

# The only way is forward



By working for cleaner traffic and transport,  
Neste Oil is helping everyone stay on  
the move – today and tomorrow.



**NESTE OIL**

Annual Report 2012 / Review by the Board of Directors

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Review by the Board of Directors

## Review by the Board of Directors 2012

Neste Oil's comparable operating profit was EUR 352 million compared to EUR 178 million in 2011, which reflected the significantly improved result of the company's Oil Products and Renewable Fuels businesses. Refining margins and gasoline margins, in particular, were higher in 2012 compared to 2011, mainly due to capacity closures, low inventories, refinery maintenance and other supply limitations. Good progress was made in Renewable Fuels business as new markets were opened and NExBTL diesel sales volumes were increased by more than a million tons from 2011. Although the Renewable

Fuels segment remained loss-making in 2012, it reached close to breakeven result in the fourth quarter. In line with the company's feedstock strategy the use of waste- and residue-based feedstock was increased significantly in 2012. The Board of Directors will propose a dividend of EUR 0.38 per share for 2012, totaling 97 million.

Figures in parentheses refer to the full-year financial statements for 2011, unless otherwise noted.

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Review by the Board of Directors ► The Group's results for 2012

## The Group's results for 2012

Neste Oil's revenue in 2012 totaled EUR 17,853 million (15,420 million). This increase resulted mainly from the growth of the Renewable Fuels business and higher product prices compared to 2011. The Group's comparable operating profit for the year almost doubled to EUR 352 million, from EUR 178 million reported in 2011. Both the Oil Products and Renewable Fuels segments recorded clear improvement in comparable operating profit year-on-year, and Oil Retail's result was also slightly higher than in 2011. The Others segment posted a significantly lower result than in 2011. The Group's fixed costs came in at EUR 666 million (613 million). This increase was mainly caused by higher staff, IT service, and research & development costs.

Oil Products' full-year comparable operating profit was EUR 396 million (271 million), Renewable Fuels' EUR -56 million (-163 million), and Oil Retail's EUR 58 million (57 million). The comparable operating profit of the Others segment totaled EUR

-46 million (9 million), of which Nynas accounted for EUR -6 million (19 million).

The Group's full-year IFRS operating profit was EUR 321 million (273 million), which was impacted by inventory losses totaling EUR 61 million (gains of 79 million) and capital gain totaling EUR 45 million (11 million). Pre-tax profit was EUR 233 million (206 million), profit for the period EUR 159 million (160 million), and earnings per share EUR 0.61 (0.62).

Given the capital-intensive nature of its business, Neste Oil uses return on average capital employed after tax (ROACE) as its primary financial target. ROACE figures are based on comparable results. As of the end of 2012, the rolling twelve-month ROACE was 4.9% (2011 financial year: 2.6%).

**Group key figures, MEUR**

	2012	2011
<b>Comparable operating profit</b>	<b>352</b>	<b>178</b>
- inventory gains/losses	-61	79
- changes in the fair value of open oil derivatives	-15	5
- capital gains/losses	45	11
<b>IFRS operating profit</b>	<b>321</b>	<b>273</b>
<b>Revenue</b>		
Oil Products	13,764	12,644
Renewable Fuels	2,163	1,026
Oil Retail	4,895	4,298
Others	199	191
Eliminations	-3,168	-2,739
<b>Total</b>	<b>17,853</b>	<b>15,420</b>
<b>Comparable operating profit</b>		
Oil Products	396	271
Renewable Fuels	-56	-163
Oil Retail	58	57
Others	-46	9
Eliminations	0	4
<b>Total</b>	<b>352</b>	<b>178</b>
<b>IFRS operating profit</b>		
Oil Products	491	373
Renewable Fuels	-183	-170
Oil Retail	58	58
Others	-45	8
Eliminations	0	4
<b>Total</b>	<b>321</b>	<b>273</b>

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Review by the Board of Directors ► Cash flow, investments, and financing

## Cash flow, investments, and financing

Neste Oil Group's net cash from operating activities totaled EUR 468 million (197 million) in 2012. The year-on-year difference is mainly attributable to more efficient working capital management in 2012.

Investments totaled EUR 292 million (364 million) in 2012. Oil Products' capital expenditure totaled EUR 180 million (131 million), while Renewable Fuels invested EUR 51 million (190 million), Oil Retail EUR 36 million (34 million), and Others EUR 25 million (9 million).

Interest-bearing net debt was EUR 1,935 million as of the end of December 2012, compared to EUR 2,080 million at the end of 2011. Net financial expenses for the year were EUR 88 million (67 million). The average interest rate of borrowing at the end of December was 3.5% and the average maturity 3.9 years.

The equity-to-assets ratio was 35.0% (31 Dec. 2011: 34.0%), the leverage ratio 42.9% (31 Dec. 2011: 45.7%), and the gearing ratio 75.1% (31 Dec. 2011: 84.3%).

The Group's cash and cash equivalents and committed, unutilized credit facilities amounted to EUR 2,135 million as of the end of December (31 Dec. 2011: 1,629 million). There are no financial covenants in current loan agreements.

In accordance with its updated hedging policy, Neste Oil has hedged the majority of its net foreign currency exposure for the next 12 months, mainly using forward contracts and currency options. The most important hedged currency is the US dollar.

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Review by the Board of Directors ► Main events during the reporting period

## Main events during the reporting period

On April 17, Neste Oil announced that it had begun a scheduled major maintenance turnaround at the Naantali refinery that would result in the refinery being shut down until the beginning of June.

On May 15, Neste Oil announced that it had expanded the range of renewable raw materials it uses by beginning to produce NExBTL renewable diesel from waste fat sourced from the fish processing industry at its Singapore refinery.

On May 30, Neste Oil announced that it had filed a patent infringement action in the US District Court for the District of Delaware to protect its innovation and patent portfolio, based on its belief that one of its patents is being infringed by Dynamic Fuels, Syntroleum, and Tyson Foods in the production of renewable diesel at Dynamic Fuels' plant in Geismar, Louisiana.

On June 4, Neste Oil announced that diesel production line 4 at the Porvoo refinery had been shut down following an unexpected production incident. Maintenance work originally scheduled for the fall was moved up and carried out during the outage, and the line brought back on-stream in mid-July.

On August 17, Neste Oil and Stora Enso announced that they had decided not to progress with their plans to build a biodiesel

plant, for which the two companies had applied for funding under the EU's NER 300 program.

On August 29, Neste Oil announced that it had completed the first phase of its project to build a pilot plant for producing microbial oil at Porvoo. The goal is to develop technology that it is capable of yielding commercial volumes of microbial oil for use as a feedstock for NExBTL renewable diesel.

On September 7, Neste Oil announced that Neste Oil's service stations in Finland would launch premium-quality Neste Pro Diesel on September 9. The new product is the world's first diesel fuel to comply with the toughest Worldwide Fuel Charter (WWFC) specification.

On October 17, Neste Oil announced that the European Commission's proposed changes to biofuel legislation support Neste Oil's ongoing efforts to extend its raw material portfolio. The proposal advocates splitting the EU's requirement for 10% mandated bio content in 2020 into two components, with biofuels produced from crops limited to providing 5% of total traffic fuel consumption, and the other 5% required to come from fuels produced from waste, residues, or completely new types of raw materials.



On October 29, Neste Oil announced that it had launched the commercial production and sale of renewable naphtha for its corporate customers. NExBTL renewable naphtha can be used as a feedstock for producing bioplastics, for example, and as a biocomponent for gasoline.

On December 13, Neste Oil announced that it had signed an agreement to sell its station network in Poland to Shell. The

agreement covers 105 sites, all of which are unmanned and located in major cities. The transaction is valued at approximately EUR 80 million, of which around EUR 50 million will be recorded as a capital gain by Neste Oil. The transaction is subject to the approval of the local competition authorities, and is expected to be closed during the first half of 2013.

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Review by the Board of Directors ► Strategy implementation

## Strategy implementation

The implementation of Neste Oil's strategy continues to be driven by a series of Value Creation programs: Profitable Growth, Productivity, Renewable Feedstock, Customer Focus, and Winning Culture. These programs have defined targets and their progress is measured continuously.

Achievements as part of the Profitable Growth program in 2012 included increased sales volumes of NExBTL renewable diesel and the opening-up of new markets such as the United States to the fuel. The development of non-road applications continued, and the introduction of renewable naphtha expanded the NExBTL portfolio. Base oil sales volumes increased and sales were expanded in Asia and North America. New retail stations were opened in Finland and North-West Russia, and Neste Oil's retail market share in Finland increased in both gasoline and diesel.

Productivity was enhanced, with the new renewable diesel refineries in Singapore and Rotterdam achieving normal operational status. Capacity utilization at the Porvoo refinery also slightly improved. Diesel production line 4 at Porvoo achieved a new production record in 2012, despite maintenance outages during the second quarter.

The main achievement in the Renewable Feedstock program was the growth in the usage of waste- and residue-based raw materials by 406,000 tons to 742,000 tons in 2012. Waste fat from the fish processing industry was also successfully added to the range of renewable feedstocks used. The opening of Europe's first microbial oil pilot plant in Porvoo was an important step forward in efforts to expand Neste Oil's feedstock base in the area of waste-based materials.

Progress in the Customer Focus program in 2012 included the introduction of a new premium-quality Neste Pro Diesel product and contactless payment for fleet customers. Customer segmentation was also further developed.

Work on the Winning Culture program is also progressing. The results of the personnel survey conducted in 2012 showed improvements in areas such as commitment and leadership. Neste Oil's internal idea system generated over 1,500 ideas from personnel, of which the most promising ones will be followed-up and implemented.

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Review by the Board of Directors ► Market overview

## Market overview

Uncertainties in the world economy, geopolitical tensions in oil-producing countries, and fears surrounding the escalating Eurozone crisis were the main drivers in the oil market during 2012. Crude oil prices peaked in early March and reached USD 125/bbl amid concerns about a deepening crisis between Iran and the West. As the summer approached, a variety of factors, including escalating fears about Eurozone economies, pushed crude below USD 100/bbl, and prices bottomed out at around USD 90/bbl in late June. They bounced back in the early fall and

traded in a relatively tight USD 105-115/bbl range for the rest of the year. Brent crude averaged USD 112/bbl in 2012.

The price differential between heavier and lighter crude was again volatile and averaged USD -1.3/bbl in 2012, which was slightly narrower than in 2011. The differential widened significantly during the spring on the back of higher crude prices and the refinery maintenance season, narrowing as the summer

progressed to around zero during early July due to the sanctions on Iran and lower Iranian crude volumes. The refinery maintenance season in the fall saw the price differential widen again, before narrowing to around USD -1/bbl, where it stood at the end of the year.

Refining margins were volatile but were stronger on average than in 2011. The year started with the insolvency of Petroplus and the closure of several of its refineries, followed shortly after by the announcement of other refinery closures in the US. Low inventories, refinery incidents, and maintenance during the spring and fall pushed margins up in a market where demand growth in many regions was weak. Middle distillates were the strongest part of the barrel. Margins for middle distillates strengthened during the year and peaked at very high levels in the early part of the fourth quarter, after which they moved down towards the end of the year. Gasoline margins were seasonally low during the early first quarter and the late fourth quarter, but were at their highest since 2008 during the summer and fall. Overall European gasoline margins in 2012 were clearly stronger compared to 2011. Rising crude prices saw fuel oil margins weaken during the early part of the year, but strong bunker demand in Asia, high Japanese energy consumption, and falling crude prices strengthened margins during the mid-summer season. Fuel oil margins weakened again towards the end of the year, hand in hand with healthy Russian product flows and low demand in Asia. Fuel oil margins were at their lowest just before Christmas.

Global biodiesel demand in 2012 grew compared to 2011. Demand growth in Europe, however, was impacted by lower road diesel consumption and the increasing use of raw materials applicable for double counting in fulfilling biofuel mandates.

Vegetable oil price spreads continued to be very volatile in 2012. Palm oil prices rose during the early part of the year due to increased palm oil demand resulting from a poor soy bean crop in South America. The price differential between rapeseed oil and palm oil narrowed to well below long-term average levels before widening again during the second half as palm oil production grew and demand declined. Towards the end of the year, the growth in palm oil production exceeded expectations and inventory levels increased, which reduced palm oil prices further.

European FAME biodiesel margins began the year positively, but became negative as overcapacity led to low sales prices. Further pressure was put on FAME profitability by biodiesel imports from Argentina and Indonesia, as well as the increased use of double countable waste and residue feedstock, such as used cooking oil. European FAME producers' margins recovered in the fourth quarter, as biofuel imports are limited in the winter season due to stricter cold property requirements.

In the US, the Renewable Identification Number (RIN) market price has been an important driver of biofuel profitability. RIN prices declined gradually during 2012 and significantly at the end of the third quarter, which was interpreted as resulting from the growing supply of local biodiesel. The reintroduction of a blender's credit was approved as part of the Fiscal Cliff negotiation compromise, and is expected to impact the US biofuel market positively in 2013. The US Environmental Protection Agency (EPA) raised the biomass-based diesel mandate by 28% from 1.00 to 1.28 billion gallons a year for 2013.

#### Key drivers

	2012	2011
Reference refining margin, USD/bbl	7.39	4.37
Neste Oil total refining margin*, USD/bbl	10.17	8.76
Urals-Brent price differential, USD/bbl	-1.29	-1.71
NWE Gasoline margin, USD/bbl	13.16	7.41
NWE Diesel margin, USD/bbl	20.60	18.12
NWE Heavy fuel oil margin, USD/bbl	-12.92	-15.96
Brent Dated crude oil, USD/bbl	111.58	111.27
USD/EUR, market rate	1.28	1.39
USD/EUR, hedged	1.33	1.35
Crude freights, WS points (TD7)	91	104

\* Adjusted according to the updated comparable operating profit calculation method

Review by the Board of Directors ► Production and sales

## Production and sales

### Production

Neste Oil's production totaled 15.4 million tons (15.0 million) in 2012, of which 1.8 million tons (0.7 million) took the form of NExBTL renewable diesel. Despite a major maintenance

turnaround at the Naantali refinery and production interruptions on diesel production line 4 at Porvoo in the spring, output increased compared to 2011, reflecting increasing volumes from the Singapore and Rotterdam renewable diesel refineries.

#### Neste Oil's production\*, by plant

(1,000 t)	2012	2011
Porvoo refinery	11,511	11,761
Naantali refinery	1,908	2,264
NExBTL refineries	1,849	682
Bahrain VHVI plant (Neste Oil's share)	128	45
Beringen polyalphaolefin plant	-	43
Edmonton iso-octane plant (Neste Oil's share)	8	191

\* Adjusted to include only products refined for sales

The Porvoo refinery operated at an average capacity utilization rate of 87% (86%) in 2012, impacted mostly by maintenance work carried out on production line 4 during the second quarter of the year. Capacity utilization at Naantali was 67% (85%), affected by the major maintenance turnaround there during the second quarter as well as other maintenance work during the second half of the year.

The proportion of Russian Export Blend (REB) in Neste Oil's total refinery input at Porvoo and Naantali averaged 63% (66%) in 2012. Production costs at the Porvoo and Naantali refineries totaled USD 4.4/bbl (4.3) for the year as a whole.

Production at the renewable diesel refineries achieved an average capacity utilization of 85% in 2012.

### Sales

Total sales in 2012 increased by almost 3%, mostly due to higher NExBTL volumes. Diesel sales increased towards end of the year, but were still lower than in 2011, while gasoline sales remained steady throughout the year. Exports exceeded domestic sales in 2012.

#### Neste Oil's sales from in-house production, by product category

(1,000 t)	2012	%	2011	%
Motor gasoline	4,281	27	4,143	27
Gasoline components	19	0	209	2
Diesel fuel	5,886	38	6,007	39
Jet fuel	651	4	763	5
Base oils	394	3	332	2
Heating oil	229	1	199	1
Heavy fuel oil	1,171	7	1,007	7
LPG	262	2	361	2
NExBTL renewable diesel	1,665	11	628	4
Other products	1,172	7	1,636	11
Total	15,729	100	15,284	100



**Neste Oil's sales from in-house production, by market area**

(1,000 t)	2012	%	2011	%
Finland	7 104	45	7 893	52
Other Nordic countries	2 563	16	2 618	17
Other Europe	4 232	27	2 988	20
USA & Canada	1 247	8	1 591	10
Other countries	583	4	194	1
Total	15 729	100	15 284	100

Review by the Board of Directors ► Segment reviews

## Segment reviews

Neste Oil's businesses are grouped into four reporting segments: Oil Products, Renewable Fuels, Oil Retail, and Others.

**Oil Products**

	2012	2011
Revenue, MEUR	13,764	12,644
Comparable EBITDA, MEUR	583	463
Comparable operating profit, MEUR	396	271
IFRS operating profit, MEUR	491	373
Total refining margin, USD/bbl	10.17	8.76
Net assets, MEUR	2,252	2,228
Comparable return on net assets, %	16.6	11.4

Oil Products' full-year comparable operating profit for 2012 amounted to EUR 396 million, compared to EUR 271 million in 2011. This improvement was largely due to a higher total refining margin. Base Oil's full-year profit contribution was lower than in

2011. Neste Oil's total refining margin totaled USD 10.17/bbl in 2012, which compares to USD 8.76/bbl in 2011. Fixed costs in refining operations were similar to those in 2011. Oil Product's comparable return on net assets was 16.6% (11.4%) in 2012.

**Renewable Fuels**

	2012	2011
Revenue, MEUR	2,163	1,026
Comparable EBITDA, MEUR	43	-85
Comparable operating profit, MEUR	-56	-163
IFRS operating profit, MEUR	-183	-170
Net assets, MEUR	1,860	1,963
Comparable return on net assets, %	-2.8	-8.7

Renewable Fuels' comparable operating profit was EUR -56 million in 2012, compared to EUR -163 million in 2011. Sales volumes in 2012 were more than 1 million tons higher than in 2011. New renewable diesel markets such as the US were opened up, and the customer base was expanded. The segment's result was negatively impacted for most of the year by low margins due to narrow vegetable oil price differentials and

the low margins of FAME biodiesel producers. These margin-related factors improved by the fourth quarter. Another factor impacting Renewable Fuels' result is the comparatively high price of natural gas in Singapore. This has increased utility costs, which are the subject of development work at the site. Renewable Fuels' comparable return on net assets was -2.8% (-8.7%) in 2012.

## Oil Retail

	2012	2011
Revenue, MEUR	4,895	4,298
Comparable EBITDA, MEUR	91	89
Comparable operating profit, MEUR	58	57
IFRS operating profit, MEUR	58	58
Net assets, MEUR	345	326
Comparable return on net assets, %	17.3	17.6
Total sales volume*, 1,000 m <sup>3</sup>	4,160	3,982
- gasoline station sales, 1,000 m <sup>3</sup>	1,256	1,279
- diesel station sales, 1,000 m <sup>3</sup>	1,620	1,479
- heating oil, 1,000 m <sup>3</sup>	651	654
- heavy fuel oil, 1,000 m <sup>3</sup>	255	263

\*includes both station and terminals sales

Oil Retail posted a full-year comparable operating profit of EUR 58 million compared to EUR 57 million in 2011. Overall sales volumes increased, but margins varied between different markets. The situation in the Baltic countries improved compared

to 2011, while Finland was clearly more competitive in 2012. Oil Retail's comparable return on net assets was 17.3% (17.6%) in 2012.

Review by the Board of Directors ► Shares, share trading, and ownership

## Shares, share trading, and ownership

Neste Oil's shares are traded on NASDAQ OMX Helsinki Ltd. The share price closed the year at EUR 9.77, up by 25.1% compared to the end of 2011. At its highest during 2012, the share price reached EUR 11.11, while at its lowest the price stood at EUR 7.28. Market capitalization was EUR 2.5 billion as of 31 December 2012. An average of 1.0 million shares was traded daily, representing 0.4% of the company's shares.

Neste Oil's share capital registered with the Company Register as of 31 December 2012 totaled EUR 40 million, and the total number of shares outstanding was 256,403,686. The company does not hold any of its own shares, and the Board of Directors has no authorization to buy back company shares or issue convertible bonds, share options, or new shares.

As of the end of the year, the Finnish State owned 50.1% (50.1% at the end of 2011) of outstanding shares, foreign institutions 15.4% (19.4%), Finnish institutions 20.0% (16.8%), and Finnish households 14.5% (13.7%).

As of the end of 2012, members of the Board of Directors and the Neste Executive Board and its secretary owned a total of 82,724 Neste Oil shares, which represents 0.03% of outstanding shares, either directly, through organizations in which those concerned have a controlling interest, or in their capacity as trustees.

**Largest shareholders as of 31 December 2012**

Shareholder	Shares	%
Prime Minister's Office	128,458,247	50.10
Ilmarinen Mutual Pension Insurance Company	6,051,486	2.36
Varma Mutual Pension Insurance Company	4,128,970	1.61
The Social Insurance Institution of Finland, KELA	2,648,424	1.03
The State Pension Fund	2,540,000	0.99
The City of Kurikka	1,550,875	0.60
Mutual Insurance Company Pension-Fennia	1,212,000	0.47
Danske Fund Finnish Institutional Equity	1,125,000	0.44
Wipunen varainhallinta Oy	1,000,000	0.39
Nordea Fennia Fund	990,000	0.39
OP-Delta Fund	940,000	0.37
Mandatum Life Unit -Linked	877,156	0.34
OP Life Assurance Company Ltd	752,459	0.29
Schweizerische Nationalbank	751,050	0.29
The Local Government Pensions Institution	746,705	0.29
Danske Fund Finnish Equity	713,703	0.28
OP-Finland Value Fund	690,000	0.27
Sijoitusrahasto Taalaritehdas Arvo Markka Osake	550,000	0.21
Mariatorp Oy	550,000	0.21
SEB Gyllenberg Finlandia Fund	526,250	0.21
20 largest owners total	156,802,325	61.15
Nominee registrations	37,849,801	14.76
Others	61,751,560	24.08
Number of shares, total	256,403,686	100.00

**Breakdown of share ownership as of 31 December 2012**
**By the number of shares owned**

No. Of shares	No. of shareholders	% of shareholders	No. Of shares	% of shares
1–100	25,914	33.3	1,492,082	0.6
101–500	33,808	43.5	8,676,897	3.4
501–1,000	9,301	12.0	7,217,415	2.8
1,001–5,000	7,534	9.7	15,560,970	6.1
5,001–10,000	644	0.8	4,688,611	1.8
10,001–50,000	406	0.5	8,144,987	3.2
50,001–100,000	50	0.1	3,649,115	1.4
100,001–500,000	63	0.1	13,295,402	5.2
Over 500,000	24	0.0	193,678,207	75.5
<b>Total</b>	<b>77,744</b>	<b>100.0</b>	<b>256,403,686</b>	<b>100.0</b>
of which nominee registrations	16		37,849,801	14.8

## By shareholder category

	% of shares
State of Finland	50.1
Non-Finnish shareholders	15.4
Households	14.5
General government	8.2
Financial and insurance companies	5.2
Corporations	4.3
Non-profit organizations	2.3
Total	100.0

Review by the Board of Directors ► Corporate governance

## Corporate governance

The control and management of Neste Oil Corporation is divided between shareholders, the Board of Directors, and the President & Chief Executive Officer. The General Meeting of Shareholders appoints the Board of Directors based on a proposal made by the AGM's Nomination Board. The term of office of the Board of Directors will expire at the end of the next Annual General Meeting following its election. A person who has reached the age of 68 cannot be elected to the Board of Directors. Neste Oil's President & CEO is appointed and expelled by the Board of Directors.

Changes to the company's Articles of Association can be made at the General Meeting of Shareholders based on a proposal by the Board of Directors.

Neste Oil's Annual General Meeting (AGM) was held on 28 March 2012 in Helsinki. The AGM adopted the company's financial statements and consolidated financial statements for 2011 and discharged the Supervisory Board, the Board of Directors, and the President & CEO from liability for 2011. The AGM also approved the Board of Directors' proposal regarding the distribution of the company's profit for 2011. A dividend of EUR 0.35 per share was paid on 11 April 2012.

In accordance with the proposal made by the AGM Nomination Board, the AGM confirmed the membership of the Board of Directors at seven members, and the following were re-elected to serve until the end of the next AGM: Mr Michiel Boersma, Mr Jorma Eloranta, Ms Maija-Liisa Friman, Ms Nina Linander, Ms Laura Raitio, Mr Hannu Ryöppönen, and Mr Markku Tapio. Jorma Eloranta was elected as Chair and Maija-Liisa Friman as Vice Chair. The AGM decided to keep the remuneration paid to Board members unchanged.

Convening after the Annual General Meeting, the Board of Directors elected the members of its two Committees. Jorma Eloranta was elected Chair and Maija-Liisa Friman and Markku Tapio as members of the Personnel and Remuneration Committee. Nina Linander was elected Chair and Michiel Boersma, Laura Raitio, and Hannu Ryöppönen as members of the Audit Committee.

In accordance with a proposal by the Board of Directors, Ernst & Young Oy, Authorized Public Accountants, were appointed as the company's Auditor, with Authorized Public Accountant Anna-Maija Simola as Senior Auditor, until the end of the next AGM. Payment for their services will be made in accordance with their invoice.

Following a proposal by the Prime Minister's Office, representing the Finnish State, the AGM decided to establish an AGM Nomination Board to prepare proposals covering the members of the Board of Directors and their remuneration for consideration by the next AGM. The Nomination Board comprises representatives of the Company's three largest shareholders and also includes, as an expert member, the Chair of the Board. In 2012, the Nomination Board comprised Senior Financial Counselor Jarmo Väisänen of the Ownership Steering Department at the Prime Minister's Office; Timo Ritakallio, Deputy CEO, Ilmarinen Mutual Pension Insurance Company; and Mikko Koivusalo, Director, Investments, Varma Mutual Pension Insurance Company. The Chair of Neste Oil's Board of Directors, Jorma Eloranta, served as the Board's expert member.

Neste Oil's Corporate Governance Statement is issued as a separate document.

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Review by the Board of Directors ► Personnel

## Personnel

Neste Oil employed an average of 5,031 (4,926) employees in 2012, of which 1,450 (1,427) were based outside Finland. As of the end of 2012, the company had 5,022 employees (4,825), of

which 1,474 (1,407) were located outside Finland. Wages and salaries paid by the company totaled EUR 253 million (240 million) in 2012.

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Review by the Board of Directors ► Health, safety, and the environment

## Health, safety, and the environment

Neste Oil's focus on safety continued in 2012, with the main emphasis on people and process safety. The year's achievements included implementation of 12 safety elements and self-assessments at all business units. This work will continue in 2013, with detailed action plans at site level. Overall safety performance declined in 2012, however. The total recordable injury frequency (TRIF, number of cases per million hours worked) was 3.6 (2.7); this figure combines the company's own and contractors' personnel. The corporate target was 2.0. The method used for calculating TRIF was adjusted in 2012 to exclude off-duty hours at Shipping. In general, the severity of injuries has decreased. The record-low frequency of lost workday injuries – 1.5 (1.9) – was very positive. Process Safety Events (PSE) frequency in 2012 was 5.6 (4.8). Substantial efforts were made to improve working practices at heights. Over 800 people were trained in this high-risk area and new working guidelines were implemented across the Group for both Neste Oil and contractor personnel.

Operational environmental emissions were in substantial compliance at all sites. Permitted levels were exceeded four times, once at Porvoo and Singapore and twice at Naantali. No serious environmental incidents resulting in liability occurred at Neste Oil's refineries or other production facilities in 2012, with the exception of the accidental release of diesel-class fuel at a third-party terminal operated by Neste Oil in Kajaani in April.

Neste Oil has received emission rights for 3.2 million tons of CO<sub>2</sub> emissions per year between 2008 and 2012, and has acquired further rights from the market to cover the deficit between its allocated rights and verified emissions. The verification of emissions for 2012 is scheduled, and Neste Oil will be able to report and surrender allowances equal to its total emissions in 2013. Neste Oil has used rights received from clean development mechanisms to help meet its requirements.

The European Renewable Energy Directive (RED) was still being implemented in some EU member states as of the end of 2012. Neste Oil's internal procedures have been updated to meet the directive's requirements, and the company has filed a voluntary scheme for verifying the sustainability of its biofuels with the EU. All of Neste Oil's NExBTL plants have received International Sustainability and Carbon Certification (ISCC) system certificates, ensuring that their output is eligible for use on the European biofuel market. All Neste Oil sites are also EPA-approved for the US market.

Neste Oil retained its position in a number of sustainability indexes during 2012, and was included in the Dow Jones Sustainability World Index for the sixth year in succession, for example. It was also selected for inclusion in The Global 100 list of the world's most sustainable companies for the sixth year in succession, and was ranked 19th. Neste Oil was also rated among the top performers in the oil & gas sector by the Forest Footprint Disclosure Project, which reviews industries using forest risk commodities, and was included in the STOXX® Global ESG Leaders Index and featured in the Ethibel EXCELLENCE Investment Register in 2012, as well as the new Storebrand Trippel Smart and SPP Global Topp 100 fund.

In January 2013, after the reporting period, Neste Oil was selected for inclusion in The Global 100 list for the seventh year in succession and ranked 4th. Companies selected for inclusion in The Global 100 are considered the most capable in their sectors in managing environmental, social, and governance issues, and in their ability to make use of new business opportunities in these areas.



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Review by the Board of Directors ► Research and development

## Research and development

Research and development focusing on both crude oil-based and renewable fuels is crucial in implementing Neste Oil's strategy. Neste Oil's R&D expenditure totaled EUR 42 million (42 million) in 2012. An additional approx. EUR 8 million was invested in a microbial oil pilot plant commissioned in the fall. Extending the company's raw material base is one of the main goals of Neste Oil's R&D work. Around 70% of annual R&D expenditure goes to research into renewable raw materials. Research work is focused on both completely new types of raw materials, such as microbes and algae, and existing materials, such as used cooking oil and technical corn oil.

Neste Oil focused on expanding the use of waste- and residue-based feedstock, particularly animal fat and palm fatty acid distillate (PFAD), in 2012. Inputs coming from waste and residues increased by over 400,000 tons to 742,000 tons and accounted for approx. 35% (40%) of total renewable feedstock usage in 2012. Neste Oil's goal is to increase this volume further. Palm oil accounted for 65% (53%) of all the raw materials used in renewable diesel production in 2012.

Neste Oil's R&D personnel also played a key role in the launch of Neste Pro Diesel, the outcome of an in-house R&D project.

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Review by the Board of Directors ► Events after the reporting period

## Events after the reporting period

On January 28, Neste Oil announced that Neste Shipping will start an efficiency improvement program aimed at improving its profitability and securing the continuity of its operations. As part of the efficiency improvement program, statutory employer-employee negotiations will be started and will cover all Neste Shipping's land- and sea-based personnel in Finland, around 450 people in total. The negotiations could result in a maximum of 130 people being made redundant. The goal of the efficiency improvement program is to make the business profitable by increasing revenue and reducing costs by a total of around EUR 15 million annually.

On February 4, Neste Oil announced that it will build an isomerization unit at its Porvoo refinery. The investment, valued at approx. EUR 65 million, is intended to increase the output of high-octane gasoline and improve refining flexibility at the site. Neste Oil took the initial decision to make the investment in 2008, but announced in 2009 that it would postpone the project until the market situation improved. Neste Oil believes that the demand for cleaner fuels, such as high-octane, low-sulfur gasoline, is continuing to grow globally.

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Review by the Board of Directors ► Potential risks

## Potential risks

The oil market has been and is expected to continue to be very volatile. Oil refiners are exposed to a variety of political and economic trends and events, as well as natural phenomena that affect the short- and long-term supply of and demand for the products that they produce and sell.

Uncertainty continues to be focused on the development of the world economy, which is likely to have a material impact on the demand for petroleum products generally and diesel fuel in particular.

Sudden and unplanned outages at Neste Oil's production units or facilities continue to represent a short-term operational risk.

Rapid and large changes in feedstock and product prices may lead to significant inventory gains or losses, or changes in working capital, and may have a material impact on the company's IFRS operating profit and net cash from operations.

The implementation of biofuel legislation in the EU and other key market areas may influence the speed at which the demand for these fuels develops. Risks also include any problems or delays in capturing the anticipated benefits from the company's

renewable diesel investments. Over the longer term, failure to protect Neste Oil's proprietary technology or the introduction and implementation of competing fuel technologies or hybrid and electric engines may have a negative impact on the company's results. Renewable fuels margins can be volatile in various markets due to rapidly changing feedstock and product prices, and affect the profitability of the Renewable Fuels business as a result.

Over the longer term, access to funding and rising capital costs, as well as challenges in procuring and developing new competitive and reasonably priced raw materials, may impact the company's results.

The key market drivers for Neste Oil's financial performance are refining margins, the price differential between Russian Export Blend (REB) and Brent crude, the USD/EUR exchange rate, and the price differentials between different vegetable oils.

For more detailed information on Neste Oil's risks and risk management, please refer to the company's Annual Report and Financial Statements.

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Review by the Board of Directors ► Risk management

## Risk management

Neste Oil recognizes that risk is an integral and unavoidable component of its business and is characterized by both threat and opportunity. Neste Oil uses risk management in order to enhance opportunities and reduce threats, thus gaining competitive advantage. Risk management is a central part of Neste Oil's management system, and its importance has only grown as the company has moved ahead with its major projects and as turbulence has continued in the global economy. Neste Oil aims to manage the impact of risks on its operations through a range of risk management strategies. The Corporate Risk Management Policy and Principles approved by the Board of Directors define the principles to be used for managing the risks associated with the strategic and operational targets of the Group as a whole and its business areas and common functions.

Business areas and common functions have additional principles, instructions, and procedures related to risk management, approved by the President & CEO.

Risk management in the area of strategic and operational management aims at recognizing risks on a rolling basis, assessing and prioritizing them on a consistent basis, and managing them proactively.

For more detailed information on Neste Oil's risks and risk management, please refer to the company's Corporate Governance Statement, which has been published as a separate document, and to the note 3 of Financial Statements for 2012.

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Review by the Board of Directors ► Outlook

## Outlook

Uncertainties in the global economy have been reflected in the oil, renewable fuel, and renewable feedstock markets and this volatility is expected to continue. Global oil demand is generally forecasted to grow moderately in 2013, but new refining capacity is likely to put pressure on simple refineries. Complex refiners such as Neste Oil, are expected to remain the most competitive. Diesel is projected to be the strongest part of the barrel going forward, and gasoline margins are expected to improve seasonally by summer. The base oil market is likely to be under pressure due to sluggish demand in the automotive industry. The renewable fuels market is based on biofuel regulations, and biofuel demand is expected to continue growing. Vegetable oil price differentials are expected to vary, depending on crop outlooks, weather phenomena, and variations in demand for different feedstock.

Production line 4 at the Porvoo refinery is scheduled to be shut down for maintenance for up to eight weeks starting in the second quarter. The shutdown includes a four-week regulatory pressure vessel inspection. No other major oil refinery maintenance is planned for 2013.

Renewable Fuels' full-year comparable operating profit is expected to improve from that seen in 2012 and be positive. The result will depend on market volatility and successful sales allocations. The average margin hedging ratio used in Renewable Fuels is currently clearly lower than in 2012. A shutdown of three weeks at the Singapore NExBTL refinery due to a utility supplier's maintenance work in January will reduce the sales volumes in the first quarter.

The Group's investments are expected to total approx. EUR 300-350 million in 2013.

The Group's full-year comparable operating profit is expected to improve compared to 2012, assuming that Neste Oil's reference refining margin remains at the average level of approx. USD 5/bbl typical of the last few years and that Renewable Fuels' result will develop as expected.

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Review by the Board of Directors ► Dividend distribution proposal

## Dividend distribution proposal

The parent company's distributable equity as of 31 December 2012 amounted to EUR 1,035 million, and there have been no material changes in the company's financial position since the end of the financial year. The Board of Directors will propose to

the Annual General Meeting that Neste Oil Corporation pays a cash dividend of EUR 0.38 per share for 2012, totaling EUR 97 million based on the number of registered shares as of 4 February 2013.