative than the industry, still proved to be overly optimistic. However, Terra Firma does not believe that the shortfall in the digital forecast had a major effect on the investment.

# EMI

## LESSONS LEARNT

Hindsight demonstrates that the market-driven factors – securitisation, syndication, asset valuation multiples, and the co-investment sell down – all became highly correlated as a result of the extreme market events in 2007–2008. Terra Firma, along with most private equity firms, viewed these factors as relatively independent in underwriting deals. In fact, we believe if Terra Firma – or any private equity firm – were to approach deals with the expectation that all four of these market factors could simultaneously go terribly wrong, then there are few, if any, deals that could be done: hardly the purpose of LBO funds. Since these sizable shocks seem to occur every 5 to 15 years, or about once in every three funds, what can we do to mitigate at least some of the impact on any fund?

### STRUCTURAL CHANGES TO LIMIT RISKS:

In light of our experience with EMI and the entire pre-credit crisis period, we have concluded that Terra Firma can mitigate the downside risks of these transactions by:

- prohibiting cross-fund investments; and
- reducing the targeted co-investment on any deal from 20% to 5%.

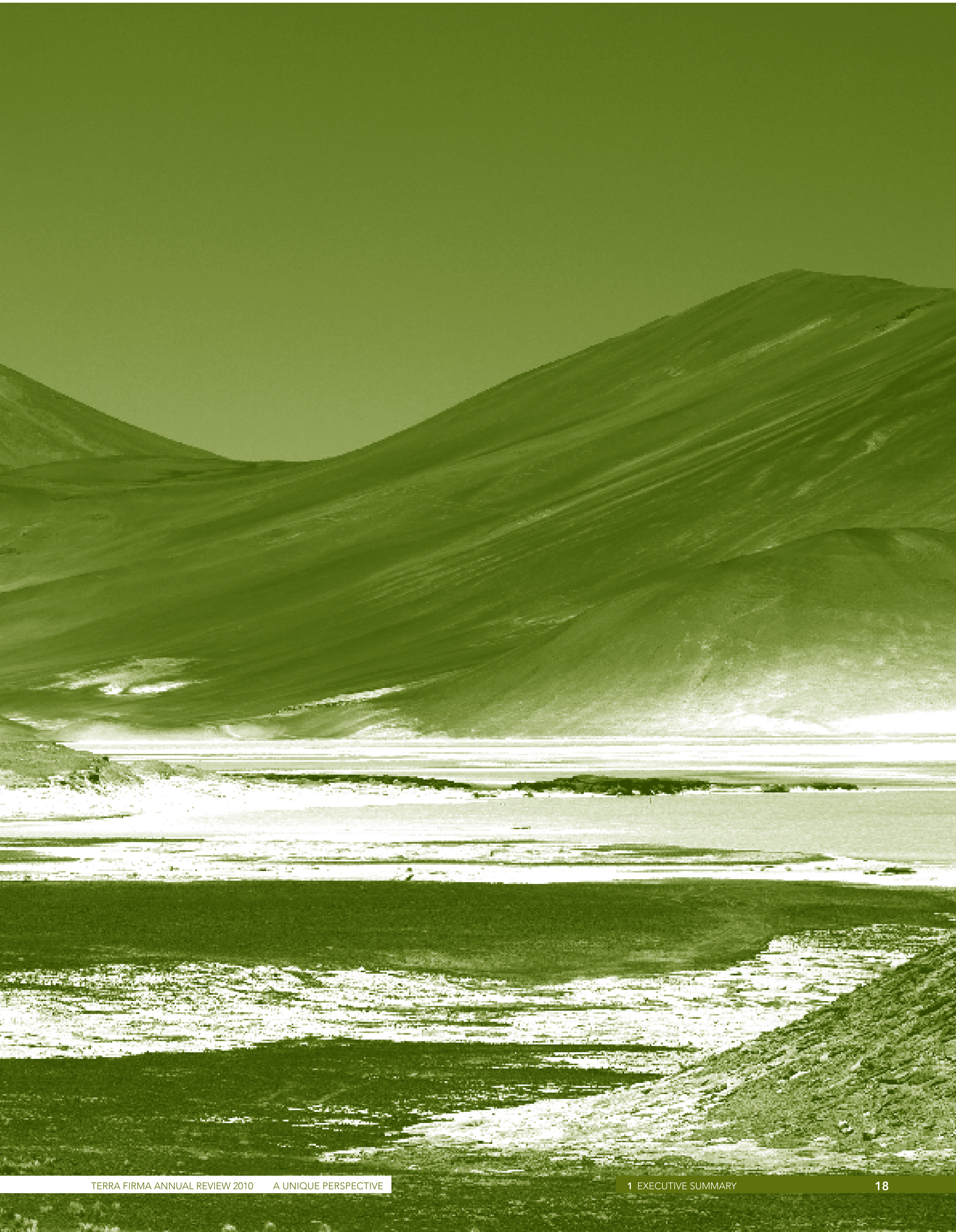
Going forward, Terra Firma will implement these structural limitations. Terra Firma will limit its concentration in any one investment to 15% with the intention of selling it down by 5%, leaving our funds with a net 10% exposure. We will also encourage LPs interested in committing to substantial co-investment to ensure that they are in a position where they are able to underwrite and commit to the deal at the same time that we do.

### OPERATIONAL ASSESSMENT:

After review and extensive discussion, Terra Firma is entirely comfortable that its strategy of moving EMI to a music rights management company and the implementation of these changes at EMI, were not causes of the losses flowing from the EMI investment. Indeed, our investment thesis has largely been validated, and our operational transformation at EMI was successful.

## CONCLUSION

The risks associated with EMI were not fundamentally different from those that we assess with every transaction. The six factors described earlier demonstrate how market conditions coupled with too great a risk allocation can converge and create unacceptable results. Of course, we would never have purchased EMI on the day we did at the price we did had we known about the nature of the auction and the fact that without our bid it would have been busted. Regardless, what Terra Firma now intends to do, armed with these insights and lessons learnt, is to ensure that history is not repeated.



## ABOUT TERRA FIRMA

# TERRA FIRMA MEANS 'SOLID GROUND' AND REFLECTS OUR CONSISTENT APPROACH OF BUYING COMPANIES WITH A STRONG ASSET BASE

**Terra Firma invests in underperforming assets and transforms them into exceptional businesses through a combination of strategic and operational change, sustained investment and improved management.**

Terra Firma seeks to invest in basic industries that have underperforming assets and are not dependent on technological innovation or branding. We commit capital on the basis of our own analysis and research which often leads us to form opinions and develop strategies that are different from the market consensus. Whether by coming up with a different approach to the running of a business, finding solutions to problems which others have considered intractable or taking contrarian views on macro issues, Terra Firma has identified hidden value in many businesses.

We identify industry trends and sectors first and then find specific investment opportunities to which we can apply our ability to change businesses. This 'macro-to-micro' approach to identifying investment opportunities underpins our investment strategy.

We add value through being directly involved in the companies we buy. We overhaul the business both strategically and operationally and often make significant changes to management. Making such fundamental changes in a business takes time, but a long-term approach to investment is vital in order to create successful, sustainable businesses.

Our highly diverse team of in-house specialists provides us with the requisite financial, operational, legal, tax and structuring skills to pursue a differentiated investment strategy and strategically reposition businesses.

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, Terra Firma Capital Management (Guernsey) Limited, Annington Management Services (Guernsey) Limited and any of their affiliates.

The financial information contained in this Annual Review is as at 31 December 2010.

# €17 bn

OF EQUITY FUNDS RAISED
AS AT DECEMBER 2010

# €14bn

OF EQUITY CAPITAL INVESTED IN BUSINESSES AS
AT DECEMBER 2010

# €18 bn

OF REALISED AND UNREALISED EQUITY VALUE IN
OUR BUSINESSES AS AT DECEMBER 2010

## ABOUT TERRA FIRMA

# TERRA FIRMA IS A LONG-TERM INVESTOR AND OUR BUSINESS PLANS ARE DESIGNED TO DELIVER SUSTAINABLE GROWTH

### OUR INVESTORS

Terra Firma invests on behalf of pension funds, insurance companies, government investment funds and endowments from around the world. The success of Terra Firma's businesses helps to provide enhanced income for all our investors, and Terra Firma is very aware of its fiduciary duty to these underlying beneficiaries.

### OUR STRUCTURE

Terra Firma's funds are typically Guernsey Limited Liability Partnerships. It has three active funds, namely Terra Firma Capital Partners II (TFCP II) and Terra Firma Capital Partners III (TFCP III), which are general private equity buy-out funds, and Terra Firma Deutsche Annington (TFDA) which is a specialist German residential real estate fund. Terra Firma's investors invest as Limited Partners within the fund, and the day-to-day affairs of each Partnership are managed by its General Partner, a Guernsey-based management company. The General Partners make all investment decisions on behalf of the relevant funds.

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 60 countries.

Terra Firma Capital Partners Ltd (TFCPL) in the UK, with support from terrafirma GmbH in Germany and Terra Firma Capital Management Ltd (TFCML) in Guernsey, provide investment advice to the General Partners, including sourcing and advising on investment opportunities and realisation strategies.

### OUR PEOPLE

We have the full range of specialist skills necessary to pursue our differentiated investment strategy and strategically reposition businesses. Our highly diverse team of financial, operational, legal, tax and structuring experts allows us to identify opportunities that are overlooked by others and to capture hidden value in businesses. From the outset, our transaction teams are multidisciplinary with each team having sector specialisations that reflect the knowledge and experience of the team members.

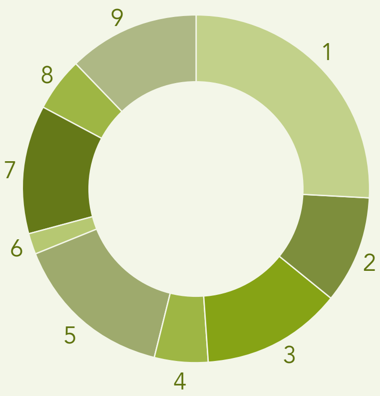
Operational expertise is fundamental to enhancing value within our portfolio businesses and in the current economic climate such skills are more important than ever. Our operational team has many years' experience in running and improving performance in numerous businesses and has strong strategic, operational and managerial expertise.

The Terra Firma advisory team is made up of approximately 90 people in London, Frankfurt and Guernsey, drawn from 21 countries and speaking 20 languages. They come from a wide variety of backgrounds, including industry, finance, consultancy, private equity, law and accountancy.

We intend to make a number of additional senior operational and financial hires over the coming year to expand our in-house capabilities and ensure that we are appropriately staffed to be able to manage new investments as well as our existing portfolio businesses.

## More than two thirds of our investors are from outside Europe

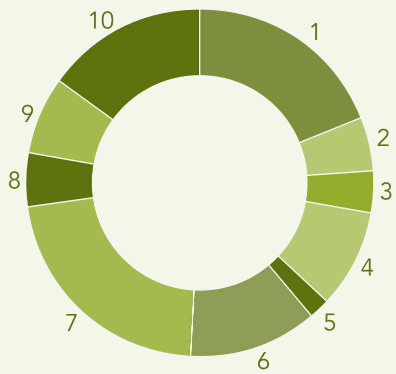
### FUND INVESTORS AND CO-INVESTORS BY REGION




1 US 26%
2 Middle East 10%
3 UK 13%
4 Asia (excl. Japan) 5%
5 Europe (excl. UK) 15%
6 Australia 2%
7 Canada 12%
8 Terra Firma 5%
9 Japan 12%

## Pension funds make up more than a quarter of our investor base

### FUND INVESTORS AND CO-INVESTORS BY TYPE




1 Fund of Funds 19%
2 Private Pension Funds 5%
3 Endowment 4%
4 Insurance 9%
5 Corporate 2%
6 Government Investment Funds 12%
7 Public Pension Funds 22%
8 Terra Firma 5%
9 Family Trusts 7%
10 Banks/Financial Services 15%

## OUR BUSINESSES

# TERRA FIRMA'S PORTFOLIO BUSINESSES DELIVERED A SOLID PERFORMANCE IN 2010

**Throughout the year, we continued to build our existing businesses through organic growth and add-on acquisitions. By focusing on maximising the potential from our existing asset base and investing further capital where appropriate, our businesses performed well in 2010. They have worked at reducing excess spending and improving operational efficiencies while working alongside our investment and operational teams on strategic plans to drive each business forward.**

By working closely together, we are able to build businesses that are operationally efficient, innovative and which have a deep understanding of the industry in which they operate. In the current economic environment, this focus is especially important and our businesses have proved themselves equal to the task once again this year.

### FINANCIAL POSITION

As liquidity improved in almost all asset classes, all refinancing requirements within the portfolio businesses were successfully addressed in 2010. As illustrations, AWAS refinanced $530 million of its Jetstream/Jetbridge debt in June and negotiated a $600 million loan in the autumn, and Odeon & UCI successfully closed negotiations to reset its operating company debt facilities thereby freeing up around £100 million of additional capital to reinvest in the business in the next few years.

We are conscious that the ability to refinance our businesses is a key component to their success. Each business will continue to actively manage its balance sheet in 2011 and follow capital market developments closely to ensure they capitalise on any attractive opportunities for refinancing.

### VALUATIONS

We firmly believe that private equity firms should be realistic and transparent about valuing their businesses on a mark-to-market basis. At Terra Firma, we engage in a thorough and detailed review of the valuations of our portfolio businesses annually or more frequently if circumstances merit, and have those processes and valuations audited by KPMG for our annual accounts.

Private equity valuations have three major elements: the operating performance of the portfolio business itself, the application of a multiple or discount rate from listed comparable companies or recent transactions to value that operating performance, and the effect of currency movements if the reporting currency of the portfolio business differs from that of the relevant fund.

Terra Firma's portfolio businesses delivered a solid performance in 2010, with most companies showing year-on-year improvement (see following table).

While the financial markets recovered from the lows of 2009, volatility remained a key feature of the public markets in 2010, and most showed little overall change over the course of the year.

The volatility of the euro, the reporting currency of Terra Firma's funds, has been a key contributor to the valuations as portfolio businesses that report in US dollars, sterling or the Australian dollar all benefited from the weakened euro.

Nearly all of the portfolio businesses' fair market valuations have increased since the end of 2009 but, as always, Terra Firma has been cautious in determining the year-end valuations for its portfolio.

Whilst fair market valuations are important indicators of value, Terra Firma is a long-term investor and our business plans are designed to deliver long-term sustainable growth rather than short-term profits. The most important valuation is the one attained when a business is ultimately sold, and we are continually working to ensure that the final performance of our investments is as strong as it can possibly be.

| EBITDA BY PORTFOLIO BUSINESS | Currency | 2009 | 2010 | Change % |
|---|---|---|---|---|
| Annington[1] | £m | 106 | 117 | 10 |
| AWAS | $m | 653 | 649 | 0 |
| CPC | A$m | 22 | 17 | (24) |
| DAIG | €m | 480 | 502 | 5 |
| EMI[2] | £m | 252 | 229 | (9) |
| EverPower | $m | (8) | (10) | (25) |
| Infinis[1] | £m | 49 | 75 | 52 |
| Odeon & UCI | £m | 80 | 92 | 14 |
| Phoenix Group[3] | £m | 20 | 21 | 3 |
| Tank & Rast | €m | 186 | 195 | 5 |

[1] Based on 9 months to December 2009 and December 2010

[2] Maltby Group data at statutory rates

[3] Underlying EBITA

## OUR BUSINESSES

# WE CONTINUED TO BUILD OUR EXISTING BUSINESSES THROUGH ORGANIC GROWTH AND ADD-ON ACQUISITIONS

### OPERATING PERFORMANCE

#### ANNINGTON

Annington reported higher rental revenue for the nine months to December 2010 compared with the same period in 2009. Sales revenues and volumes, however, were influenced by the stagnant housing market in the UK and were lower than the prior year. The Ministry of Defence released a further 175 units in the first quarter of 2011, with possibly more later in the year. Sales in 2011 are expected to be down on 2010's levels due to the continued subdued market conditions.

#### AWAS

AWAS significantly outperformed its key operational and financial objectives in 2010 as a result of stringent credit and cost management as well as a faster than expected market recovery. The business will receive a further boost in 2011 as it takes delivery of 15 new aircraft, all of which are already placed with customers and expected to contribute to continuing operational PBT growth.

#### CPC

2010 has been a challenging year for CPC as a result of import restrictions that were unexpectedly imposed by the Indonesian authorities on live imports during the year. Lower export sales were partially offset by higher domestic sales, but higher associated freight costs resulting in lower margins reduced EBITDA to A$17 million from A$22 million in 2009. CPC continues to invest in its existing properties: by improving access to water, building new fencing and clearing overgrown land, the number of cattle that can be supported by the properties has consequently increased.

Work continues to identify additional acquisitions to increase the geographic diversity and the flexibility of the land portfolio and a number of additional properties have been added to the portfolio since acquisition at attractive prices.

#### DEUTSCHE ANNINGTON

Deutsche Annington continued to grow its EBITDA this year as both the Rental and Sales divisions reported increased profitability year-on-year, and the business achieved a landmark in 2010, exceeding €500 million full year EBITDA for the first time. More than 21,600 new rental contracts were signed in 2010 and sales agreed during the year were up 37% against prior year. This is an exceptional result and demonstrates the benefits of the investment in IT infrastructure, improved customer care and a new management team. Looking ahead, the business will continue to search for add-on portfolios at attractive prices.

#### EVERPOWER

In the first full year of Terra Firma ownership, EverPower continued to make good progress. Highland, its first operating wind farm, continued to perform well with turbine availability at a year-to-date average of 97% against a budget of 95%. All applicable consents have now been obtained on the next two wind farm sites and improved turbine supply arrangements have been agreed. These two sites will be fully operational by the end of 2011 and will bring total operational capacity to 189 MW. Together with the portfolio of five further near-term development opportunities, with an estimated capacity of approximately 600 MW, the business is developing in line with our long-term plans.

# 60

OUR PORTFOLIO BUSINESSES OPERATE IN 60 COUNTRIES

# €4.9bn

TOTAL REVENUE FROM OUR PORTFOLIO BUSINESSES FOR THE 12 MONTHS TO DECEMBER 2010

## INFINIS

Infinis had another good year with year-to-date EBITDA of £75 million, 52% ahead of the same period last year. Favourable pricing agreements, operational improvements and continued cost control all contributed to its strong performance. The business has continued to strengthen its position in the renewable energy market, building on the 2009 acquisition of Novera with the acquisition of Ardrossan, a fully operational wind farm in Scotland in May 2010 and the acquisition of a wind farm at Rheidol, Wales in January 2011. It also acquired a further 12.9 MW consented at two sites in Yorkshire from E.ON UK plc.

## ODEON & UCI

Odeon & UCI ended 2010 on a strong note despite the weaker film slate during the 2010 Football World Cup and the poor weather conditions experienced across Northern Europe in December; a key trading month for the cinema industry. The business achieved full year EBITDA 14% ahead of prior year as audiences embraced a strong film slate and the increased number of 3D films including ground-breaking hits such as Avatar, Toy Story 3 and Alice in Wonderland.

## PHOENIX GROUP

Phoenix reported revenues and underlying EBITA (after recovery of overpayments) ahead of prior year as the severe winter pushed up volumes and lower than expected gas input prices reduced costs. On new connections, the business has delivered an exceptional performance again this year, exceeding budget in spite of the challenging economic environment and weather conditions.

## TANK & RAST

2010 was a difficult trading year for Tank & Rast as German consumer confidence remained low and severe winter weather reduced the volume of traffic on the autobahn. Despite this, the business delivered EBITDA ahead of 2009, as cost-saving programmes that were introduced continued to yield savings and the customer-focused initiatives that have been rolled out to improve the quality and consistency of the facilities improved revenues against prior year.

## VALUE CREATION

# DELIVERING A BLOCKBUSTER PERFORMANCE

## THE ODEON & UCI STORY

**Terra Firma acquired Odeon in September 2004 and UCI in October 2004 with a clear strategy of unlocking value through bringing the two businesses together to take advantage of the consolidation that was expected within the European cinema industry and driving operational change. Enhancing the consumer experience has been a key element of Odeon & UCI's business plan and the case study below shows how this focus has benefited the business.**

A trip to the cinema has changed a lot in recent years. Today's film-goers expect more than just a big screen and a bucket of popcorn, and the cinema experience has evolved to meet demand. Odeon & UCI has been driving that change for years. Since these two leading names were acquired by Terra Firma in 2004 and merged to form Europe's largest cinema group, the emphasis has been on continual improvement. The businesses have since worked in tandem, investing time and resources and anticipating trends to make sure Odeon & UCI cinemas are delivering exactly what today's customers want – from comfier seats and extra screens to quality coffee and great food choices.

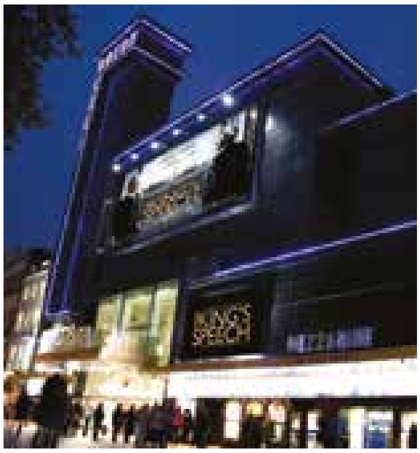
All of these changes have made a huge difference to a visit to the cinema for the customers who queue up at Odeon & UCI box offices across Europe, and in the process they've also helped to boost the company's performance. The cinema industry has proved to be a resilient sector in difficult economic times, and Odeon & UCI has worked hard to ensure it maximises that opportunity while continuing to invest and innovate in order to carry on significantly outperforming the competition.

### NEW AND IMPROVED CINEMAS

In line with the overarching strategy created in partnership with Terra Firma, Odeon & UCI has focused on finding new ways to deliver the best cinema experience. As well as building ten new cinemas across Europe in the six years since the acquisition, the company has completed 16 major refurbishments and acquired six existing sites in addition to the acquisition of six competitor cinema circuits in its existing markets. This investment of around £135 million means that thousands more people are able to see the latest films at their local Odeon or UCI cinema in state-of-the-art surroundings.

As well as offering extras such as premier seats and better food and drink choices, Odeon & UCI's new breed of cinema also gives film fans access to the most advanced cinema technology, from IMAX screens to digital.

The company has led the way in embracing digital technology. The roll-out of digital screens across the estate is now well under way and, with the six major Hollywood studios signed up, the future of the format is assured. This has allowed the company to capitalise on the huge



explosion in 3D films. In fact, 3D films accounted for 25% of Odeon & UCI's ticket sales in 2010, with customers showing that they are happy to pay a premium for the 3D experience. Odeon & UCI is way ahead of its competitors in providing the 3D experience.

Besides customers paying more to see 3D films, other benefits of investing in digital film technology for Odeon & UCI include improved operational flexibility, leading to lower costs and the fact that it provides a better platform for screen advertising and alternative content, with sports, opera and concerts all popular.

## RAMPING UP RETAIL

Terra Firma's experience of realigning businesses to capitalise on new opportunities has proved to be especially valuable and relevant in the changing world of cinema. Food and drink have become a much bigger part of the cinema experience in recent years and this is reflected in the new offers and retail brands now available in Odeon & UCI cinemas. With screens across seven countries in Europe, Odeon & UCI has had to work hard to understand its different markets and deliver a retail experience that is both relevant and profitable.

The company has discovered the right formulas for each country after trialling various options across its territories. In the UK, for example, coffee and ice-cream were at the top of customers' wish lists, while it was pizza and focaccia bars in Spain, and pizza and panini in Italy. By teaming up with the leading brands in these areas – including Ben & Jerry's, Telepizza and Pane e Sapori – Odeon & UCI has given customers several more reasons to watch the latest blockbuster at their local cinema.

The company is continuing to develop its retail offering and looking for ways to give customers even more of what they want. For instance, following the 2010 Retail Matters research programme, Odeon's UK cinemas are now introducing changes such as guest popcorns, smaller-sized dispensed drinks, better quality hot dogs and nachos.

**Odeon & UCI has led the way in embracing digital technology**

# VALUE CREATION

## TURNING CINEMA-GOERS INTO LOYAL CUSTOMERS

Odeon & UCI's loyalty schemes have proved to be a hugely successful way to thank customers for choosing the brand and to give them an incentive to come back. In the UK, the 'Odeon Premiere Club' had over one million members by the end of 2010, the largest scheme of this type in the UK. In Continental Europe, UCI's various loyalty card schemes grew 23% on 2009 and now have over 1.4 million members. In the UK, customers have the opportunity to sign up to one of three different Film Fan packages, each offering the opportunity to earn points that can be redeemed for drinks, film tickets and popcorn as well as regular updates and access to exclusive Odeon Premiere Club promotions. For the company, it can build up a better understanding of what its customers want, track customer patterns and ensure that Odeon remains competitive in a burgeoning market.

## CINEMAS WITH A SMILE

Of course, one of the most important parts of the cinema experience is the service that cinema-goers receive from the Odeon & UCI teams. That is why the company has invested significantly in its learning and development programmes, making sure its people are well-trained and motivated. In the UK, all employees benefit from a structured ongoing training and development programme that starts with an induction of up to 16 weeks. Online learning and development courses are also used extensively across Europe and the company runs a wide variety of workshops for team leaders and managers. Every customer who visits an Odeon or UCI cinema benefits from this commitment to great service and the Mystery Shopper scores underline that – Odeon & UCI are consistently being scored ahead of the competition by these anonymous customers who evaluate service quality.

All of this innovation and investment has been steered by the strategy that Terra Firma developed during its 2004 acquisitions of Odeon & UCI and which have been fine-tuned together ever since. The changes have unquestionably benefited Odeon & UCI's customers, but they are also clearly reflected in the company's most recent set of figures.

They show a business that is outperforming its market despite a difficult economic climate that has had a clear impact on screen advertising. Against this backdrop, Odeon & UCI has generated a continuing growth in revenue per head (both in ticket and retail sales) that is well ahead of inflation. At the same time, its compound EBITDA growth rate is over 10% per annum.

By keeping pace with technology and listening to its customers – then investing to deliver a better and better cinema experience – Terra Firma and Odeon & UCI are delivering an outstanding performance for customers and stakeholders alike.


**11** IMAX SCREENS – LARGEST IMAX OPERATOR IN EUROPE

**2.4m** LOYALTY CARD HOLDERS

**16** MAJOR REFURBISHMENTS OVER THE LAST SIX YEARS

## LONG-TERM ALIGNMENT

# BY INVESTING IN OUR FUNDS, WE ARE ALIGNED WITH OUR INVESTORS

**Private equity funds are typically structured as partnerships between the investors who provide capital and the private equity fund that invests that capital. At Terra Firma, we strongly believe in this partnership.**

Whilst not perfect, the long-term nature of private equity is reflected in its reward structure. The long-term alignment of interest between investor and private equity employee has always been of the utmost importance for the private equity model.

Terra Firma's compensation for its employees reflects this alignment, especially amongst its senior personnel where compensation is focused on carried interest. Carried interest is performance-based and only results in rewarding 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- to 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. When carried interest payments are payable to Terra Firma, they are held in reserve until five years after the fund closes before being released to the team.

We believe that this type of incentive structure is vital in ensuring that private equity employees are focused, not only on the careful selection of investments, but also on nurturing each investment to exit, in order to ensure maximum return for the investors and – ultimately – the transaction team.

While carried interest is an important way of aligning the interest of a private equity manager with its investors, it is no substitute for the manager actually investing in its funds. Each time we have raised a fund, nearly all of our employees have invested capital. Overall, we have committed more than €520 million to our funds and are the largest investor in TFCP III and one of the largest investors in TFCP II. At Terra Firma, our belief in the future success of our investments is demonstrated by us investing our own personal savings, as well as our careers, in them.

**Everyone at Terra Firma has one goal – to ensure our investments are as strong as they can possibly be**

## TRANSPARENCY AND STAKEHOLDER INTERACTION

# IT IS ESSENTIAL THAT EVERYONE UNDERSTANDS OUR OBJECTIVES, PLANS AND RESULTS

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

Terra Firma has been a strong supporter of the application of the guidelines established by the Walker report in November 2007 and we are pleased that our efforts have been acknowledged by the Guidelines Monitoring Group, chaired by Sir Michael Rake.

We remain committed to following – and in many areas exceeding – the Walker guidelines. The two Terra Firma businesses that are required to report according to the guidelines, Odeon & UCI and Annington, have complied fully. The rest of our portfolio businesses have all committed to the guidelines on a voluntary basis. In total, we manage seven of the 58 firms who either meet the criteria or have committed to them on a voluntary basis; more than any other private equity firm.

In September 2009, the ILPA issued Private Equity Principles that addressed alignment, governance and transparency. Many of these principles have been part of Terra Firma's modus operandi from the very beginning and Terra Firma formally endorsed them in March 2010.

Tim Pryce, Guy Hands

We believe that a progressive approach to transparency gives us a competitive advantage by making us more attractive to potential staff, to companies that we wish to invest in, and to governments and unions with whom we interact. Of course, to our investors, who provide the capital that we invest, the financial workings of our businesses have always been visible.

## OUTLOOK FOR 2011

# ALL WESTERN ECONOMIES FACE MOUNTING INFLATIONARY PRESSURES


Robbie Barr, Quentin Stewart

Although there has been a general improvement in the global economic and financial environment over the past year, it is the emerging markets – especially China, India and Brazil – that are driving the overall global recovery. While there has been a mild upturn in many Western economies, a number of countries are running uncomfortably large deficits while continuing to struggle with high unemployment and low levels of consumer confidence.

Western governments have been divided into two camps in responding to this environment: those that are willing to ignore their rising fiscal deficit and are attempting to boost their economies through fiscal stimuli and quantitative easing; and those that are attacking their deficits by cutting public expenditure and increasing taxes. No matter what their approach is, all the economies of the Western world face mounting inflationary pressures, driven mainly by growing demand from the emerging economies for food, raw materials and consumer goods.

As world financial markets continue to recover, private equity firms will increasingly look to IPOs as an exit for their portfolio businesses. Private equity deal volume and size were higher than expected in 2010, especially for secondary buy-outs. These trends are likely to be maintained this year as debt availability continues to improve. However, the large overhang of private equity capital and resultant increased competition for assets means that finding a business at a reasonable price will continue to prove challenging.

## We believe that 2011 will present opportunities to invest in businesses where we can add value through strategic and operational change

Private equity firms will continue to have to enhance value in their portfolio businesses by making tangible operational and strategic improvements rather than just relying on leverage. At Terra Firma, a strong operational team has always been a key part of our business. This embedded knowledge and experience allows us to deliver strategic change, resulting in improved long-term operating performance.

While the markets in 2011 will remain challenging, we believe there will be opportunities for us to grow our existing businesses through bolt-on acquisitions and development capital. We also believe that there will be opportunities this year to invest in businesses where we can add value through strategic and operational change. While maintaining our focus on asset-backed businesses in basic industries, we will also seek to acquire businesses that will benefit from inflation as well as businesses that are based in Europe, but which have the potential to draw a substantial portion of their sales and profits from the emerging markets.

## SENIOR PERSONNEL

# OUR SENIOR MANAGEMENT TEAM HAS THE FULL RANGE OF FINANCIAL SKILLS, STRATEGIC INSIGHT AND OPERATIONAL EXPERTISE NEEDED TO PURSUE A DIFFERENTIATED INVESTMENT STRATEGY

### Guy Hands
Chairman and
Chief Investment Officer

Guy is Terra Firma's Chairman and Founder. He is the Chief Investment Officer and sits on the boards of the General Partners.

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 Sachs in 1994 to establish the Principal Finance Group 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 by 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.

### Tim Pryce
Chief Executive Officer

Tim is a founder member of Terra Firma and its Chief Executive Officer. He chairs the board of TFCPL and its Investment Review and Remuneration Committees.

Tim joined Terra Firma as its General Counsel. In this role, he built and led the legal, structuring, tax and compliance teams. He was also a member of its Investment Advisory and Remuneration Committees.

Tim began his career practising law at Slaughter and May after which he worked for GE Capital, Transamerica and the Principal Finance Group of Nomura International plc.

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 speaks French in addition to his native tongue, English.

Tim and his partner enjoy travel, skiing and the arts.

Robbie Barr
Chief Financial Officer

Robbie is Terra Firma's Chief Financial Officer with overall responsibility for the financial management of Terra Firma's portfolio businesses. His responsibilities include pre- and post-acquisition operational change planning and implementation, performance monitoring and governance processes. Robbie has a board seat on a number of the portfolio companies. He has a team of operational, finance and change management professionals which enables hands-on involvement in specific areas.

Prior to joining Terra Firma in 2009, Robbie held a number of senior positions at Vodafone Group Plc including the role of Group Financial Controller and was most recently regional CFO for Vodafone's businesses outside Western Europe.

Robbie is a Fellow of the Institute of Chartered Accountants in England and Wales and has an MA in Mathematics from Magdalen College, Oxford University.

Robbie is married with three children. His interests include tennis, golf and skiing.

Peter Cornell
Managing Director,
Stakeholder Relations

Peter's role focuses on Terra Firma's key relationships with investors, regulators and governments. Peter sits on the General Partners' Boards and chairs the Advisory Boards.

Peter joined Terra Firma in 2007. Previously, he 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 and History from the University of Exeter. He was elected 'Lawyer of the Year' by Legal Business in 2007. He is a Council Member of the BVCA and vice-chairman of the BVCA's Global Buyout Committee.

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

## SENIOR PERSONNEL

Chris Barnes
Finance Director

Chris is responsible for investor reporting, fund accounting and transaction equity funding. He is also responsible for internal financial management and all tax issues for Terra Firma, together with the IT and Facilities teams.

He joined the group in 2001 and has worked on the structuring and execution of many of Terra Firma's investments.

Prior to Terra Firma, Chris worked in the Private Equity Tax group at Arthur Andersen. Chris is a Chartered Accountant and has a Double First in Economics and History from Cambridge University.

Chris is married with three children and is a keen Chelsea fan.

Arjan Breure
Financial Managing Director

Arjan plays an active role in deal origination and portfolio value optimisation. He focuses on commercial real estate, telecommunications, and retail.

Prior to joining Terra Firma in early 2008, Arjan was Head of Asset Management at Citi Property Investors, Terra Firma's co-investor in DAIG. He previously worked for Cherokee Investment Partners, and in the New York offices of Prudential Securities Merchant Banking and Rabobank International.

Arjan has an MBA from INSEAD and a Masters in Economic History from the University of Utrecht. In addition to English and German, Arjan speaks Dutch, his native language.

Arjan is a struggling golfer and enjoys travel and music.

Damian Darragh
Financial Managing Director

Damian has completed a wide range of deals at Terra Firma, including the sale of WRG, the spin-out and development of the Infinis renewable energy business, the acquisitions by Infinis of Summerleaze Re-Gen and Novera Energy Plc, the refinancing of Phoenix and the acquisition of EverPower.

Damian specialises in the energy and infrastructure sectors, with a particular focus on renewable power.

Damian joined Nomura in 1993, following his graduation from the University of Manchester and L'Institut Supérieur D'Electronique du Nord with a degree in Electronic Engineering Science (M.Eng), where he worked with Terra Firma's forerunner, Nomura's Principal Finance Group. Following a sabbatical when he completed a Sloan Fellowship MSc at London Business School, he re-joined Terra Firma in 2005.

Damian is fluent in French in addition to his native language, English.

Damian is married with three children. He enjoys skiing, golf, scuba diving and watching football.

Karen Dolenec
Financial Managing Director

Karen has been involved in a wide variety of the group's investments including many of the various pub companies, the acquisition and partial sale of Tank & Rast and the investment in CPC.

Karen has responsibility for agriculture, natural resources and food and beverages.

Prior to joining the group in 2001, Karen spent some years in both the M&A advisory business and the private equity arm of JP Morgan in New York.

Karen has a BSc in Economics, and a BA in Asian and Middle Eastern Studies, from the University of Pennsylvania and an MBA from INSEAD. She is fluent in Taiwanese and English.

Karen is married with two children. She enjoys travelling, scuba diving and entertaining friends.

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 investments. Mayamiko has responsibility for retail financial services, insurance, passenger transportation and support services.

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 speaks French as well as English.

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, the UK landfill businesses of WRG and Shanks, and East Surrey Holdings. He is currently the Chairman of the Odeon & UCI Cinema Operating Company, Chairman of Infinis Capital Limited and a director of the board of the CPC Governance Company. His other portfolio responsibilities include EverPower.

Prior to joining the group in 2000, Mike was Group Chief Executive Officer of Stagecoach Holdings Plc (FTSE 250), and Chief Executive Officer of Power Distribution and Water Operations for Scottish Power Plc (now part of Iberdrola, an IBEX 35 company). 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 1998–2002.

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.

## SENIOR PERSONNEL

Lorenzo Levi
Operational Managing Director

Lorenzo has been involved in a number of the group's investments and is currently on the boards of Phoenix Group, AWAS and Tank & Rast.

Prior to joining the group in 2002, his career ranged from sales management and corporate development roles for companies such as IBM (an S&P 500 company) and Nortel Networks to strategy work for management consultants Bain & Co.

Lorenzo is an Italian national. He has a BSc in Electrical Engineering and a BSc in Economics from MIT as well as an MBA from Harvard. Lorenzo speaks English and French in addition to his native tongue, Italian.

Lorenzo is married with two children. He enjoys football, listening to music and travelling.

Bill Miles
Managing Director,
Investor Relations

Bill has represented Terra Firma in North America from an investor relations perspective since 2002 when Terra Firma was beginning the fundraising for its first externally raised fund. Previously, Bill was Managing Director and Co-Head of Fixed Income Sales and Trading at First Union Capital Markets (now Wells Fargo Bank). From 1982–1997, he was a Vice President, Fixed Income at Goldman Sachs.

Bill has a BA in Political Science from Vanderbilt University. Upon graduation, he was commissioned and served in the US Navy; primarily in south-east Asia. He retired as a Lt. Commander after seven years on active duty and in the Reserves.

Bill is married with two daughters. The Miles family are avid boaters and spend much of their leisure time on the waters around South Florida and the Bahamas.

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 portfolio responsibilities include Tank & Rast as well as working with the deal teams on new investment opportunities.

Prior to joining EMI in 2007, Pat was the CEO of Northern Foods plc, a FTSE 250 company, where she led the restructuring of its portfolio. She is also a Non-Executive Director and Chairman of the Remuneration Committee and on the board of Xchanging plc (FTSE 250).

Pat holds a degree in Sociology from Exeter University and is a Fellow of the Royal Society of Arts. She 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 enjoys literature and theatre as well as good food and wine.

Quentin Stewart
Financial Managing Director

Quentin has expertise in the agricultural, energy, utilities and waste management sectors. He led the investments in WRG, Shanks' UK landfill business, East Surrey Holdings, CPC and EverPower. He oversaw the sale of WRG, the establishment of Infinis and its subsequent acquisition of Novera Energy Plc as well as various sales from East Surrey Holdings. Quentin was also involved in the acquisition and sale of William Hill and the businesses in the Thorn Group.

Quentin is a Chartered Accountant and holds a degree in Business from De Montfort University Leicester. Prior to joining the group in 1997, Quentin worked for Arthur Andersen.

Quentin is married with one daughter. He enjoys 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. Julie is responsible for hospitality, leisure, and media.

Prior to joining the group in 1998, Julie worked for Nomura heading the legal team that provided legal risk analysis and transaction execution support to 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.

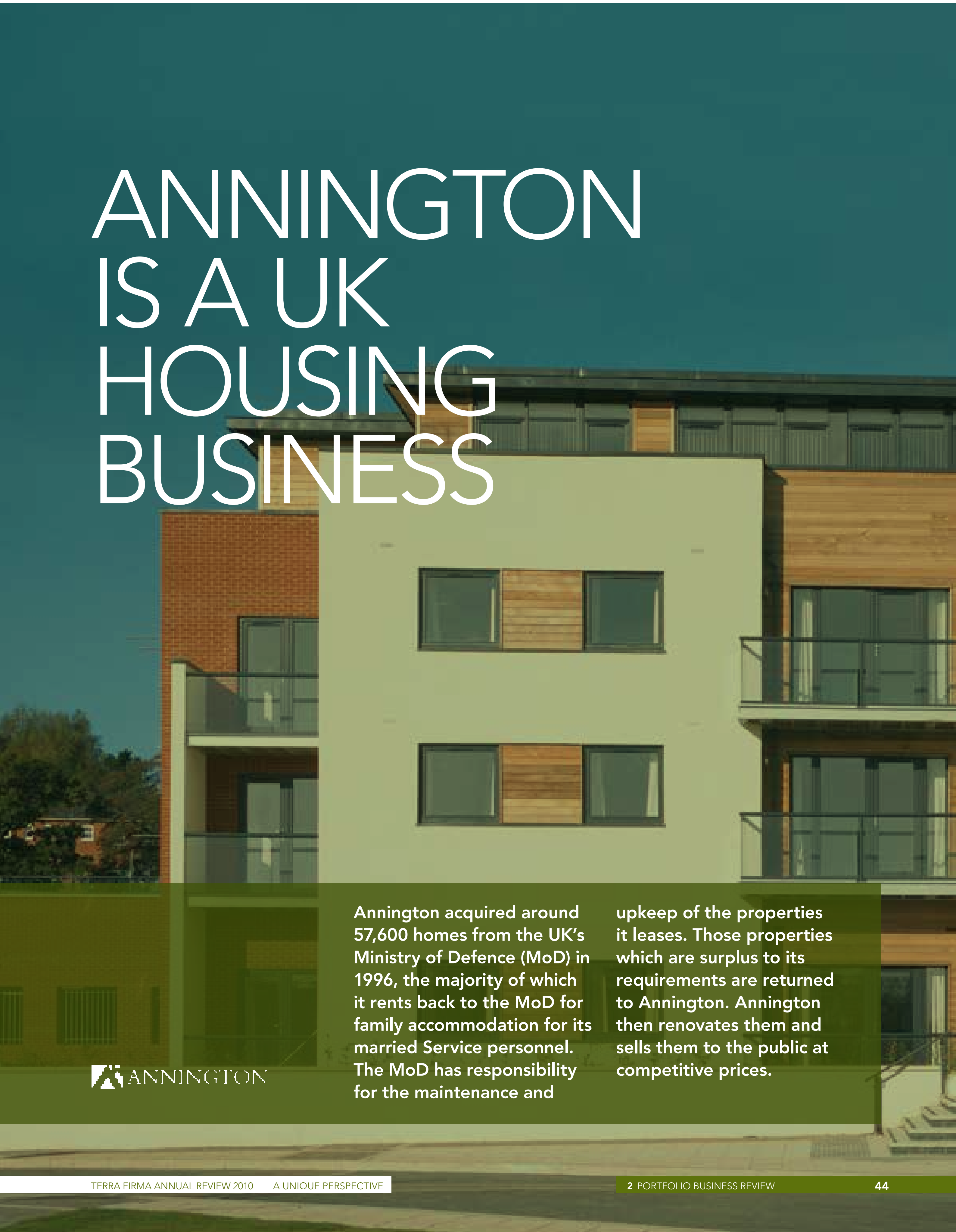
Julie is married with one son and enjoys skiing and mountain hiking.

# 2 Portfolio Business Review

## INTRODUCTION

# CREATING VALUE IN BUSINESSES REQUIRES INSIGHT, STRATEGY AND TENACITY

| | |
|---|---|
| ANNINGTON | UK residential housing – sales and rentals |
| AWAS | Worldwide aircraft leasing |
| Consolidated Pastoral Company Pty Ltd | Australian cattle farming |
| DEUTSCHE ANNINGTON | German residential housing – sales and rentals |
| EMI | Global music publishing and recorded music |
| everpower | US wind power |
| infinis | UK renewable energy |
| ODEON / UCI | Pan-European cinema operator |
| PHOENIX NATURAL GAS | Irish natural gas distribution and supply |
| TANK & RAST | German autobahn services |



# ANNINGTON IS A UK HOUSING BUSINESS

ANNINGTON

Annington acquired around 57,600 homes from the UK's Ministry of Defence (MoD) in 1996, the majority of which it rents back to the MoD for family accommodation for its married Service personnel. The MoD has responsibility for the maintenance and upkeep of the properties it leases. Those properties which are surplus to its requirements are returned to Annington. Annington then renovates them and sells them to the public at competitive prices.

**60%** OF HOMES SOLD TO FIRST-TIME BUYERS

**35%** OF HOMES SOLD TO KEY WORKERS

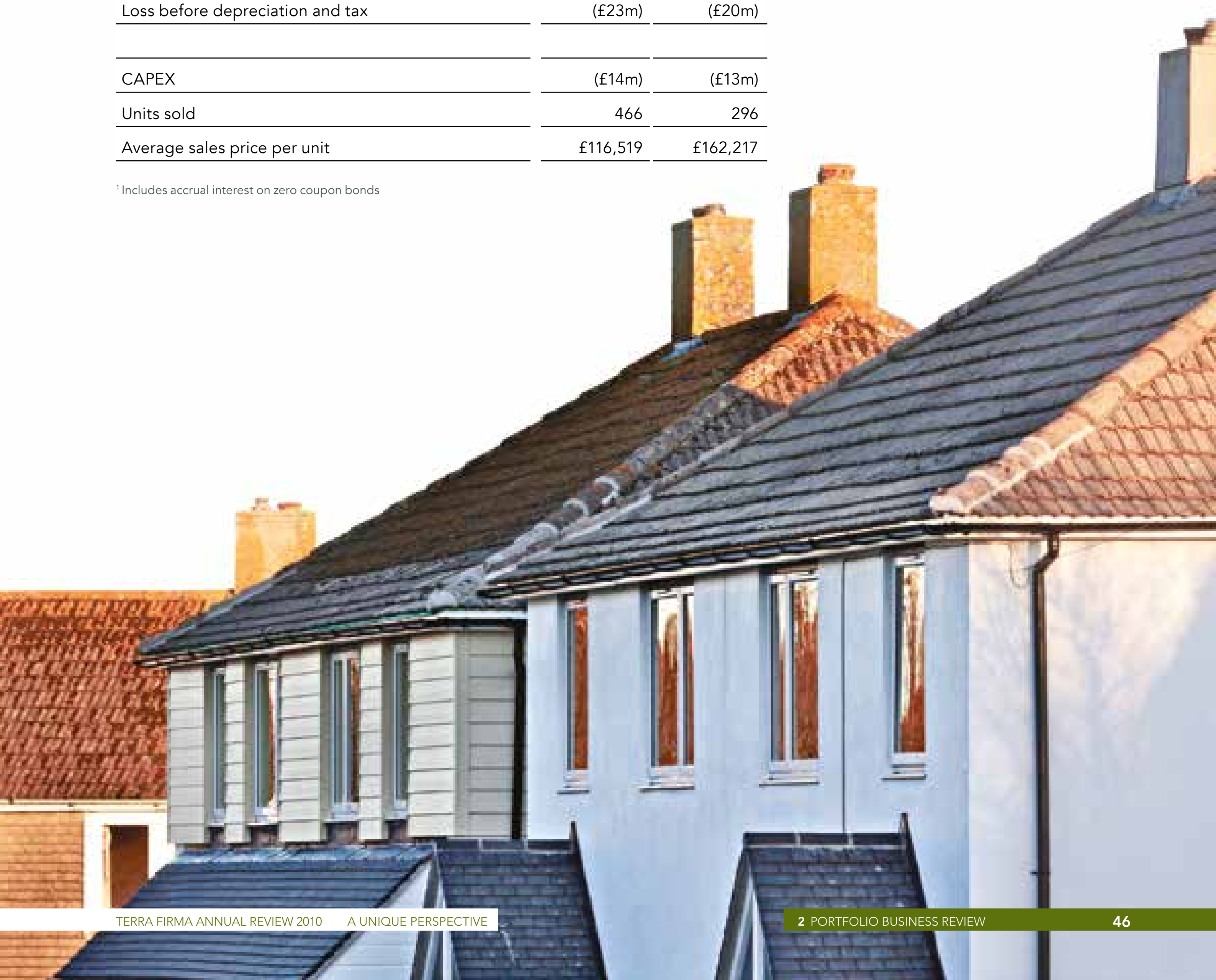
**296** PROPERTIES SOLD IN 2010

## ANNINGTON

# ANNINGTON HAS SOLD MORE THAN 16,000 HOMES TO THE PUBLIC

| YEAR END: 31 MARCH | YTD Dec 09 | YTD Dec 10 |
|---|---|---|
| Rental business revenue | £124m | £125m |
| Sales business revenue | £54m | £50m |
| Costs | (£72m) | (£58m) |
| **EBITDA** | **£106m** | **£117m** |
| Net interest expenses – external[1] | (£129m) | (£137m) |
| Loss before depreciation and tax | (£23m) | (£20m) |
| | | |
| CAPEX | (£14m) | (£13m) |
| Units sold | 466 | 296 |
| Average sales price per unit | £116,519 | £162,217 |

[1] Includes accrual interest on zero coupon bonds



As well as renovating and selling properties, Annington also privately rents a number of properties and occasionally redevelops sites or builds new homes.

## 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 also looked likely that the MoD would release surplus properties for redevelopment and sale earlier than it had agreed to do.

Terra Firma predicted that more cash would be generated more quickly than many other bidders were expecting and reflected this in the price it paid to the MoD. At the same time, 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.

## ACHIEVEMENTS

One of Annington's key strengths has been the efficiency of its sales operation. Since 1996, the MoD has returned 16,826 units to Annington, of which more than 16,000 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, 30% have been sold to Service or ex-Service personnel and 35% have been sold to people who the UK Government classifies as 'key workers'.

Annington predicted the end of the housing boom for some time before it occurred and spent the past several years rationalising the business in readiness for falling release numbers and the anticipated decline in sales levels. Annington's operating model is based on a small core team that uses 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.

Annington has also been able to offset some of the challenges in the market by taking advantage of increased demand from investors and bulk users such as housing associations which are suffering from lack of supply, principally because the development pipeline has dried up.

These combined actions have meant that adapting to the current environment has been a lot less painful for Annington than for many in the property sector. Furthermore, in January 2008, Annington reached a point where it was no longer reliant on house sales for cash flow to service its loans. Debt service and operating expenses are now fully covered by rental income received from the MoD.

## CURRENT FINANCIALS

For the nine months to December 2010, Annington reported rental revenue of £125 million and generated a further £50 million of sales revenue from the sale of 296 units. Sales volumes were behind budget as a result of the subdued demand, and sales stocks are currently low and lack geographic spread. Annington received a further 175 units from the MoD in the first quarter of 2011 and current forecasts indicate a further 140 units over the next 12 months.

With its long-term financing structure in place, the business has no new near-term funding requirements.

## DEVELOPMENT PLAN

The biggest single challenge facing Annington continues to be the uncertainty in the housing market. The market has recently shown some signs of improvement; however, the availability of mortgages remains the single largest obstacle to recovery, particularly for Annington which operates predominantly at the first-time buyer end of the market. Stock levels are low, but Annington will continue to refurbish and sell available properties to reduce its debt levels as appropriate.

Historically, Annington's primary business has been the refurbishment and sale of previously-owned homes. However, the deterioration in the UK housing market, in terms of both volume and prices, continues to be mitigated by the stable rental income from the MoD. This may well 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 by acquiring properties that exceed its threshold return criteria. Annington is also working with the MoD to find creative solutions to its housing challenges.

The Strategic Defence and Security Review (SDSR) and Comprehensive Spending Review were announced in the third quarter of 2010. It is expected that these will reduce Service personnel numbers and hence future housing requirements. The SDSR also announced timescales for forces returning from overseas, which may increase the demand for military housing. The MoD is currently preparing detailed plans to accommodate these changes, but it is expected that new housing will be required in certain areas, whilst redundant stock should continue to be released in future years.

# ANNINGTON

## COMPANY STRUCTURE

Annington Homes manages the core business of renting approximately 40,500 properties to the MoD along with the refurbishment and sale of homes on the open market.

Annington Rental Holdings owns 1,435 flats and houses let on individual and bulk leases on the open market. It manages a further 322 properties on behalf of other Group companies.

Annington Developments seeks opportunities for infill or wholesale redevelopment 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.

Barry Chambers, Robbie Barr, Nils Steinmeyer, James Hopkins, Andrew Chadd

James Hopkins, Karen Dolenec

## MANAGEMENT

James Hopkins
Chief Executive Officer
James joined Annington Homes Ltd as CEO 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.

# ANNINGTON THROUGH AND THROUGH

Annington has changed hugely in the 15 years since it was launched, and there are only a handful of people who have been there from the start. Peter Clarke is one of them.

With Peter set to retire soon, the business is looking back over his career and paying tribute to the huge contribution he has made to its growth and success.

Peter's early career was at the Government Property Services Agency (PSA) where he spent 23 years. A Chartered Engineer, his roles included responsibility for the MoD & Civil Service Estates in Devon & Cornwall.

When the PSA was privatised in 1993, Peter became an employee of the AMEC group of companies. In 1996, AMEC was brought in by Nomura to provide technical expertise for its tender for the Married Quarters Estate. Peter's experience was to prove invaluable as he had looked after about 7,000 married quarters while at the PSA.

By August 1996, Nomura had been nominated as the preferred bidder by the MoD and Peter was asked if he would join Annington on secondment from AMEC. When asked what persuaded him to take the job, he says "I was excited by Nomura's plans to transform military housing sites into vibrant housing communities." It was a secondment that would turn into a 15-year working relationship.

From the start, Peter has been Annington's key point of contact with the MoD. In essence, this means that anything which has something to do with the MoD – pretty much everything Annington does, in fact – involves Peter. His responsibilities range from getting to grips with a very complex contract and making it work on a practical level through to helping to handle the PR exercise surrounding what was seen as a very controversial deal.

Peter Clarke

Annington owes a lot to Peter's patience, persistence and professionalism in establishing and maintaining good working relations at all levels within the MoD and with its agencies. He has helped to steer the business through periods of great change and built up a truly encyclopaedic knowledge of the sale contract with the MoD along the way. In October 2011, Peter retires from Annington at the age of 67. He intends to spend time with his local church and doing voluntary work for Christian charities, a passion he shares with his wife Bridget. Everyone at Annington and at Terra Firma wishes him well and hopes he enjoys a retirement that is extremely well-earned.

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

AWAS was acquired by Terra Firma in 2006 and this was followed by the 2007 acquisition of Pegasus Aviation Finance Company.

The combined business has over 200 owned aircraft and a delivery pipeline of 115 aircraft from Boeing and Airbus.

AWAS

**200** MORE THAN 200 AIRCRAFT IN THE PORTFOLIO

**40** AWAS LEASES ITS PLANES TO CUSTOMERS IN 40 COUNTRIES

**25** AWAS CELEBRATED 25 YEARS IN THE AVIATION BUSINESS IN 2010

## AWAS

# AWAS IS LOOKING TO DEPLOY IN EXCESS OF $1 BILLION IN 2011 TO GROW ITS PORTFOLIO OF ASSETS

| YEAR END: 30 NOVEMBER | 2009 | 2010 |
|---|---|---|
| Revenue | $743m | $726m |
| Costs | ($90m) | ($77m) |
| **EBITDA** | **$653m** | **$649m** |
| EBIT | $114m | $389m |
| External interest expense | ($223m) | ($228m) |
| **Operating PBT** | **($109m)** | **$162m** |
| | | |
| CAPEX | ($395m) | ($468m) |

Figures may not add downwards due to rounding

## INVESTMENT RATIONALE & REDEFINITION OF STRATEGY

Since its acquisition by Terra Firma, AWAS has been repositioned to build long-term value by pursuing 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 emphasises a rigorous, investment-led approach to all leasing and asset trading decisions, looking particularly at 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. In addition, the strategy seeks to grow the overall level of assets under management by taking advantage of the aviation cycle.

Alongside the redefinition of strategy, the investment in AWAS and Pegasus has involved a high degree of operational change. Following the initial acquisition of AWAS, that change was heavily focused on centralising the business in Dublin and significantly increasing its operational efficiency. The follow-on 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 unit 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.

In order to deliver the shift in strategic direction, Terra Firma improved the overall quality of the management of the business and introduced disciplined, investment-led analysis and decision making. Under Terra Firma's ownership, there have been new appointments to key management roles, 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.

During fiscal year 2010, the business successfully refinanced three of its main facilities, thereby removing any near-term refinancing risk. In addition, it secured significant new equity which means that its forward order book is now fully equity-funded and a substantial amount of capital is available to deploy on additional portfolio expansion.

The business has pro-actively managed the downward swing of the aviation cycle in the last two years and value has been protected by an aggressive focus on the minimisation of default costs. Improvements in traffic, profits and forecasts for the airline industry were evident in 2010 and with its forward order book and new growth capital, AWAS is well positioned to exploit the opportunities of the cycle and emerge with growing profitability when the cycle moves into an upswing phase.

## CURRENT FINANCIALS

While 2010 saw improvements in the outlook for the industry, many airlines still remained cautious with their fleet replacement and growth plans, meaning that it continued to be a challenging year. In spite of this, AWAS outperformed its key operational and financial objectives primarily due to stringent credit and cost management as well as a faster than expected market recovery.

Revenue exceeded budget by $14 million largely due to budgeted repossessions not having occurred, which more than offset lower variable revenues that resulted from lower than expected Libor rates. The remaining upside was driven by better than expected credit performance, tight cost control and higher gains from sales, although somewhat offset by higher finance charges (largely due to one-off break costs associated with the early refinancings that were completed during the year).

Overall, the business performed well in challenging conditions with EBIT and Operating PBT ending the year significantly ahead of prior year. The variance on both these measures is mainly due to a non-cash impairment charge that was booked in 2009.

2010 also started to see an increase in the new aircraft deliveries from AWAS' forward order book. The company took delivery of, and immediately placed on lease, seven new planes, compared with three in 2009, continuing the renewal of its fleet and further bringing down its average age. This is set to continue, with the number of new deliveries increasing to 15 in 2011.

## DEVELOPMENT PLAN

The outlook for the airline industry has continued to improve throughout 2010. The International Air Transport Association (IATA) issued an updated financial forecast for the global airline industry in December 2010 raising its estimated industry net profits for both 2010 and 2011. However, IATA remains concerned about the potential for further hikes in oil prices in 2011. We continue to believe that AWAS' strategy puts it in a good position in this environment.

The business is planning to deploy a significant amount of new equity on an accretionary basis this year and is intending to secure debt financing to accompany these investments. Together with the funds to be spent on new deliveries in 2011, the business is looking to deploy in excess of $1 billion to grow its portfolio of assets.

# AWAS

Orla Gillan, Werner Seifert , Ray Sissons

Nils Steinmeyer, Simon Glass

## MANAGEMENT

Ray Sisson
Chief Executive Officer
Ray joined AWAS as CEO in August 2010. He brings with him extensive aviation industry experience gained at GE Commercial Aviation Services, where he was successively responsible for the Asia Pacific and EMEA regions, Titan Aviation, where he was CEO, and SR Technics where his last position was Chief Commercial Officer.

Simon Glass
Chief Financial Officer
Simon joined the business as CFO in February 2011. Simon has over 25 years of international business experience in the banking and financial services industries. Prior to joining AWAS, Simon was most recently at the Royal Bank of Scotland Group plc where he held the position of Deputy Group Finance Director. Over the past 20 years, he has held a number of senior finance positions within the global banking industry.

Daniel Bunyan
Head of Portfolio Management
Daniel joined the business as Head of Portfolio Management in October 2010. He brings with him a wealth of experience in the sector, including as a Partner in the Aviation practice of Oliver Wyman/MMC with a particular focus on strategy development and financial analysis.

Angus Williamson
Head of Risk Management
Angus 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 and Business Development at AerCap.

# INVESTING IN THE TALENT OF TOMORROW

When AWAS moved its headquarters to Dublin in 2006, the business's Corporate Social Responsibility team immediately set about investigating ways that it could build links with the community and start to make a positive contribution to local life.

A key area that was identified was training and development – the team believed that AWAS could share its skills and help young people to learn more about engineering, to decide if it might be the right career for them long term. One of the initiatives to come out of this has been the successful internships programme for students at Dublin City University (DCU).

AWAS has a lot to offer in terms of giving undergraduates exposure to the corporate environment – as well as helping students to develop their skills and knowledge, this programme would also serve to promote interest in the aviation finance industry. The fact that the industry has a large number of aviation lessors headquartered in Dublin made the programme an even better fit. It would give young people a real insight into a major local industry and could help to create a talent pipeline for the future. Good news for the students and the industry alike.

The programme started in 2008 and, with many DCU degree subjects including a 6- to 11-month work placement, there has been a steady stream of students arriving at AWAS' Dublin offices. So far, DCU students from the Business Studies, and Marketing, Innovation & Technology programmes have all spent time working at AWAS.

The process is simple. DCU posts available AWAS roles, students apply and are given a standard business interview – another valuable part of the learning experience.

A DCU intern at work at AWAS' Dublin office

Ian Wheatley is an intern in no doubt about the advantages of the programme. "Since day one," he says, "I've been treated as a part of their team – not simply as an intern. The experience has helped me realise what direction I'd like to go in after college and it's been fascinating learning about the whole aircraft leasing business."

Karla Baylis has been part of the Market Development team and says, "Working at AWAS has given me invaluable first-hand experience – I've definitely become more confident in my abilities and I've had a real taste of working life."

The DCU internships programme is one of a number of similar student and professional secondment programmes that AWAS is running. In 2011, the company is planning to build on its success and welcome even more students to experience working life at AWAS.

# CPC IS ONE OF THE LEADING AUSTRALIAN BEEF PRODUCERS

CPC is the second largest beef producer in Australia with 357,000 head of cattle. Its operations include breeding and grass-fattening cattle across its 16 properties, which are located in the northern part of Australia.

The properties together comprise 5.8 million hectares, which represents around 0.8% of Australia's land mass. CPC also has a 50% interest in a feedlot operation in Indonesia.

Consolidated Pastoral Company Pty Ltd

**357,000** HEAD OF CATTLE

**16** PROPERTIES

**5.8m** HECTARES – 1.4X SIZE OF SWITZERLAND

## CPC

# CPC HAS CONTINUED TO IMPROVE THE HERD-CARRYING CAPACITY AND EFFICIENCY OF ITS PROPERTIES

| YEAR END: 31 DECEMBER | 2009 | 2010 |
|---|---|---|
| Revenue | A$44m | A$41m |
| Costs | (A$30m) | (A$42m) |
| Cash EBITDA | A$14m | (A$1m) |
| Purchase and non-cash livestock adjustment | A$8m | A$18m |
| **EBITDA** | **A$22m** | **A$17m** |
| External interest expense | (A$15m) | (A$16m) |
| | | |
| CAPEX | (A$11m) | (A$5m) |

2010 numbers are subject to final audit approval

## INVESTMENT RATIONALE

The strategic rationale underlying Terra Firma's acquisition of CPC in April 2009 was driven by a number of global macroeconomic themes, in particular: population growth, a shift in Asian diet towards higher protein consumption and a limited supply of productive land.

Recent years have seen significant increases in the demand for food. Population growth and GDP growth are combining to create increased demand for higher value protein. Many of the most promising areas of demand are in Asia which are geographically well-located for Australian exports.

While demand for beef is increasing, supply is constrained due to the limited availability of suitable land and access to water combined with competing demands for these resources through urbanisation, cropping for biofuels and demand for other agricultural uses.

Investment in the agricultural sector has been limited and capital expenditure on developing land or increasing productivity has been low. Australia is attractive as a source of beef supply because of the quality and cost efficiency of its grass-fed cattle, its ability to reliably supply large quantities into the Asian market and the fact that its herd is free from major disease.

## STRATEGY

The business is led by Chairman and CEO Ken Warriner, a well-regarded industry leader with around 40 years of experience in the beef cattle industry. When Terra Firma acquired CPC, Ken took the opportunity to roll his existing minority interest in the company, staying invested alongside Terra Firma.

Terra Firma, together with the CPC management team, has identified a number of potential operational opportunities that will improve the business in the coming years. These range from growing the earnings of the business through selective capital investment to finding higher value activities for parcels of land within the portfolio.

Approximately 60% of CPC's sales in 2010 were made into Indonesia which is a large and rapidly growing market. Although CPC was adversely affected during the year by unexpected government restrictions on the import of cattle into Indonesia, CPC continues to focus on further developing its position in this important market, whilst also exploring opportunities in other export markets.

CPC is actively searching for potential add-on acquisitions in Australia at attractive prices to grow the business and complement the company's portfolio of properties.

## ACHIEVEMENTS

In keeping with its growth strategy, two additional properties were acquired in 2009, one of which was Wrotham Park, a large property in the far north of Australia which added over 55,000 cattle to the CPC herd. A third property, Cooinda was acquired in early 2010 and towards the end of the year agreement was reached to acquire a further fattening property in Queensland. This transaction completed early in 2011, bringing the total amount invested in bolt-on acquisitions by CPC under Terra Firma's ownership to approximately A$57 million.

During 2010, CPC has continued with its capital expenditure programme to improve the herd-carrying capacity and efficiency of its properties. Major projects completed during the year included building new fencing, clearing overgrown land and increasing the availability of water by drilling bore holes plus building water pipes, tanks and troughs. The carrying capacity of CPC's properties has been materially increased as a result of these development projects.

## CURRENT FINANCIALS

CPC reported EBITDA of A$17 million for 2010, which was A$5 million below the prior year. Revenue of A$41 million, which included the sale of over 32,000 live cattle to markets in Indonesia, was A$3 million lower year-on-year.

CPC's results for 2010 were adversely affected by the decision of the Indonesian authorities to restrict the issue of cattle import licences and to impose a maximum per animal weight limit. As a result, some of the cattle that would have been exported had to be sold to Australian meat processors for lower net prices than would otherwise have been realised. Prices being paid by meat processors strengthened during the year, driven by growing global demand for beef protein.

Costs too, were higher than 2009, principally due to the costs of transporting cattle that had been due for export to Indonesia to fattening properties and markets in South Eastern Australia.

Capex spend was A$5 million, with CPC completing all its major projects during the year.

## DEVELOPMENT PLAN

In addition to the steps that have been taken to increase the number of cattle that can be supported by its properties, CPC has a number of initiatives underway to improve the management of its herd. This includes improving productivity through the deployment of more sophisticated herd management techniques in order to maximise births (brandings) and minimise deaths (mortality). Nutrition, timing of joining bulls with cows and pregnancy testing are also some of the factors which are now being more closely monitored.

Work continues to identify further acquisitions with the aim of increasing the geographic diversity and flexibility of the land portfolio, thereby widening market access and developing opportunities for higher value use.

# CPC

Jackaroos at work

Robbie Barr, Ken Warriner, Karen Dolenec, Mike Kinski

## MANAGEMENT

### Ken Warriner

Chairman and Chief Executive Officer

Ken has been Chairman and CEO of CPC since 1983. Previous to this role, Ken was General Manager of King Ranch Pastoral Company from 1970–1979, after which he became Partner of Ashburton Pastoral Company. Ken was Chairman of the Consolidated Meat Group in the 1990s, as well as Chairman of Road Trains Australia and of Australian Fuel Distributors from 1980–2000.

### John Stevenson

Chief Financial Officer

John is an Australian Chartered Accountant with over 25 years' working experience in Australia and Asia. Prior to joining CPC in June 2010, John was a Finance and Managing Director for Jardine Matheson Limited in Indonesia for 10 years and has extensive experience as a Financial Manager throughout the South-East Asian region. In Australia, John practised as a Chartered Accountant with Coopers & Lybrand Deloitte and his pastoral experience includes working as the Financial Controller for Heytesbury Beef in the mid 1990s.

### Geoff Warriner

Chief Operations Officer

Geoff joined CPC on a full-time basis at the beginning of 1985. Two years later, he was given the responsibility of managing the initial conception of the Newcastle Waters Brahman stud. In the early 1990s, Geoff managed breeding properties in the Northern Territory and backgrounding properties in Queensland. In 1993, Geoff was appointed to manage Carlton Hill Station in Western Australia, where he doubled the holding capacity over the subsequent nine years. In 2000, Geoff became Pastoral Inspector of CPC's Northern Territory and Western Australia holdings, comprising some 200,000 head of cattle.

# THE ANNUAL JACKAROO AND JILLAROO DRIVE

Every year, CPC gives 60 young people a unique opportunity – the chance to be a jackaroo or jillaroo on one of its vast Australian cattle stations.

Some of these 'first years', as they are known, have grown up on family farms. Others come from the city with little or no experience of station life. All of them discover that their first mustering season is unlike anything they have done before.

Work starts before dawn and they spend weeks in stock camps living and working outdoors and sleeping under the stars. They make new friends, develop new skills and learn a huge amount about themselves. It is a life-changing experience that for many will help them to decide the course of their careers.

The first years start with an intensive training period at rural colleges to prepare them for the season ahead. At colleges in Katherine in the Northern Territory and Longreach in Central Queensland, they are put through their paces in everything from horsemanship skills, first aid and cattle handling theory to welding, health and safety, and general farm maintenance. On graduation, they head for their allotted CPC stations in Western Australia, the Northern Territory and Queensland.

When the first years arrive on station, their skill levels are assessed and the on-the-job training starts right away. It covers areas such as cattle mustering, drafting of yarded cattle, branding, fencing, bore maintenance, and horse and motorbike mustering skills. And with every station having its own way of working, there is site-specific training as well.

To keep skills sharp and ensure that every jackaroo and jillaroo understands how to stay safe on what is usually an isolated location, the educational work continues throughout the season. They are supervised by experienced personnel who have worked on cattle stations for many years – it is a mentoring role, but one that allows the individuals to take responsibility and use their initiative.

The jackaroos and jillaroos are an invaluable part of the CPC team and many stay on to take up roles as stockmen and stockwomen. Some go on to become senior managers in the company and it is a source of great pride that some of the leading figures in the industry started out as first years at CPC.

Whatever their ambitions for the future, these 60 young people learn a great deal about themselves in their 12 months at CPC, and the lessons they learn will stay with them for life.

# 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 almost tripled in size. DAIG is now the number one privately-owned residential landlord in Germany by number of units (c.190,000) with a proven track record in privatisation.

DEUTSCHE ANNINGTON

€170m
MODERNISATION AND MAINTENANCE WORK UNDERTAKEN IN 2010

190,000
RESIDENTIAL UNITS OWNED ACROSS GERMANY

2,100
HOMES SOLD IN 2010

## DEUTSCHE ANNINGTON

# €70M INVESTED OVER THE PAST TWO YEARS IN IMPROVING CUSTOMER SERVICE

| YEAR END: 31 DECEMBER | 2009 | 2010 |
|---|---|---|
| Rental business gross rents | €763m | €784m |
| Rental business costs | (€299m) | (€314m) |
| Sales business revenue | €150m | €225m |
| Sales business costs | (€128m) | (€185m) |
| Other | (€6m) | (€8m) |
| **EBITDA FROM CONTINUED OPERATIONS[1]** | **€480m** | **€502m** |
| Cash external interest expense | (€257m) | (€274m) |
| | | |
| Overall vacancy rate | 5.9% | 5.1% |
| Units privatised | 1,620 | 2,164 |

[1] Excludes exceptional costs

DAIG focuses 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 successfully applied its management approach to newly-acquired portfolios of residential property as well as those it manages on behalf of third parties (c.25,000 units).

## 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 revenue. Furthermore, rents were substantially below market levels and could be modestly increased to improve cash flow. The apartments were owned and managed by ten 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 strategy and processes.

German residential real estate is an intrinsically low-risk asset class and the business benefited from strong asset backing with a geographically diversified portfolio. The original housing portfolio was supplemented by the acquisition of Viterra 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 one of the largest residential housing management companies in Germany and has proven its ability to acquire new portfolios and successfully integrate them into its operations.

## STRATEGY

DAIG's strategy has proven to be successful in different market conditions and has solidified its market leadership over the past few years. DAIG's business model focuses on three core elements:

### Long-term, value-enhancing property management

DAIG offers its customers a competitive range of properties with excellent service. The company has established an industry-leading platform for the management of its portfolio and is constantly striving to further improve service quality, customer focus and efficiency.

### Socially responsible privatisation via retail sales of units

DAIG offers property ownership at affordable prices. It only sells carefully selected units, often to its tenants, but also to investors. DAIG involves tenants and local authorities in this process at an early stage.

### Strategic acquisitions of residential housing portfolios

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

## ACHIEVEMENTS

DAIG is now the prime consolidator of housing portfolios in Germany, with the company's acquisition platform opportunistically replenishing the portfolio and building a rental asset base that provides stable, recurring cash flows.

The portfolio of approximately 4,500 units in Berlin that DAIG acquired in 2009 was successfully integrated during 2010. The new portfolio outperformed the acquisition plan by almost 20% against its first year budget and ended the year with a vacancy rate of only 1.2%. The business is well-positioned to take advantage of similar opportunities in 2011.

DAIG continues to strengthen relationships with its tenant communities, improve the quality of the living environment and provide ancillary benefits to its customers. New initiatives in 2010 included a collaboration with the 'Deutsche Auslandsgesellschaft' offering free German language courses to support the integration of non-native speakers in its estates. DAIG provides the space and pays for the first course. DAIG's other initiatives revolve around reducing energy costs and consumption. The business has established framework contracts with utility providers to reduce the energy costs for DAIG's customers (see the feature that follows).

Finally, the tenant privatisation programme continues to give people the opportunity to own their own homes for the first time. 2010 has been particularly successful with the privatisation of more than 2,100 units. Over the last ten years, DAIG has sold more than 51,000 homes.

## SETTING NEW STANDARDS IN THE INDUSTRY

In 2008, DAIG announced a comprehensive strategic initiative to increase customer satisfaction across its operations and enhance operational efficiencies. The plan provided for a complete overhaul of the group's structure and organisation. After investing more than €70 million, the project was completed in 2010 and DAIG believes that it has set new standards in the German residential housing industry.

## CURRENT FINANCIALS

DAIG finished the year strongly, outperforming budget, forecast and prior year. EBITDA from continued operations was above €500 million for the first time in DAIG's history, 5% up on 2009. The main drivers behind this performance were a stable rental business, despite high vacancies at the start of the year, and a strong performance in privatisation sales. Total vacancies fell from 5.9% to 5.1% and are forecast to reach 4% by the end of 2011, based on the faster cycle times now being achieved for new rentals. More than 25% of all reservations for new rental viewings are now booked online – one example of the increased productivity resulting from the new business processes.

# DEUTSCHE ANNINGTON

Sales of units were up by more than a third year-on-year, largely as a result of the business strengthening its sales team with new external hires and the new systems and processes put in place to drive significant improvements. The business also continued to divest non-core assets at attractive prices.

## DEVELOPMENT PLAN

DAIG continues to invest in enhancing the attractiveness of its properties to tenants. In 2010, it spent more than €170 million on maintenance and property improvements. As part of this programme more than 130 modernisation projects were completed, positively impacting over 2,000 units. As in previous years, the main focus of the programme was on energy-saving measures such as the thermal insulation of outside walls and roofs and the fitting of new windows.

Dr Stefan Kirsten, Robbie Barr

Mark Ennis, Klaus Freiberg, Arjan Breure, Dr Wolfgang Beck, Wijnand Donkers, Dr Stefan Kirsten, Dr Michael Bütter

DAIG has access to significant committed capital funding and Terra Firma believes the business is in a strong position to selectively acquire further residential property portfolios as opportunities arise. The business expects several substantial portfolios to come to market in the short- to medium-term.

## 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. He ran several large businesses in the foodstuffs, petrochemicals and gas sectors where customer orientation was the priority and he has worked and lived in Europe, the US and Asia. He was a member of BP Chemical's Germany supervisory board from 2001–2005. Wijnand is Vice Chairman of GdW, the association of residential housing companies in Germany.

### Dr. Stefan Kirsten

Member of the Management Board

Stefan joined the Deutsche Annington Management Board as CFO in January 2011. In his last role, he was CEO at Majid Al Futtaim Group LLC, a real estate business in the Emirates. Prior to that, Stefan held senior leadership roles in German industry, including CFO of both Thyssen Krupp AG and Metro AG.

### Klaus Freiberg

Member of the Management Board

Klaus has been a member of the Deutsche Annington Management Board since February 2010 and is responsible for Property Management. He joined from Arvato Group (Bertelsman) where he was CEO. In his various roles with Arvato, which he joined in 1995, Klaus supervised and optimised the service centres of Deutsche Post and Deutsche Telekom.

# DRIVING DOWN TENANTS' ENERGY BILLS


DAIG recognises that, in the current climate, rising energy bills are a key challenge for the thousands of people living in its properties. So this year, the company has been working hard to reduce that burden and to reduce the environmental impact of its properties in the process.

With millions of euros spent every year on energy by DAIG tenants, the company has been able to put its considerable buying power to work for its tenants. As Wijnand Donkers, CEO of DAIG, explains, "From a financial point-of-view, our tenants are the sole beneficiaries of our energy management successes. Energy bills are the service charge cost which hit the tenants hardest."

The company started by bringing in experts to look at its procurement strategy and advise on renegotiating the agreements it has in place for utilities such as gas, electricity and oil. These renegotiations have already made a big impact. New gas supply contracts for the central heating systems of around 14,500 apartments in areas including Dortmund, Hanover, Witten and Frankfurt am Main have now been signed, with savings adding up to more than €1 million a year – all of which has directly reduced tenants' bills.

The team achieved these savings by putting the contract out to tender and negotiating more favourable conditions with one of the biggest municipal gas utilities in Western Europe. Building on this success, the company will be announcing more gas supply tenders in 2011 for other regions that have DAIG apartments.

A new electricity contract has also been signed that delivers great savings to 82,000 DAIG homes in Frankfurt am Main, as well as the Rhine-Ruhr region including Cologne and Düsseldorf. The new and improved contract for communal electricity (powering areas such as stairway and outdoor lighting) will see the tenants' bills reduced by around 16%. That is a saving of some €500,000 a year. Again, this is the first renegotiation of many and the company will be seeking tenders for the supply of communal area electricity for more regions in the first quarter of 2011.

As well as reducing bills, DAIG has also been working hard to increase efficiency – with great results for both tenants and the environment. Alongside its energy consultants, the company has been using the latest technology to adjust the settings of large central systems that heat the properties' communal areas so that they achieve maximum energy efficiency. The figures have been startling – delivering reductions in energy consumption of up to 30%. As well as the obvious environmental benefits of using less fuel, these changes have meant smaller bills for tenants and so more disposable income at the end of the month.

2010 has seen great strides being made in reducing the cost and impact of energy being used in DAIG properties, and the company has set even more ambitious targets for 2011. Its focus is now on delivering better value energy and more efficient systems right across the estate.

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

EMI operates directly in 32 countries, has licences in a further 20 countries and employs over 3,275 people. The business is made up of two divisions – EMI Recorded Music and EMI Music Publishing.

21 GRAMMY AWARDS 2011

7 BRIT AWARDS 2011

3 CLASSICAL BRIT AWARDS 2010

## EMI

# EMI HAS FOCUSED ON DEVELOPING ARTIST BRANDS AND A DEEPER CONSUMER UNDERSTANDING

| YEAR END: 31 MARCH | YTD Dec 09 | YTD Dec 10 |
|---|---|---|
| **RECORDED MUSIC** | | |
| Gross margin – net domestic sales | £298m | £268m |
| Gross margin – licence income and neighbouring rights | £90m | £82m |
| Overhead and miscellaneous[1] | (£238m) | (£221m) |
| EBITDA at constant exchange rates[2] | £149m | £129m |
| | | |
| **MUSIC PUBLISHING** | | |
| Net revenue | £351m | £314m |
| Royalty costs, overheads and associates | (£243m) | (£216m) |
| EBITDA at constant exchange rates[2] | £108m | £98m |
| | | |
| **GROUP** | | |
| **EBITDA at constant exchange rates[2]** | **£258m** | **£227m** |
| External interest expense | (£139m) | (£144m) |

[1] Includes corporate overhead allocation and share of associates

[2] Constant exchange rates are used to aid comparison between current and prior year. These rates are the statutory average exchange rates for the financial year 2009/2010

EMI Recorded Music represents recording artists spanning all musical genres. The business signs and develops artists, marketing and promoting them as well as distributing their music to retailers and licensed users. EMI Recorded Music owns a catalogue of over three million tracks. EMI Music Publishing is a leading global music publisher and has one of the world's largest catalogues of songs, including more than a million contemporary and classic titles. Its business is focused on the acquiring, protecting, administering and exploiting of rights in musical compositions, with revenue coming from licensing the right to use its music.

## INVESTMENT RATIONALE

EMI drew 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 had been particularly detrimental to the consumer-facing Recorded Music division.

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

After acquiring EMI in August 2007, Terra Firma embarked on a major restructuring of the business to transform EMI. The goal was for EMI to become the most innovative, artist-friendly and consumer-focused music company in the world, generating revenues from multiple sources while delivering the financial performance needed to build a sustainable business.

EMI Recorded Music, like the other major music companies, had traditionally focused on producing successful albums. This 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. By refocusing its operations, EMI would be positioned to provide the best service to artists while maintaining the company's cost base at a level that could ensure profitable growth.

## ACHIEVEMENTS

Terra Firma radically changed EMI Recorded Music's existing organisation from a plethora of local labels to a globally-led and locally-operated business. This streamlined structure has three global business units focused on New Music, Catalogue and Music Services which are supported by global functions in marketing and other support areas. As a result of this change, the business was able to streamline activities, avoid duplication and create real focus on developing artist brands and a deeper consumer understanding. The restructuring of the organisation reduced headcount and, together with a rigorous focus on all cost areas, savings of £200 million were achieved. A key area of focus was EMI Recorded Music's artist roster. At acquisition, EMI had more than 15,000 artists on its roster, of which just 200 accounted for half of revenues. The business was actively working with 1,300 artists, but only a small number of those relationships were profitable. EMI has since been more selective in its artist relationships with a focus on developing a broader relationship with its new artists.

## DEVELOPMENT PLAN

Roger Faxon, formerly Chairman and CEO of Music Publishing, took on the role of Group CEO in June 2010 setting the following priorities for EMI management:

(i) to continue to drive the Catalogue business through ever improving consumer insight and marketing analytics via Music Key and through new channels to market;

(ii) to deliver a New Music business that breaks even and has the right capabilities and delivery processes to build a stronger release schedule over the coming years;

(iii) delivery of the first phase of an £80 million cost savings plan;

(iv) the disposal of certain non-core assets and building of strategic alliances in territories where EMI is subscale; and

(v) for Music Publishing management to continue its restructuring programme. Phase II of the programme was expected to deliver over £5 million in sustained annual savings primarily through headcount reductions of approximately 10%.

This would yield a two-year payback on the costs necessary to realise these savings of £11 million and were reflected in the FY 2011 budget.

# EMI

## CURRENT FINANCIALS

EMI Recorded Music reported EBITDA for the nine months ended December 2010 of £129 million which was £15 million above budget, though £20 million below last year. The lower performance against prior year was primarily driven by the one-off impact of the Beatles Remastered box sets (released in September 2009), as well as the successful Depeche Mode release in the first quarter of fiscal year 2009.

The Catalogue business EBITDA was £14 million ahead of budget year-to-date; driven in part by strong catalogue campaign/new release performances across most territories (in particular Iron Maiden, Lennon, Beatles Red & Blue and Beatles iTunes), several one-off deals and balance sheet releases. New Music EBITDA was £0.5 million ahead of budget, despite a sales shortfall of £58 million versus budget which was primarily driven by delays to key releases now scheduled for later in the year and a difficult licensing market. However, these factors were outweighed by a reduction in direct costs, some timing-related, together with a better digital sales mix (higher margin) and an underlying saving in overheads. Music Services EBITDA was £1 million better than budget as it continued to build new business lines.

Music Publishing's results for the nine months ended December 2010 were broadly in line with expectations; EBITDA of £98 million was £2 million below budget and £10 million below last year due to lower sales, especially physical market and mobile revenue declines, and a significant one-off licence receipt in the prior year. These were partially offset by a favourable margin rate that was driven by an external royalty rate adjustment.

Group results for the nine months ended December 2010 were encouraging, with EBITDA of £227 million, £13 million ahead of budget.

## MANAGEMENT

### Stephen Alexander

Chairman of Maltby Capital

Stephen was appointed Chairman of Maltby Capital, the holding company of EMI, in June 2010. He was previously President of EMI Music Catalogue, a role which he had held 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 & Furst's European food businesses and had enjoyed a 17-year career with Allied Domecq PLC.

### Roger Faxon

Chairman and Chief Executive Officer of EMI Group

Roger took on the role of Group CEO in June 2010. He took up his previous role as Chairman and CEO of EMI Music Publishing in March 2007 and before that held a number of senior roles at EMI including President and Co-CEO of EMI Music Publishing, COO of EMI Music Publishing, CFO of EMI Group and Executive Vice President and CFO of EMI Music Publishing. Roger joined EMI from Sotheby's, where he was CEO of Sotheby's Europe and previously COO of Sotheby's North and South American operations.

# EVERPOWER IS A US WIND POWER DEVELOPMENT & MANAGEMENT COMPANY

**EverPower is headquartered in New York, with active wind farm operations and a development pipeline concentrated in the attractive North East and West Coast US power markets.**

everpower

63MW OPERATING CAPACITY

126MW ADDITIONAL OPERATING CAPACITY BY END OF 2011

2,600MW PIPELINE

## EVERPOWER

# HIGHLAND HAD AN AVERAGE TURBINE AVAILABILITY OF 97% IN 2010

| YEAR END: 31 DECEMBER | 2009 | 2010 |
|---|---|---|
| Revenue | $4m | $11m |
| Costs | ($12m) | ($21m) |
| **EBITDA** | **($8m)** | **($10m)** |
| External interest expense | ($3m) | ($7m) |
| Non-recurring items | – | ($4m) |
| Earnings before depreciation and amortisation | ($11m) | ($21m) |
| | | |
| CAPEX | ($20m) | ($22m) |

EverPower has one operating wind farm, Highland, which started commercial operations in 2009 with 63 MW of operating capacity. Two sites at Howard, New York and Highland North, Pennsylvania (with 51 MW and 75 MW capacity respectively) are fully consented and in construction with a portfolio of five further near-term development opportunities with an estimated capacity of approximately 600 MW. It also has a pipeline of longer-term development opportunities with estimated capacity of over 2,600 MW.

## INVESTMENT RATIONALE

EverPower Wind Holdings was acquired by Terra Firma in November 2009. The strategic rationale underlying its acquisition was to profit from the expected significant increase in demand for renewable energy in the US, at a time when regulatory change, a lower energy price environment and financing challenges were reducing the supply of new generating assets into the market.

In 2009, the US government introduced a grant of 30% of construction cost to support investment in wind assets. Terra Firma believes that US policy is increasingly likely to support renewable energy with the possibility of Federal renewable energy credits and, in the longer term, the possibility of a Federal carbon scheme strengthening the current regional standards. Despite pressure on government spending, the 30% Section 1603 ARRA grant was extended to December 2011, giving the potential to qualify further sites during 2011, and we believe this support for investment in the sector will continue, though its form may change over time.

Over the medium term, we expect US demand for natural gas to grow and that the move towards non-conventional sources of supply will increase the production cost of gas and introduce significant volatility into gas prices. In turn, we expect that there will be periods when this will drive up the price of electricity, helping to further increase the economic attractiveness of wind energy power generation.

Terra Firma has seen many potential opportunities in this sector in recent years and believes that EverPower is the most promising of these. EverPower has been carefully built by its founder CEO, who has created a high quality development business. The company has a significant portfolio of development assets which are concentrated in the attractive North East and West Coast US power markets. EverPower is a low-cost operation with a high calibre team that has a proven track record in wind development.

## STRATEGY

The business continues to be led by its founder, Jim Spencer, as CEO. Jim has taken the opportunity to reinvest his entire equity interest in EverPower and remains a significant minority investor alongside Terra Firma.

The strategy for the business is the construction, financing and operation of a portfolio of new wind farm projects over the medium term to create a wind energy business of substantial scale. EverPower will seek to secure proven reliable turbine assets on favourable commercial terms, and will build a commercial capability to ensure its generation output is sold with the optimal mix of contracted and merchant contracts.

## ACHIEVEMENTS

The first operational site, Highland, had an exceptional first full fiscal year of operation, with a full year average turbine availability of 97% against a budget 95%. This is a function of good operational management, which will be transferable to the new sites under construction.

All applicable consents have now been obtained on the next two wind farm sites, at Highland North and Howard, which will bring operational capacity to 189 MW by the fourth quarter of 2011. Turbine supply arrangements have been agreed with suppliers at prices preferential to both forecasts and the existing Highland site, and both projects were sufficiently advanced to ensure they qualified for the existing Section 1603 grant regime by the end of 2010. In January 2011, EverPower also successfully applied for a $6 million grant for Highland North from the Pennsylvania Commonwealth Financial Authority.

## CURRENT FINANCIALS

EverPower is still an early-stage business, with one full fiscal year of operation since its acquisition by Terra Firma. Its one operational site has been operating commercially since August 2009 and there is a cost base to drive the future development of the business. As a result, the business was loss-making in 2010 and is expected to remain so in the near term until the portfolio of operational assets is increased in scale. Reported revenue in 2010 was $11 million and EBITDA was ($10) million.

Costs were materially higher in 2010 compared to 2009 reflecting the first full year of operations at Highland, spending on near-term development opportunities and establishment of a scalable platform. Looking ahead at 2011, operations are due to commence in the fourth quarter at Highland North and by year-end at Howard, with the resulting increase in revenue expected to be offset by further costs relating to project development and the costs of building commercial capability.

## DEVELOPMENT PLAN

With a further two sites now under construction, and a high quality portfolio of wind energy projects in development, EverPower is well positioned for a significant expansion of its operations.

As EverPower moves to build, own and operate a substantial array of wind assets, the intention is to create an operating platform to support this business. Terra Firma will be able to use its substantial operational skills to help drive this development, with clear similarities to the success already achieved in building Infinis.

There are currently a number of potential bolt-on acquisition opportunities in the US wind farm sector, which Terra Firma and EverPower are actively investigating.

# EVERPOWER

## MANAGEMENT

Jim Spencer
Chief Executive Officer
Jim founded EverPower in 2002. Prior to that, he served as an adviser to Renewable Energy Systems Limited and was instrumental in establishing its Asia Pacific presence in NSW Australia. His earlier roles included President of Sithe Asia Holdings and Vice President of Prudential Capital Corporation in the Utilities & Finance Group. Jim has over 20 years of experience in the power industry managing the development and financing of energy projects.

Jim Spencer, Mike Kinski

Charles H. Williams
Chief Financial Officer
Charlie joined EverPower in 2009 and is responsible for the company's financial activities. He was previously CFO and Executive Director of Clipper Windpower Plc, a utility scale wind turbine manufacturer and project developer, and CFO of Sithe Asia Holdings, a Hong Kong-based independent power producer.

Andrew Golembeski
Executive Vice President and Chief Operating Officer
Andrew is one of the founders of EverPower and has more than 20 years' experience in the electricity industry. Prior to EverPower, he was Vice President of Sithe Energies Inc. Andrew's expertise spans a variety of technologies in the US and internationally, and includes wind, solar, coal, combustion turbines and hydro plants.

Christopher Shears
Senior Vice President, Development
Chris joined EverPower in 2008. He has over 15 years of experience in the wind and renewable energy fields including GB Business Development Manager for Renewable Energy Systems Ltd where he was responsible for wind strategy and building the company's UK project portfolio.

George Henderson
Chief Commercial Officer
George joined EverPower in 2010 and is responsible for all activities in the energy and renewable credit markets, including energy operations, portfolio hedging and commercial risk management. Prior to EverPower, he held senior roles in energy trading and marketing for PSEG Energy Resources & Trade LLC and Lehman Brothers Commodity Services. George has also been an international crude oil and petroleum product trader for various public and private companies.

Carol Strickland
Corporate Secretary & Chief Administrative Officer
Carol joined EverPower in 2008 and is responsible for corporate governance-related matters and administration. Prior to joining EverPower, she was the corporate secretary and chief of staff at US Trust Corporation.

# IN PITTSBURGH, CHARITY BEGINS AT HOME

As part of its commitment to being a good corporate citizen, EverPower is participating in one community event a year in each city where it has an office. For the Pittsburgh office in 2010, the event was all about taking a day to help those in the community most in need. So in April, 26 EverPower employees and family members took part in the 18th annual Rebuilding Together-Pittsburgh event.

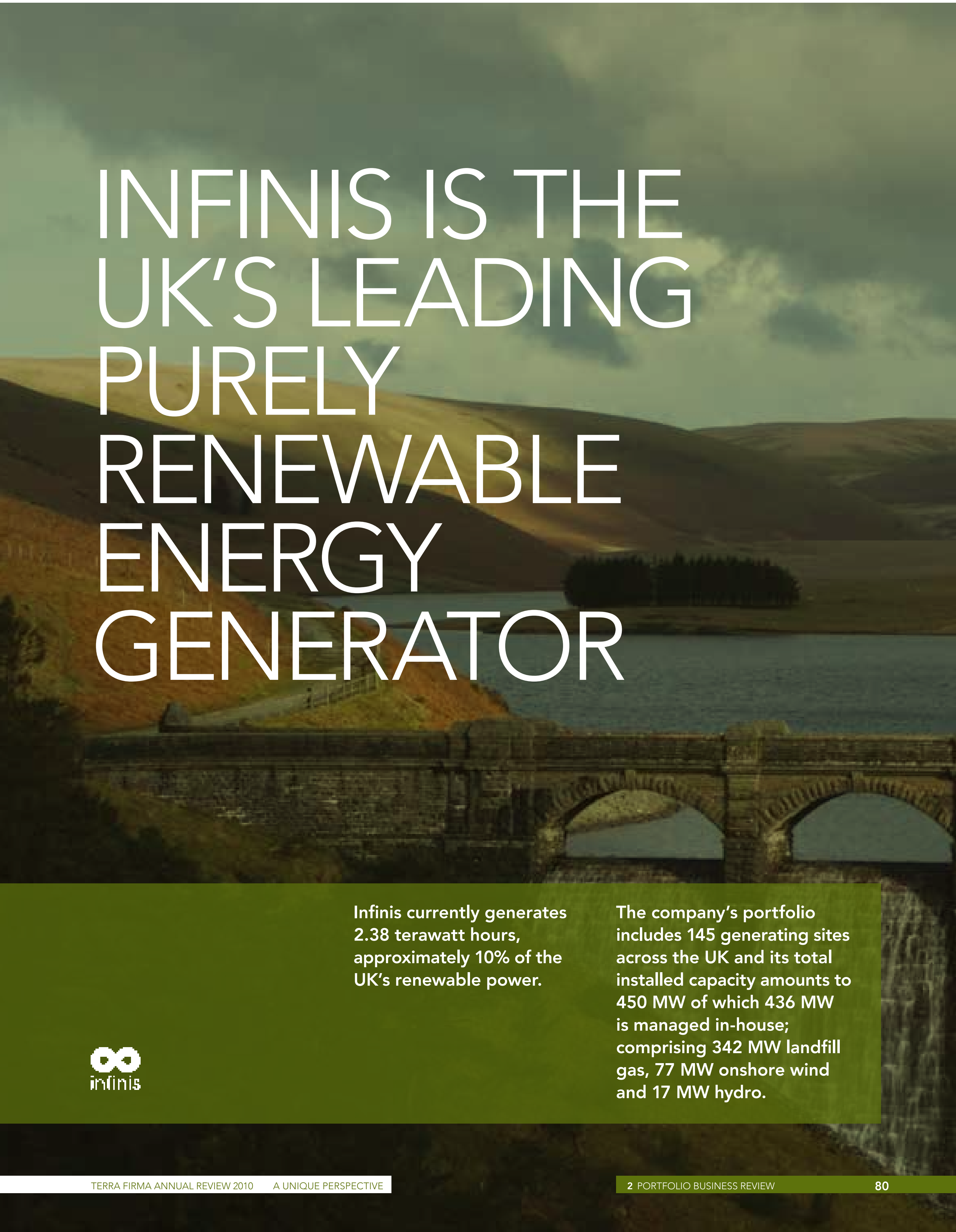
Rebuilding Together is one of the US's leading charitable organisations – it provides free rehabilitation and critical repairs to the homes and community centres of low-income Americans, helping to preserve affordable home ownerships and revitalising communities.

It is a vital support network at a time when the economic pressure on low-income families is growing steadily greater. Financial worries mean that more and more families are having to forego carrying out essential home repairs and modifications in order to provide the basic necessities for their family needs such as food and heating. The situation is particularly difficult for low-income elderly and disabled homeowners who are physically unable to do their own home repairs and are forced to live in unsafe and often unhygienic homes. The kind of problems Rebuilding Together tackles includes faulty electrical services, inadequate plumbing, broken boilers, gas leaks, crumbling walls, and damaged ceilings and roofs.

The EverPower team's project for the day was Hosanna House, a multi-purpose community centre in Allegheny County. The centre is a valuable asset in the local community and offers a wide variety of health and social services including early childhood education, healthcare, youth recreation, mentoring, technology training and employment support.


EverPower employees at work

Every year, around 35,000 people use the services of Hosanna House and the building was in urgent need of some repairs and upgrades. The list was a long one. It included both interior and exterior painting, cracks to repair, tennis courts that needed resealing plus various carpentry and plumbing projects throughout the property. By lending their time and their skills, the EverPower team helped to shorten the 'to-do' list and leave Hosanna House looking brighter and in much better shape to welcome the people who rely on it every day.



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

Infinis currently generates 2.38 terawatt hours, approximately 10% of the UK's renewable power.

The company's portfolio includes 145 generating sites across the UK and its total installed capacity amounts to 450 MW of which 436 MW is managed in-house; comprising 342 MW landfill gas, 77 MW onshore wind and 17 MW hydro.

infinis

No.1
WINNER OF THE 2010 HSBC EUROPEAN BUSINESS AWARDS, GROWTH STRATEGY OF THE YEAR

145
ELECTRICITY GENERATING SITES ACROSS THE UK

10%
OF THE UK'S RENEWABLE POWER PRODUCTION

## INFINIS

# THE ACQUISITION OF THE ARDROSSAN WIND FARM HAS ADDED A FURTHER 30 MW TO INFINIS' ONSHORE WIND GENERATING CAPACITY

| YEAR END: 31 MARCH | YTD Dec 09 | YTD Dec 10 |
|---|---|---|
| Revenue | £92m | £138m |
| Costs | (£43m) | (£63m) |
| **EBITDA** | **£49m** | **£75m** |
| External interest expense | (£5m) | (£25m) |
| Earnings before depreciation and tax | £44m | £49m |
| | | |
| CAPEX | (£18m) | (£35m) |
| Average megawatts / hour | 192 | 257 |

Figures may not add downwards due to rounding

## 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. 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 and the financial incentives put into place by the government to encourage investment.

Terra Firma de-merged the waste-to-energy business from WRG in May 2006, renamed the business Infinis and appointed a new management team. 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 50% of landfill gas is methane, 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.

## REDEFINITION OF 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 with an operating portfolio of landfill gas, onshore wind and small hydro power stations, and a large pipeline of renewable energy development projects. Its strategy is to strengthen its leading position in the industry through investment in additional capacity on existing sites and by playing an active role in the industry's consolidation via acquisitions.

As well as developing its wind and hydro portfolios, Infinis is investigating other renewable energy technologies such as biomass, solar and anaerobic digestion.

## ACHIEVEMENTS

Infinis is the UK's largest purely renewable energy generator, thanks to its sector-leading position in the UK landfill gas industry. Infinis' generation capacity has grown from 57 MW in 2003 to 450 MW in 2010. 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 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.

Infinis acquired Novera in 2009, adding a 141 MW renewable energy generating portfolio comprised of 79 MW of landfill gas, 17 MW of hydro and 45 MW of onshore wind generating assets. The acquisition brought benefits of additional scale to Infinis, expanding its in-house generating capacity and increasing its development pipeline. It significantly enhanced Infinis' position in the onshore wind market as well as adding hydro-generating assets to the portfolio.

In May 2010, Infinis completed the acquisition of Ardrossan, a fully operational wind farm located in a high wind area in the west of Scotland. This site was acquired with a capacity of 30 MW from the large Scottish utility SSE. In January 2011, Infinis acquired a 2.4 MW operational wind farm at Rheidol, Wales, plus a further 12.9 MW consented at two sites in Yorkshire from E.On UK plc.

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

Infinis successfully completed a refinancing of the business in December 2009 with Infinis plc issuing £275 million of high yield bonds, a strong result in challenging markets.

## CURRENT FINANCIALS

Infinis reported strong results for the nine months to December 2010 with EBITDA of £75 million, up 52% on the prior year. This year-on-year increase was in large part due to the additional capacity arising from the Novera acquisition in late 2009 and the OFGEM announcement of a price increase in the recycled element of the Renewable Obligation Certificate.

Infinis continues to take a cautious approach to capital expenditure, in particular on new development spend. As a result, whilst capital expenditure has increased year-on-year, it is being managed well within budget.

The outlook for 2011 remains positive and Infinis has largely secured its revenue for the next two years through forward contracts.

# INFINIS

## DEVELOPMENT PLAN

Infinis' landfill gas business is strongly cash generative, enabling it to further invest in capacity, systems processes and its people. Infinis has substantially built out its landfill gas portfolio and the main development activity for the business is to develop a strong onshore wind farm pipeline, aiming for 500–800 MW of installed capacity in the medium term.

Infinis now has an attractive onshore wind portfolio that comprises 77 MW operating assets, 97 MW consented development projects, 110 MW under consideration by planning authorities and a further pipeline of earlier stage developments. Construction is now underway on the 22 MW Glenkerie project in the Scottish borders which will be operational by the end of 2011.

The emerging hydro portfolio which was acquired as part of the Novera deal is being optimised and further developments are being actively pursued.

The integration of the Novera business has been a major focus of the organisation over the last 12 months. There is a high degree of overlap between the two businesses' activities which has, and will, provide opportunities to reap significant synergies.

Front Row: Jane Aikman, Stewart Gibbins, Andrew Chadd, Eric Machiels, Damian Darragh. Back Row: Steven Hardman, Tavraj Banga

## MANAGEMENT

Eric Machiels
Chief Executive Officer
Eric was appointed full time CEO in October 2010, having been the acting CEO and a member of the Infinis plc Board since August 2009. He had previously been Development Director at Infinis from January 2008 to July 2009. Eric joined Terra Firma as a Business Director in September 2007 and began working with Infinis at a very early stage in his time at Terra Firma. Prior to that, he held executive positions within two portfolio companies of Clayton, Dubilier & Rice, a US private equity firm, and most recently as Managing Director of Sirva Inc.'s Continental European division from 2004–2007. Eric worked as an Investment Director at UBS Capital from 1999–2002.

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 housebuilding 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 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.

# RISING TO THE INFINIS ENERGY CHALLENGE


Sywell school pupils and the Energy Challenge judging panel

The pupils from award-winning Sywell School

As part of Infinis' commitment to being a responsible business and good neighbour, all employees are encouraged to support charitable activities in the areas where they live and work.

The 'Infinis Energy Challenge' is just one example of how the company is making a difference and raising awareness of its work in the local community.

During National Science Week, a competition was launched – supported by the University of Northampton and Northamptonshire County Council – which invited primary schools in the county to find innovative, unusual or effective ways of reducing energy consumption. Infinis donated a smart energy meter to each school so they could measure their carbon saving efforts.

The competition attracted a great deal of interest in Northamptonshire with 17 schools showing their creativity by producing some fantastic energy-saving ideas. They ranged from launching 'switch-it-off weeks' through to schools starting their own smallholdings. By the end of the two-month challenge, some schools were growing vegetables and collecting eggs from their own hens to be used in the school canteen!

As well as supplying the meters, Infinis also recruited 17 volunteers from its staff to be 'Science and Energy Ambassadors'. Their role was to provide encouragement and advice through regular visits to the schools, with some even going along to school assemblies to make presentations and keep enthusiasm levels high. As well as creating strong links with local schools, this proved to be a great exercise for employees' personal development.

When the time came to select a winner, the six finalists were invited to the Infinis head office to present their entries to a judging panel made up of senior managers from Infinis, the University of Northampton and Northamptonshire County Council.

After a tightly contested final round of judging, Sywell Church of England Primary School emerged as the winner for its pupil eco monitors and a wormery for consuming waste, and received the £500 prize donated by Infinis.

The 'Infinis Energy Challenge' was a wonderful opportunity to forge closer links with the local community. There is no question that it has given the area's children an even clearer idea of what carbon footprints are all about and given them the knowledge and tools to do something to reduce their future impact on the environment.

# ODEON & UCI IS THE No.1 PAN-EUROPEAN CINEMA OPERATOR

Odeon & UCI Cinemas Group is the number one cinema operator in Europe, with a presence in the UK and Ireland and five Continental European markets. The Group has a total of 1,884 screens in 207 cinema locations which are a combination of freehold, long leasehold and short leasehold sites.

The business operates under the name of Odeon in the UK, UCI in Germany, Italy, Austria and Portugal and Cinesa in Spain.

25% — 3D FILMS ACCOUNTED FOR 25% OF 2010 TICKET SALES

50 — SITES ADDED UNDER TERRA FIRMA'S OWNERSHIP

800 — DIGITAL SCREENS

## ODEON & UCI

# OVER 40% OF ODEON & UCI'S SCREENS ARE NOW DIGITAL

| YEAR END: 31 DECEMBER | 2009 | 2010 |
|---|---|---|
| Revenue | £641m | £650m |
| Costs | (£561m) | (£558m) |
| **EBITDA** | **£80m** | **£92m** |
| External interest expense | (£19m) | (£19m) |
| Earnings before depreciation and tax | £61m | £73m |
| | | |
| CAPEX | (£35m) | (£33m) |
| Attendance | 75m | 73m |

2010 results are subject to final audit approval

## 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 which 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 unlock value from selective properties owned by the company.

## REDEFINITION OF STRATEGY

Post-acquisition, the strategy was focused on realising savings from merging Odeon and UCI in the UK. 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, 3D, IMAX and new ticketing systems. The strategic development of the business also involved looking for acquisitions in the key markets that would offer benefits from economies of scale and taking the opportunity to dispose of any cinema assets and property that would achieve a significant premium.

## ACHIEVEMENTS

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

As part of the policy to acquire individual cinemas and cinema chains, Odeon & UCI successfully integrated Warner Lusomundo Sogecable and the Iberian assets of AMC with its existing Spanish business. Two further acquisitions in Italy (Europlex and Cinestar) enabled UCI to develop its position in this important market. Four sites were acquired from Hoyts in Germany in 2008 and in 2009, Odeon & UCI took over two existing sites in Italy (Florence and Venice) and one in Barcelona. In 2010, UCI opened a brand new cinema in Palermo, Sicily, took over an existing site in Murcia, Spain and in December further strengthened its position in Italy by acquiring three state-of-the-art cinemas from Pathé in the key cities of Rome, Turin and Florence. Odeon has also purchased six further IMAX digital systems in the UK – taking it to a total of 11 IMAX cinemas and making it the largest IMAX operator in Europe.

The current focus for the business is the roll-out of digital technology and it has continued its roll-out of 3D screens across the group along with the introduction of digital projectors. It now has some 800 digital screens, over 40% of all screens in the estate. The use of digital technology offers long-term print cost savings to the distributors, an improved advertising platform, greater flexibility in programming and alternative content capability, such as live opera, theatre and sports.

In terms of the cinema-going experience, the business has invested heavily in 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 and sandwich bars. It has increased the number of Costa Coffee franchises in the UK and is the biggest franchisee of Ben & Jerry's in the world.

The performance of the UK loyalty card, the Odeon Premiere Club, which was launched last year, has continued to be very strong with more than one million cards sold, making it by far the largest cinema loyalty card programme in the UK. In Continental Europe, loyalty card membership has grown 23% year-on-year and there are now over 1.4 million members. The cards offer significant opportunities for the business to develop a closer understanding of its customers and to be able to make innovative consumer offerings.

2010 was the second full year of operation for Odeon's screen advertising joint venture, Digital Cinema Media. It was pleasing to note an improvement in screen advertising over the prior year following the general downturn in consumer advertising that was experienced in 2009.

## CURRENT FINANCIALS

Odeon & UCI had another extremely strong year in 2010, reporting EBITDA of £92 million, £12 million ahead of the prior year. This strong growth was achieved despite the severe snow and cold weather which badly affected much of Northern Europe in the key trading month of December. This performance reflects the strength of the film slate in a year that saw the latest Harry Potter and Shrek instalments, as well as the growing number of 3D films such as Avatar, Toy Story 3 and Alice in Wonderland.

The film slate for the year ahead looks strong with films such as The King's Speech in the UK and Che Bella Journata in Italy performing well and the final Harry Potter film and the latest instalments of Pirates of the Caribbean and Transformers due for release later in the year.

# ODEON & UCI

## DEVELOPMENT PLAN

The most significant development opportunity is the full scale roll-out of digital projectors which is now underway in all territories, together with the associated roll-out of 3D screens. Odeon & UCI completed negotiations with all the major Hollywood studios during the year in relation to funding arrangements for the roll-out.

The business will continue to focus on improving its customer product offering and on enhancing its customer experience. The successful retail initiatives will continue to be rolled out at additional sites and the increasing number of loyalty card members is providing many opportunities for innovative offers to customers.

Odeon & UCI continues to review further opportunities for growth and improved efficiency, both organically through opening new sites and via acquisitions. The business is also looking to take over lease agreements for existing sites when opportunities arise.

Mayamiko Kachingwe, Jonny Mason, Rupert Gavin

## MANAGEMENT

Rupert Gavin
Chief Executive Officer
Rupert was appointed as CEO 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 over 20 years. He held a number of positions at Famous Players prior to 2002 including Senior Executive Vice President and General Manager.

José Batlle
Chief Operating Officer, Continental Europe
José 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.

# HOW THE BIG SCREEN IS MAKING A BIG DIFFERENCE


From the days of single screen cinemas to today's multiplexes, Odeon cinemas have played a big part of British life for generations. The films have changed hugely along the way, but what has remained constant has been the company's commitment to having a positive impact in the communities where it operates.

Every year, Odeon is involved with initiatives that support local people in different ways, from providing subsidised screenings for older film fans through to events that champion new young talent.

Looking back at 2010, Odeon has supported a number of initiatives with the aim of making a real difference to the lives of young people.

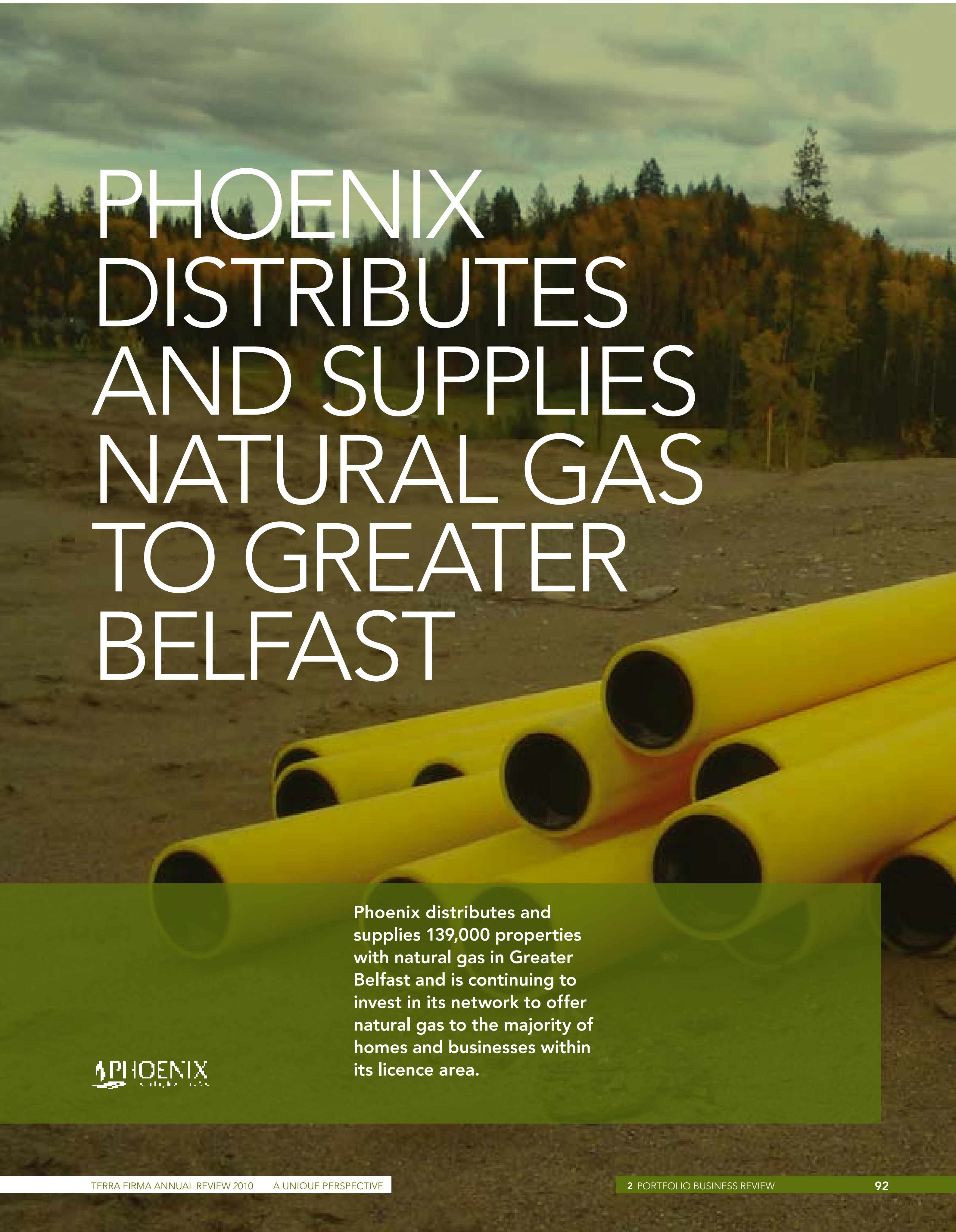
The Bright Futures Internship Programme is a joint initiative between employers and schools in Manchester that gives a group of 14- and 15-year-old students the chance to experience the workplace for themselves. As well as helping them to think about their career options and the kind of skills employers look for, it has been great for helping the youngsters to build self-confidence.

National Schools Film Week is an annual event which is funded by the film industry and Odeon is one of the biggest participants and contributors. Attractions include free screenings of educational films as well as previews of Hollywood films yet to be released in the UK and Ireland.

First Light is a popular programme that helps youngsters from all backgrounds to sharpen their creative skills, showcase their work and learn a bit about the workings of the film business. Odeon is a keen supporter of this programme, and the free screen time it donates is giving the public its first glimpse of the next wave of British cinematic talent.

This year has also seen Odeon continuing its work with its exclusive Charity Partners – Variety Club and the NSPCC. So far, over £200,000 has been raised through a variety of events and Odeon has been named a Patron of the NSPCC.

These are a just a few examples of how Odeon is continually finding new ways to contribute to local life at the 100 or so locations where it operates. Comparable schemes are run in the European countries in which the company has a presence. One of the additional benefits of these initiatives is the way they boost staff morale – employees are always saying how much they enjoy getting involved and doing their bit. Which, of course, gives Odeon another great reason to keep up the good work in 2011.



# PHOENIX DISTRIBUTES AND SUPPLIES NATURAL GAS TO GREATER BELFAST

Phoenix distributes and supplies 139,000 properties with natural gas in Greater Belfast and is continuing to invest in its network to offer natural gas to the majority of homes and businesses within its licence area.

3,100km OF GAS MAINS NETWORK

139,000 CUSTOMERS

45,000 SERVICE ENGINEERING VISITS IN 2010

## PHOENIX GROUP

# NATURAL GAS PRODUCES AT LEAST 25% LESS CARBON DIOXIDE EMISSIONS THAN OTHER FOSSIL FUELS

| YEAR END: 31 DECEMBER | 2009 | 2010 |
|---|---|---|
| Gross turnover | £108m | £111m |
| Gas purchases | (£62m) | (£64m) |
| Gross gas margin | £46m | £47m |
| Costs including depreciation | (£23m) | (£26m) |
| **EBITA** | **£24m** | **£21m** |
| (Over)/under-recovery | (£4m) | – |
| Underlying EBITA | £20m | £21m |
| External interest expense[1] | (£15m) | (£18m) |
| | | |
| CAPEX | (£12m) | (£13m) |
| Customers | 129,000 | 139,000 |

[1] Excludes exceptional costs, including swap break costs due to refinancing

Numbers may not add downwards due to rounding

2010 numbers are subject to final audit approval

## INVESTMENT RATIONALE & REDEFINITION OF STRATEGY

When Terra Firma acquired East Surrey Holdings, a portfolio of regulated utility businesses, it recognised the growth prospects of Phoenix, the gas business in Northern Ireland (NI). 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 worked with Phoenix's management and the regulatory authorities to agree a mutually satisfactory regulatory framework to allow Phoenix to develop its business and thereby also benefit its customers.

## ACHIEVEMENTS

When Phoenix 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. Phoenix has now made gas available to more than 285,000 properties, with 139,000 already connected, and it is investing to expand the network further and connect an additional 50,000 homes and businesses by the end of 2016. The Phoenix distribution network is considered a world-class benchmark of best practice in gas infrastructure development and the lessons learned in NI are influencing natural gas development around the world.

In January 2008, Phoenix separated its distribution business from its transmission assets in order to comply with the EU Gas Directive. This facilitated the sale of its transmission business to Northern Ireland Energy Holdings Ltd in March 2008; the resulting proceeds of £99 million were used to pay down debt.

A regulatory framework governing the business's connection incentives, permitted market development costs, and other operating costs was agreed with the regulator in 2009 providing clarity on the economics of the planned network expansions. This framework operates alongside the 40-year licence and five-yearly price control process.

In November 2009, the business completed a refinancing which provided the business with eight-year bond financing (£275 million) and three-year capital expenditure and working capital facilities.

## COMPANY STRUCTURE

To comply with regulatory requirements, the business is split into several independent divisions:

### Phoenix Natural Gas Ltd (PNG)

PNG is the owner and operator of the licence for the distribution network in the Greater Belfast area and Larne. It is responsible for the development of the pipeline network and for providing a 24/7 operational and transportation service platform to gas suppliers under the rules of the Companies Network Code. The PNG network currently extends to 3,100 km and distributes natural gas throughout the licence area, representing around 50% of the population of NI.

### Phoenix Supply Ltd (PSL)

PSL is the market leader in gas supply in NI and is responsible for the provision of natural gas to customers from PNG's distribution network and supplies 128,000 residential and 10,000 industrial and commercial customers with gas. In addition, it trades gas on the wholesale market.

### Phoenix Energy Services Ltd (PES)

PES is the leading provider of natural gas boiler and appliance servicing, emergency response, gas metering and meter reading services in NI. The company undertakes more than 45,000 service engineering and 262,000 meter reading visits annually.

### Phoenix Energy Ltd (PEL)

PEL was established in 2008 to supply natural gas in the Republic of Ireland (RoI) and expand the service offering of PSL across the whole of Ireland. PEL was awarded a licence to supply natural gas in December 2008.

## CURRENT FINANCIALS

2010 was the coldest year on record in NI. The resulting increase in gas consumption together with net customer growth in both NI and RoI, as a result of the development of its new subsidiary, offset the impact on pricing of lower average gas costs within the contract and tariff sectors. Gross turnover in 2010 was £111 million, £3 million higher than in 2009 whilst margin grew by £1 million across the same period, with margin in part being impacted in the year by PSL returning savings from prior year to customers. Operating costs increased in line with expectations as the initial network installations are coming off warranty and the business is incurring maintenance and support costs in line with the long-term plan. Depreciation is also increasing as the network expands and the asset base grows.

For new connections, which are the main growth driver, the business delivered an exceptional performance, beating the full year budget of 8,025 in spite of the challenging economic environment. Strong owner occupier conversions to gas have offset the gap in new-build connections driven by lower new-build activity.

# PHOENIX GROUP

## DEVELOPMENT PLAN

The distribution business, PNG, is well-placed to serve Belfast's long-term growth prospects and address the still comparatively low market penetration compared to the UK mainland, where about 90% of consumers use gas, compared with only about 49% in Belfast. PNG is committed to achieving an overall market penetration of 60% by 2016 by continuing to invest in its distribution infrastructure and increasing the number of users connected to its network. PNG has now submitted its forecast data to the NIAUR with regards to its next price control commencing 1 January 2012. The process is expected to conclude in the final quarter of 2011.

Julie Williamson, Nils Steinmeyer, Michael McKinstry, Peter Dixon, Lorenzo Levi

Julie Williamson, Peter Dixon, Robbie Barr, Guy Hands, Michael McKinstry, Sami Kassam

PSL aims to continue to provide a stable environment for the market development and future growth of the distribution business by servicing PNG customers. While the gas supply market in the industrial and commercial sector has been open to competition for some years now, domestic customer competition only started in November 2010. Despite anticipating further volume losses as a result of this over the next few years, PSL expects to remain subject to tariff price caps and reviews for the foreseeable future.

Phoenix will seek to expand its supply business, PEL, in the ROI to capitalise on the expertise and activities of PSL as well as offsetting some of the volume losses in NI.

## MANAGEMENT

**Sir Gerry Loughran KCB**
Group Non-Executive Chairman
Sir Gerry's role as the Non-Executive Chairman of the Phoenix 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 Phoenix board as CEO 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 stand-alone businesses, before joining Phoenix as Commercial Director in 1997.

**Michael McKinstry**
Group Finance Director
Michael joined Phoenix 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 Phoenix includes roles in heavy engineering with GEC, the textiles industry with Ulster Weavers and the energy industry with Premier Power after its purchase by British Gas.

# EDUCATION OUTREACH


Peter Dixon and Christopher Doherty from Phoenix taking part in the 'Time to Read' programme


Launching the Phoenix Carbon Calculator

Phoenix is a business that has always taken its responsibilities to its staff, the local communities it operates in, and the environment extremely seriously. To help coordinate its efforts, the company set up an integrated – and award-winning – Corporate Social Responsibility (CSR) programme called LIFE.

LIFE stands for Leadership in the marketplace, Investing in our people, Fostering our community and Environmental responsibility, and is run by the Kellen Group (Phoenix's parent company) on behalf of Phoenix.

The fact that it has received national recognition for the sixth year running with a Business In The Community 'Big Tick' award for CSR excellence is an indication of just how successful the programme has been.

One of the key projects within LIFE is the Education Outreach programme. In recent years, this has seen Phoenix staff working with pupils of primary school age right up to college and university students.

2010's initiatives included a collaboration between Phoenix and students from Queen's University to develop a 'Carbon Calculator' As part of their consultancy module, Environmental Management post-graduates reviewed the Phoenix carbon savings model. The Carbon Calculator is designed to help householders and businesses track their carbon dioxide emissions savings since switching to natural gas from an alternative fuel such as oil or coal.

Another highlight of 2010 was a site visit from a large number of first year secondary school children wanting to learn more about possible careers in engineering. The pupils were given a guided tour of Phoenix's Belfast headquarters and also had several presentations from senior engineering managers from the company.

The event was part of National Engineers Week and was run in conjunction with the Institution of Civil Engineers. This was one of many initiatives that Phoenix has been involved with in response to the Government's push to encourage more children to study science, technology, engineering and maths.

Phoenix staff also take time out regularly to help in local primary schools on a range of educational projects. Most recently, that has involved mentoring a group of 8-year-olds as part of Business In The Community's 'Time To Read' programme. By committing to attend local schools once a week for a full year and read with the children, Phoenix staff are playing a key role in helping to improve literacy levels.

# TANK & RAST OPERATES 90% OF THE CONCESSIONS ON GERMANY'S MOTORWAY NETWORK

These concessions include around 380 restaurants, 350 petrol stations and 50 hotels. The company's key revenue streams are lease income from tenants and fuel supply commissions from the oil companies.

Tank & Rast's efforts to modernise autobahn services to meet customer needs and to introduce high quality performance standards have won it widespread independent acclaim.

TANK & RAST

500m VISITORS A YEAR
400 SITES
130 TENANTS
RÜCKENRASTHAUS FRANKENWALD

## TANK & RAST

# THE PREMIUM WASHROOM CONCEPT 'SANIFAIR' HAS BEEN ROLLED OUT ACROSS NEARLY ALL TANK & RAST'S SITES

| YEAR END: 31 DECEMBER | 2009 | 2010 |
|---|---|---|
| Revenue | €270m | €279m |
| Costs | (€84m) | (€84m) |
| Bank interest | (€144m) | (€152m) |
| **Earnings before depreciation and tax** | **€42m** | **€43m** |
| | | |
| CAPEX | (€52m) | (€37m) |

## INVESTMENT RATIONALE

Terra Firma believed that Tank & Rast could capitalise further on its strong position on the German autobahn, which was 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 the 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 capital investment in customer-focused initiatives. Further changes would be focused on the business operating model, with the priority of creating an environment in which the most entrepreneurial tenants could 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 130 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 – which supply branding and fuel, but do not operate the fuel stations – and the tenants, which 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 at the time of acquisition, Tank & Rast was lagging behind comparable European networks in terms of penetration, conversion and customer expenditure.

Tank & Rast's response was threefold: it improved 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'; 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 consolidated the operation of its c.400 individual sites under around 130 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 long-term €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.

## ACHIEVEMENTS

The refocused strategy has resulted in a service station network that compares favourably with the best international benchmarks. Consumer choice has significantly increased and customer satisfaction has jumped. Almost all of Tank & Rast's sites now have motorway signage and the implementation of well-known brands is proceeding well.

Tank & Rast officially launched its Serways brand in 2008, with a big consumer campaign that contributed to a significant increase in the brand awareness. Serways continues to be rolled out across the network and in August 2010, the first Serways hotel was opened on the motorway and is meeting initial performance targets.

The premium washroom concept Sanifair has been an enormous success and has been rolled out across nearly all of Tank & Rast's sites. In 2010, Sanifair was further improved to provide the consumer with greater service and better facilities. The price was increased to 70 cents, with the consumer continuing to receive a 50 cent voucher that can be redeemed in Tank & Rast retail shops and restaurants. Full roll-out of the improved concept is nearly complete. The Sanifair concept continues to attract enquiries from different sectors in Germany and in other countries and is now operating in a number of locations off the motorway. Planning is well advanced for the roll-out of further sites in shopping centres and railway stations in 2011.

## CURRENT FINANCIALS

Tank & Rast reported revenue and earnings before depreciation and tax ahead of prior year despite trading conditions remaining generally difficult throughout the year. The business was also adversely affected during the year by extraordinary weather conditions, most recently by heavy snow and freezing temperatures which significantly reduced traffic volume. These trends resulted in lower fuel volumes and gastronomy sales compared with 2009, although retail sales were ahead of prior year.

Costs for the year were similar to last year's, reflecting a continued focus on cost control, in particular on consulting and project-related items.

Capex for 2010 was lower than the previous year, as management has taken a cautious approach to investment in the current environment and construction projects towards the end of the year were delayed by the exceptionally cold winter weather.

# TANK & RAST

## DEVELOPMENT PLAN

Tank & Rast is continuing to progress opportunities to implement Sanifair at new locations away from its network and roll-out onto a larger number of sites is expected during 2011. Following the successful opening of a Serways hotel in 2010, the business has plans to open additional Serways hotels in 2011.

Tank & Rast agreed a new pilot project with the Federal government to create additional parking spaces close to the motorway service areas and successfully opened its first such private parking area during the year. Implementation of this concept on other sites is under negotiation.

The team has made good progress in working with its tenants on its major investment programme to develop and implement an Electronic Point of Sale and cash desk system, which should drive cost and working capital efficiencies in the network.

Tank & Rast has a long-term capital investment programme with several new sites planned every year and an ongoing refurbishment programme to keep all sites up to date. During 2010, Tank & Rast opened one new site and two further sites opened in early 2011.

The existing fuel supply contracts expire at the end of 2012. In preparation for this, the business submitted proposals to the Federal Cartel Office (FCO) for a new fuel supply model. Following an extensive industry consultation process, the FCO announced in January 2011 that it is satisfied with the model proposed by Tank & Rast and the business is now working on the detailed planning for its implementation.

Dr Karl-H Rolfes

## MANAGEMENT

Dr Karl-H. Rolfes
Group Chief Executive Officer
Karl was appointed as CEO 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.

Dr. Jens Kimmig
Chief Financial Officer
Jens joined Tank & Rast in 2010 as CFO. His previous role was CFO of Plastal Group. Jens' previous roles include various leading functions in the fields of controlling, finance and accounting within GEA Group AG, including CFO of the Strategic Business Field Plastics at Dynamit Nobel Kunststoff GmbH and CFO of the Strategic Business Unit Thermosets at Menzolit-Fibron GmbH.

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.

# HELPING TO MAKE MOTORWAYS SAFER FOR EVERYONE

School group visiting Tank & Rast's Rhynern site

Tank & Rast has been actively engaged in improving motorway safety for many years. The aim has been to educate grown-ups and children alike about road safety and increase their awareness of the risks of motorway travel.

There are lots of ways Tank & Rast is making a difference. As well as running its own initiatives every year, the company is also a member of the key road safety organisations and has for many years worked closely with the Federal Ministry of Transport, Building and Urban Development. Tank & Rast also supports nationwide initiatives such as Road Courtesy, which was originally started by a consortium of German newspapers.

During the summer of 2010, the focus was on educating tomorrow's drivers when Tank & Rast invited a school class of 9- to 10-year-olds to take a celebrity guided tour of its Rhynern site in Westphalia. The children were welcomed by Matz – the clever bear – a well-known character from a family magazine. Matz explained how a busy location like Rhynern works and the children got to take a closer look behind the scenes of the service site and the motorway hotel.

Some of the important lessons they learned during their visit were how to behave on a service site, the safety rules they should remember to follow and exercises that they should do during long journeys.

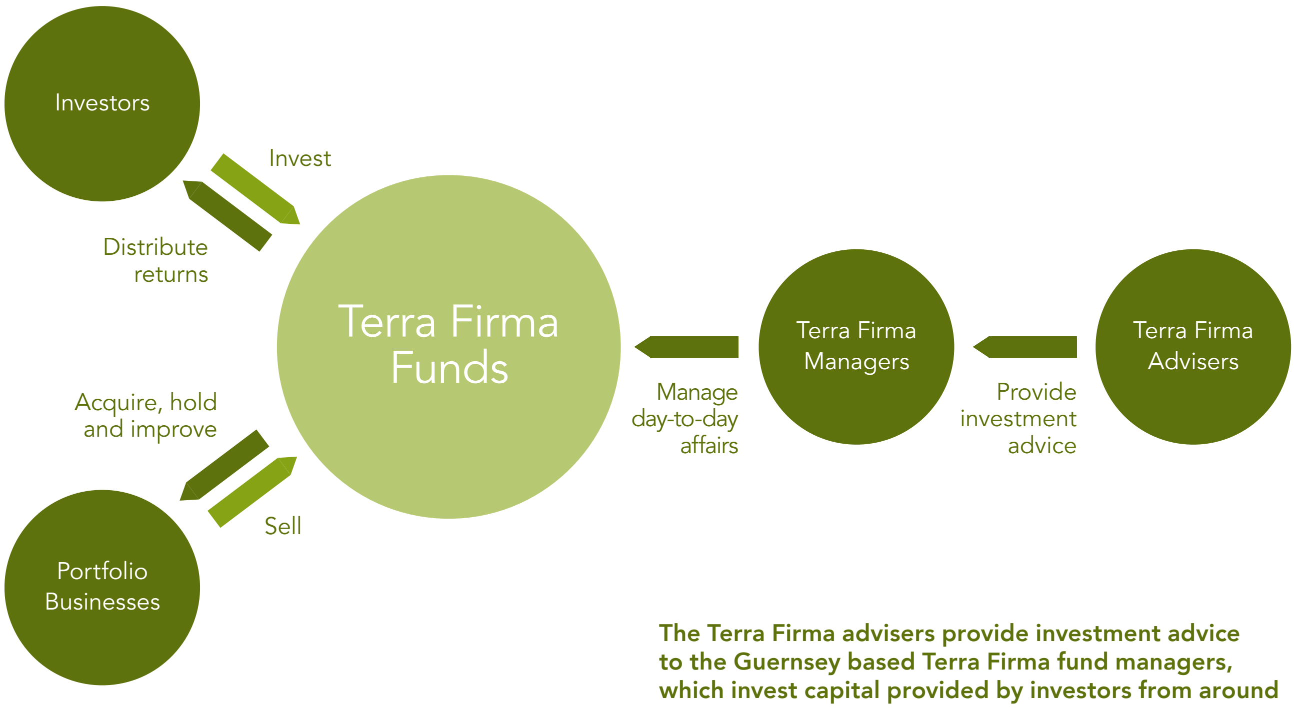
In 2010, Tank & Rast also launched an initiative to improve the sometimes strained relationship between car drivers and truckers. In co-operation with the internet-based truck drivers' association, truckerfreunde.de, Tank & Rast created a campaign to make car drivers aware of the specific challenges for truck drivers and the safety issues they have to deal with on the road. The campaign was named 'Hand in Hand' and can be seen on the website www.truckerfreunde.de.

Working with the Truckerfreunde Association, Tank & Rast created an entertaining flyer filled with safety advice and a bumper sticker featuring a truck and a car driver shaking hands. The flyer highlighted the very different driving dynamics of a truck and the limited visibility for truck drivers, and the campaign was well received by truckers and car drivers alike. Truckers have reported that it has helped to start conversations with car drivers, a positive sign that a complicated relationship on Germany's motorways could be a little easier in the future.

# 3 Terra Firma Business & Financial Review

## INTRODUCTION

# THE TERRA FIRMA ADVISERS PROVIDE INVESTMENT ADVICE TO THE GUERNSEY-BASED FUND MANAGERS




**The Terra Firma advisers provide investment advice to the Guernsey based Terra Firma fund managers, which invest capital provided by investors from around the world.**

**The Terra Firma advisory group consists of TFCPL in London, TFCML in Guernsey and terrafirma GmbH in Frankfurt.**

**Since 1994, Terra Firma has advised on investments amounting to over €14 billion of equity with an aggregate enterprise value of €43 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:

(i) have been made available in good faith based on the information available up to the time of the release of this report; and

(ii) should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information

# STRATEGY

## BUSINESS OBJECTIVE

**Terra Firma raises long-term capital from investors such as public and private pension funds, government investment funds, insurance companies, endowments and charitable foundations. This capital is channelled through Terra Firma's funds and used to acquire basic, asset-backed businesses that are underperforming in some way, with these portfolio businesses then being held by the funds. The funds are managed by the Terra Firma managers with investment advice provided by the Terra Firma advisers**.

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.

These revitalised companies are later sold, usually after a number of years, to realise a return for the investors in Terra Firma's funds.

## OUR INVESTMENT APPROACH

Since 1994, Terra Firma has consistently applied an investment strategy that focuses on identifying and capturing value in underperforming businesses in basic industries. Terra Firma favours asset-backed businesses that will benefit from our ability to implement strategic, operational or management change.

Through conducting our own research and analysis to identify trends and sectors that are attractive, we form a view of how those macro themes affect the participants in those sectors. This approach of identifying macro themes first, followed by identifying specific opportunities, underpins Terra Firma's investment strategy.

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

## DIFFERENTIATED STRATEGY

Our rigorous analysis regularly leads us to develop strategies that are different from the market consensus and to identify opportunities missed by others. It is for this reason that Terra Firma has often invested in sectors that have been overlooked or undervalued by the investment community. Whether by coming up with a different approach to the running of a business, finding solutions to problems which others have considered intractable or taking contrarian views on macro issues, Terra Firma has identified hidden value in many businesses.

## TAILORED ORGANISATION

Terra Firma has the full range of specialist skills necessary to pursue a differentiated investment strategy and strategically reposition businesses:

- Our financial professionals are drawn from a wide variety of backgrounds including investment banking, consultancy, accountancy, law and direct from university. These financial professionals form the core of the transaction teams.

- Our in-house operational team has decades of industry experience. Our most experienced operational experts are the Operational Managing Directors who have been former CEOs of FTSE 250 companies or have run substantial divisions of multi-national businesses. Each of them has worked in many different sectors. Working closely with them is a group of Business Directors who have all had line P&L responsibility in a number of areas and have often spent time working as management consultants. They are also supported by a group of Finance Directors who have many years of operational finance experience working in a wide range of industries and in accountancy practices.

- Our in-house legal, tax and structuring specialists have all had careers at leading law firms or accountancy practices before joining Terra Firma. In these positions, their focus was on transactional work: acquisitions, disposals and complex financings.

## LIFE CYCLE OF A TERRA FIRMA FUND

## STRATEGY

Arjan Breure, Robin Boehringer, Florian Goldgruber

William Burnand, Aneeqa Khan

## We involve ourselves directly in the businesses that we acquire

In analysing a potential new investment, each transaction team is drawn from this diverse pool of in-house talent. From the outset, our transaction teams are multi-disciplinary with each consisting of a Financial Managing Director, an Operational Managing Director and such number of financial, operational, legal, tax and structuring resources as the investment requires.

Each transaction team has sector specialisations which reflect the investment experience and knowledge of its members. All team members, from whatever background, are expected to contribute to the development of the portfolio businesses. We believe that having our own team of in-house specialists, in addition to outside third parties, gives us an advantage in identifying proprietary ideas for improvements and changes that can be made in the businesses we acquire.

Our culture is an open one that demands debate and discussion across every level of our organisation. Creative tension and a willingness to challenge orthodox views with innovative approaches are key characteristics of our teams. This approach, together with the breadth and diversity of our team is vital for our value approach to investing.

## OPERATIONAL EXPERTISE COMBINED WITH ACTIVE MANAGEMENT

Operational expertise is fundamental to enhancing value in our businesses and we involve ourselves directly in the businesses that we acquire. Our Operational Managing Directors can act in a number of different capacities in relation to the portfolio businesses for which they have responsibility, including acting as interim CEO pending appointment of a permanent CEO.

This gives Terra Firma flexibility when it is making an investment or when it determines that an existing business needs to move in a different direction. It also allows Terra Firma to address short-term management changes whilst the business is transitioned to a longer-term management solution. In addition to this, an Operational Managing Director acts as a mentor to the portfolio business's senior management.

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.

Ongoing oversight is provided by the portfolio business team which ensures consistent contact with different levels of management and continually evaluates the performance of the investment, the management team and the strategy. This approach ensures that the management team has the support it needs on operational matters and that it continues to follow Terra Firma's defined strategy to enhance value.

Although the level of direct involvement in a portfolio business is likely to decrease during Terra Firma's ownership, Terra Firma remains integrally involved in the strategic decisions its businesses make. In particular, Terra Firma maintains strict control of how capital is invested in a business, whether that capital comes from the business's cash flow or from Terra Firma's funds, through its corporate governance structure.

## BUSINESS MODEL REDEFINITION AND PERFORMANCE IMPROVEMENT

Our rigorous analysis and research into an acquisition target's strategy and operations 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 developments in its industry.

Terra Firma is willing to add additional capital to its investments in order to help the business grow organically or expand through acquisition and we have done just that with most of our existing portfolio businesses. Our initial investment is frequently used to create a platform that can be used to execute our strategic vision. As our strategy takes hold, further value can be created by expanding the scale of operations through acquiring other players in the sector, as evidenced by Infinis's acquisition of Novera Energy Ltd, one of the UK's leading renewable power generators, or through capital expenditure on internal projects such as CPC's focus on increasing the overall herd-carrying capacity of its existing portfolio. The portfolio businesses are heavily involved in any decision to invest further capital.

Terra Firma fundamentally revises both strategy and operations within its businesses to create significant improvements in performance. These types of changes take time, and are not always easy or welcome, but investing for the long term is a vital element in creating successful and sustainable businesses.

# BUSINESS DESCRIPTION & ENVIRONMENT

## OUR MARKETS

Terra Firma has offices in Guernsey, London and Frankfurt. We have focused on investments in Western Europe, but have reviewed and made investments around the world when appropriate opportunities have arisen and have acquired businesses in Australia (CPC) and the US (EverPower).

Many of our portfolio businesses have extensive overseas operations. Of the 28 investments that Terra Firma has made, 24 have been headquartered in Europe. Taking the current portfolio as a whole, 27% of its revenues come from outside Europe, with 75% from outside the UK. While we continue to evaluate investment opportunities around the globe, we are particularly interested in pursuing European-based opportunities, especially in some of the stronger continental economies such as France and Germany.

## TERRA FIRMA'S DIFFERENCE

Terra Firma's skill is forming an independent view on a sector, understanding how that view affects the sector's individual participants and then using its extensive operational resources to act as change agents on a particular company within that sector. This 'macro-to-micro' approach to identifying investment opportunities underpins Terra Firma's investment approach.

The shift in a company's strategic and operational direction often places it at the forefront of developments in its industry, as seen with Odeon & UCI's drive to introduce digital projection technology across its portfolio. Playing such an active role in transforming an industry differentiates Terra Firma from other private equity firms.

Simon Holden, Lisa James

**We use our extensive operational resources to act as change agents**

## THE OUTLOOK FOR PRIVATE EQUITY AND TERRA FIRMA

Private equity deal volume and size were higher than expected in 2010, especially for secondary buy-outs. These trends are likely to be maintained this year as debt availability continues to improve. However, the large overhang of private equity capital and resultant increased competition for assets means that finding a business at a reasonable price will continue to prove challenging.

Private equity firms will have to build value by finding assets that will benefit from an overhaul in their strategy and operations. In this regard, Terra Firma is well placed. Our strong operational team has always been a key part of the business and is vital not only to delivering strategic change, but also for optimising company performance. Already in 2011, we have seen both sectors and strategies with excellent investment potential for private equity firms that have this type of strategic and operational expertise.

While Terra Firma will continue with its main focus on businesses located in Europe and the West, we are looking to invest in companies with exposure to the emerging economies. We are also seeking asset-rich businesses that can provide a meaningful hedge against inflation. Many of these opportunities are in sectors that are fragmented and amenable to bolt-on acquisitions, businesses that require sizeable capital expenditure or development capital and companies that require hard, intensive operational involvement to make them more efficient.

For our existing portfolio, we believe 2011 will provide opportunities for us to continue to grow our existing businesses through bolt-on acquisitions and the injection of development capital.

Quentin Stewart, Guy Hands

Monika Trebert, Felisa Schmidt

# BROAD-BASED EXPERTISE

## OUR REPUTATION

Since 1994, Terra Firma has developed a strong reputation in the investment community for independent thought and the ability to execute transactions that capture value in underperforming industries through strategic and operational improvement. 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 offer. Across our offices in London, Frankfurt and Guernsey, the Terra Firma advisory team has around 90 people from 21 countries speaking 20 languages. Our team of over 60 investment professionals is drawn from a wide variety of backgrounds including finance, industry, law, tax and structuring, and gives us the diverse expertise we need to analyse each opportunity in detail and to drive value in the businesses we acquire.

## 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 spend substantial time with the group's senior executives to ensure they have a good understanding of Terra Firma and how it operates.

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

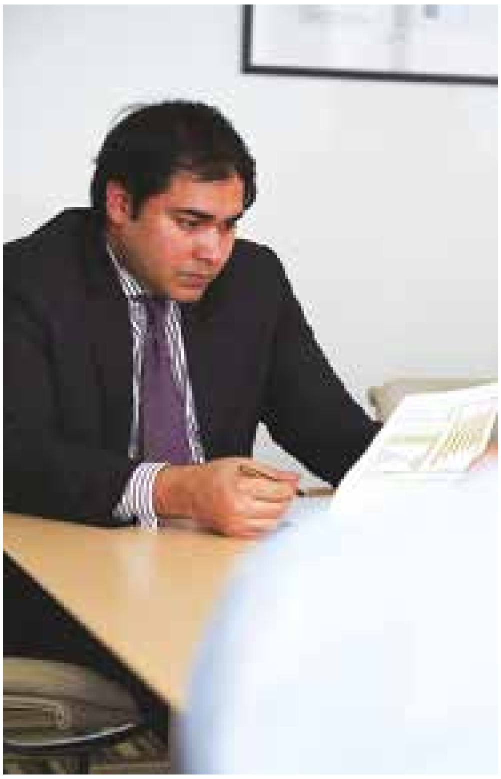
Throughout our business, we encourage our people to take responsibility for their own personal and professional development. That development can take many forms such as on-the-job coaching, counselling and job enrichment as well as formal training programmes, courses and professional qualifications. Our sponsorship programme helps those wishing to gain recognised professional qualifications and Terra Firma has a policy of supporting employees in pursuing qualifications that will help their work and career development.

All TFCPL investment professionals up to the level of Associate Director are encouraged to obtain the CFA qualification. The CFA Program® sets the global standard for investment knowledge, standards and ethics. Passing the CFA exam enables the holder to prove that they have mastered a broad range of investment topics and are committed to the highest ethical standards in the profession.

In 2009, TFCPL accepted six entrants onto its Graduate Training Programme. This is a two-year scheme where graduates are given an opportunity to learn about all aspects of Terra Firma and to work with Investor Relations, Finance, the Transaction Teams, the CIO office and the Operational Teams. This has been a great success with the graduates who, as a result, have developed a broad base of skills on which to build their careers. In 2011, TFCPL plans to expand the scheme to offer ten places on the programme.

Terra Firma also offers internship opportunities to undergraduate and postgraduate students, allowing individuals to gain an insight into life at work. In 2010, Terra Firma made five internships available and plans to do the same in 2011.

## Terra Firma has developed a strong reputation for independent thought



Tavraj Banga

### SPECIALIST ADVISERS

As well as its in-house specialists, Terra Firma is advised by an array of distinguished professionals from the realms of international politics, economics and business.

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

This group consists of: Lord Birt, Fraser Duncan, Professor Gordon Edge, Elizabeth Filkin, George Greener, Michael Kern, Wolfgang Koenig, Axel Nawrath, Klaus Rauscher, Werner Seifert and Karsten Voigt.

The Terra Firma managers are also advised by external professional firms in addition to the Terra Firma advisers. These include: lawyers and accountants to help carry out due diligence, structure and execute transactions; investment banks to provide financial advice; tax specialists to optimise the tax efficiency of investments; environmental consultants; industry specialists; and business change consultants to assist on strategic change programmes within the portfolio businesses.

# CORPORATE SOCIAL RESPONSIBILITY

**At Terra Firma, we take our responsibility to the wider community very seriously. We recognise that our portfolio businesses 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, our portfolio businesses 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 a strict equal opportunities policy 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, comply with industry standards and local regulations and that act in a socially responsible manner.

## COMMUNITY SUPPORT

TFCPL is fully committed to supporting its local community of Southwark in inner-city London. From 2006–2008, TFCPL donated 10% of its net annual profits to the Terra Firma Charitable Trust. In 2009 and 2010, this donation was split between the Terra Firma Charitable Trust and the Private Equity Foundation. These donations have enabled the Trust to make total commitments of over £1.2 million to charitable organisations working in and for our local community.

Terra Firma is a founding member of the Private Equity Foundation, an organisation that aims to invest the capital and expertise of the private equity community in selected charities in order to help them achieve a step change in their impact.

TFCML is fully committed to supporting its local community in Guernsey and in 2010, made donations to the Guernsey Dyslexia Centre, Les Bourgs Hospice Redevelopment Appeal and Headway, Guernsey (an independent charity that provides support to those who are living with the long-term effects of brain injury).

## TERRA FIRMA CHARITABLE TRUST

The mission 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 the local community in the London Borough of Southwark, where our London office is located.

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 donations.

We will principally 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.

The Terra Firma Charitable Trust is proud to support the charities and initiatives detailed on the following pages.

**10%** OF TFCPL PROFITS DONATED TO THE TERRA FIRMA CHARITABLE TRUST AND THE PRIVATE EQUITY FOUNDATION

**£1.2m** COMMITTED SINCE 2006

# CORPORATE SOCIAL RESPONSIBILITY

## AGE CONCERN LEWISHAM AND SOUTHWARK
### 6-YEAR FUNDING (2007–12)

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 age-related health problems such as heart disease, high blood pressure and mental health conditions. Age Concern is dedicated to the promotion of the well-being of all older people and to helping make later life a fulfilling and enjoyable experience.

## CHILDREN'S COUNTRY HOLIDAYS FUND
### 5-YEAR FUNDING (2009–13)

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 ongoing support to help improve the quality of their lives, recognise their potential and achieve their goals in the safest possible environment.

## CREATE ARTS
### 6-YEAR FUNDING (2008–13)

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 in 2003, Create has run more than 2,970 workshops, mainly as part of sustained, life-changing programmes, for over 19,700 participants.

## DOWNSIDE FISHER
### 3-YEAR FUNDING (2009–11)

The Downside Fisher Youth Club has supported socially-excluded young people in the Bermondsey area for over 100 years. It was originally established as a boys club in 1908 and since that time has worked with disadvantaged children, helping them learn from each other and offering challenging experiences and learning opportunities that are not otherwise easily available in Bermondsey.

## KIDS COMPANY
### 4-YEAR FUNDING (2007–9, 2011)

Kids Company is a charity founded by Camila Batmanghelidjh in 1996 in order 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 based in Southwark. 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, including helping young people get their driving licence, passport and register with a doctor along with study and business skills, Maths and English, drama, film production, fashion studies and more.

## PRINCE'S TRUST
### 6-YEAR FUNDING (2006–11)

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- to 30-year-olds realise their potential and transform their lives.

### ST CHRISTOPHER'S HOSPICE
### 3-YEAR FUNDING (2008–10)

Founded by Dame Cecily Saunders, St Christopher's has been caring for people in the final stage of their lives since 1967. The charity is a pioneer in the arena of palliative care and the first to combine pain and symptom control with emotional, spiritual and practical support. The hospice cares for around 2,000 people a year, including around 850 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 7,000 health professionals annually.

### THE LONDON MUSIC CENTRE – SOUTHWARK
### 3-YEAR FUNDING (2009–11)

The London Music Centre was founded 18 years ago with its centre in Islington, and opened a centre in Southwark in 2010. Its philosophy is that children and young people who sing go on to learn instruments more quickly and play them more musically. The children are encouraged to sing and play music in many different styles and genres, from 14th century canons to MC and rap and from opera to rock and music from around the world. Classes are open to all and are offered for a minimal charge or for free.

### 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 44,000 people across the UK who had been resigned to long-term unemployment and welfare dependency. They operate a range of programmes ranging from their Working It Out programme, which helps excluded young people from deprived neighbourhoods into jobs, to The Junction, a unique residential community that provides intensive support for men aged over 21 who face serious barriers to employment, including ex-prisoners and ex-armed forces personnel.

### VICTIM SUPPORT
### 2-YEAR FUNDING (2009–10)

Victim Support in Southwark was set up as an independent charity in 1983 to work with victims and witnesses of crime across the borough. Staff and volunteers are trained to contact people affected by crime to offer free, confidential support and practical advice. People are referred to the charity by the police and agencies or they make direct contact themselves for help. This extends to families and friends of those who have been affected by crime and witnesses who are called to give evidence.

### VITALISE
### 3-YEAR FUNDING (2009–11)

Vitalise has been operating since 1963 and provides an alternative to traditional residential respite care. Each Vitalise holiday centre offers short breaks in a relaxed, holiday-style environment with a variety of trips and activities. Guests, who include disabled and elderly people who require a high level of care, are supported by volunteers who provide companionship and assistance.

### XLP
### 5-YEAR FUNDING (2008–12)

XLP is a charity dedicated to tackling social violence, poverty and educational failure among young people across seven of London's most deprived boroughs including Southwark. 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 include running a homework club on a bus which visits London estates and COACH, a community mentoring scheme.

## CORPORATE SOCIAL RESPONSIBILITY

# COOKING UP A STORM IN SOUTHWARK

**Encouraging a teenager to join the boxing team instead of a street gang. Advising a school leaver on how to find a job in the middle of a recession. Teaching a group of children how to cook a healthy meal. These are just some of the many ways that the Downside Fisher Youth Club is helping Southwark's youngsters to develop skills and self-confidence and fulfil their potential.**

**Today's Southwark is very different from the one that existed when the charity was started over 100 years ago, but it remains one of the UK's poorest boroughs and there is still a very real need for Downside Fisher's work supporting disadvantaged young people in the area.**

### THE EARLY DAYS

The Club was set up in 1908 by Father Stephen Rawlinson together with a group of alumni from Downside School. The founding mission of the Club was to give disadvantaged children an environment where they could congregate, learn from each other, challenge themselves and develop skills that would help them take the critical first steps to becoming capable and confident adults.

Boxing was a big focus in the early days. Having produced three world champions in its history, it continues to be one of the things Downside Fisher is best known for, but the list of activities the Club offers has grown substantially over the years. Alongside the boxing, there are other sports including football and tennis, plus everything from dance clubs to employment workshops to cooking classes.

### GROWING ALL THE TIME

With 1,700 young people using the Club regularly, and over 400 new members in the last year, all of the activities are well-subscribed. Although it caters to members from the ages of 9–25, most are aged 11–18 years, and they come from a wide range of social and ethnic backgrounds. Some come along simply to socialise, some to spar in the gym or play pool, while others enrol in classes so they can work towards formal qualifications.

The Club moved to its current premises – less than a mile from Terra Firma's offices – in 1974, and the building was refurbished in 2008 following a partnership with another charity. It was a critical time in the charity's history. With a track record of supporting similar causes in the local area, Terra Firma was impressed by Downside Fisher's ability to inspire the local children with its array of activities and was keen to get involved. Starting in 2009, the company has pledged several years' funding to support the work of the Club.

### CAN COOK, WILL COOK

Half of Terra Firma's annual funding contribution is used to support Downside Fisher's hugely popular cookery programme. Inspired by the government's anti-obesity agenda, the cookery programme was trialled in 2008 and is now a firm fixture on the Club's timetable. With media figures like Jamie Oliver campaigning for healthy eating for young people and bringing cooking to younger audiences, it seems that the kitchen has become a cool place to be and Downside Fisher is making the most of this.

The programme gives 10- to 19-year-olds the opportunity to learn not just about a healthy diet, but how they can cook healthy, nutritious meals, and is run by an experienced nutritionist and dietician.

Everyone who takes part in the nine two-hour sessions receives a certificate of achievement at the end of the course. One of the highlights of the course is when the youngsters get the chance to show off their skills by cooking for their families.

## There is a very real need for Downside Fisher's work supporting young people in the Southwark area

Members of the Downside Fisher Club at work in the kitchen

### PROMOTING VOLUNTEERING AMONG YOUNG PEOPLE

Most of the remainder of Terra Firma's annual donation goes towards an initiative called Volunteer Horizons. This programme is aimed at 16- to 25-year-olds – the age group that is currently finding it extremely difficult to find work or a college place after school – and it encourages them to develop their skills through volunteering. By helping to run various activities at Downside Fisher, the youngsters are gaining accredited training in areas that interest them such as first aid, swimming, fitness, youth work and food hygiene. It gives them valuable responsibility and experience, and it is enabling Downside Fisher to build up a roster of qualified volunteer activity leaders.

Terra Firma's contribution helps to pay for a Volunteer Manager and other related costs, and as an added bonus, the money is matched by 'V', an external funding organisation that has been set up with government support to develop volunteering among young people.

### SHARING SKILLS

At the moment, Terra Firma's involvement is purely financial; however, the company is working closely with the Club on ways in which it can use its wider skills to contribute to both day-to-day operations and long-term strategy.

"Terra Firma's model of having one point of contact has made it easy for us to build what we hope is a symbiotic relationship," one of the Trustees explains. "They give freely without using us to promote themselves. We would welcome their commercial skills in assisting us to run our club more effectively and we hope that this will become a true long-term relationship."

In the meantime, Terra Firma is delighted to be supporting the great work that goes on every day at Downside Fisher and to be playing a small part in helping youngsters to get involved in whatever inspires them, from boxing to baking.

# CORPORATE GOVERNANCE

## Terra Firma has a highly effective corporate governance framework

### FRAMEWORK

TFCPL, TFCML and terrafirma GmbH have highly effective corporate governance frameworks. 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.

### TFCPL
### THE BOARDS OF DIRECTORS

TFCPL is managed and controlled in the UK. It has a board of UK-based directors comprising three Executive Directors – Tim Pryce, Robbie Barr and Chris Barnes, and one Non-Executive Director – Deborah Pluck.

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 anti-money laundering and compliance reports, and appointment of members of sub-committees of the Board. These include the Investment Review Committee, the Remuneration Committee and the Portfolio Finance Committee.

William Burnand is Company Secretary and is a qualified solicitor in England and Wales.

William qualified in 1994 and trained at Slaughter and May for seven years, in London and New York, before moving to Nomura International plc in 2000 where he worked for its Principal Finance Group. William joined Terra Firma in 2002 when it spun out from Nomura.


Sami Kassam


Anne Sheedy, Chris Barnes

## INVESTMENT REVIEW COMMITTEE

The Investment Review Committee (IRC) consists of Tim Pryce, Robbie Barr and Chris Barnes. The IRC meets weekly or more often if business activity requires. Its role is to review all potential transactions that are due to be proposed to the fund managers in Guernsey. These transactions include, among other things, potential new investments, refinancings or disposals, as well as follow-on financing for the portfolio businesses and post-investment appraisals.

The members of the IRC have the specialist skills to support the transaction teams. The fact that the IRC members are not members of any particular transaction team increases the objectivity which the IRC brings to its role.

## REMUNERATION COMMITTEE

The Remuneration Committee consists of Tim Pryce, Robbie Barr and Mel Willsmore (Head of Human Resources) and meets as required. It is responsible for all compensation and benefits issues, including Terra Firma's broad policies and principles in this regard and the individual remuneration packages for all TFCPL employees.

## PORTFOLIO FINANCE COMMITTEE

The Portfolio Finance Committee (PFC) consists of Robbie Barr, Mike Kinski, Lorenzo Levi, Pat O'Driscoll and Nils Steinmeyer. The PFC usually meets on a monthly basis and its role includes the review of the performance of Terra Firma's portfolio businesses and the determination of the strategic initiatives to be pursued by them. The PFC is a forum for the relevant Terra Firma team to raise any opportunities, issues and concerns relating to the portfolio businesses. This allows appropriate resources to be deployed and critical decisions to be made in a timely and focused manner.

## CORPORATE GOVERNANCE


Peter Cornell, Guy Hands


Nigel Carey, John Stares, Peter Bruges

**The processes in place enable the business to develop flexibly and securely**

## TFCML

TFCML has a board of Guernsey-based directors comprising three Executive Directors – Guy Hands, Peter Cornell and Peter Bruges and three Non-Executive Directors – John Loveridge, John Stares and Nigel Carey.

John Loveridge was a Managing Director and Principal Shareholder of Redbridge Offshore Limited which was sold in 2002 to Mourant, the Jersey legal and specialist administration firm where he remained as Managing Director until 2003. From 1996–1999, he was a Principal and Managing Director of Bridgewater Administration which was subsequently sold to Royal Bank of Canada in 1999. He previously held senior positions with Guernsey International Fund Managers (Barings) and was Managing Director of Butterfield Fund Managers in both Guernsey and in Grand Cayman.

John has extensive experience in the management and administration of a wide range of institutional, private equity and fund of funds' investment vehicles for a worldwide client base. He currently sits on the offshore boards of the Terra Firma funds' General Partners and underlying corporate structures of several major investment groups worldwide.

Nigel Carey is a prominent advocate in Guernsey. He qualified in 1974 and was called to the Guernsey Bar in 1975 (partner in Carey Langlois, 1977, and in Carey Olsen, 2003) and has been a consultant to Carey Olsen since 2008. Nigel is a former chairman of the Guernsey Bar Council and a former Commissioner of the Guernsey Financial Services Commission. He serves as a director of many Guernsey-based mutual fund companies and investment companies.

John Stares has been a resident of Guernsey for the past nine years, during which time he has taken on a carefully selected set of part-time roles including Managing Director of the Guernsey Enterprise Agency, Non-Executive Director to four Channel Island-headquartered businesses, developer of his own business/charitable interests and leadership roles with two local service and professional organisations.

Before joining Accenture, John worked for three years with KPMG, during which time he qualified as a chartered accountant, and for two years with Lucas Industries working in information technology. Prior to moving to Guernsey, John spent 23 years with Accenture as strategic, financial, change & IT consultant, 15 years of which he spent as a Partner. He also held a wide variety of leadership roles in Canadian, German, French, European and global consulting practices.

## TERRAFIRMA GMBH

The Geschäftsführer of terrafirma GmbH is Arjan Breure and the Prokurist is Chris Barnes.

## CONFLICTS OF INTEREST

Terra Firma 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 other things, business or other activities outside TFCPL, entertainment and gifts, personal account dealing and directorships in the portfolio businesses.

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 a conflict arising.

# GENERAL ACCOUNTABILITY

## AUTHORISED STATUS

TFCPL is authorised and regulated by the UK FSA to provide investment advice to, and arrange deals for, the Terra Firma funds. TFCML is licensed by the Guernsey Financial Services Commission. terrafirma GmbH is mandated to provide TFCPL with investment advice in relation to investment and divestment opportunities in Germany and other countries which TFCPL nominates from time to time. terrafirma GmbH is not required to be regulated.

## COMPLIANCE OFFICERS

David Sanders is the Compliance Officer of TFCPL. The Compliance Officer's function is to, among other things, ensure that the UK-based directors and employees of TFCPL 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.

State Street Global Services is the Compliance Officer of TFCML. The Compliance Officer's function is to ensure that the Guernsey-based directors and employees of TFCML comply with the rules of the Guernsey Financial Services Commission and other relevant local legislation.

There is no requirement for terrafirma GmbH to have a Compliance Officer.

## FINANCIAL STATEMENTS

TFCPL prepares annual audited financial statements. These accounts, which are prepared following UK company law, give a true and fair view of the state of affairs of TFCPL and its subsidiary, terrafirma GmbH. 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 of TFCPL are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of TFCPL and enable them to ensure that the financial statements comply with the Companies Act 2006. 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.

TFCML prepares annual audited financial statements. These accounts are prepared following the Companies (Guernsey) Law, 2008 to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. TFCML's year-end is March and its auditor is Deloitte.

The TFCML directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of TFCML and enable them to ensure that the financial statements comply with the Companies (Guernsey) Law, 2008. They are also responsible for safeguarding the assets of TFCML and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

terrafirma GmbH prepares annual audited financial statements, its year-end is March and its auditor is Deloitte.

## CONTINGENCIES – LITIGATION

TFCPL, TFCML and terrafirma GmbH are not currently involved in, and have no knowledge of, any threatened litigation involving any of them which would have a material adverse impact on their results, operations or financial condition.

## OWNERSHIP

Guy Hands is the ultimate beneficial owner of the share capital of TFCPL and its wholly-owned subsidiary terrafirma GmbH.

The ultimate beneficial owners of the share capital of TFCML are discretionary trusts of which Guy Hands and his family are amongst the beneficiaries.

# SENIOR PERSONNEL REMUNERATION

## REMUNERATION POLICY

The remuneration of our Senior Personnel is designed to attract, motivate and retain staff of the highest calibre. A high quality senior team is essential to maintaining our position as one of the leading contrarian private equity firms.

## REMUNERATION PACKAGE

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

## ANNUAL SALARY

For 2010, the total cash compensation paid to Senior Personnel was £11,866,407 and the average for these 16 individuals was £742,900. Salaries are reviewed annually and are set in relation to an individual's performance and market comparator groups. Senior Personnel are not eligible for discretionary 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 Senior Personnel are eligible to join one of the company's medical insurance schemes. Each respective employer pays the premium and the respective employee pays tax at source for this benefit via the monthly payroll.

### Permanent Health Insurance

All Senior Personnel are eligible to join one of the company's permanent health insurance schemes. These policies provide up to 75% of pre-disability income once an individual exceeds six months' continuous sickness absence, subject to a maximum payment of £250,000 per annum.

### Pension Arrangements

Senior Personnel are all eligible to be members of a company personal pension scheme. A range of benefits are provided in the event of death whilst employed by the company:

(i) a lump sum payment up to four times basic annual salary at the date of death
(ii) a pension will be provided to an individual's spouse, civil partner or dependants at the date of death, equivalent to 25% of Final Pensionable earnings, together with pensions for each of up to four children under the age of 18 (or 23 if in full-time education) equivalent to 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 his or her dependants.

## SENIOR PERSONNEL CONTRACTS

It is the company's policy that Senior Personnel have contracts with an indefinite term which provide for a minimum of three 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 Personnel 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 – in each case for a period of at least three months following the termination of their employment.

## ALIGNMENT OF INTEREST

Simon Palethorpe

As well as investing capital on behalf of others, Terra Firma and its team have committed more than €520 million to the Terra Firma funds. As one of the largest investors, Terra Firma prospers along with its investors by developing and growing successful businesses.

This alignment of interest is fundamental to the way Terra Firma operates. 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 been repaid their investment and received 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 have historically existed in public companies and investment banks.

Robin Boehringer

**Alignment of interest is fundamental to the way Terra Firma operates**

# RISKS AND UNCERTAINTIES[1]

## RISKS AND UNCERTAINTIES

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

## RISK MANAGEMENT

In reaching their decisions, the Terra Firma fund managers take into account the advice of the Terra Firma advisers as well as the fund managers' strategy and 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 Terra Firma fund managers bring objective discipline to the review of each investment opportunity. The ongoing dialogue between the Terra Firma fund managers 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 transaction team.

The advice that the Terra Firma advisers provide 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 their view, the Terra Firma advisers constantly review advice from economic,
political, legal, financial, tax and accounting advisory firms.

Terra Firma is advised by an array of distinguished professionals from the realms of international politics, economics and business. 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.

## CORPORATE RISK

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

### Liquidity Risk

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

### Leverage Risk

Terra Firma has no current borrowings.

### Interest Rate Risk

Terra Firma 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.

TFCML has no currency risk.

### Competitor Risk

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

### Key Man Risk

The operations of Terra Firma are highly dependent on a small number of senior personnel, including Guy Hands, being able to perform their roles. Terra Firma 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.

[1] The risks outlined here represent those faced by Terra Firma. 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.

# 4 Terra Firma's Funds – TFCP II, TFCPIII, TFDA

# TERRA FIRMA FUNDS

## AGGREGATED FUND FINANCIAL STATEMENTS

| BALANCE SHEET | Note | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|---|
| **FIXED ASSETS** | | | |
| Investments | 3(b), 6 | 4,230,711 | 5,106,831 |
| | | | |
| **CURRENT ASSETS** | | | |
| Cash at bank | | 79,880 | 60,193 |
| Accounts receivable | 7 | 32,762 | 4,374 |
| | | | |
| **CURRENT LIABILITIES** | | | |
| Accounts payable | 8 | 8,673 | 1,862 |
| **NET ASSETS** | | **4,334,680** | **5,169,536** |
| **PARTNERS' LOAN AND CAPITAL ACCOUNTS** | | **4,334,680** | **5,169,536** |
| Revaluation surplus/(deficit) not included in Net Assets | | 1,596,388 | (153,810) |
| **Estimated Fair Value of Net Assets** | | **5,931,068** | **5,015,726** |

| PROFIT AND LOSS STATEMENT | Note | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|---|
| **INCOME AND EXPENDITURE** | | | |
| Bank interest | 3(d) | 311 | 4,982 |
| Realisation of investment | | 25,861 | – |
| Foreign exchange gain | 3(e) | – | 74 |
| Interest on investments | 3(d) | 25,553 | – |
| Realised gain on investments | | 5,900 | – |
| Equalisation adjustment | | – | (248) |
| Partnership expenses | | (36,515) | (12,811) |
| Foreign exchange loss | 3(e) | (596) | (25) |
| Auditor's remuneration | | (229) | (175) |
| Bank charges | | (22) | (13) |
| **Net Income** | | **20,263** | **(8,216)** |
| Provision for impairment | 3(b) | (1,133,641) | (255,649) |
| **NET RESULT FOR THE YEAR** | | **(1,113,378)** | **(263,865)** |

| CASH FLOW STATEMENT | Note | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|---|
| **RECONCILIATION OF NET RESULT TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES** | | | |
| Net result for the financial year | | (1,113,378) | (263,865) |
| Add back impairment loss on investments | | 1,133,641 | 255,649 |
| Equalisation adjustment | | – | 248 |
| Decrease in receivables | | 1,310 | 131 |
| Increase in payables | | 6,810 | 359 |
| Deduct realisation of investment | | (25,861) | – |
| Deduct realised gain on investments | | (5,900) | – |
| Deduct interest on investments | | (25,553) | – |
| **Net Cash Outflow from Operating Activities** | | **(28,931)** | **(7,478)** |
| | | | |
| **CAPITAL EXPENDITURE AND FINANCIAL IINVESTMENT** | | | |
| Purchase of fixed asset investments | | (373,521) | (762,290) |
| Proceeds from sale of investments | | 144,836 | – |
| **Net Cash Outflow from Investment Activities** | | **(228,685)** | **(762,290)** |
| | | | |
| **FINANCING** | | | |
| Drawdowns on Partners' commitments | | 487,705 | 873,274 |
| Repayment of Partners' commitments | | (113,015) | – |
| Return of Special Limited Partners' distribution held in escrow | | – | 73,710 |
| Advance of General Partners' share | | (94,323) | (97,671) |
| Gross distributions during the year | | (3,069) | (78,340) |
| **Net Cash Inflow from Financing Activities** | | **277,298** | **770,973** |
| | | | |
| Foreign exchange impact | 3(e) | 3 | 9 |
| **NET INCREASE IN CASH** | | **19,685** | **1,214** |

# 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 |
| TFCP III Co-Investment B LP # | 2 July 2009 | Terra Firma Investments (GP) 3 Ltd |
| TFCP III Co-Investment 2A LP # | 24 May 2010 | Terra Firma Investments (GP) 3 Ltd |
| TFCP III Co-Investment C LP # | 19 November 2010 | 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 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 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 profit share equal to the lesser of 0.001 per cent of Partnership Profits and €1,000 (£1,000 in the case of TFCP II Co-Investment 1 LP).

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.

| | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|
| Advance of General Partners' share at 1 January | 343,906 | 246,235 |
| General Partners' shares for the year | 94,323 | 97,671 |
| **TOTAL** | **438,229** | **343,906** |

# NOTES TO THE 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

Investments are carried at cost less any provision for impairment. When there is an indication of impairment, the General Partner conducts an impairment review of the investment based on whether current or future events and circumstances suggest that the recoverable amount may be less than the carrying value. This review includes techniques such as analysing cash flows, discounted using the market rate of return for similar assets.

In accordance with the Limited Partnership Agreements, investments in subsidiaries and associates are held as part of an investment portfolio with a view to the ultimate realisation of capital gains and hence fully consolidated financial statements are not prepared nor are associates equity-accounted.

### (c) Fair Value

The General Partner has determined the fair value of all investments in accordance with the IPEV Guidelines and these are disclosed in aggregate in Note 6 to the accounts.

### (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 rates achieved in the transaction. The assets and liabilities of TFCP II Co-Investment 1 LP have been translated into euros at the reporting date.

## 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 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 Partnerships.

| 6. INVESTMENTS | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|
| **EQUITY AND EQUITY-RELATED INSTRUMENTS:** | | |
| As at 1 January | 5,106,831 | 4,741,855 |
| Additions during the year | 373,521 | 619,076 |
| Disposals during the year | (116,583) | – |
| Equalisation adjustment | – | 222 |
| Provision for impairment of investments | (1,133,641) | (255,649) |
| Foreign exchange impact | 583 | 1,327 |
| **COST OF INVESTMENTS AT 31 DECEMBER** | **4,230,711** | **5,106,831** |
| | | |
| **ESTIMATE OF FAIR VALUE** | **5,827,100** | **4,953,020** |

| 7. ACCOUNTS RECEIVABLE | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|
| Drawdowns receivable | 2,848 | 2,212 |
| Divestment proceeds receivable | 29,061 | – |
| Recoverable costs receivable | 853 | 2,162 |
| | **32,762** | **4,374** |

| 8. ACCOUNTS PAYABLE | Aggregate 2010 €'000 | Aggregate 2009 €'000 |
|---|---|---|
| Accrued expenses | 1,232 | 517 |
| Other creditor | 7,441 | 1,343 |
| | **8,673** | **1,862** |

# NOTES TO THE ACCOUNTS

## 9. 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 some 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 of 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, sterling and Australian dollars 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 arising from changes in interest rates. As at year-end, none of the Partnerships had loans outstanding.

### 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 the 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
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Peter Cornell
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John Loveridge
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