

Business Principles

Progress Report 2012



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Editorial comment.

Thank you!

At this time last year we requested input to help update our Business Principles. I would like to thank everyone who contributed. The major changes to the Business Principles are described in the 2012 Sustainability Report section of the Annual report.

The most significant change is the incorporation of the “Protect, Respect and Remedy” concept of the United Nations Guiding Principles on Business and Human Rights which is also reflected in the 2011 revision of the OECD Guidelines for multi-national enterprises.

More words but the same meaning?

At face value the changes to our Business Principles look rather subtle and many of our employees could well say “It’s the same thing but with more words!”. In some respects they would be correct, except that the “more words” are rather significant.

The “Protect, Respect and Remedy” concept is a significant change for all multi-national enterprises: We are now expected to conduct our human rights risk assessments based on the risk of contributing to human rights abuses throughout our value chain. Previously, risk assessment has been done in relation to the risk to our business, our brand and people in our direct business relationships. The new concept will move us to consider some human rights impacts that we have not considered before. We describe how we have made a tentative start to this in the social section of this report.

Are we mature enough for the Protect, Respect and Remedy approach?

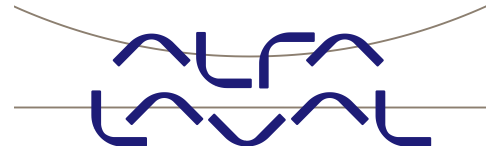
In a couple of areas of this report you will find that our lack of progress of implementing our existing Business Principles tells us that we face a challenge if we are to reach our aspirations of the Protect, Respect and Remedy approach.

However, the positive engagement of everyone in the revision process of our Business Principles gives us a fantastic starting momentum.

David Ford, Corporate Social Responsibility, Alfa Laval.

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1.0 About this report.

Alfa Laval's Business Principles form the basis for our work on Sustainability.

The [Sustainability Report](#) within the Alfa Laval Annual Report 2012 gives a summary of some of the sustainability highlights for the Group.

This report supplements the Annual Report with additional information about key initiatives in 2012. It should be read together with our [GRI \(Global Reporting Initiative\) Sustainability Report](#). Each paragraph in this report is cross referenced with the most relevant section of the GRI report.

In 2012, to make this report shorter, we have moved some repetitive explanations to the GRI report and tried to focus on our key targets and topical subjects.

The three reports together, (Sustainability Report, Progress Report and GRI report) represent the Annual Communication of Progress required by being a member of the UN Global Compact.

2. Environment Progress 2012

2.01 New key environmental goals.

During 2012 we announced new key targets:

Key Environmental targets for workshop units (baseline 2011, target 2015)

- Improve energy efficiency by 12%
- Reduce water consumption by 20%
- Reduce restricted "grey" chemicals usage by 50%.

In addition, Manufacturing units must:

- Reduce Greenhouse gas from freight transportation by 12%

2.02 We sharpen our focus on the "Vital Few"

With 137 (132) reporting units in our Environmental Management system, reporting on over 25 lines of environmental data it is easy to lose track of the major environmental impacts of our operations. It becomes particularly difficult when the reporting units may vary each year through acquisitions, the opening of new sites, closures, relocations and mergers.

If one wishes to follow the development of our environmental performance the consolidated environmental data at group level becomes rather meaningless with such regular structural change. For example we are trying to identify relatively small energy savings in the order of 3 to 5% each year whilst our production volumes of different products may vary by more than this at the same time.

To try to follow our environmental progress in a more meaningful way, we have selected the 23 manufacturing sites that, combined, accounted for over 85 percent of our manufacturing energy consumption in 2011. All of these sites are certified for ISO14001. These sites have a critical mass that means their environmental performance will not fluctuate significantly if there are small

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changes of production volume or product mix. Hopefully, over the four year period of our targets (2012-2015) this will give us a clearer picture of our achievements. We are calling these sites our “Vital Few” manufacturing sites

The environmental section of the GRI report is thus changed in 2012 with two tables of environmental data: One shows the “Vital Few” 23 sites; the other is a consolidation of all the other sites with workshops.

Because of these changes, historic information prior to 2011 has been dropped but can be found in the archive GRI reports.

2.03 Our targets apply to all sites which have a workshop

Even though we focus on the “Vital Few” sites from a reporting point of view, the environmental targets apply to every site that has a workshop. Notably, the service workshops all have similar environmental impacts and we have corporate level resources to help these small sites focus and improve on the most significant impacts (mainly water, energy and chemical consumption).

2.04 Acquisitions are included in Table 2 “Other sites with workshops”.

When we include acquisitions into our GRI report the data will appear in the Table: “Other Sites with Workshops”. Acquisitions are required to report their full environmental indicators within three years of their acquisition.

2.05 Please take care when making conclusions from our environmental reports.

Each table in our GRI report describes which organisations are covered by each data table. Users are advised not to add the data from each table together to compare one year with another; the data does not necessarily relate to the same organisations and so conclusions drawn may not be valid.

Our financial figures will always have total sales data accurately for the whole enterprise including recent acquisitions whilst the energy data from acquisitions may not be included for up to three years. Thus, in our opinion, using ratios such as Tonnes of GHG per Million Euro of sales tends to make our environmental performance look better than it really is and so we discourage such a methodology.

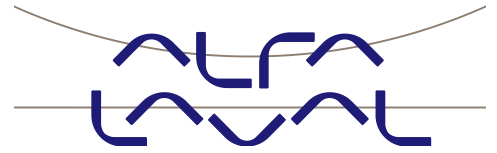
2.1 Environmental Progress in the “Vital Few” manufacturing units:

2.1.1 Focus to eliminate hazardous chemicals (M-EN1) .

All manufacturing and workshops sites in Alfa Laval are required to have careful control of all substances used in their processes and must have product safety data sheets available at the place of work. The product safety data sheets must be scrutinised to identify whether the substance appears on the “Black or Grey list”. The list is continuously updated and 149 changes were included in 2012 (49 in 2011). The changes in 2012 included 57 substances being added to the “Black” list.

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During 2012 the amount of “Black” chemicals increased to 1 070 kg (993) mainly due to the increased number of substances added to the list in 2012. These chemicals were present in 5 (3) out of the 23 sites in 2012.

Our target is to replace “Black” substances with alternatives within 3 years of identifying the chemical. However, three production processes still use substances from the black chemical list even after the three year period. Extensive work has been conducted to try to find alternative substances and alternative production processes but without success. These substances are essential in a particular production process (which is a common process in the relevant industrial sector and believed to be used by our competitors). The substances have known health risks and so employees working with these substances are protected and trained in how to deal with the substances safely. The substances are not present in the finished product.

We aim to cut the use of potentially hazardous “grey” chemicals by 50% between 2011 and the end of 2015. The amount reported increased in 2012 to 20 500kg (9 900) in 2012. This was partly due to additional substances on the list, but also because some sites were better at identifying the chemicals.

2.1.2 Direct and Indirect Energy Consumption: Early days for our new target but project pace still has to be raised (M-EN3 M-EN4).

In 2012 we published new environmental targets (see para 2.01 above). After one year of the four year target period it is too early to see if we are on track to reduce our energy consumption.

2.1.3 Environmental impact from new products continues to be reduced. (M-EN6)

In 2012 the environmental impact of 21 (26) new product development projects were assessed using the Life Cycle Assessment (LCA) method that we have used since 2007. Of the 21 assessed 8 (14) were replacements of existing products, 4 (13) had a lower environmental impact than the product replaced; no new product had a higher environmental impact.

The new CB110 heat exchanger, for example, has approximately 30% lower environmental impact than the product it replaces. The optimized heat transfer surface design has a higher thermal efficiency as well as a lower pressure drop (which means the power consumption of the pump required in the customer process will be lower); resulting in less raw material used, and the finished product takes less space in the customers process line.

2.1.4 Water consumption reduced but too early to tell if this trend will continue (M-EN8).

In 2012 Alfa Laval used 10% less water in the production processes than in 2011. However, it should be noted that consumption in 2011 was 6% higher than in 2010 due to some leaks and a failed cooling system both of which have now been repaired.

2.1.5 Total Direct and Indirect Greenhouse Gas emissions (GHG) by weight: (M-EN16)

Nearly all the GHG from our production processes are from energy use of which roughly 70% is indirect energy (electricity and district heating). Our environmental targets focus on efficiency improvements in both direct and indirect energy which will have a consequential improvement on our related GHG emissions.

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Our “Vital Few” factories account for approximately 40 000 tonnes of CO₂-e. However 45 % of the electricity consumption of these sites is in France and Sweden. Both these countries have globally low levels of GHG emission from electricity generation (77 and 22 grammes per kWh respectively according to the 2012 IEA emission factors).

In the future, we can expect proportionally more production to be in China and India as those (already large) markets continue to grow. These countries have globally high emissions factors for electricity generation (790 and 936 grammes per kWh respectively). Consequently we can expect our GHG emissions (from production processes) to increase. We can see this effect when comparing 2012 data with 2011 where total energy consumption fell by 8.1% (from 146 825 to 134 874MWh) but GHG emissions from energy consumption dropped by only 3.3% (from 41 340 to 39 937 tonnes CO₂-e).

However, increased production emissions will be partially offset by a reduction of emissions from transporting imported goods into these countries and it is worth noting that our total GHG from goods transportation is very similar to the amount from our in-house production processes.

2.1.6 Significant environmental impacts of transporting products and other goods and materials used for the organisation's operations (M-EN29 (goods)).

Total emissions from goods transportation in 2012 was 47 217 tonnes CO₂. (50 720). Emissions per tonne of shipped weight per kilometer travelled was 108.2g/tonnekm. (110.3). When we started to focus on this issue in 2007 the rate was 115,8 g/tonnekm.

2.1.7 We also focus on our suppliers. (EI-2)

In 2012; approximately 69% (67%) of purchased value was from suppliers that have ISO14001 certification (or equivalent). Our target is that 80% of our suppliers will be certified by the end of 2015.

2.2 Environmental Management Progress in “Other Sites with Workshops”:

2.2.1 More sites submit environmental reporting (O-EN0)

The data from sites 114 (109) is consolidated in the “Other Sites with Workshops” GRI report. However, because several of the sites will be different from year to year (acquisitions; closures; mergers) it is not particularly useful to compare the consolidated data year-on-year.

76 of these sites are service and repair workshops. Typically they employ 15 or fewer people and it is therefore not realistic to expect them to submit detailed environmental measurements. Our focus is to help them conserve water and energy whilst protecting themselves and the environment from pollution risks.

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3.0 Social Progress 2012

3.1 Significant suppliers have undergone screening on human rights but change is taking too long. (HR 2).

One of our highest priorities is to improve our knowledge of the health and safety, labour conditions and the working environment of our suppliers' employees in countries and industries of high risk. Where the standards need to be improved we are committed to influence the supplier to make changes.

We started this work in 2004 and we felt we were making reasonable progress with over 200 suppliers in India and China included in this process.

However, following our own critical review, we have come to a disappointing realization that the improvements are not happening fast enough. In particular in China, we still find suppliers whose management have an unacceptably low respect for their workers' rights to a fair wage, clean and safe working environment even after repeated audits and reminders.

What hampers the progress?

China is Alfa Laval's second largest market in the World, we still import more goods to China than we export. We are continuing to invest heavily in China both with new factories and acquisitions. In short, the Chinese market is fast moving and relentless.

It is not easy to secure the supply of the high quality components that we need because the market is very competitive and the supplier base for engineered products is not growing as fast as the demand.

Under-supply and over-demand means that our influence over the supplier is not as great as we need to drive improvements in working conditions. It seems that if our share of a supplier's business is lower than around 15%, many suppliers will repeatedly fail to deliver promised changes.

We sometimes find it difficult to move the business away from these suppliers because we do not find enough technically qualified alternatives.

Our competitors (local and international) are also present in some of our suppliers, but since they may be less active with supply chain social development processes the suppliers believe they can ignore our demands with impunity.

The regulatory authorities are not yet effective in enforcing the law, either through lack of resources, training or the desire to challenge companies that are contributing economic growth.

What we will do about this:

The problems are complex and so we will undertake a review of our approach to suppliers' compliance with our Business Principles during 2013. Our revised Social Business Principles are a further spur to greater action.

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3.2 Group Management take part in an awareness exercise on “Protect Respect Remedy”.

As a part of the introduction of the revised Business Principles, the Group Management undertook an awareness exercise according to our strengthened Human Rights Principles. This consisted of a short workshop in which the management team had to identify the highest risks of complicity in human rights abuses in our supply chain, our own operations and in doing business with our customers.

This allowed them to think about and practice working according to the risk assessment principles of the UN Guiding Principles on Business and Human Rights and our new Business Principles and to experience the ethical dilemmas that this could raise.

It is anticipated that the methodology used in the workshop will be further developed into a new human rights risk assessment process that could be implemented in the Group through the line management.

3.3 Rates of injury, occupational diseases, lost days, and absenteeism, and total number of work-related fatalities. (LA7)

- Total number of reportable accidents (including travel accidents): 205 (237)
- The number of accidents per million working hours: 8.40 (9,93)
- Days lost per million working hours due to accidents: 216 (357)
- Days lost through any form of illness as % working days: 2,02 (1,77)

Tragically, there was one fatal accident in 2012 when a worker fell from a mechanical hoist whilst working on a large fabrication project. A full investigation has been conducted and health and safety non-compliances were identified as contributing to the tragic incident. The over-riding conclusion was that although training, safety equipment and notices were correctly implemented a lack of appropriate supervision had allowed a dangerous situation to develop.

3.4 Near Misses in focus

We have been putting a focus on increasing the number of reported “near misses”. A “near miss” is when an incident occurs that, in other circumstances, could have been an accident. The number reported increased in 2012 by 21%, but several companies failed to report any. The identification of “near misses” is essential if corrective actions are to be taken before an accident occurs the lack of reporting indicated that we still have some training and safety awareness issues.

3.5 More focus on Human Rights Issues.

During 2012 Alfa Laval joined (as one of the founder members) the Swedish Network for Business and Human Rights. This is a group of Swedish companies who wish to share experience (good and bad) and best practice in the field of implementing the United Nations Guiding Principles on Business and Human Rights. Companies are cross-sector and the sessions have already included a speaker from a large electronics company from the USA. With so many companies in Sweden taking the Guiding Principles so seriously we are fortunate to have this

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opportunity to learn from others. This forum also provides a supportive environment in which we can discuss our dilemmas and obtain advice from fellow practitioners.

UNICEF have a vast experience of handling human rights issues relate to children. With the publication of the United Nations Global Compact Children's Rights and Business Principles in 2012 we are very pleased to participate in regular meetings where the implementation tools developed by UNICEF are presented and tested. This group consists of government officers, companies and NGO representatives and again provides a forum in which we can share experience and try to understand how we can use our role as a global company to help children in need.

4.0 Business Integrity Progress 2012

4.1 Anti-Bribery and Anti-Corruption (ABAC) initiatives come to the agenda.

We have conducted wide ranging anti-bribery and anti-corruption training in previous years.

To reinforce the implementation of the revised Business Principles it was decided that we would review our processes and implementation of ABAC activities during 2013. This led to the formation of a new body called the Commercial Ethics Council headed by the CEO

The responsibilities of the Commercial Ethics Council (CEC) includes Export Control matters, Group Policies on general compliance (including ABAC), the Fair Competition policy as well as providing guidance on the commercial implications of the Business Principles. The 2013 review of ABAC policies and procedures will therefore report to the Commercial Ethics Council (CEC).

5.0 Transparency Progress 2011

5.1 A special Sustainability Issue of our customer magazine HERE was published.

Issue 31 of our customer magazine Here was published during 2012. It highlights several of Alfa Laval's recent product developments and customer projects that have a specific focus on environmental protection and energy savings.

[Follow this link to the home page of Here Magazine.](#)

5.2 We received positive feedback on our sustainability report structure.

As a part of our stakeholder dialogue several SRI analysts who use our sustainability reports to make ratings were asked about our reporting.

In general the feedback was positive. In particular the ability to download the GRI and Progress Reports as files compared to having to extract information from different pages of a corporate web site was mentioned. On the flip side of this we scored poorly in reports that rate our use of web pages for communicating sustainability information.

Our "tell it as it is" approach to reporting also received favourable comments from some analysts.

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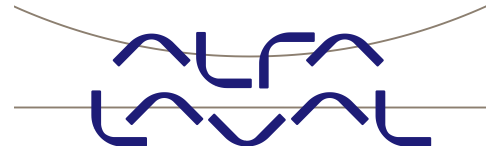
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On the negative side, we were told that we need to report more information on our social Business Principle and Human Rights activities. Hopefully this request will be better met when we report our progress of implementing the revised Business Principles with their stronger focus on Human Rights.

We are grateful to students who, during the year pointed out some omissions in the text of our GRI report.

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5.3 We continue our policy towards SRI Questionnaires.

From January 2011, Alfa Laval adopted a policy of no longer populating external databases nor completing other types of questionnaire about these matters (except customer questionnaires) and instead, refer people to this, our Annual Report and the GRI report.

Since adopting this policy in 2011 we have not received any adverse reactions, and we thank agencies for their understanding.

We are very pleased to comment on any draft reports that analysts produce based on our published information. Whilst we will not check these reports in detail, we will have the opportunity to point out any obvious factual errors, or obviously misunderstood qualitative information. Some analysts routinely send us a draft report prior to publishing.

5.4 We continue to meet interested external parties

Meetings with SRI analysts have continued in 2012 as in previous years. We are very pleased to meet SRI analysts: please contact david.ford@alfalaval.com or gabriella.grotte@alfalaval.com to arrange a meeting.

Students show a great interest in our Business Principles activities and there have been a number of student visits and discussions during 2012. Students can contact david.ford@alfalaval.com to arrange a meeting either by telephone or face-to-face.

CEO Statement of continued commitment to the Global Compact:

I am pleased to submit this Progress report and the associated sustainability report and GRI report as Alfa Laval's Annual Communication on Progress.

Alfa Laval is committed to continuing to make the UN Global Compact and its Principles an integral part of business strategy, day-to-day operations, and organizational culture.

Lars Renström
March 28th, 2013