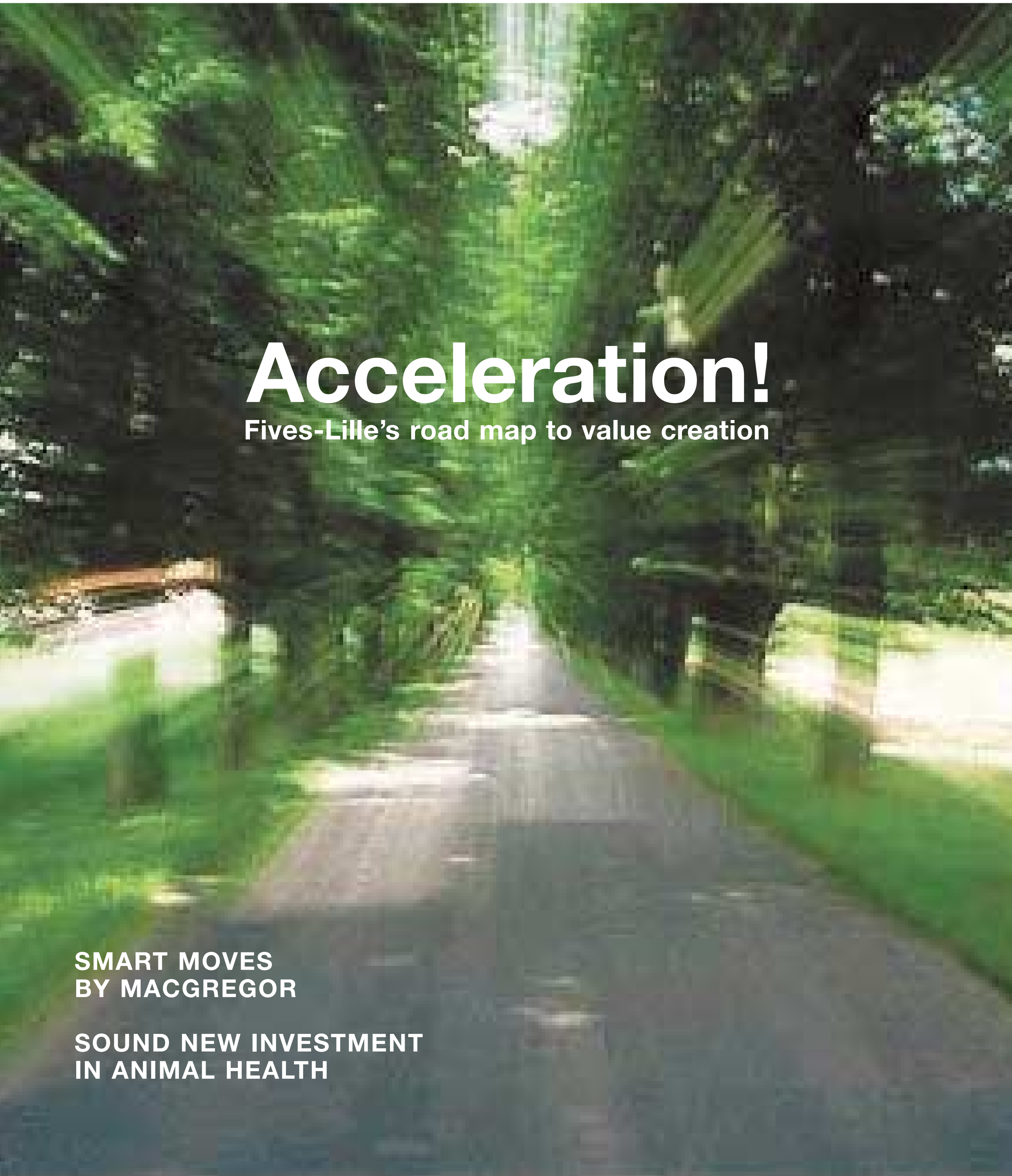
news

UPDATE FROM INDUSTRI KAPITAL **ISSUE 8** AUTUMN 2003

"A paradigm shift, in which we mentally accept that we now not only live in an industrial society but also in a service society, is necessary."

VIEWPOINT, PAGE 2



Acceleration!

Fives-Lille's road map to value creation

SMART MOVES BY MACGREGOR

SOUND NEW INVESTMENT IN ANIMAL HEALTH

Challenging times ahead after Sweden's No

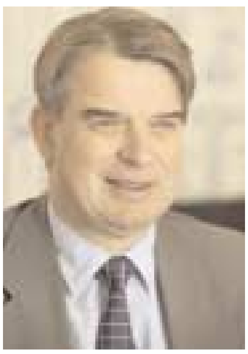
After the strong No win in the referendum, Sweden's adoption of the euro has been postponed, and an increased currency risk must be offset by more growth-oriented policies.

SEPTEMBER WAS A DIFFICULT month for Sweden. The events of one week, characterised by shock and sorrow, forced us to reassess the way we view ourselves and to reflect upon Sweden's role in the international arena.

On 10 September, Sweden's foreign affairs minister Anna Lindh was stabbed in the NK department store in central Stockholm. She passed away the next day. Sweden, in the middle of its euro referendum campaign, ground to a halt.

Anna Lindh was a politician with qualities rarely seen in Sweden or elsewhere in the world, a fact that further aggravated the already tragic event. She was also one of the most charismatic standard-bearers of the pro-euro movement.

The referendum was held three days later in an atmosphere of national gloom. The results were surprisingly clear: 56 per cent of voters opted to retain the krona. Sweden, along with Britain and Denmark, will continue to stand apart from the 12 European Union countries that have abandoned their traditional currencies.



Björn Savén
Chief Executive,
Industri Kapital

As one of Sweden's business representatives strongly committed to a Yes in the Swedish referendum, I believed that the issue was not only important for the Swedish companies in our portfolio, but also because a Yes vote would have supported the emergence of a new and more open Sweden.

The results mean that the majority of Swedes prefer to stand on the sideline rather than participate and take responsibility for the evolution of a more integrated Europe. We have seen this wait-and-see attitude before, particularly during the debate prior to the EU referendum in 1994. Many voices were raised in favour of Sweden remaining outside the EU for a while longer.

Some opponents to a Swedish euro entry claimed that Sweden would no longer be able to maintain an independent currency and monetary policy. Yes campaigners believe that the No campaigners' argument mostly concerned being able to continue to undermine the value of the krona through excessive budget deficits as well as wage and salary increases.

Thirty years of devaluation policies have made Swedes poorer than our neighbours. The drawbacks of such policies are not only the absence of growth, but also that the nation's own currency becomes an obstacle to trade (due to currency risks). This results in fewer direct investments and in fewer new jobs.

Many people have US dollars in their investment portfolios, but few have odd currencies like the Swedish krona or the Canadian dollar. A small currency will always be more unstable than a major currency.

In the short term, the effects of the Swedish No will be relatively minor – both for Industri Kapital and Sweden's venture-capital sector. In the long term, however, particularly if the value of the krona continues to rise, the No vote will place increased rationalisation demands on our businesses. With greater fluctuations, direct investors will become more irresolute, while portfolio investors, who have a more short-term perspective, will be able to exploit the instability.

Swedish companies, particularly small and medium-sized businesses, cannot gain full access to the benefits of the European market when they are faced with the trading obstacles that different currencies imply, such as transaction costs and exchange risks. Furthermore, currency risks reduce the credit scope of companies in Sweden, which are already short of equity, thus dampening their potential expansion.

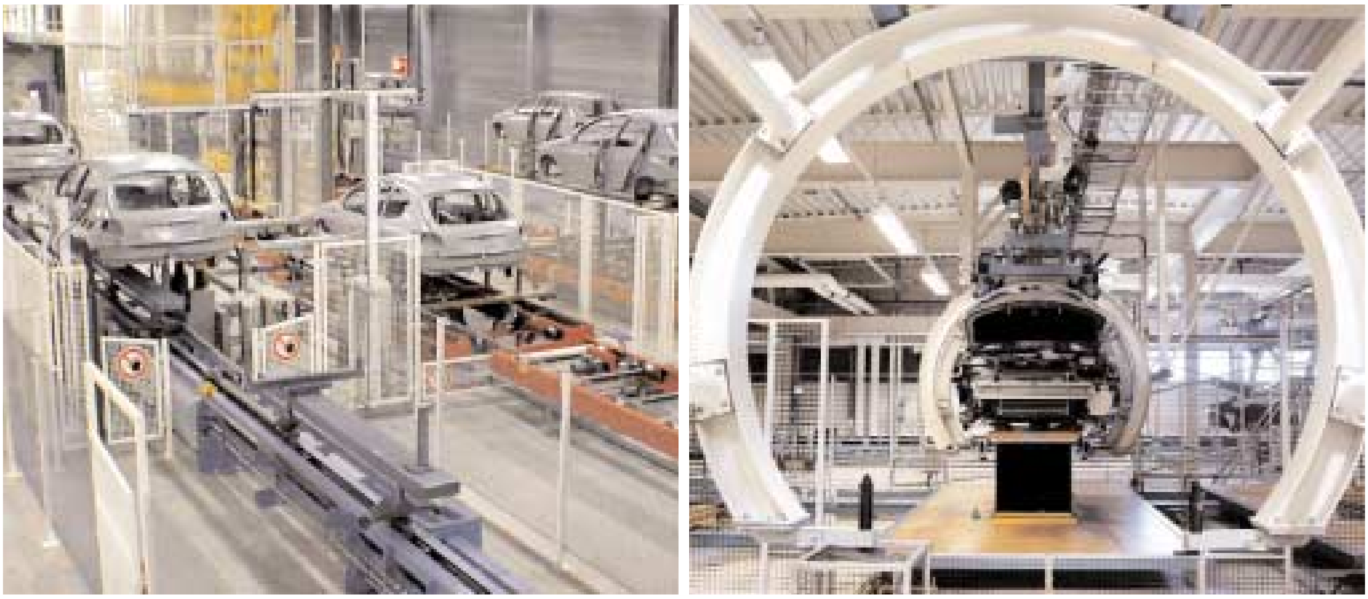
Had the euro been accepted, the path of inflation and devaluation would have been closed off. The Economist magazine wrote: "With time, and assuming that the EU will eventually repair its defective euro arrangements, the price for retaining the krona is likely to be some net loss of investment due to exchange rate uncertainty. The smaller and the more open the economy, the greater the benefits of a fixed exchange rate; and Sweden is small and very open."

Sweden must now live with an increased currency risk, which must be offset by more growth-oriented policies. Prime Minister Göran Persson says he wants to counteract the trend of large Swedish export companies leaving Sweden for the euro zone.

A paradigm shift, in which we mentally accept that we now not only live in an industrial society but also in a service society, is necessary. A considerable number of reforms must be introduced so that the service sector finds Sweden equally attractive as, for example, the United States or Great Britain.

On a positive note, the referendum result will perhaps lead to increased opportunities for cooperation among growth-oriented political parties and partners, as per the Finnish model.

Sweden's adoption of the euro has been postponed for the time being, but our efforts to achieve a positive return for our investors will be strengthened by the subsequent challenge.



FIRM FOUNDATION. Founded near Lille in 1812, GFL is one of France's most established industrial names. Today GFL is structured around four main business lines – automotive, aluminium, steel and cement – for which it designs and supplies process equipment.

Strategic road map drives Groupe Fives-Lille forward

Under Industri Kapital's stewardship, Groupe Fives-Lille has been transformed from an unwieldy conglomerate to a focused pure-play engineering group.

JUST 30 MONTHS after it was backed by IK in a €235 million public-to-private (PTP) from the Paris Stock Exchange, Groupe Fives-Lille (GFL) – a leading global engineering group – has completed a highly-successful recapitalisation.

The enthusiasm and appetite within the senior debt market for exposure to GFL is testament to the strength of the company's management, its ability to perform under pressure and the rationale behind its strategy to streamline and refocus the group.

The PTP in February 2001 heralded an intensive restructuring programme. As Chief Executive Frédéric Sanchez observes: "Looking back it is incredible to see what we have achieved in such a short time frame."

> "Everything which is said is done, the words are in-line with the facts. This gives us confidence in the shareholder message and fosters a great deal of mutual respect."

Over the last two years the group's overheads have fallen by €37 million whereas EBITDA per employee, at the time of the MBO, amounted to some €5,900. Today it stands at some €11,000. Meanwhile, the total number of companies within the group has been dramatically reduced.

Gross margin has increased by 4.1 percentage points in three years with GFL's EBIT up by 75 per cent over the LBO period. In 2002, GFL generated sales of €729 million and EBIT of €32 million. This compares with turnover of €900 million and EBIT of €18 million in 2000.

A shift from production to design

This performance is the product of GFL's transformation over the last few years from an unwieldy conglomerate to a focused pure-play engineering group. GFL is now structured around four main business lines – automotive, aluminium, steel and cement – for which it designs and supplies process equipment.

IK sees GFL's management as having done an excellent job on the first phase of restructuring. The team has also handled other important aspects of the rationalisation extremely well, notably accelerating an operational shift from production to concentrating on design and integration.

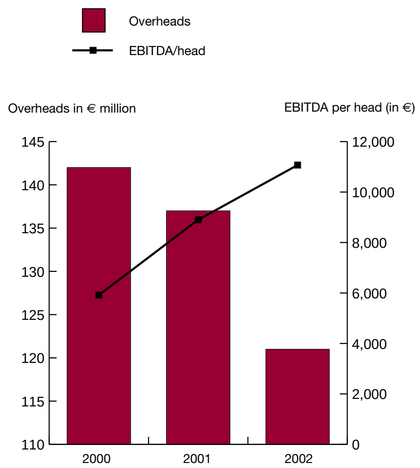
"The result is a streamlined, highly-skilled engineering workforce with a more flexible cost structure. Now GFL no longer has to take on low-margin contracts just to cover fixed costs," asserts IK Director Christopher Masek, head of IK's French team.

The management team has also performed well in terms of simplifying the group. "They have taken a disparate collection of businesses and really sorted it out – not just through divestments but also through closures and inter-company mergers and by reorganising and rebranding companies and cutting costs. Now we don't just have profitability but also visibility of earnings within the group," says Masek.

Founded near Lille in 1812, GFL is one of France's most established industrial names, best known for high-profile projects such as making the elevators for the Eiffel Tower. Despite its illustrious past, however, GFL began to lose its way in the 1970s with some ill-advised diversification.

Remedial action was taken by BNP-Paribas, which held a 30 per cent stake, in the 1990s. It stepped in and hired a manager to make divestments, slim down the 15,000-strong workforce and turn the company around.

While this returned GFL to its engineering roots, with 15 business lines it was still too diversified, and with its reputation tarnished by its turbulent past its shares



IMPRESSIVE FIGURES. Strong reduction in overheads and increase in contribution per head.

were lowly-rated on the stock market.

"The company also suffered from having to account for long-term contracts – the revenue swings this produced were not understood by investors. Smaller companies and 'old economy' stocks were also out of favour," notes IK Deputy Director Jean-Baptiste Wautier.

"This combination of factors meant that the company was significantly undervalued – so much so that when we bought GFL the cash on its balance sheet alone was equivalent to the purchase price," he says.

A number of private equity houses were interested in buying GFL, but IK was, ultimately, the most in-tune with GFL and its management. "Of all the firms we spoke with IK was by far the most convincing," recalls Sanchez.

"They were genuinely interested in GFL and its industry and had clearly done their homework. They were very professional and completely straightforward in their approach. This made our discussions so much easier," he says.

IK was already well-acquainted with the engineering sector having previously invested in Crisplant, KCI Konecranes and Alfa Laval. It was also impressed by GFL's management.

"They were completely on the same page as us, and had already made a good start at cleaning up the business," says Masek. The team was also strong on project and risk management – fundamental in a business based on long-term contracts. "Overall we felt we were buying a good base with good prospects and a coherent strategy to refocus and develop the business, particularly on the automotive side," he continues.

Recap conducted at brisk pace

Having established a rapport with management and won the support of GFL's two major shareholders – BNP-Paribas and financier Allan Green, who together accounted for 50.2 per cent of the shares and 52.2 per cent of the voting rights – IK launched its public offer at the beginning of December 2000. The deal completed in February 2001 supported by a €150 million mezzanine and senior debt package led by the Royal Bank of Scotland.

With the value creation process at work, GFL began to comfortably outperform the original LBO business plan.

By the time of the recapitalisation it had generated €40 million of cash from operations, improved working capital by €12 million, raised €35 million from disposals and made an early debt repayment of €61 million.

As with the restructuring, the recap was conducted at a brisk pace. IK initiated discussions with the banks at the end of 2002. The deal was signed in July 2003 and the debt syndicated by the end of August 2003.

Releveraging GFL has given IK a partial exit, boosted its internal rate of return and enabled GFL to continue with its external growth plans. Having experienced weak demand when syndicating the debt on the original LBO, however, the lead banks were initially not very receptive.

Comments Wautier: "Even though GFL is now performing well and has a strong track record, engineering remains a mature sector and relies on long-term contracts. This throws up off-balance sheet commitments and makes the financials difficult to understand. This will remain the case no matter how much GFL is rationalised or restructured."

In addition, because the recap also provides for a partial realisation for IK, the banks naturally questioned whether most of the upside had already been extracted from the business. "But we had some frank discussions with the

GFL's Chief Executive Frédéric Sanchez, right, views IK as a facilitator of ideas. Christopher Masek and Jean-Baptiste Wautier of IK's French team, left.

Pressure, pain and performance

GFL is a great success story and a clear illustration of how value creation can be achieved – but it requires dedication and hard work.

As GFL's Chief Executive Frédéric Sanchez observes: "IK has us under constant pressure and is in continuous contact." Sanchez explains that if GFL has agreed a plan of action, for example, then they have to get right on and do it. "There is a big difference between the new GFL and its culture pre-LBO. Now nothing gets put on the back-burner, there can be no excuses for not having done something," he says.

But, continues Sanchez: "Although we have to work hard, we know that IK is working just as hard. And we are all very well motivated – we all know what we are doing and where the company is going."

On this front, Sanchez has always found IK to be very consistent and reliable.

"Everything which is said is done, the words are in line with the facts. This gives us confidence in the shareholder message and fosters a great deal of mutual respect," he says.

IK is recognised as a hands-on investor but Sanchez regards the firm as a facilitator, rather than an originator, of ideas. "When we put up the operational plan for the LBO, IK approved it and did not add anything. But then if you work at a company all the time you know what needs to be done. The firm is always very supportive and it is extremely helpful to have them as a sounding board," he says.

"We have lots of interaction with Frédéric and his team but we are not managing the business on a day-to-day level, that is absolutely not our role," agrees IK's Jean-Baptiste Wautier. "Our prime impact has been in summarising and crystallising the 'strategic road map' and increasing the time pressures. GFL would have done 90 per cent of what has been done by itself – just not in the same time frame," he says.

"Typically we discuss what we want to do and IK then accelerates the process," laughs Sanchez. "What we have done with IK in two years would, pre-LBO, have taken us six to ten years."

"We know that we are demanding, but Frédéric is an outstanding manager and we have a very good, open relationship. It is a partnership with a common goal and it is highly effective," Masek says.

banks and really put a lot of energy into making things happen," Wautier recalls.

Thorough due diligence

Frédéric Sanchez also made a series of banking presentations in France. Having done this type of thing many times before when GFL was listed, this, in itself, was not a problem. "The difficulty was to be dealing with the day-to-day running of the company at the same time," he says. "This was very tough – more so than doing the original LBO."

The banks also wanted to carry out far more due diligence than they had been able to do previously – when GFL was listed the information available had been limited. "This time the due diligence was very thorough and a further burden on management resources," says Sanchez.

"But even though the recap was not in our original business plan, and put us under even more pressure, ultimately it has been a great success and we are very happy to see the results," he adds.

The €134 million refinancing has allowed GFL to fully repay the convertible bonds and shareholder loans put in place at the time of the PTP. IK has realised 50 per cent of its original €93 million investment through the recapitalisation, and will be able to recoup another 30 per cent within a short time frame, subject to certain disposals.

The lending terms are quite standard with the debt – which was 30 per cent over-subscribed – written on a margin of 2.25 per cent at market rates. Post-refinancing, GFL's leverage remains at 1.6x EBITDA and 2x EBIT – in line with its initial LBO levels.

WORLDWIDE PRESENCE. GFL's Hoang Mai cement plant in Vietnam.

Add-on acquisitions ahead

The strategy for GFL now is to continue to develop its automotive and aluminium operations and, to a lesser extent, its steel and cement businesses. It is also looking to complete several more non-core disposals.

Add-on acquisitions in Europe and the US are also on the agenda for GFL's automotive operations before the end of this year, with deals designed to strengthen the group's position both geographically and in terms of relations with manufacturers. "We have not made any acquisitions since the LBO and need to take time to work on this aspect to build up the business," Sanchez concludes.

NEW ACQUISITION

Good prospects for CEVA Santé Animale

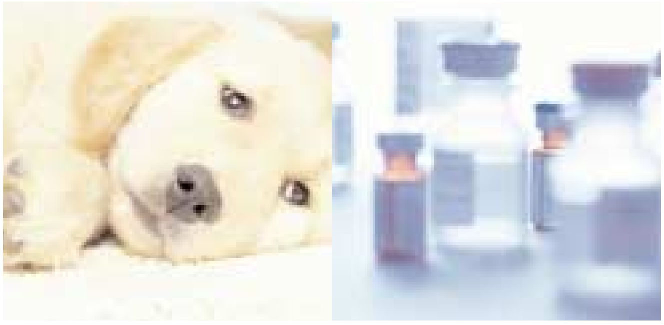
With a niche-market position, an innovative product portfolio and a strong sales organisation, IK´s latest acquisition, CEVA Santé Animale, looks set to exploit new opportunities.

CEVA OPERATES in the animal health industry, which provides for the diagnosis, prevention, treatment of diseases and general well-being of livestock and companion animals. The company's main expertise lies within the anti-infectives, vaccines and reproduction control devices areas.

CEVA operates in all key European Union markets and has a strong presence in growing international markets such as eastern and central Europe, Middle East and Turkey, Africa, Asia and Latin America. CEVA's net sales for 2003 are estimated to approximately €219 million. The company employs 1,200 people and is headquartered in Libourne, near Bordeaux (France).

In a comment to the acquisition, Christopher Masek, Director of IK's French team, said: "With a strong and very successful management team, a unique strategy and an innovative product portfolio, we believe that CEVA will be able to leverage its current position and accelerate its development in areas such as companion animals, vaccines and new geographies. We are convinced that the animal health industry will be fundamentally reshaped in the medium term, and intend to support CEVA in seizing acquisition opportunities and becoming a major independent international player."

Philippe du Mesnil, Chief Executive of CEVA, added: "CEVA is now well positioned to capitalise on its broad international basis and to exploit new opportunities. We are confident that IK will be a good shareholder, continuing to support the development of our business according to our strategic plan."



IN GOOD HEALTH. The animal health industry is on the verge of a reshaping.

CEVA: KEY INVESTMENT HIGHLIGHTS

- High growth history and prospects thanks to a niche-market position, an innovative product portfolio and a very strong sales organisation
- Highly diversified portfolio, client base and geographical coverage on a stable market
- Very strong management team with a proven track record, in an MBO context, of growing the company both organically and through acquisitions
- Sound financial performance with constantly improving profitability and upside potential through operational leverage, better product mix and complexity reduction
- Favourable M&A dynamics, which will lead to numerous acquisition opportunities for CEVA as well as a more fundamental reshaping of the industry resulting in attractive exit prospects

Simpler structure strengthens MacGREGOR

The MacGREGOR Group is implementing a restructuring plan to strengthen its position as the leader in providing marine cargo flow solutions and service for ship owners, ship operators and shipyards.

"Service is the primary area of future growth for MacGREGOR," said the Group's President and Chief Executive, Hans Pettersson, when he announced a plan that will simplify the organisation's structure to increase its efficiency. "And improved service includes concentrating on getting even closer to our customers: some parts of the Group's headquarters completed a move to Copenhagen in July, nearer the vital European ship-owner and ship-manager community. The future Dry Cargo division that we're establishing will be run from Shanghai, at the heart of the world's shipbuilding centre, which of course is Asia."

Hans Pettersson, President and Chief Executive, MacGREGOR

After his appointment in August last year, Pettersson initiated an exhaustive performance improvement programme that examined every aspect of MacGREGOR's activities.

"For more than 60 years we've consistently come up with revolutionary cargo-handling solutions that have become the standard. We have a truly global presence, both in terms of manufacturing and our service network. More than 13,000 ships use MacGREGOR products. Why weren't we more profitable?" he said.

"The performance improvement programme identified productivity as the main culprit," Pettersson said. "The organisation of the Group was too complex. We should have taken better advantage of the synergies available from our highly skilled resources. We've identified that working more efficiently should produce an overall cost reduction of at least €8 million."

One step in the new plan has been to form a new division to pull together all the Group's customer-oriented responsibilities: sales & operations, after sales and new products. Pettersson considers this new Service division to be crucial.

"The net benefit of the Service division to our customers will be improved efficiency," he explained. This will be achieved by economies of scale in, for example, logistics and spare parts handling, and a single spare parts unit will now handle spares for all of the Group's divisions.

Another new division, the Dry Cargo division, will combine the activities of the Hatch Cover and Cranes divisions. "For ship owners and shipyards who want both products, this creates a common MacGREGOR 'face' to deal with, and our focus on ship types will be increased," Pettersson said. Dry cargo ships benefiting from single-source supply and servicing of cranes and covers include general cargo ships, container carriers, reefer ships, bulkers, heavy-lift ships, and special-purpose ships.

"However this cannot be achieved overnight – most likely it will happen over the next couple of years or so. More immediately, the Hatch Cover division's general manager will move from Europe to Shanghai before the end of 2003. MacGREGOR is one of the pioneers in the marine industry in Asia and will now further strengthen its presence and operations in the Asian region," Pettersson concluded.

MacGREGOR is the global market leader in providing marine cargo flow solutions and service for ship owners, ship operators and shipyards. The products include hatch covers, cranes, RoRo equipment, shipboard elevators and escalators, galleys, cargo securing systems and refrigeration systems.

The Group reported net sales of approximately €370 million in 2002 and it employs approximately 1,200 people. The Industri Kapital 1997 Fund acquired MacGREGOR from Incentive in 1998.

Dynea wins Eastman supplier excellence award

Dynea has received an accolade from Eastman Chemical Company in the US having been awarded a coveted 'Supplier Excellence Award' for their excellent products and service in 2002. The award is in recognition of Dynea's servicing of Eastman's formaldehyde requirements for its plant in Longview, Texas.

Paul Palmero, Eastman's Procurement Manager, Global Chemical & Energy Procurement, has high praise for the 'world class group' at Winnfield where Dynea has its formaldehyde production unit.

"This award is based on several criteria, including 100 per cent in-specification and at least 95 per cent on-time deliveries. One of the other major factors that contributed to Dynea being selected for this award was its excellent customer service and business relationship with Eastman," he said.

Dynea's Market Development Manager, Neville Fernandes, applauds the close and long co-operation between Dynea and Eastman. "Our two companies have enjoyed a long and strong relationship and it is great to know that all our efforts are appreciated," he said. "Our mutual respect and openness with each other are a legacy that we cherish and will continue to nurture."

Fernandes explained that Dynea aims to provide a high level of service to all its customers through monitoring product quality closely and taking great care over aspects such as supply security.

"We also track our deliveries to ensure that they arrive on time and try to be flexible in accommodating customer needs. This year we knew that we had performed particularly well on the Eastman account and so it was gratifying to find out that we had been selected for the award," he added.

EXCELLENT SUPPLIER: Paul Palermo, Jr, Eastman, presents the award to Neville Fernandes, Dynea. They are surrounded by the Dynea Winnfield team.

Dynea has 3,200 employees spread between 52 production units in 24 countries in Europe, the US and Asia Pacific. The company had combined revenues last year of approximately €1 billion. Dynea is one of the world's leading providers of formaldehyde and adhesive and surfacing solutions.

Dynea continues to work closely with Eastman at Eastman's US facilities in Kingsport, Tennessee; Longview, Texas; and Batesville, Arkansas. Dynea also has close ties with the company abroad, servicing its formaldehyde requirement in Singapore, for example.

PORTFOLIO COMPANY NEWS

Fortex opens new factory

In September the textile rental and industrial laundry company Fortex opened its new factory in Eindhoven.

The plant is one of the largest and most modern of its kind and services hospitals, other care institutions and holiday parks. Dutch Government Minister Dekker, herself an ex-entrepreneur, performed the official opening and complimented Fortex management and shareholders on their vision to modernise the industrial laundry industry. The new plant replaces five smaller production plants, including the Vught plant that was destroyed by fire. Other plants were closed, reducing the overall number of employees by 10 per cent. The new plant has a 40 per cent lower water usage than the older plants and processes 260 tons of linen per week, including 200,000 towels.

Fortex is a leading provider of textile rental and industrial laundry services in the Benelux countries. Main customer categories include hospitals (bed linen, hygienic products and work-wear) and different kinds of companies (uniforms and work-wear). Fortex also provides special cleaning services for surgical tools and textiles.

MODERN PLANT. The new Fortex factory in Eindhoven, The Netherlands.

The company had sales of €58 million in 2002 and employs approximately 1,000 people.

CALENDAR

4 December
Annual Investor Meeting, Stockholm

Industrial Advisory Board Meeting, Stockholm

During December
Annual Update distributed to investors

30 September 2003 Reports, including Valuations, distributed to investors

13 January, 2004
US Investor Meeting, New York City

KNOWLEDGE DEVELOPMENT

IK encourages young people to undertake postgraduate studies

Nelli Öster received this year's Industri Kapital scholarship of €25,000

This year, BSc (Hons) Nelli Öster, 25, was chosen as the third recipient of a €25,000 scholarship named after its donor, Industri Kapital. The Industri Kapital scholarship is awarded annually to a young Finnish student of economics or technology, to pursue postgraduate or parallel studies in the United States.

The number of Finnish students pursuing postgraduate studies abroad is below the Nordic average and, thus, the grant is seen as one means of increasing the willingness and possibilities for such studies. By directing the grants to economics and technology students, Industri Kapital naturally hopes to form a recruitment base for the future.

Öster started her 4–5 year PhD in Finance at Stanford Graduate School of Business, California, in September. Her chosen field of research is behavioural finance.

Öster is a good example of a talented and ambitious 'rising star' and, thus, exactly the type of student IK wishes to support. She has obtained a BSc (Hons) in Management Sciences from the London School of Economics and has worked in London at the Mergers and Acquisitions and Investment Research departments of the investment banks Schroder Salomon Smith Barney and Goldman Sachs respectively. Nelli has also studied finance at the Helsinki School of Economics and cognitive science at the University of Helsinki.

RECEPTION. Nelli Öster received her scholarship at a ceremony in Helsinki. From left: Martin Saarikangas and Laura Noreila-Manninen from the League of Finnish-American Societes; Björn Savén, IK; Nelli Öster; Michael Rosenlew, IK; and Stig Gustavsson, KCI Konecranes.

PERSONNEL

New recruits

Astrid Heskamp
German. Office Assistant/Receptionist
Based in London

Promotions

(during the last six months)

Thomas Ramsay to Director, Finnish team

Martin Backman to Deputy Director, Finnish team

Jokke Paananen to Associate Director, Finnish team

Erik Larsson to Deputy Director, Swedish team

Kristiaan Nieuwenburg to Deputy Director, Benelux team

Jean-Baptiste Wautier to Deputy Director, French team

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