3i Group
Capital Markets Seminar
17 September 2018

Introduction and Welcome

Simon Borrows

Chief Executive Officer

Introduction

Good afternoon everyone. Welcome to another 3i capital markets seminar. We are going to focus on three companies today: Audley, the UK travel business; Cirtec, one of our US healthcare companies; and Lampenwelt, a German company, which is our first pure online retailer. At the end, I will also give you a brief update on Action.

Slide 3: Our business model – delivering sustainable returns

I don't think I need to remind many of you of our business model, but since restructuring in 2012 our aim in Private Equity is to invest up to £750 million per annum across four to seven companies, with a view to doubling their earnings over a four to five-year period.

Slide 4: Strategic clarity and focus in our approach to Private Equity investing

Over the last five years, we have focused on three sectors: Consumer, Industrial, and Business and Technology Services, but earlier this year, we decided to break out our Healthcare activity into a separate sector. We have focused on companies that are likely to benefit from a megatrend, i.e. have a good market backdrop. Importantly, we have the flexibility, given our model and experience, to refine and change our focus over time.

Slide 5: Flexible approach to follow developing themes and megatrends

This slide illustrates some of the themes we have been focusing on, as well as highlighting today's companies, and those we covered last September.

The focus today is around demographics, healthcare and the power of digital in the retail sector.

Slide 6: Our approach to Private Equity investing is producing good results

Of course, we aim to buy well in these strongly growing themes but, over time, it is our active management and investment experience that adds significant value during our ownership. As mentioned in May, our 2013 to 2016 vintage is already valued in excess of two times cost, with considerable value growth still to come. Now the value in our 2016 to 2019 vintage is beginning to accelerate and Cirtec and Lampenwelt are a part of this.

Slide 7: Today's seminar

Here are the basic facts behind today's investments. I would now like to introduce the 3i private equity executives who will be presenting each case.

Slide 8: Today's presenters

Alan Giddins, on my left, who is the managing partner of our Private Equity team and in our UK team, will talk you through Audley. Rich Relyea, in the middle, who you met last year, is co-head of our New York team and head of our Healthcare sector. He will take you through Cirtec. Last but not least is Peter Wirtz, who co-heads our German team. He was very busy earlier this year with our Scandlines transaction, and he will be taking you through Lampenwelt. There will be time for questions after each presentation. I will now hand over to Alan.

Audley Travel

Alan Giddins

Managing Partner, Head of Private Equity

Slide 10: 3i in the UK

Thank you, Simon. I am very pleased to talk to you about Audley, not least because there are a huge number of potential clients in this room. Before I do that, I will give you a bit of context on our business in the UK. 3i clearly has a fantastic heritage in investing in the UK. We have 11 investment professionals based in London and I think these logos really are a good example of where we try to source deals. Marken and Element were both carve-outs from larger corporates; from Deutsche Post and from Stork. With AES and MKM, we were backing the original founders of those businesses: David Kilburn at MKM, where we made 5.9 times our money when we sold that business last year; and Chris Rea at AESSEAL. Then two deals, Civica and Mayborn, which were take-privates: Civica in 2008, Mayborn in 2006. They both delivered very good returns.

Then we have Aspen and Audley. Pete Wilson talked about Aspen last year, a business we bought from Inflexion. It is a specialist in condensation removal pumps for air conditioning units. Audley Travel had been an investment by Equistone. Both were secondary buy-outs, but I think the key thing with both of these businesses is that when we bought them they were at a point of inflection in terms of the international growth potential they had and what 3i could bring to them as a new investor.

Slide 11: Audley is a market leader in tailor-made travel in the UK and US

The key is in the strapline. This is about tailor-made travel. The business was founded in 1996 by Craig Burkinshaw and John Brewer. They actually met at university. Craig then went on to be a tour guide in Vietnam. They saw, as people were increasingly attracted to travelling to South-East Asia, an opportunity to give people a different, more tailored experience, built around excellent customer service and geographic specialisation. Their belief was that, if you could offer that, you would develop a repeat and recommend model, where your clients would keep coming back. I will talk you through the financial implications of that but, ultimately, if you get a repeat customer your cost of customer acquisition is minimal.

Here you see the map. In the dark blue, those are all the geographies that we are taking clients to. In terms of where our own staff are based, the business is headquartered in Witney, just outside Oxford. We have 330 people based there. Audley then opened an office in London in 2014. We have 250 people based in London. Also in 2014 Audley opened an office in Boston, and there are 230 people based there. As Simon said, we invested £156 million in Audley in December 2015. This business has circa £300 million turnover and has delivered in excess of 16% EBITDA organic CAGR since our investment.

Before telling you more about Audley, I am just going to play a brief video. There are three things to get out of that video. First, clearly, this is all about giving people experiences that they cannot get through normal travel. It is about understanding how the country specialists think about their clients. What are they trying to provide to their clients? Then we have three clients talking about what it is that made it a really special experience for them.

[Video shown]

Slide 12: Audley creates complex journeys tailored to each client

What are the key dynamics of the Audley business? It is personalised long-haul travel. The company is taking people to 80 different countries around the world. Audley is organising the flights, the transfers and the accommodation, but then the absolutely key bit is: what is the experience that someone can really believe is unique to their journey? The business has no inventory, so our focus is about finding the best itinerary for each client. The average booking value is about £14,000; it is slightly higher in the US. The average is six locations per trip. If you are going from the UK to Bangkok, there is limited reason to book with Audley. What you want in an Audley client is someone who wants the complexity of the experiences they are getting. The average party size is 2.5 passengers and people are typically booking about seven to eight months ahead of when they travel. As a result, you get very good revenue visibility and good cash conversion.

Slide 13: Growth in the tailor-made travel market is supported by strong underlying drivers

Why is tailor-made travel growing? There are three key reasons. People are genuinely motivated by experiences. It is then about the growing demand for personalisation of those experiences, but, underlying all of it, it is about travel. We are focused on the over-55 category, but, whether it is students travelling or it is people who have worked for two or three years travelling, the appetite for travel around the world is enormous. We are playing on that megatrend.

We see the UK market as probably about a 10%-plus growth market. It is very difficult to assess what the growth is in the US as Audley is part of creating that market. Our due diligence thesis was that the US market is probably about three times the size of the UK market. In the UK, Audley is bigger in aggregate than its next three competitors.

Slides 14 and 15: The combination of Audley's positioning and business model provides an attractive platform for growth

a. Broad product offering

Why does the model work? It really works because of six key factors. The first is the breadth of the product offering. The 80 countries are important for two reasons. First, you get macro diversification. Whereas Burma three or four years ago was one of Audley's biggest sellers, today very few people are going to Burma due to political tension. Audley is able to direct traveller demand to other locations due to its destination breadth. Also, it links into the repeat and recommend model. Someone who has been to South America this year is very unlikely to go back to South America. A typical traveller will think about their next journey and re-book within six to nine months, so, when they come back, you want the country specialist to be helping them think about the experiences that they had in South America that they want to transfer into another geography. As a result, while Audley might be competing with another supplier in South America, that party cannot take that client to another geography and continue to build that client's advocacy.

b. Passionate country specialists with destination expertise

It is about country specialists who are absolutely passionate about travel. That was right at the heart of what Craig and John created. The typical country specialist at Audley will be someone who travelled in their year off, probably worked for three or four years, then took another year off travelling. Travel really is in their genes. As the lady who was on the video was saying, Audley sends its country specialists on 400 familiarisation trips a year, each lasting for one or two weeks. If they are covering Southern India, we will send them to Kerala to go and see the hotels, to meet the ground agents, to experience some of the trips there, so that when they are talking to their client on the phone, they really can relate to what they are trying to arrange for them.

c. Affluent customer base with high expectations

We have a customer base that is relatively affluent, but it is also demanding. We have an 80%-plus 'excellent' score from people when they come back from an Audley trip.

d. High level of repeat & recommend customers

Repeat & recommend is important to Audley's model. Audley has a roughly three times better conversion rate from somebody who has already been on an Audley trip. 75% of our revenues in any one year come from repeat & recommend.

e. Revenue visibility and cash conversion

We have very attractive revenue visibility and cash conversion.

f. Continued product development

The profit and cash generation from this model enables continued development. That can be going to other source markets. It can be adding other geographies. Audley has added 10 new countries since we invested in 2015. It is really that circle that makes this such a powerful model.

Slide 16: We developed conviction early on, enabling us to acquire Audley in a process which played to our strengths

How did we come to buy Audley? The first thing was really focusing down on travel. It was probably obvious to a lot of people, five or six years ago, that travel was a growing market. The key was to understand where we wanted to invest in that market. Did we want to play in the online market? Did we want to be in traditional travel? What we found with Audley was a very unique model. We were also able to build up a very good relationship with Richard Prosser. Richard had been the buy-in executive chairman when Equistone bought the business. Through Richard, we were able to develop a very good relationship with Ian Simkins, the CEO, and the rest of the management team. We also had some good points of reference from businesses we had invested in before. Ultimately, though, it was this: management wanted a partner who genuinely had that appetite for international investment, and this created a strong fit with 3i.

Slide 17: US Market - over $100 million sales expected in 2018

The US was key to our interest in Audley. In the US, Audley had identified a market that was probably about three times bigger than the UK market. The market distribution was structured around travel agents. They are also typically focused on providing group travel. Audley had found that they were getting calls from the US into the UK, for people wanting to go to Vietnam or New Zealand. The key reason people gave them was, 'this simply is not offered in the US.' They saw the opportunity for a first mover advantage into the US market with their direct to consumer personalised model.

What has happened since 2015? Bookings have grown by 3.5 times. Audley has more than doubled its headcount. Today, the US is 25% of Audley's sales, but the other interesting thing we found is that, when Audley was set up, the thought process was that clients living in the UK would not want to travel or get someone to arrange their travel to Italy and France. What they found in the US was clients kept saying, 'Can you help us go to Italy? Can you help us go to Madrid? Can we go to Portugal?' 18 months ago, Audley started first in Italy. They have opened up six destination geographies in Europe. Today, Italy is the second biggest seller for Audley in the US. We see the US as a significant market in terms of European travel.

Slide 18: Strong growth delivered in the UK and US with attractive financial characteristics

In terms of the financials, Audley's performance is impressive. Between 2012 and 2018, it has delivered a 24% revenue CAGR. The dark blue on the chart is UK revenue, and this is departure revenue rather than bookings. Then the top, lighter blue is the US. US CAGR over the last three years has been 67%. UK CAGR has been 14%. To this, I would add:

- 100% plus cash conversion. The reason that happens is, when you book with Audley, you pay a deposit for the trip on booking. You then pay the balance of it eight weeks before you travel, then Audley pays the suppliers after you travel. It is also a business that has no inventory and limited capex.
- 16% organic EBITDA CAGR since we invested.
- The business has deleveraged from 4.6 times leverage to 1.4 times since we invested. Clearly, that is something we will look at over the next six to nine months, in terms of addressing the right capital structure for the business.

Slide 19: Ongoing digital evolution supports Audley's omnichannel model

Digital is extremely important to Audley, while remembering that this is an omnichannel model. Audley's website is award-winning and has 7.1 million unique visitors per year, up 46% since we invested. We have invested to develop our app. That is critical in terms of how we communicate with our clients before they travel, when they are travelling and when they come back. At the end of the day, all of this is about getting the client to talk to the country specialists. Audley delivers a five times better conversion rate when speaking to someone than if the client enquires online.

Slide 20: Strong management team and Board

We also acquired a very strong management team. This had been a management buy-in in 2012, led by Richard Prosser and Ian Simkins. We did feel, though, coming out of due diligence, that there were two areas we really wanted to focus more on. One was the finance function, so we brought in Nils Steinmeyer as CFO nine months after we invested in the business. He was previously CFO of Wyevale, and he has strengthened the people in the finance function, but he has driven a much more KPI-focused business. Also, coming out of our due diligence, we felt that the attrition among country specialists was probably higher than it should have been. We linked that partly to needing better training and development processes in the business. Since Jemimah came on board as HR Director, we have seen a seven percentage point reduction in attrition. Both the finance and HR functions are now capable of supporting the growth potential of the business.

Slide 21: Nick Longman joined the team on 10 September 2018, transitioning to CEO in January 2019

The other important change here is Nick Longman. He joined last week as COO and he will be stepping up to CEO on 1 January and Ian is going to step up to a non-executive role.

In terms of background on Nick, he has 20 years of experience in the travel industry, formerly as Managing Director of Tui in the UK and Ireland, a £6 billion revenue business. Nick is also able to bring a very international perspective.

Slide 22: Future value creation

Where is the value creation in this business? Underpinning it is the growth in people's appetite to travel, particularly people in the 55+ age category. It is about repeat and recommend. As the US business matures, we are starting to see those repeat and recommend KPIs coming up.

The digital evolution of the business is absolutely at its heart. It is about how we enable our country specialists to provide superior destination expertise and how we communicate with our clients digitally. Before they travel and when they travel, digital is absolutely key.

It is about new product launches, so that means going into new geographies, but it is also about ensuring that the whole time we are continually refreshing the types of experiences we can offer our clients.

Then it is looking at new source markets. Having gone into the US in 2014, we see a number of other very attractive source markets.

Audley is a fantastic business. It has excellent financial KPIs and we are very proud to be invested in it.

Questions and Answers

Participant

For the 25% of customers that are not through repeat and recommend, what are Audley's routes to market and how much would the cost of acquisition be when you are starting to open a new territory?

Alan Giddins

PPC (pay-per-click) spend is the core of the original Audley model for acquiring new customers. We are, however, increasingly looking at how we acquire new clients in the most cost-effective manner.

Participant

How cyclical have sales and profits been?

Alan Giddins

Through the recession, revenues were flat, but what was critical is that we saw an increase in the numbers of repeat clients, which are more profitable.

Participant

Is there a risk from the development of DIY travel? Do people use the Audley website, particularly as it is very informative, to then book their own holidays?

Alan Giddins

I think it depends what you are after when you are booking your holiday. DIY, in terms of booking a holiday, is incredibly easy. However, I have been on three of Audley's holidays and I think, for your Audley client, what they are after is a perfect holiday, where when they arrive at the airport the ground handler who is meeting them is there, gets them to the right hotel. All of the travel and all of the experiences that they're getting, as you picked up in that video, are different and better than you are going to get if you book it yourself. Now, you might book it yourself and get it absolutely right, but if you are going to travel around South America for three weeks you would rather get it 100% right than 85% right. The sort of person who is going on an Audley holiday is going on that holiday probably every two to three years, so it is something that they have thought about and they want to get absolutely right.

Participant

Is Audley entirely online or does it also have shops?

Alan Giddins

Audley has no shops. Essentially it has about 400 country specialists, around 120 of them in the US in Boston. Roughly half of its country specialists in the UK are in Witney and half are in London. The interaction with customers is over the phone.

Participant

Can you comment on the level of attrition now amongst your country specialists? Also, what are you seeing in respect to your competition? Have you seen any new players come into this space in the last one to two years?

Alan Giddins

I do not think that attrition among country specialists is a stat we would disclose, but I would say that Audley's attrition is probably about 10% lower than we would see in similar businesses. In terms of competition, there are always small niche players coming into the market, but the cost of acquisition of new clients is very expensive, making it hard for companies to come into the market and scale up in an economically effective way. We do see start-ups.

Participant

As a follow-up question, in terms of your addressable market, are you trying to size up the opportunity that is available overall in the US and the UK, just to have an idea of your current market share and the potential going forward?

Alan Giddins

It is a good question. It is a very tough market to currently quantify.

Participant

What are the margins of the business and what has the trend been since you invested?

Alan Giddins

We do not disclose Audley's margins, albeit they have increased during our investment period.

Participant

You mentioned leverage. It is obviously an asset-light business. Can you just take us through what sort of levels of leverage you think this business can carry or should carry? What would you do with cash if you did not re-lever? It does not sound like there are acquisitions that you could do, but I am just interested in what you do with that.

Alan Giddins

The business has delevered from 4.6 times at acquisition to 1.4 times today. We may well look at a distribution, subject to agreement with the CAA, which regulates UK travel companies.

Participant

Can you just talk about how you have incentivised the employees, how you got that attrition rate down and the work-life balance among the people in employment?

Alan Giddins

How has Audley got that attrition rate down? First, it was actually about having a much more granular view of why country specialists have been successful and why they have not and Audley refining its recruitment process to take this into account. The second thing was further improving the training. When you join, you now have three weeks of training, particularly on the systems. I think that has meant that Audley has had fewer people leaving in the first six to nine months. We have seen a significant reduction in attrition rates. In terms of incentives, people are on a commission based remuneration structure. They are receiving part of that commission when they make the booking, and they are receiving the rest of it post-departure, but critically it is dependent on the quality of the feedback the client gives.

Participant

I just wondered if I might ask a few questions on the US. I know that it currently is still loss making on an adjusted EBITDA basis, but I just wondered whether you might be able to tell us when you see it breaking even. I know that at the minute you are pushing it from a volume perspective and pushing the brand to gain scale. How long are you willing to sustain that trend and at what point does it break even?

Alan Giddins

I am pleased to say that the US business is not loss making. It is actually now profitable on a departure basis, and it is significantly profitable on a booking basis. This is up from losing around $3-3.5 million per year when we invested.

Participant

How do you see the margin profile in the US now? Do you see it approaching the UK, or should it be higher at some stage? How do you see it structurally?

Alan Giddins

I think it will take quite a long time to get the US margins to UK levels, because the repeat and recommend model has been building here for over 20 years.

Participant

Remaining with the US, in terms of the very early adoption in the market you mentioned earlier, I was just wondering whether you have seen any competitors come into the market, what the competitive landscape is today, since you entered into it.

Alan Giddins

We have two board meetings in the US every year and I ask that same question at each one. You instinctively think that, because you are growing quickly, new entrants will come into the market. In fact, we have seen no real new competition in the US.

Participant

Audley's US office is based in Boston at the minute, but what is the geographical spread within your client base amongst the US states? Is it literally anywhere and everywhere?

Alan Giddins

Audley's US consumers span across the country from coast to coast. Their client base is higher in more affluent states such as California, Massachusetts, New York and Florida.

Participant

On the volatility of the business model, are you skewed at all in revenue or profit towards any country or continent specifically? Does Audley see any volatility around global events? How do you deal with that sort of geopolitical risk across your business? Obviously, people are booking seven to eight months in advance.

Alan Giddins

We did a lot of work on geopolitical risks during our due diligence before acquiring the business. After the Paris bombings, we saw bookings stalled for two or three weeks, but then picked up quite quickly afterwards. There was a similar pattern in the UK after the Brexit referendum, when bookings flattened out for a couple of weeks, but then picked up to pre-referendum levels. Audley's customer base is reasonably resilient and the breadth of Audley's geographic offering helps to protect against geopolitical events materially impacting the business.

Participant

Just in terms of the specialism of your destination specialists, how do you deal with the mix and perhaps the obsolescence of that experience? Do they transcend lots of different markets? They might be specialists in three markets and then as their destination comes on and off, do they rotate on and off?

Alan Giddins

No, principally they are specialists in one region. If we see a geography or region is losing popularity, then yes, Audley will look to move people into other geographies, send them on familiarisation trips and actually get them embedded in the team, but you try to avoid that. Once you have real expertise in a particular geography, you do not want to lose that.

Cirtec Medical

Rich Relyea

Partner and Managing Director, North America

I. 3i's approach to Healthcare

Slide 24: 3i in North America

Good afternoon. It is a pleasure to be here. I look forward to telling you, first, about our activities in healthcare. As Simon mentioned, we are placing an increased emphasis on the sector. Then I will also talk to you about Cirtec Medical, which is our latest platform asset in this space. But for context about our US operations, my name is Richard Relyea, Partner and Co-Head of our North American business. We have nine investing professionals in the New York office, where we focus on the healthcare, industrials and business and technology services sectors primarily. We have been operating in the market for a little over 10 years and have put to work roughly £1.5 billion of equity across 10-plus platform companies and a number of add-on acquisitions.

Slide 25: Increasing our focus on Healthcare

Our focus on healthcare: why? As a starting point, healthcare offers a deep pool and a tremendous number of opportunities that are good fits for 3i's investment strategy, with good market growth, rich and fragmented submarkets that allow you the opportunity to find above-market growth, opportunities to build international leaders and sub-segments that are big enough to be narrow. An example of that would be Medical Device Outsourcing, or MDO, is a cross-section between healthcare and industrials. Overlapping layers with the business technology services space might include the pharma services, staffing, recruiting and training business models, and then in the consumer space, health and wellness. It takes advantage of core knowledge that 3i has in certain business models and depth of knowledge that we have in the healthcare space.

Importantly, we will look to continue to build on the recent momentum that we have in the sector. Over the last four years, we have invested in three additional platform acquisitions, a number of follow-ons and put to work roughly €560 million of capital during that time.

Slide 26: Global healthcare - A significant market with macro trends driving long-term growth

It goes without saying that the healthcare market is a large, global market. It has good growth overall, but I think importantly, as we look at opportunities, we look for niches within niches of large categories like pharma, like medical technologies, that will offer disproportionate growth relative to the overall market.

It is a very multinational environment and increasingly so. We look for opportunities that play to 3i's strengths, where we can take European or North American businesses, grow them across the Atlantic, increase their penetration into emerging markets, and importantly they play on secular trends: things like ageing populations, increasing prevalence of chronic diseases, cancers, cardiovascular disease, diabetes, obesity, increasing access to healthcare in emerging markets, again providing opportunities to grow disproportionately in those markets, and importantly advances in treatments driven by innovation, by technology and by increasing prevalence of data, access to data, ability to process that data and use it in the delivery of care.

Slide 27: Accelerating innovation unlocking new markets – intersection of technology and life sciences

a. Biologics

As I said, one of the core focus areas we have is where technology and innovation is hitting traditional business models. An example of that would be the biologics space, not a new trend within the pharmaceutical industry but, over the last number of years, biologics and large molecule biologics have been replacing small molecule chemical-based drugs. You see that in the number and the proportion of blockbusters that are made out of biologics rather than chemical drugs. You also see that in big pharma pipelines and in clinical trials.

The important thing for us is that a market trend like that offers the opportunity for increasing focus on derivative business models. Q Holding, for example, makes octopus assembly bioreactors for the bioprocessing space. We make aseptic connectors. We make tubes. The cost to manufacture a biologic drug relative to a chemical drug is roughly 100 times. The cost to take it to the clinical trials is significant as well. Derivative plays, businesses, products and services that play to 3i's comfort level, 3i's strength, which will have the opportunity to take advantage of those large trends in an underlying industry, without exposure to specific blockbusters, are where we try to spend our time.

b. Advanced medical device technology

Another example of that would be in the medical device technology space: areas like bioelectronics, wearables, considerable attention on the medical devices sector by traditional OEMs, increasing the technology of the product, as well as new entrants like the Googles and Apples of the world. The cross-section of technology and medical devices is giving rise to a number of new treatment categories and a number of opportunities for players, such as in the outsourced med device manufacturing space, to sell components, to sell services into those segments, many of which are new players without the historical healthcare competencies that you can bring as a knowledgeable outsource manufacturing partner, to help them bring devices to market.

c. Genomics

Another compelling area is genomics. With the cost of mapping the human genome down dramatically and the rise of gene editing technologies such as CRISPR/Cas9, there is a lot of attention on the genomic space and what it could mean for treatment in the long term. There are bioethics concerns and considerations, but several developments over the last couple of years give a little bit of an insight into what this area has as potential for the market.

For example, in 2015 two infant girls in the UK who had Leukemia were given gene edited cells as a last resort after having gone through the traditional pathways. This eliminated their Leukemia and both children are alive today with no signs of regression. There is a similar story with SMA, a devastating killer of infants, in North America, where a trial was run two years ago. All the children who participated in that study are now alive. Many of them are not just alive but they are actively participating as though they have never had the condition: walking, talking, and playing actively. These are amazing indications of what genomics can do.

Similar to the other areas, there are opportunities for us to play the service model and derivative products that will help enable these types of therapies to come to market.

d. Artificial intelligence

Needless to say, artificial intelligence across the board is going to have an influence on the healthcare industry.

Slide 28: How are we currently capitalising?

How are we capitalising on these trends within 3i? Importantly, within these major markets we are not looking to be investors across the board. We are very focused on clear and defined niches. We like to say we aspire to be an inch wide and a mile deep, in a very limited number of target sub-sectors, ones with attractive characteristics that play to 3i's strengths. Areas like pharma services, bioprocessing products, MDO, diagnostics, research tools and health and wellness are business models that have attractive and clear revenue characteristics. These areas are driven by strong, long-term trends for sustainable growth, sticky revenue base and defensive characteristics. Importantly they avoid some of the risks that we tend not to try to get exposed to: limited direct reimbursement risk, single product and single technology risk, local regulatory or local consumer behaviour patterns. These are derivative plays and a defined set of markets that we will be focusing on within the healthcare sector in 3i.

Slide 29: 3i focus area - Outsourced medical device manufacturing

To dig into one of those, which is relevant to Cirtec, the outsourced medical device manufacturing space is, essentially, what we just described. You have a med-tech market growing at roughly 5% globally. Outsourcing is driving growth at a faster rate for those players who are able to help OEMs bring technologies to market faster and manage their supply chain more effectively. There is high single digits and low double digits growth across the board for the outsourced manufacturing space and a highly fragmented market with a number of add-on acquisition opportunities for consolidation and to vertically integrate to provide more value to customers. As a result, you end up with an attractive financial profile, high cash flows and good growth.

We have two platforms in the sector right now: Q Holding, which we discussed last year; and Cirtec Medical, which we will talk about in a moment. Importantly, within 3i, we have a defined investment thesis in this space. Deploying it across both Q Holding and Cirtec, our objective is to target fast-growing therapeutic categories with underlying tailwinds in the markets and volume increases in the devices that you are serving; focus on high-value competencies, avoiding commodity segments; focus on high-end, complicated materials like silicone, like nitinol; bring value add and focus on complex device categories where you can be a sticky long-term supplier to your customers; vertically integrate, so you can control more of your supply chain, have faster turnaround for your customers, a safer supply chain and better reliability; and importantly establish an international presence.

The market itself is growing internationally and that could be into the mature markets, where you are closer to your customers' development centres, such as Europe for Cirtec over the last year, or that could be in low-cost areas, such as, in Q's case, the Indian cardiovascular market. I will mention a couple of those that will then relate to Cirtec as we get along.

II. Cirtec

Slide 31: Cirtec – Leading provider of outsourced medical devices

What does Cirtec do? Cirtec focuses on complex Class II and Class III medical devices. The principal market exposures for Cirtec today are active implantables and, in particular, neuro stimulation, implantable drug delivery and certain other areas like leadless pacing. Cirtc also focuses on minimally invasive interventional therapies that leverage the metals and material science capabilities that Cirtec has; nitinol-based components and systems; other niche minimally invasive devices; neurovascular, whether that be coils or stents. They are high-end, very targeted categories that are at the upper end of the growth spectrum in their respective device categories. We invested in the business in August 2017, so we are roughly one year into our hold. In November 2017, we made a further investment to support our acquisition platform. At that time, we closed the transaction with Vascotube and have completed a total of three acquisitions to date. One of the others being at the time of our original acquisition, and the last being an IP acquisition that closed in the last month.

Slide 32: What we like about Cirtec

What do we like about Cirtec? This plays very much to the theme of what we like in outsourced medical device manufacturing: a strong base of industry growth, particularly good growth within the device categories that Cirtec serves, and we will talk a little bit more about that in a moment; differentiated solutions in the complexity of what they do, but also in the full sweep of what they are able to provide for their customers; platform for additional acquisitions, where we have been able to buy in everything from subcomponent suppliers to adjacent product categories à la Vascotube, getting us into structural heart, getting us into deeper minimally invasive categories; and an attractive financial profile that fits that: historically good growth; outlook for continued good growth; and a lot of that being very transparent through the pipeline of engineering projects that are moving into production right now. We were able to diligence, when we did our original acquisition, at the device platform level, the growth outlook and took good comfort that it would continue to drive strong growth.

Slide 33: Cirtec is exposed to some of the fastest growing, niche therapeutic areas of the medical device market

To give a bit of perspective on why we are excited about the end markets Cirtec is exposed to, the total med device market is growing at circa 5% globally. The chart also shows the categories that represent the vast majority of Cirtec's revenue today. Neuromodulation and structural heart are the largest two categories from a profitability standpoint, and the largest two categories in the pipeline. They will drive much of the growth of the business going forward. Cirtec is exposed to several of the hottest medical technologies in the industry. We look at a lot of MDO players and I can say we do not see many that have the focus and the concentration of high-quality, high-end, high-growth device categories that Cirtec has. The weighted average across all of its end markets in terms of its customers' volume growth is roughly 11%.

Slide 34: Consolidated pro forma financials – strong growth trajectory since 2013

This has translated into strong historical financial performance, where over the last five years Cirtec has grown at a compound growth rate of 13%. Over that time, it has rationalised certain product lines out in order to concentrate its efforts on that core, active implantable, neurostimulation minimally invasive, structural heart set of markets. Having performed that rationalisation, it has also been able to move into appropriate profitability levels, corresponding with the complexity and the growth of those devices, and so has grown its earnings at a faster rate.

Slide 35: Visibility into sustained organic growth

Looking forward, the two major foundations for growth, which we think can continue at a similar rate to what we have seen historically, are the existing platforms that they are serving and new programs won recently. The existing platforms are anticipating volume growth of roughly 10% per year. Again, the transition of active engineering programmes and even multi-year programmes mean you get a good deal of visibility going forward, with active engineering programmes moving into large-scale production programmes. Complementing that is, over the last 12 months, a number of a very significant new platform wins. When we look forward, we believe Cirtec is well positioned to continue the kind of growth that it has seen in the last number of years.

Slide 36: Neuromodulation overview

Stepping back, I will just give you a bit of perspective on what neuromodulation is. At its basic, neuromodulation involves implanting in the body an implantable pulse generator (IPG), about the size of a tic-tac box, with leads that come off the IPG that are placed by the surgeon against a nerve, for example, on the spinal cord. The IPG sends an electrical stimulation into the body that elicits a natural response. One of the major categories historically has been spinal cord stimulation for pain. Patients who have gone through traditional pain pathways, rehab, surgery, even pharmaceutical treatments, but have not been able to address what is an extreme, high-acuity, level of pain have experienced incredible results with neurostimulation. Importantly, at a time when people are particularly concerned, and appropriately so, about opioids, neurostimulation is a non-opioid and non-addictive therapy.

As for the potential market size, the market today is very small relative to the number of prospective patients for whom neurostimulation may apply. Innovations like shrinking the IPG size and being able to non-invasively insert the device, so in an outpatient surgery, have the potential to expand the market penetration significantly. Even today, it is a $2.5 billion market that is growing at roughly 10% to 15% per annum. Importantly, with innovations in the technology and increasingly sophisticated knowledge of how to apply it, the number of indications that are being addressed with neurostimulation is increasing significantly.

Any neurological disease, theoretically, is open for exploration with a technology like neurostimulation. Another in-market example is sleep apnoea. Other companies are addressing indications like migraine, Parkinson’s, obesity, ADHD and epilepsy. There are roughly 60-plus indications for different therapies in the market today, in various forms of either commercial, clinical or research application. Cirtec is working with a number of those companies.

Slide 37: Vascotube, a leading provider of precision engineered nitinol tubes

Why are we excited about Vascotube? Vascotube is a transformative acquisition for Cirtec for a number of reasons. Number one: it expanded our capabilities into nitinol. I will touch on what that means in a moment. It gave us a European footprint and significantly expanded our minimally invasive franchise, and gave us the opportunity to work with a principal materials supplier and combine that with the processing capabilities that Cirtec has. We can now offer, in minimally invasive and nitinol-based devices, a more comprehensive offering to the market than exists today.

What is nitinol? Nitinol is a nickel-titanium alloy. Vascotube makes the highest-end nitinol tubes. Nitinol is interesting for a couple of reasons. First, it is inert, so it can be used in implantables. Secondly, it has super elasticity. As a metal, it is 10 to 30 times more elastic than other traditional metals. Thirdly, it has shape memory capabilities, which means one can cut a stent or a valve out of nitinol that can be very flexible and, because it is heat-set to maintain its structure at a certain temperature, when implanted in the body it will always return to its original designed shape. In areas of the body where we require flexibility or where there is motion, it works very effectively as the scaffold for a stent or a valve.

Why is that interesting? Vascotube is the leading player in the space, with the highest quality, widest diameters, and tightest tolerances. As a result, it is a very good material for structural heart devices. That includes transcatheter aortic heart valves (TAVR) and mitral valve replacement devices. I will touch on why we think that is so compelling in a moment. It also gives us a great entry point into neurovascular stenting, peripheral stenting and a couple of others.

Slide 38: TAVR and TMVR market opportunity

Similar to neurostimulation, TAVR is one of the most exciting medical device innovations and one of the hottest areas of medical devices today. The procedure, fundamentally, is a replacement for open-heart surgery. With a TAVR procedure, a surgeon is able to make a small incision and, with guide wire or catheter, deliver a replacement valve into the aortic valve of the heart and soon be into the mitral valve of the heart, and is able to make that a two-day recovery procedure. Versus the historical standard surgical procedure, which involves cracking open the chest cavity and performing open-heart surgery, there are fewer complications and recovery times are significantly shorter, resulting in better patient outcomes and lower cost to the system.

The first TAVR device was approved by the FDA in 2011 and it is today a $3–3.5 billion market, with only two FDA approved devices out on the market. A number are coming in through clinical trials, and the market is growing at a high-teens growth rate. When mitral valve devices make their way through the FDA and European regulatory bodies, the belief is that the transcatheter mitral valve replacement market could be as large as the aortic valve replacement market and possibly larger. Given the concentration that Vascotube has as a tubing supplier to this market, it is a compelling derivative play on what is one of the most interesting areas of med-tech.

Slide 39: 3i and Cirtec

Hopefully, this gives a little bit of a sense for why we are excited about Cirtec. It leverages very well our sector knowledge and focus on MDO, gives us great exposure to a number of the hottest technologies in medical devices, and is diverse across blue-chip OEMs and emerging innovators. We have been able to use our international resource base to transform the business in the first year. We are also building a Costa Rica facility to give it a low cost footprint and significant growth. We have very high aspirations for the business and will look to continue to fund both organic growth as necessary and M&A over the next number of years.

I think, importantly, the way that we won it is reflective of what we are trying to do our inch-wide, mile-deep approach. We knew the CEO for a number of years before it came to market and had strong confidence in him. We were able to validate the thesis before it came to market and, in what was a limited but still a very competitive process for a high-end asset, we were able to move decisively and quickly.

We had a similar fact pattern in Vascotube, the only distinction being that, in that case, our international network German colleagues were particularly relevant, because Vascotube was owned by three German entrepreneurs. That local connectivity was very important, as was the knowledge of the business, the knowledge of the markets and the strategic value that Cirtec would bring to the table. In that case, we won it in a limited process as well, and were the only strategic in the process. Today, Vascotube represents the kind of transformative acquisition that we look to make in the MDO space.

Those of you that were here last year will remember us talking a bit about Q Holding’s Degania transformative acquisition. Degania was an opportunity to significantly expand the international footprint and the capabilities of the business, but required material operational and commercial work, which continues to be undergoing and is driving significant changes in the platform and will continue to deliver strong growth for Q over the next number of years. In Cirtec’s case, it is a little bit of a different story, and this was part of the sell to them. We are looking to further build the existing Vascotube facility, backing the same people and leveraging the current processes and strong competencies. We will also bring on additional supporting leadership and plan to invest heavily in the business. That investment commitment into a very proud German business was extremely important. Again, 3i's international network and global/local approach allowed us to buy one of the top assets in the sector outside of a traditional process.

III. Questions and Answers

Participant

You mentioned reimbursement pressure and risk. Is that a concern at Cirtec or is it mitigated by the diversity of products and the number of OEMs that you service as well?

Rich Relyea

Yes, it is a very diversified product portfolio. I think it is public that most TAVR devices now are in the ballpark of $32,000 a device. Our cost, as a proportion of the selling price, is extremely low. Other devices which we produce or into which we sell components often sell for thousands of dollars in the market and our cost is typically a fraction of that. The reality of the healthcare industry is that you will find over time new innovative technologies are introduced, they grow, they have price sustainability, and then at some point in time there will be increasing regulatory pressure on them. That is just the natural curve of it.

Importantly, you want to be ahead of that with next generation devices. Cirtec's design and development capability, its partnership with its customers, its ability to offer a full complement of capabilities from upfront engineering to manufacturing, supply chain management, kitting, packing, sterilisation, etc puts it in a unique position to help customers with their next generation devices. We address your question with product diversity and ensuring that we are part of the next generations.

Participant

Is there any concern about maybe a Chinese manufacturer coming in and replicating exactly what you do, or is there some sort of barrier to entry there?

Rich Relyea

Yes, the sensitivity on the part of the OEMs to their supply bases is extremely high: certainty as to what types of materials are being used, certainty as to the consistency of the processes. That has not been a significant industry issue to date, especially not with extremely high-end class II and class III complex medical devices, particularly implantables. The Chinese industry is going to evolve quite a bit and it will be a very compelling medical device market, but at this point in time we do not see a major trend towards outsourcing complex medical devices to the Chinese on the part of the OEMs in North America and in Western Europe.

Lampenwelt

Peter Wirtz

Partner and Managing Director, Germany

Slide 41: 3i in Germany

I have the pleasure of leading you through our investment in Lampenwelt that we did in 2016. But before we do that, again, I will talk briefly about our operations in Germany. Our Frankfurt office opened in 1984. At that time, what we were doing was not called private equity, but it is fair to say that we really have been one of the pioneers of the industry in Germany. Today, we have 13 investment professionals to look after six investments. We have a very strong core team. I have been with 3i now for almost 20 years, on 1 October. My colleague, Ulf von Haacke, who I think some of you met last time presenting ATESTEO, has probably worked with me for 18 years. Our third partner, André Perwas, has been with us for 10 years as well.

Our reputation is one of the longest-established players in the German market. I think we are taking it a step further when we present 3i. We often compare 3i to the German institution Kreditanstalt für Wiederaufbau, which is the German reconstruction bank. It was formed after the war, to help the German economy back to its feet, and we draw a parallel with 3i, which has done the same thing in the UK. That resonates very well with German entrepreneurs, owners and management teams and positions 3i as a very reliable and trustworthy partner, which clearly differentiates us from some of our competitors.

You can see on this slide some of the investments we have done. Simon was nice enough to mention Scandlines. ATESTEO, which we sold in December, was an investment that Ulf did. We bought that from the founding family. I think another one that we are particularly proud of is Norma Group, which is a business that I bought with Ulf in 2006. We bought that from the family and then floated it on the stock exchange. It is a very successful member of the MDAX, which is the equivalent of the FTSE 100. That is just a little snapshot of where we are in Germany.

Slide 42: Lampenwelt - it all started in a garage…

Lampenwelt is our first pure play eCommerce investment and, like a lot of businesses in the digital space, it started in a garage. It was started by Thomas Rebmann in 2004. He was a student of electrical engineering and started to sell his own products through eBay. Over the years, he grew the business and then set up his own webshop called Lampenwelt.de with his brother, and then grew the business to what it is today.

Slide 43: Leading European eCommerce player in the lighting space

Lampenwelt was founded in 2004. Today, it is the leading European online specialist in the lighting space. It sells around 45,000 SKUs and 50% of sales are through private label products. I will come to talk about the relevance of that later on. We have webshops in 15 countries and we have a strong market position, particularly in Germany but also in France, Switzerland, Austria, the Netherlands and Poland. We are also active in other countries. Lampenwelt has had 23% revenue CAGR over the last five years. We invested £95 million in Lampenwelt, alongside co-investor Project A, an operational venture capital fund in May 2017.

Slide 44: Broad product base and wide geographic reach

At the top of the slide, you see some pictures of Lampenwelt's own products. You can see all of the diversity of the products it sells, which include indoor, outdoor, office lights, decorative designer lights, but also very simple lighting fixtures. Below you see some of the brands that it sells. You probably recognise some of them: Artemide, of course; Osram, for example. Below you have some of Lampenwelt's 15 websites. All of them are in their own language, so the Finnish website is in Finnish and customised for local particularities like language, of course, but also payment methods, which can be very different in each country. Also, it is important to note that we have local specialists that you can call. We have Finnish-speaking people in our organisation, who can take the calls and can advise the customers on the products, and help them to make the right choice. We have that for Finland. We have that for Spain. We have that for France, Germany, the UK and so on.

I would now like to show you a brief video to give you a sense of Lampenwelt's product offering.

[Video shown]

Slide 45: We acquired Lampenwelt in a proprietary process that leveraged our strengths

Now, let us talk about how we got into Lampenwelt. We had followed the sector for quite some time, by looking at various businesses in the lighting sector. In 2016, we were very involved in one of those transactions, when it came up for sale. We participated in the auction. We did not do the deal, but we did a lot of due diligence in the process. In that due diligence process, we identified Lampenwelt as probably the most interesting player in Europe in that space, because it was pure digital, pure eCommerce, and it has been growing at the fastest rate. That is how it got our attention.

Then over the last three or four years we looked at a lot of eCommerce players in Germany, in different sectors, and we could compare the strengths of the business models to each other. What we could see at Lampenwelt, we liked a lot. Then we saw how we could approach the owners of the business. We did that together with one of our business contacts in Germany. I am going to talk about Jochen Wilms later in more detail. Basically, he got us through the door, we made contact with the owners of the business, and we hit them at the right time. They were just about to sell a minority stake to strategic investors. We were able to talk them out of that, and instead to sell the business to us, convincing them that it was actually best for the business going forward.

We made use of 3i's BLN. We bought the business outside of a process. I think for the size a business like Lampenwelt, the fact that there was no investment bank involved on either side is quite remarkable and a good result for us. I think it is fair to say that we bought the business at a reasonable price. We did not buy it cheap, but I think it was a very good process for us. It was a reasonable price and everyone was happy.

I will come back to the local network. I think that was extremely important. Walter Neumüller, one of the sellers, told us afterwards that he was sceptical taking the meeting, but the brand name of 3i made a difference to him. It also made a difference that he had someone at the table who had been there for 20 years with the business. It gave him the impression of continuity and consistency.

Slide 46: What we like about Lampenwelt

What we like about Lampenwelt can be summarised in four main areas. First is the market. I am going to talk about this in more detail, then Lampenwelt's position in that market, then how this is reflected in the financials of the business, and finally the management team that we invested in.

Slide 47: Favourable market dynamics

As you can see, these are our main markets: Germany, France and Switzerland. The overall lighting fixtures market in those geographies is growing between 3% and 3.5%, mainly driven by renovation. It is a refurbishment market mainly. However, the online penetration, so how many people buy online instead of offline, is growing at 10-13%. If you combine those two figures, you come up with the CAGR that we expect for 2016 to 2021 of 12% to 14%. At the same time, we know that, from our business that we did and our work that we did on the sector, that this business offers a very high margin in the value chain. That is a very stable profit pool in that industry. Why is that? Why do we have such a stable profit pool? It is the market structure. You have so many SKUs. You have a lot of manufacturers. You have a lot of brands. You have a lot of distribution channels. You have a highly fragmented customer base as well. There is no dominant player in the whole value chain who grabs a big part of the profit. As a result, everybody seems to make quite a good amount of money in that industry.

Slide 48: Leading online specialist with scale advantages

Of course, you can ask yourself: if you invest into an online business or an eCommerce business today, can it survive against Amazon? We believe we can, first of all because the sector as such is not big enough and is too complicated for Amazon to focus on it heavily. There are so many other priorities to go after, that the lighting market is not the most attractive for them. If you look at food, clothing and so on, those are areas that are way more attractive to them. We do not expect Amazon to focus on lighting, but, even if they were focused on it, Lampenwelt has a differentiated offering.

I think we all feel that. If you go on the website, which is lights.co.uk here in the UK, if you want to have a look, try to look for a certain product. Try Lampenwelt or lights.co.uk, and try Amazon. On Amazon, of course, you get a broad offer of lights or lighting, but it is not curated. You have all kinds of products, somehow unstructured and not shown in an appealing way. Lighting fixtures are also somehow an emotional buy. It is very important that our team’s focus is on that assortment, on the operation of the assortment, and then adding the service to it. As I said before, we have people you can call in your own language to help you make the right decision. You do not get that at Amazon, so that for us is a key differentiator.

Then the private label assortment is absolutely key to Lampenwelt. It is now more than 50% of sales, and it is important because it obviously provides a very high gross margin. You need to have a high gross margin if you want to compete on the internet. If you are only selling other people’s products, that is not sustainable in the long term unless you are Amazon. You need to have your own expertise in sourcing products. 80-90% of them come from China, and they come with a high gross margin. That differentiates us against a lot of smaller players, who simply do not have the capabilities of sourcing products from China or such a strong position in the private label market.

Finally, we are building our B2B offering. We work with electricians and installers. The nice thing about them is that they come back much more often than the consumers do. They are not as profitable customers, because you have to give them higher discounts, but they come more often and then long term, on a customer lifetime value, they are probably better customers than the average consumer.

Slide 49: Resilient financial profile

Lampenwelt’s competitive advantage is reflected in the financial performance of the business. You can see it in this chart here, not a lot happened until 2008, but then the business really took off: 23% percent CAGR over the last five years, with a very attractive gross margin. We also have a very attractive EBITDA margin, particularly for a fast-growing eCommerce business, to an extent that we think that it might actually be too high and that we need to invest more into the structure of the business, to make sure that we have this growth going forward in the future. That is why we invest quite heavily into the business. We hire ahead of the curve. We have just invested in and opened a new distribution centre last year. We really have prepared the business for further growth. This also compares very favourably with listed companies in adjacent markets that have floated over the last 12 months, where the difference in profit margins is more than 20 percentage points and our growth is significantly higher than theirs.

Slide 50: Dedicated and proven management team

Finally, on the management team, I have spoken about Thomas Rebmann before. He founded the business, together with his brother. When we came into the business, there was a strong team around him. We helped to build around this team. We brought in a very strong CFO. As I said, we are trying to hire ahead of the curve. We hire people who, at the time when we hire them, are probably too big for the company, but we want the business to grow and therefore we make that investment. I think there is also a very strong alignment with 3i. They are co-shareholders with us and they are fully committed to the success of the company.

Slide 51: Strong BLN contribution

We complemented that management team with very strong BLN. We have been working with Jochen Wilms for a number of years now, looking at businesses in the construction supply area. He is a former Schüco manager and, in Schüco, they do windows, doors and façade elements from aluminium. He has very deep knowledge in the construction supply area. He also advised the CEO of GROHE sanitary fittings in its digitalisation. He has a very strong digital background, has invested in a number of start-ups and he really has helped us with that business. He spends probably one to two days in the company and he also helped in us winning the deal.

Walter Neumüller is one of the former owners and we have a very good relationship with him. He co-invested with us.

Then Florian Heinemenn is probably one of the most influential and respected people in the Berlin start-up community. He has been an MD of Rocket Internet and was instrumental in building Zalando. He founded his own private equity venture fund called Project A. He is also on the board and I think together they bring an amazing amount of expertise and knowledge to the company.

Slide 52: Project A involved as minority co-investor to support further eCommerce professionalisation

Talking briefly about Project A, as I said, it is a Berlin-based operational venture capital investor. Operational venture capital means that they have their own experts in-house, in areas such as marketing, business intelligence and information technology. Why have we brought them in? We think these people are really cutting edge in eCommerce. We wanted for Lampenwelt to be exposed to best practice and to development in that industry. Therefore, we have asked them to co-invest alongside us, which they did, and it is a really strong partnership that we have with them. There is a great exchange of knowledge and ideas amongst the teams and, so far, it has gone really well for us.

Slide 53: Significant opportunities for value creation over the next 3-5 years

Going forward, in the next three to five years, I think we will focus on more of the same: to continue to keep the strong position that we have in Germany, to participate in market growth, to further internationalise the business, to open stores in new countries, to increase the penetration in those markets, and finally to push the B2B side of the business. As I have said, B2B customers are interesting for us because they come back often. It is a more stable customer group, so to speak.

Slide 54: The growth story continues

I am going to close with a picture of Thomas and Andreas from covers of magazines and newspapers. *brand eins* is a business magazine targeted to the digital community. *Frankfurter Allgemeine Zeitung Sonntagszeitung* is the equivalent of the *Sunday Times*, where Thomas and Andreas have been featured lately. The good thing about it is that, when they are portrayed as a success story in eCommerce in Germany, 3i is also always mentioned in it, which is positive marketing for us.

Questions and Answers

Participant

Thank you for the Amazon slide. Are you able to put any numbers to that in terms of how your market share compares with Amazon in lighting or growth rates? Then, can I ask a second, completely unrelated, question? I had an eCommerce business talk to me the other day about the cost inflation of acquiring customers. They said that the cost of acquiring customers through Facebook had doubled and gone up 60% through Google. I do not know how you acquire customers, but can you talk about any cost inflation in terms of getting hold of customers?

Peter Wirtz

Of course, that is the key challenge: to acquire customers at a sensible rate. First of all, we have very good SEO (search engine optimisation) visibility. The mix between unpaid traffic and paid traffic is pretty good for us. We are investing more into SEO, so that we are the first up in the unpaid traffic. Of course, you can see that there is some cost inflation there that you have to deal with. It has not doubled, but it is a constant fight in that area. It is also a reason why we moved down the B2B route a little bit more: to understand your customers, how often they are coming back, your customer lifetime and so on. This is hugely important.

Participant

Then on Amazon, can you make any sort of comparison in terms of size?

Peter Wirtz

You always have Amazon, through its own offering and then the marketplace. Everyone else is selling on them and Lampenwelt is also selling its own products partly through Amazon. I cannot tell you exactly, because Amazon would not tell you how big they are. They never tell you, but they are probably the biggest in terms of lighting sales in Germany.

Participant

I have another question. Is there any interest in perhaps expanding to the US? Obviously, you are in most of the European markets. There might be a few on the fringe, but is the US a potential market for you?

Peter Wirtz

I think the business has so much to do still in Europe before we consider the US. Today, it is a highly efficient system. Lampenwelt runs everything out of its one distribution centre. It is getting a bit difficult if you want to serve the UK, because there seems to be a customer that expects delivery in one day and that is more difficult from a warehouse in Germany. In the US, you would have to set up the whole infrastructure, warehouse and everything. I think the business has so much to do in its home market that it probably not going to be the next thing.

Participant

What is your cash conversion like, given that you have such a broad range of SKUs?

Peter Wirtz

Yes, in theory it is pretty good because we do not manufacture. We get the money from the customers right away. In the recent year, as I said, we invested in a distribution centre and a lot of structural cost but, in principle, the cash conversion is pretty good.

Participant

Does Lampenwelt hold stock on everything that it sells on the website?

Peter Wirtz

Yes, except, for some of the brands, Lampenwelt is getting more and more into drop shipping, so that we do not have to keep the stock and the brands are delivering right away to the customer.

Action

Simon Borrows

Chief Executive

Slide 55: …and a final aside on Action

I hope you have found this afternoon useful. All three of today's companies are capable of growing at more than 20% per year and in each case, we have bought well relative to their value potential.

Before I close, I would just like to touch on Action. Action announced this morning that Joost Sliepenbeek will join the group as its new CFO on 1 November. He is an experienced retail CFO. He currently works for Vion in Holland but he has also had a long career at Ahold where he was formerly CFO of Albert Heijn. He has also worked with Private Equity at HEMA and supermarket Group C1000.

Frederik Lotz will be leaving Action after three years. Frederik has done a good job at Action but Action is no longer targeting a near-term IPO and the main focus now is operational, with the aim of delivering our €10 billion of sales organic growth plan.

Action continues to grow strongly with over 130 new stores opened in the year to date.

Our two challenges this year were to tackle some specific buying issues and to improve the distribution performance in France, as well as continue the store roll out programme. The re-organisation of buying has gone well and we are pleased with progress to date. Our new Deco category is now in the stores for the important three months leading up to Christmas.

The DC (distribution centre) situation in France has improved but the challenges still remain, given the considerable attraction of Action stores to the French consumer.

This slide shows the picture of a store which opened at the end of last week in Angers. I'm afraid I haven't yet had opening day numbers for this store. Earlier last week on Tuesday we opened a store in the south of France, at Brignoles near Marseille. In this store we took over €80,000 on the first day, which is a new record for the Group and is 7 or 8 times what the average Action store takes in a day. So as you can see our French stores can be very busy.

Our two French DCs are improving, managing more stores and stronger than last year, but are still not at a level comparable to our Dutch or German DCs, which does result in weaker service level performance and too many empty shelves in some of our French stores at very busy times.

Although our sales in France are up over 40% so far this year on the back of the store opening programme, there is no question sales could be up a good bit more if DC service levels could fully match the footfall going through our French store network. This is frustrating because it is fixable, but it takes time. The draw of our model remains very powerful so in that sense this is a nice problem to have. The opening of our third DC in France at Lyons in January should make a major difference to this situation.

Thank you for coming today and we plan to repeat the event next September with three more investments from our Private Equity portfolio.

Questions and Answers

Participant

Was Frederik's departure linked to the performance issues?

Simon Borrows

No, not at all. He very much joined with an IPO in mind, with a view to being a corporate finance-type CFO.

Thanks for coming, everyone.