Nordic Environment Finance Corporation

Annual Report 2012

Contents

This is a translation from the original Annual Report in Swedish. In the unlikely event of a disagreement in interpretation, meaning or otherwise, the original Swedish version shall prevail.

Report of the Board of Directors 2012

The dire state of the economy in Europe continued to affect the Corporation's operations. For NEFCO, it meant that a longer period of time was required for planning investments and that fewer projects were approved, even though the Corporation received more inquiries than ever before over the years. Consequently, general interest in the funding available from NEFCO remained high, suggesting that international financial institutions serve an important purpose even under less favourable conditions.

At the same time, overall interest in environmental investments among municipalities has increased. A number of municipal projects to build up district heating and water management capacity were identified for closer scrutiny during the reporting period. NEFCO possesses extensive experience in municipal environmental investments and the growing interest in Russia and Ukraine is perceived as an important positive development and a result of the cooperation and project support provided by the Northern Dimension Environmental Partnership (NDEP) in Russia and the Eastern European Energy Efficiency and Environment Partnership (E5P) in Ukraine.

The year was one of vigorous project activity. A total of 65 new projects were approved in 2012 by the various funds managed by NEFCO as compared to 66 the year before. The volume of new projects financed by the NEFCO Investment Fund fell to EUR 5.7 million while the corresponding figure for 2011 was EUR 13.5 million. However, the value of provisionally approved projects amounted to EUR 51.8 million, much higher than the 2011 level of EUR 28.7 million. At the end of 2012, there were 46 active projects financed by NEFCO's principal fund, the NEFCO Investment Fund, with total investments amounting to EUR 115.9 million. As disbursements are made with a certain delay, a larger proportion of NEFCO's resources was actually allocated than indicated in the statement of financial position.

Just like the operations of the Investment Fund, NEFCO's other main line of activity – fund management – was also successful. In June 2012, NEFCO signed an agreement with the USA on participation in the Project Support Instrument (PSI) to be administered by NEFCO on a mandate from the Arctic Council. A more detailed description of the fund scheduled to commence operations in 2013 is provided later in this report.

One of the Corporation's climate funds – the Baltic Sea Region Testing Ground Facility (TGF) – completed its primary investment phase with the expiry of the first commitment period under the Kyoto Protocol in 2012. The other climate fund, NEFCO Carbon Fund (NeCF), cut down on its investment activities drastically as a result of the weak market for emission reductions. While NeCF will continue to operate for several years to come, investments in new purchase agreements will most likely be limited and the fund will primarily focus on managing its existing agreements.

Three new funds were established and five dissolved during the reporting period. Swedish funding was made available for environmental projects in Russia; funding from the Northern Dimension Environmental Partnership (NDEP) for a wastewater project in Petrozavodsk, Russia; and funding from the Eastern Europe Energy Efficiency and Environmental Partnership (E5P) for financing an energy-efficient district heating demonstration project in Ukraine.

At the end of the year, NEFCO had 27 funds (excluding the Investment Fund) with total assets of EUR 346 million under management. NEFCO renders separate accounts for all these funds. The funds are not included in NEFCO's statement of financial position.

The financial result was modest, which was mainly due to the foreseen appropriation of EUR 1.5 million for NEFCO's contribution to the Nordic Environmental Development Fund (NMF). This was the last tranche of NEFCO's total commitment of EUR 5.75 million to the NMF fulfilled over the past three years. In all other respects, the net balance between capital gains and losses provided no surprises.

As expected, environmental performance during the reporting period was also sound compared to previous years. A more detailed account of environmental performance is presented in the annex.

NEFCO's area of operations was expanded during 2012 when the Board of Directors authorised NEFCO to commence operations in Moldova. Underlying this expansion was the decision of the Eastern Europe Energy Efficiency and Environmental Partnership (E5P) to intensify its efforts in the country. Cooperation within this E5P partnership is carried out by the European Investment Bank (EIB); the Nordic Investment Bank; the World Bank; and the European Bank for Reconstruction and Development (EBRD). E5P finances energy-efficiency and other environmental schemes funded by the Nordic and Baltic countries, the EU, the USA, Ukraine and, in 2013, by Moldova. NEFCO has held the presidency of the E5P management team as of July 2012.

Assessment of the environmental impact of projects

In line with the procedures developed over time by NEFCO, each project is assessed in terms of its expected environmental impact before a decision on financing is made, followed by a review of the actual effects upon completion of the project. The analysis of the

A total of 65 new projects were approved in 2012 by the various funds managed by NEFCO as compared to 66 the year before.

projects launched under both the Investment Fund and the Environmental Development Fund (presented below in greater detail) indicates that, on average, the positive environmental impacts are at the expected level. Of the 67 on-going projects assessed in terms of environmental impact, 15 were deemed to have exceeded expectations, 7 were at the expected level and 14 failed to meet expectations. In 30 cases, no conclusions could yet be drawn. Of all the analysed projects, 128 have been completed. A summary of the assessment is provided in an annex.

NEFCO also systematically assesses the environmental cost-effectiveness of projects in relation to the cost of attaining comparable levels of emission reductions in the Nordic countries. On average, the costs of NEFCO's projects are roughly one eighth of the corresponding project costs in the Nordic countries.

Investment Fund

In 2012, the Board of Directors approved four new investments plus one supplemental investment in a project approved earlier. In addition, 21 'expressions of interest' were approved signifying initial approval for further review.

During the year, NEFCO completed five projects: three concerned water management in Lithuania while the other two focused on oil collection and destruction equipment for Russia and the recovery of scrap metal in Poland. By the end of 2012, NEFCO had completed 68 projects to which it had contributed a total of EUR 75 million. Two projects were abandoned in the course of the year as they were no longer deemed to be capable of being implemented as planned.

As a result, 46 active projects approved by the Board remain with agreements signed on a total of 30. With regard to the outstanding 16 projects, negotiations and analyses are still underway. NEFCO's commitment to these 46 projects amounts to EUR 115.9 million with a total investment of approximately EUR 740 million, suggesting a major leverage effect. Thus, a larger share of NEFCO's resources is committed than the total investments of EUR 43.8 million (net after amortisation and depreciation) shown in the statement of financial position (balance sheet), indicating an increase relative to the EUR 33 million at the end of 2011.

NEFCO's investments in the 30 projects on which agreements have been signed amount to EUR 80.4 million while the total investments are roughly EUR 550 million.

NEFCO has injected its own capital in 13 of these projects, two of which have also received loans from NEFCO. In 17 cases, NEFCO's funding consists exclusively of loans. On the whole, performance by the 30 companies with which NEFCO has signed an agreement is satisfactory. According to the 2011 financial statements of the respective companies, nine projects had posted a profit, seven had broken even and eight posted losses; six companies had not yet commenced operations.

Two of the new projects consisted of investments in the energy sector: one involved the establishment of an energy service company to promote energy efficiency measures in municipally-owned buildings; the other saw the establishment of a service company to provide installation and maintenance services for wind power plants. The third new project is a scheme to acquire equipment for environmental monitoring purposes. Of these projects, two are located in Ukraine and one in Belarus.

Of the 21 expressions of interest given a green light during 2012, eleven were projects to be implemented in Russia, nine in Ukraine and one in Belarus.

MANAGEMENT MANDATES

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Nordic Environmental Development Fund

NEFCO has managed the Nordic Environmental Development Fund (NMF) on behalf of its member states since 1996. The NMF is financed with annual contributions from the Nordic countries and the Nordic Council of Ministers. At the end of the year, NMF's total budget stood at EUR 67.6 million. The NMF is managed by NEFCO and also partly by the Nordic Investment Bank (NIB), which is involved in the evaluation of projects considered for financing. Final decisions on the financing extended by NMF are made by NEFCO's Board of Directors.

Since 2010, revolving loans have been administered by NMF Credits, a special fund established with funding from the NMF. Separate accounts are rendered for the NMF and NMF Credits.

During 2012, NMF and NMF Credits gave final approval for a total of 21 new projects including two supplemental investments in projects approved earlier. Of these, nine related to the energy saving loan programme and eight to the Cleaner Production Programme.

All in all, 64 projects have received funding under NEFCO's energy saving loan programme to finance measures to save energy, while 81 projects have been granted funding under the loan facility for Cleaner Production for projects in Russia, Ukraine, Belarus and the Baltics.

When all the individual projects financed by both funds are taken into account, the total number of projects approved, agreed upon and implemented came to 236 (including two expressions of interest). Of the current total budget, EUR 58.2 million was committed at the end of 2012.

Barents Hot Spots Facility

NEFCO has managed the Barents Hot Spots Facility (BHSF) since 2004. Financed by the Nordic countries and funding provided by the Nordic Environmental Development Fund (NMF), BHSF is primarily intended for project development purposes. The objective is to cooperate with the Russian authorities and project owners to continue to pursue high-priority environmental projects ('hot spots') in northwest Russia identified in a 2003 report issued by NEFCO in collaboration with the Arctic Monitoring and Assessment Programme (AMAP). To date, a total of EUR 6 million has been allocated to the fund.

In 2012, the fund granted financing for three new projects. In total, 68 feasibility studies and pre-project measures have received BHSF financing. Efforts to put in a place an efficient framework for working with 'hot spots' in Russia have been intensified. A number of 'hot spots' may be deemed to be addressed to the extent that they can be removed from the list while measures have been taken and proposals fielded to deal with the remaining problems. To support these processes, the BHSF has relied upon a Nordic-Russian consultant that will evaluate the original NEFCO-AMAP reports and propose how certain 'hot spots' should be revised and redefined. Projects and studies completed during the year included a programme for district heating and energy-efficiency projects for small towns in Karelia, and an investment programme for a cement factory in Vorkuta that will address a number of environmental issues, including dioxin emissions.

Arctic Council Project Support Instrument

Since 2005, NEFCO has also managed the Arctic Council Project Support Instrument (PSI), a project preparation fund. NEFCO was part of the group of experts who were appointed by the Arctic Council to both develop and establish the fund. The PSI has been set up for project preparation, development and demonstration purposes, primarily in the context of the Arctic Council Action Plan (ACAP). The donors are Finland, Iceland, Norway, Russia, the Sámi Parliament, Sweden and, as of 2012, the USA. While there has been a certain delay in the commencement of operations, a meeting of financiers was held in 2012 to discuss strategic issues. The fund is expected to become operational during 2013.

NEFCO Carbon Finance and Funds - CFF

Because of the weak carbon credit market, 2012 was a year of intensive trading for NEFCO. As a result, investments declined and the Corporation focused on re-negotiating the existing purchase agreements insofar as they allowed for adjustment or termination in order to bring them in line with the prevailing market conditions.

Since 2003, NEFCO has managed the Baltic Sea Region Testing Ground Facility (TGF) carbon fund, which was established in conjunction with the Baltic Sea region's testing ground for Joint Implementation (JI), one of the mechanisms under the Kyoto Protocol. Its aim is to procure cost-effective Certified Emission Reductions for its investors from energy-related and other projects. The fund's total capital is EUR 35 million. With the expiry of the first commitment period under the Kyoto Protocol in 2012, the fund brought its primary investment phase to conclusion.

Since 2008, NEFCO has also managed the global NEFCO Carbon Fund (NeCF). Its mission is to finance environmental projects that meet the requirements of the Kyoto Protocol on Joint Implementation (JI) or the Clean Development Mechanism (CDM). The fund can also finance projects that reduce greenhouse gas emissions upon expiry of the Kyoto Protocol's first commitment period in 2012, provided that the projects meet the EU's emissions trading requirements. The fund's total capital is EUR 165 million. By the end of 2012, NeCF had made 27 purchase agreements for totally 11 million Certified Emission Reductions (CER).

Established in 2009, the Nordic Climate Facility (NCF) is financed by the Nordic Development Fund and administrated jointly with NEFCO. The fund finances climate projects in the poorest countries in Africa, Asia and Latin America. It promotes innovative cooperation with Nordic organisations and companies engaged in climate-related fields. Operations have been successful and the fund has already been expanded twice. In the first call for tenders, financing was granted to 14 projects and in the second call to 12 projects. The third call produced 13 approved projects selected for closer review. A total of EUR 18 million has been allocated to the fund to date.

In an effort to develop the climate market, NEFCO coordinates an inter-Nordic project in collaboration with the Nordic Working Group for Global Climate Negotiations (NOAK) regarding Nationally Appropriate Mitigation Actions (NAMA) in the waste management sector in Peru. The project is part of a programme launched by the Nordic Partnership Initiative (NPI).

NEFCO, the Nordic Council of Ministers and UNEP organised jointly an international seminar on the financing of NAMA schemes. The seminar was held in Helsinki, Finland, and was attended by participants from 13 countries.

Other management mandates

In addition to the above funds, NEFCO also manages a number of other external funds. These are trust funds in which capital is injected for a specific purpose or project determined by the donor. NEFCO is responsible for the utilisation of this capital.

The analyses, preparation and monitoring of these projects are funded by contributions from Finland, Norway and Sweden. NEFCO is also managing Norwegian funds intended for water management in the Kenozero National Park in Russia; measures to clean up oil-contaminated waters in the Barents Region; and for co-financing project identification, development and monitoring efforts in collaboration with the Barents Hot Spots Facility. Swedish funds have been allocated for cooperation in district heating with the Ukrainian government; for the preparation of environmental projects given priority under BSAP and/or NDEP; for environmental projects in the Solovki Islands in the Russian Barents region; and for environmental investments in the Kaliningrad region. Swedish funds have also been made available for projects designed to reduce SLCF emissions, a district heating demonstration project in Ukraine and an inter-Nordic initiative for promoting an emission reduction programme for developing countries. Finland and Sweden have also earmarked funds for an investment programme for small wastewater treatment plants in Kaliningrad. Additionally, Finland and Sweden have provided funding for the development and financing of a demonstration project for the disposal of substances harmful to the ozone layer through the market for voluntary carbon credits. Similarly, Finnish and Swedish funds have been allocated to administer a project development fund to support the implementation of the Baltic Sea Action Plan together with NIB. Additionally, NEFCO was tasked to administer funds provided by the Northern Dimension Environmental Partnership (NDEP) for four specific projects as well as funds from the Eastern Europe Energy Efficiency and Environmental Partnership (E5P) for one project. NEFCO renders separate accounts for all these funds.

To date, these funds have been allocated EUR 59.3 million by various donors, with contributions to concluded management mandates accounting for EUR 45.3 million of the total.

Personnel

At the end of 2012, NEFCO had 30 employees, one of whom was a part-time Special Adviser. NEFCO also engages consultants.

Financial result

The financial statements show a surplus of EUR 27,499.73. In accordance with previous practice, the Board of Directors proposes that the surplus be allocated to operations in the form of retained earnings.

Helsinki, 7 March 2013

Harald Rensvik
Chairman

Jon Kahn
Deputy Chair

Danfríður Skarphéðinsdóttir

Søren Bukh Svenningsen

Ann-Britt Ylinen

Magnus Rystedt
Managing Director

Environmental status report 2012

Figure 1

BOD	Biochemical oxygen demand
CO_2	Carbon Dioxide
MWh	Megawatt hours
Nox	Nitrogen oxides
Ntot	Nitrogen total
Ptot	Phosphorus total
SO_2	Sulphur oxides
SS	Suspended solids
VOC	Volatile organic compounds
t/y	tonnes per year

NEFCO makes use of funding provided by a variety of donors. The present report addresses activities within the framework of the Investment Fund and the Nordic Environmental Development Fund. The Investment Fund, which has the larger resource base of the two, is divided into four environmental sectors: water and wastewater management, energy, industry, and waste. The environmental benefits of the credit facility for cleaner technology administered by the Nordic Environmental Development Fund are reported separately.

The fundamental goal of NEFCO's operations is the reduction of pollution originating in Eastern Europe. This means support for projects that, for example, reduce discharges into the catchment areas of the Baltic Sea and the Barents Sea or reduce transboundary airborne emissions of pollutants. As projects having a major impact on the Nordic region are given priority, the efforts focus on protecting water and air quality.

When NEFCO considers projects for support, it first assesses their expected environmental benefits to ensure that projects with direct and clear benefits for the environment are given priority. In principle, any measures that can help to reduce the burden on the environment, such as improved treatment capacity or advanced industrial processes, are eligible. NEFCO's evaluation is also based on an analysis of the relationship between the investment and its anticipated quantitative effects in order to identify the projects that are environmentally the most cost-effective.

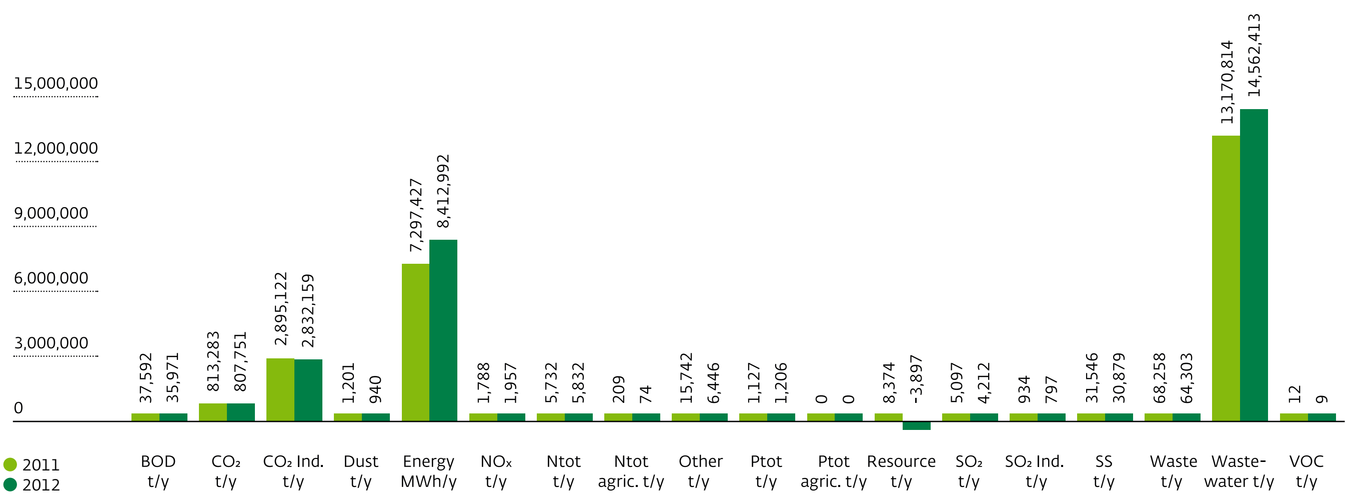
Typical projects include:

- modernisation of industrial and power plants that will bring environmental benefits to the Nordic region and the surrounding seas;
- partnerships with municipal and other authorities to deliver environmental services such as water treatment; and
- companies that manufacture environmental equipment (such as emission control equipment, measuring instruments and water treatment equipment) and equipment to increase energy efficiency; or companies that provide services in the environmental and energy fields and thereby contribute to creating a better basis for the implementation of environmental initiatives.

Environmental benefits gained in projects that have been completed or in which NEFCO's involvement has ceased are shown in Figure 1. For purposes of comparison, the data are shown as reductions or savings per annum.

NEFCO's environmental database also takes into account projects in which its involvement has ceased. The justification for including emission reductions from projects in which NEFCO is no longer involved is that the relevant facilities have in post-evaluation been found to match or even significantly exceed expected reductions. The service life of an industrial facility is substantially longer than the repayment period of a loan, and as a result, the positive environmental effect of the facility will in all likelihood continue in a linear way for a long time into the future.

Figure 1 NEFCO: Total reductions



> The reduced discharges of nitrogen and phosphorus exceed the previous year's levels by a narrow margin, which is due to the fact that on-going wastewater projects have further improved their performance.

Even though the favourable effects of a project are felt for a number years after the repayment of the loan, a reasonable technical depreciation period should be afforded for investments. In its environmental monitoring, NEFCO applies an annual depreciation rate of 5% on all actual reductions as of the beginning of the year following final repayment. This method was first applied in 2011. As a result, depreciation charges have accumulated for NEFCO's closed projects, decreasing reductions as of 2010.

The results achieved in 2012 in terms of the determinant indicators CO_2 and energy fell slightly short of the 2011 levels, an outcome due to depreciation charges and the fact data on some of the projects are still missing (Figure 1). No progress was made in the substantial reductions in indirect CO_2 emissions reported last year because the manufacturer was only able to sell fossil-fuel boilers to outside Europe while selling no new biofuel-fired boilers in Europe.

The figures for nitrogen (N) and phosphorus (P) exceed the previous year's levels by a narrow margin, which is due to the fact that on-going wastewater projects have further improved their performance.

Performance in the water and waste management, energy, industrial, and waste sectors are shown in specific sections below. Emission reductions associated with the Nordic Environmental Development Fund and the Cleaner Production Facility are presented at the end of this environmental status report. Indirect CO_2 reductions are shown as a separate bar.

WATER AND WASTEWATER MANAGEMENT

While great importance is attached by NEFCO to benefits such as acceptable quality of drinking water and higher water connection rates, top priority is given to reduced BOD, phosphorus, and nitrogen emissions to water areas, especially the Baltic Sea. Work is continued along with the efforts to achieve further reductions under HELCOM's Baltic Sea Action Plan.

Figure 2 shows a slight improvement in 2012 as compared to 2011. All the indicators show improvements year-on-year, except for slightly weaker performance in BOD and energy consumption. Because of the dominant position of the Southwest Wastewater Treatment Plant in St. Petersburg in terms of volumes (80 million m^3) and energy consumption, its impact was excluded from the 2012 figures indicating the volume of wastewater treated, just as was done in 2011. Overall, the treated volumes vary considerably from one treatment plant to another, due to climatic and economic conditions, among others.

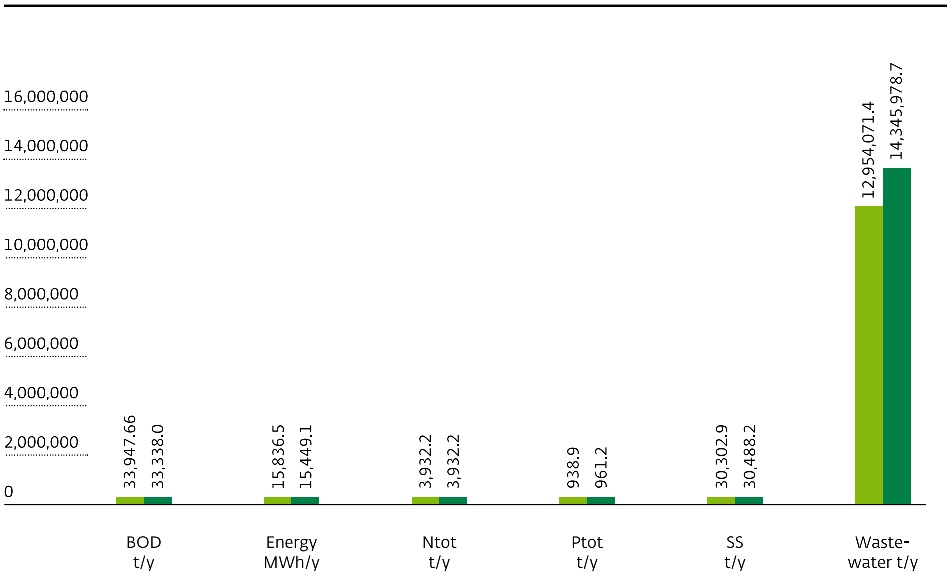
As in the past, the continued reduction in suspended solids (SS) was primarily due to the improved efficiency of the Southwest Wastewater Treatment Plant in St. Petersburg.

Overall, the water sector continued to put in a good performance in 2012.

Energy

The combustion of fossil fuels produces acidifying emissions, CO_2 (which contributes to the greenhouse effect), and emissions of hydrocarbons, dust, and heavy metals, among others. With the appropriate technology and

Figure 2 Investment Fund: Water sector



dimensioning, emissions can be reduced and efficiency increased substantially. More efficient energy production and conversion to less polluting fuels leads to reduced atmospheric emissions of sulphur dioxide (SO2), nitrogen oxides (NOx), CO2, heavy metals, and dust from combustion processes.

All of NEFCO's energy projects aim at improving energy efficiency in order to generate positive effects for the environment. Typical goals for these projects include a general reduction in energy consumption, more efficient production and/or conversion to less polluting fuels.

Where quantitative targets have been set, reductions have been measured, as shown in Figure 3.

Within the energy sector, the rate of reduction in carbon dioxide emissions increased slightly compared to 2011. Unlike in 2011 when energy consumption increased, major progress was made in this respect in 2012. An energy project tabled in Russia no longer affects the outcome while at the same time wind power production in the Baltics expanded. On the whole, the sector' performance in terms of CO2 reductions was positive. Overall, no major changes in reductions took place in 2012. The indicators are shown in Figure 3.

Industry

Industrial activity impacts on the environment in a number of ways:

- the extraction of raw materials has a physical impact on the environment;
- emissions affect air, land, and water;
- the manufacture of certain goods such as chemicals can be environmentally harmful;
- landfill sites pollute groundwater through various types of leakages, and many end-products tend to burden landfill sites at the end of their lifecycle;
- some industries cause odours and create noise; and
- industrial buildings and roads have an impact on the landscape and plant and animal habitats.

NEFCO's industrial projects aim at improving resource efficiency in order to reduce emissions to air, soil and water. Environmental benefits can be achieved as a direct consequence of investments but also indirectly as NEFCO supports companies manufacturing environment-related products, such as water cleaning agents and insulation materials. In these cases, the benefits are only felt at the consumer level.

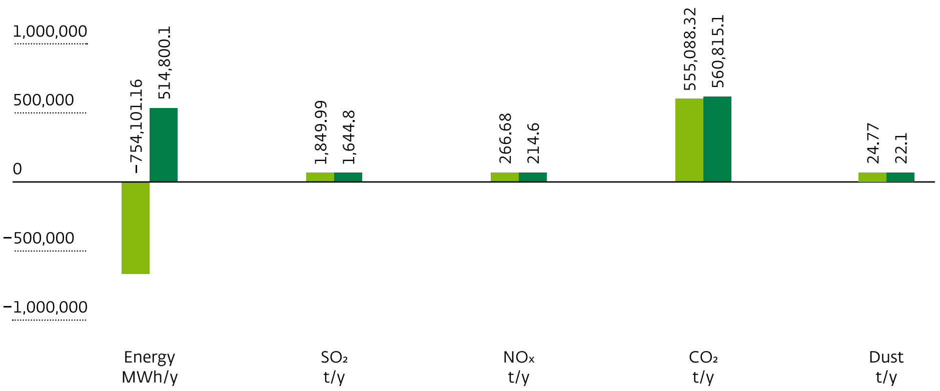
Compared with 2011, the rate of reduction in CO2 emissions slowed down during 2012, which is explained by the fact that major industrial projects dating back to the early 2000s are being written off while now large projects have not yet compensated for this write-off. Similarly, the slightly lower reductions in NOx and SOx can be explained by the write-offs. That industrial projects lead to higher rates of reduction in wastes goes to show that industry in NEFCO's host countries is improving its performance in recovering and recycling resources in its processes. The indicators for the industry sector are shown in Figure 4.

Waste

Waste causes a range of environmental problems:

- toxins and other pollutants escape from landfill sites into air, soil, and water;
- waste incineration causes air pollution;
- waste management involves extensive transportation; and
- waste depletes natural resources if not recycled.

Figure 3 Investment Fund: Energy sector



A new waste management project was launched in Belarus during 2012 to recover gas from landfills.

The overall aim of NEFCO's participation in waste projects is to minimise the amount of waste and to deal with the ever-increasing amount of waste in improved ways, e.g. through sorting, re-use, and/or recycling. These projects target both household and industrial waste, which can include paper, plastics, chemicals, and heavy metals.

A new waste management project was launched in Belarus during 2012 to recover gas from landfills. Work on plans to improve efficiency in waste management in Karelia continues. However, the new biogas project in Belarus has not reached the stage of completion required for reporting.

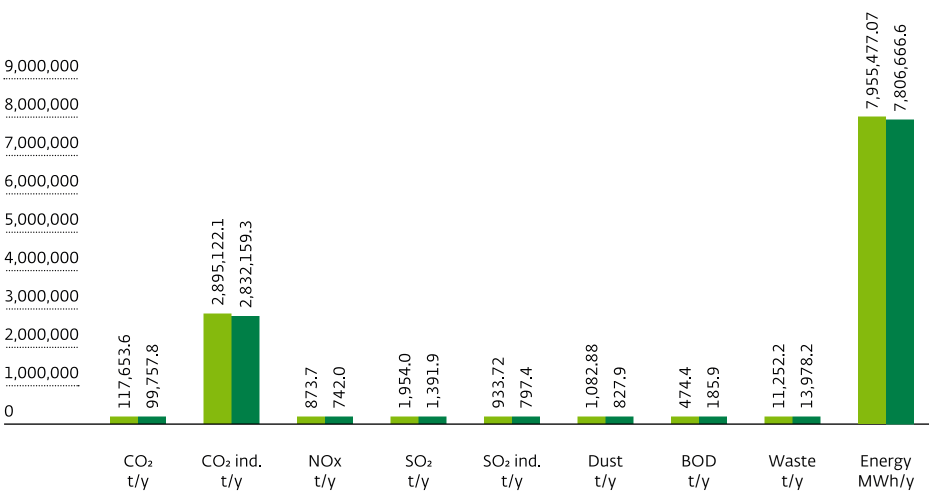
The reduction in nitrogen emissions (Ntot) from the landfill in Sillamäe continues to play an important part in the efforts to manage nutrient levels in the Baltic Sea. Aside from nitrogen, the project has also helped to stop the entry of significant amounts of radioactive isotopes into the Gulf of Finland by stabilising and covering the landfill and isolating it from the sea.

Nordic Environmental Development Fund (NMF)

Financing from the Nordic Environmental Development Fund is used to support specific environmental projects in the regions neighbouring the Nordic countries. The goal is to attain environmental benefits by enhancing the potential profitability of high-priority environmental projects, facilitating financing with higher risk, advancing the completion of projects, or by attracting additional environmental investments. This support is intended to complement bilateral initiatives.

Compared with 2012, an improvement in the rate of reduction in CO2 emissions can be noted (Figure 5). The same applies to atmospheric emissions of NOx. As far as nutrients such as nitrogen and phosphorus are concerned, the situation with phosphorus was somewhat improved whereas performance with regard to nitrogen showed a slight decline in 2012 because a number of projects are no longer included in the reporting system. The same applies to N emissions from agriculture. While some of the clients have failed to submit reports, it may be noted that performance in this respect has improved as a result of revised procedures. Further support is still needed by these borrowers to improve their performance and reporting. NEFCO is making continuous efforts to develop advice and consultancy services in the target countries.

Figure 4 Investment Fund: Industrial sector



Cleaner Production

Cleaner production aims at reducing industrial pollution through improved resource and energy efficiency, process modifications, and reduced wastage. The overriding objective of this financing facility is to use a series of positive examples of 'win-win' projects to instil a mindset that is compatible with sustainable development in industry and other forms of production. The starting point for each project approved under the scheme is that it should bring about clear and measurable environmental benefits.

Investments in cleaner technology result in real reductions in emissions and/or waste. More environmentally friendly production and consumption are achieved through, for example, the use of less resource-intensive processes. Priority is given to projects that provide environmental benefits to the Nordic region, i.e. projects that will result in reduced emissions into the Baltic Sea or Barents Sea, or those resulting in reduced transboundary and global air pollution. In particular, small and medium-sized private companies have helped to reduce emissions to air and water by making investments in cleaner technology in their processes.

Selected parameters relevant to environmental benefits are presented in Figures 6a-b, where quantitative results have been reported. Favourable developments are noted in terms of reductions in certain areas compared to 2011, such as atmospheric emissions of CO2 and NOx (Figure 6a). In contrast, BOD and SS emissions have nosedived since 2011 because a plywood factory in Komi stopped production following bankruptcy. Other indicators suggest a level of performance similar to 2011 or a slight reduction in atmospheric emissions.

Figure 5 NMF: Total

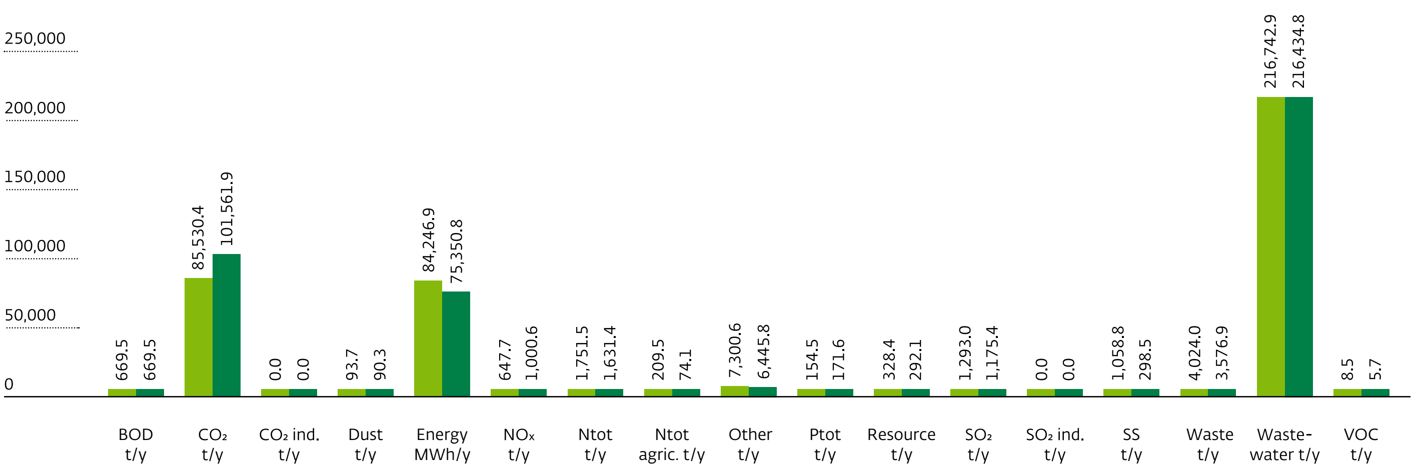


Figure 6a NMF: CPF. Reduction of emissions to air

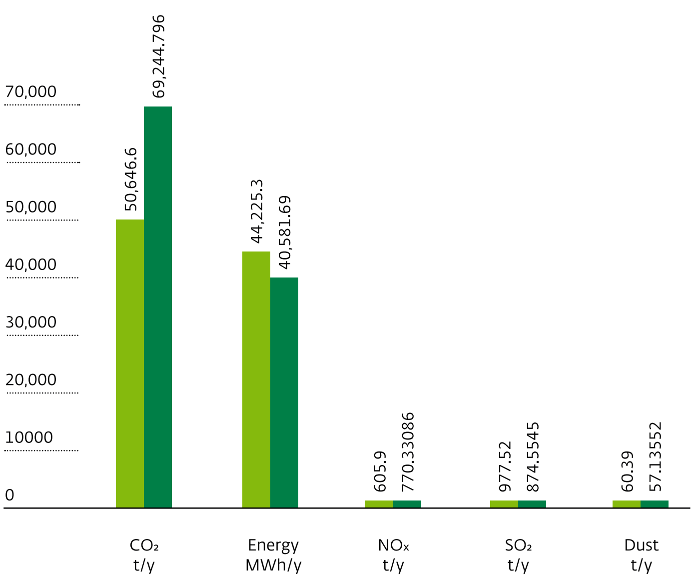
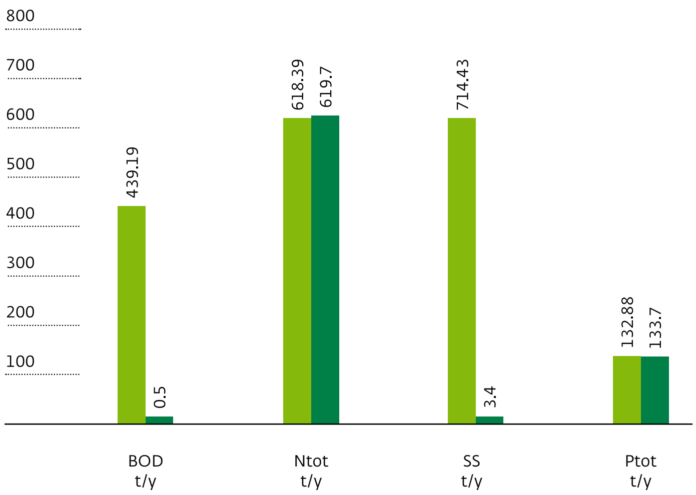


Figure 6b NMF: CPF. Reduction of emissions to water



Financial statement

Statement of comprehensive income

1 January — 31 December

(Amounts in EUR)	Note	2012	2011
Income			
Interest income, placements with credit institutions	(4)	878 243	1 133 149
Interest income, lending		1 446 568	1 025 875
Net result of financial operations	(1)	-1 606 654	-549 713
Other income		4 795 214	4 802 745
Total income		**5 513 372**	**6 412 056**
Operating expenses			
Administrative expenses	(2) (3) (4)	5 465 878	5 380 242
Depreciation and write-down in value of tangible and intangible assets	(9)	23 047	19 172
Foreign exchange gains and losses		-33 493	117 939
Impairment of loans / reversals	(6)	30 441	62 831
Total operating expenses		**5 485 872**	**5 580 184**
RESULT FOR THE YEAR		**27 500**	**831 872**

Statement of financial position

31 December

(Amounts in EUR)	Note	2012	2011
ASSETS			
Cash and cash equivalents	(4) (5)	4 839 013	37 924 887
Placements with credit institutions	(4) (5)	107 349 612	78 747 438
Total cash, cash equivalents and placements with credit institutions		**112 188 625**	**116 672 325**
Other receivables		239 194	173 944
Accrued interest		865 992	838 569
Loans outstanding	(6)	23 579 115	18 296 442
Investment assets	(7)	16 453 827	15 753 827
Other placements	(8)	3 750 836	3 921 843
Intangible assets	(9)	28 676	30 011
Tangible assets	(9)	6 226	13 813
TOTAL ASSETS		**157 112 491**	**155 700 774**
LIABILITIES AND EQUITY			
Liabilities			
Other liabilities		2 132 544	748 327
Equity			
Paid-in capital	(10)	113 406 560	113 406 560
Reserve for investment/credit losses		24 557 177	24 557 177
Operational fund		4 500 000	4 500 000
Retained earnings		12 488 711	11 656 839
Result for the year		27 500	831 872
Total equity		**154 979 947**	**154 952 447**
TOTAL LIABILITIES AND EQUITY		**157 112 491**	**155 700 774**

Changes in equity

(Amounts in EUR)	Paid-in capital	Reserve for investment/ credit losses	Operational Fund	Retained earnings	Result for the year	Total
Equity as of 1 January 2011	113 406 560	24 557 177	4 500 000	11 197 961	458 877	154 120 576
Appropriation to the retained earnings				458 877	-458 877	-
Appropriation to the reserve for investment/credit losses		-				-
Appropriation to the Operational Fund			-			-
Paid-in capital	-					-
Result for the year					831 872	831 872
Equity as of 31 December 2011	**113 406 560**	**24 557 177**	**4 500 000**	**11 656 838**	**831 872**	**154 952 447**
Equity as of 1 January 2012	113 406 560	24 557 177	4 500 000	11 656 838	831 872	154 952 447
Appropriation to the retained earnings				831 872	-831 872	-
Appropriation to the reserve for investment/credit losses		-				-
Appropriation to the Operational Fund			-			-
Paid-in capital	-					-
Result for the year					27 500	27 500
Equity as of 31 December 2012	**113 406 560**	**24 557 177**	**4 500 000**	**12 488 711**	**27 500**	**154 979 947**

Proposed allocation of the year's result	**2012**	**2011**
Appropriation to the retained earnings	27 500	831 872
RESULT FOR THE YEAR	**27 500**	**831 872**

Cash flow statement

1 January — 31 December

(Amounts in EUR 1,000)	**2012**	**2011**
Cash flow from operating activities		
Result for the year	27	832
Depreciation and write-down in value of tangible and intangible assets	23	19
Value adjustments, investment assets	-	-1 500
Value adjustments, other placements	1 683	3 017
Capital adjustments, other placements	185	636
Impairments, lending	-451	63
Change in accrued interests	-24	-316
Lending		
Disbursements	-11 924	-6 821
Repayments	3 826	2 064
Premature repayments	2 919	-
Realised credit losses	333	-
Capitalisation of interest and loan receivables	-	-594
Exchange rate adjustments	-41	104
Change in investment assets	-700	144
Cash flow from operating activities	**-4 143**	**-2 352**
Cash flow from investing activities		
Change in placements with credit institutions	-28 602	2 701
Change in other placements	-1 697	-2 535
Change in other receivables and liabilities, net	1 370	-745
Change in tangible and intangible assets	-14	-22
Net cash flow from investing activities	**-28 943**	**-602**
Change in cash and cash equivalents	**-33 086**	**-2 954**
Breakdown of cash and cash equivalents		
Cash and balances with banks	4 839	7 904
Placements with a maturity of less than six months	-	30 021
TOTAL CASH AND CASH EQUIVALENTS	**4 839**	**37 925**

Notes to the financial statement

GENERAL OPERATING PRINCIPLES

—

The operations of the Nordic Environment Finance Corporation (hereinafter the Corporation or NEFCO) are governed by an agreement that was made on 6 November 1998 between the governments of Denmark, Finland, Iceland, Norway and Sweden and related statutes, which replaced the previous agreement of 2 March 1990 regarding the formation of the Corporation on 9 October 1999. This agreement both strengthened the Corporation's status as a multilateral institution, as well as its legal position.

NEFCO's role is to promote investments of Nordic environmental interest in Eastern Europe by helping to finance companies in these countries.

The Corporation is an international legal person with full legal capacity and is exempt from payment restrictions and credit policy measures in the member countries. In addition, the 1998 agreement contains immunity provisions exempting the Corporation from all taxation.

The Corporation operates from the Nordic Investment Bank's premises at Fabianinkatu 34, Helsinki.

The Corporation also manages trust funds on behalf of various principals.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

—

Basis for preparing the financial statements

The Corporation's financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB). The accounts of the Corporation are kept in euro.

The Corporation's financial statements are presented in euro. With the exceptions noted below they are based on historical cost.

Assessments made in preparing the financial statements

In preparing the financial statements, the management is called upon to make estimates that have an effect on the reported result, financial position and other disclosures. These estimates are based on the information available and the judgement of the management. Actual outcomes may deviate from the assessments made, and these deviations may be significant in relation to financial statements.

Foreign currency translation

Monetary assets and liabilities in currencies other than the euro are converted at the exchange rates published by the European Central Bank at the balance sheet date (see Note 12). Realised and unrealised exchange gains/losses are recognised separately in the statement of comprehensive income under 'Foreign exchange gains and losses'. Non-monetary assets are converted at the exchange rate applied on the transaction date.

Cash and cash equivalents

Cash and cash equivalents comprise monetary assets and placements with an original maturity of up to six months.

Placements with credit institutions

NEFCO invests its short-term liquidity, which is primarily in euros, with credit institutions, preferably Nordic banks.

According to IAS 39, placements with credit institutions are classified as held-to-maturity financial assets and are recognised at cost (normally nominal value) on the settlement date. These placements are carried at amortised cost in the annual financial statements. Accrued interest on these placements is recognised as 'Accrued interest' in the statement of financial position. Due to the short maturities of these placements, the difference between their fair value and book value including accrued interest is not significant.

Lending

Loan receivables are recognised in the statement of financial position on the transfer of funds to the borrower. Loans are initially recognised at historical cost as determined by NEFCO to reflect the fair value inclusive of any transaction cost. Loans outstanding are carried at amortised cost after deductions for any impairment losses.

Loans to public-sector borrowers are issued primarily against municipal risk, while loans to private-sector borrowers are generally secured by a lien on the company's assets or with a negative pledge clause and other financial covenants.

In the absence of a relevant market interest rate reflecting the loan terms, it has not been possible to calculate the fair value reliably for disclosure in the notes. However, NEFCO is of the opinion that fair value is not lower than book value.

According to IAS 39, loans outstanding are classified as loan receivables.

Impairment of loans

The treatment of impairment losses is based on individual testing of loans outstanding. Impairment losses affect the result for the year and are recognised as a separate item in the statement of comprehensive income.

Intangible assets

Intangible assets are primarily investments in software and licenses for the development of NEFCO's *Project Registration and Information System*. The investments are carried at historical cost and amortised over the assessed useful life of the assets estimated to be 3 to 5 years. The amortisations are made on a straight-line basis.

Tangible assets

Tangible assets include inventories. Tangible assets are recognised at historical cost less accumulated write-downs and impairment. Tangible assets are amortised on a straight-line basis over their useful life of 3 to 5 years.

Write-downs and impairment of intangible and tangible assets

NEFCO's assets are reviewed annually for impairment. If there is any objective evidence of impairment, the impairment loss is determined based on the recoverable amount of the assets.

Financial assets

Measurement of financial assets at fair value is carried out according to the following hierarchy based on fair value:

Level 1: Market prices quoted on an active market for identical assets

Level 2: Valuation model based on observable input either directly (i.e. prices) or indirectly (i.e. derived from prices). This category includes assets valued using quoted market prices in an active marketplace for similar assets; quoted prices for identical or similar assets in a less active marketplace or other valuation method, in which all significant inputs can be determined either directly or indirectly in the marketplace.

Level 3: Valuation method using significant unobservable inputs. This category includes all assets where the valuation method includes inputs not based on observable data and the unobservable inputs have a significant effect on the valuation. If there is any objective evidence of impairment, the impairment loss is determined based on the recoverable amount of the assets.

- *Investment assets*

NEFCO's investment assets include participating interests in a number of companies. NEFCO's investment assets are carried at fair value in the statement of comprehensive income. The Corporation regularly assesses its investment assets using its own valuation model. However, the assessed fair value is greatly affected by the market conditions in the individual countries and other circumstances beyond NEFCO's control. If fair value cannot be reliably determined, the assets are carried at cost.

NEFCO's investment assets fall in either Level 2 or Level 3 categories.

For the breakdown of investment assets, see Note 7.

Even if NEFCO's participating interest exceeds 20%, NEFCO, as an investment company, recognises such investments as financial instruments instead of using the equity method.

- *Other placements*

NEFCO's other placements include placements in the NEFCO Carbon Fund and the Nordic Environmental Development Fund as well as the emission reductions received. NEFCO's other placements are carried at fair value. Changes in fair value are recognised in the statement of comprehensive income. The Corporation regularly assesses its other placements using its own valuation model. However, the assessed fair value is greatly affected by market conditions and other circumstances beyond NEFCO's control. If fair value cannot be reliably determined, the assets are carried at cost.

Emission reductions are carried at market value.

NEFCO's other placements fall in either Level 1 or Level 3 categories.

For the breakdown of other placements, see Note 8.

Equity

Paid-in capital reached its full amount of EUR 113.4 million on 31 December 2007.

Additionally, the Corporation has built up a general reserve in equity to cover the risk of losses on loans outstanding and investment assets. This reserve is used to cover major investment or credit losses arising during the course of the Corporation's operations.

NEFCO's equity includes provision for an Operational Fund to secure resources for the Corporation's development and for preparation of projects.

Administrative expenses

NEFCO purchases administrative services from a related party, the Nordic Investment Bank (NIB). The cost of these services is shown under 'Administrative expenses' (Note 2). The Corporation receives a host country reimbursement from the Finnish Government equal to the tax withheld from the salaries earned by its employees. The host country reimbursement is reported as a deduction from administrative expenses (Note 2).

Employee pensions and insurance

In accordance with the Headquarters Agreement between the Corporation and the Finnish Government, the Corporation is responsible for providing full pension security to its employees. NEFCO applies the Finnish state pension system in respect of its employees based in Helsinki. The pension contributions calculated as a percentage of the wagebill are paid to the Finnish State Pension Fund. The Finnish Government determines the basis for these contributions and the Finnish State Treasury establishes the actual percentage of the contributions.

As at the end of 2012, the Corporation's pension obligations were fully covered. The normal retirement age under the Finnish pension system is currently between 63 and 68 years.

NEFCO has also a supplementary pension insurance scheme for its permanent employees based in Helsinki. This is a group pension insurance scheme based on a defined contribution plan.

In addition to the applicable local social security system, NEFCO has also taken out comprehensive life, accident, medical, disability and travel insurance for its employees based in Helsinki.

As of 1 April 2012, the Corporation has had one employee in its Representative Office in Kiev, Ukraine, whose contract is based on the local terms of employment and health and safety requirements as defined in Ukrainian law.

STANDARDS, AMENDMENTS AND INTERPRETATIONS

—

As of 1 January 2012, NEFCO has applied the following amended standard that has come into effect. The standards do not have any significant impact on the Corporation's financial statements.

- Amendments to IFRS 7 Financial instrument: Disclosures; effective for financial year beginning on 1 July 2011 or later.

NEFCO has not opted for early application of the following standards, amendments and interpretations:

- Amendments to IAS 1 Presentation of financial statements; effective for financial year beginning on 1 July 2012 or later.
- IFRS 13 Fair value measurement; effective for financial year beginning on 1 January 2013 or later.
- Annual improvements to IFRSs 2009–2011 (May 2012); effective for financial year beginning on 1 January 2013 or later.
- Amendments to IFRS 7 Financial instruments: Disclosures; effective for financial year beginning on 1 January 2013 or later.
- Amendments to IAS 32 Financial instruments: Presentation; effective for financial year beginning on 1 January 2014 or later.
- IFRS 9 Financial instruments including subsequent amendments; effective for financial year beginning on 1 January 2015 or later. This standard is not yet finished.

These standards and amendments are not expected to have any significant impact on NEFCO's financial statements.

MANAGEMENT OF FINANCIAL RISKS BY NEFCO

—

NEFCO has adopted a risk management policy that provides guidelines for reporting and monitoring the risks associated with its operations. In accordance with said guidelines, the risk management process includes an evaluation of the portfolio four times per year accompanied by country risk reports. The goal is to provide an objective on-going assessment of the portfolio risk.

The purpose of NEFCO's business is to provide risk capital and loans to finance investments in Eastern Europe that are of interest to the Nordic countries from the environmental point of view. The paid-in authorised capital – the Investment Fund – is used to finance NEFCO's investments. In addition, NEFCO has a risk reserve fund comprising approximately 21.7% of the authorised capital. The main financial risks – credit risk, foreign exchange rate risk, interest rate risk, price risk, liquidity risk and operational risk – are carefully managed and risk management procedures are closely integrated into NEFCO's business routines. NEFCO's financial investments cannot exceed the paid-in authorised capital.

Market risk

- *Foreign exchange rate risk*

Outstanding loans are denominated in euros and rouble. Rouble-denominated lending accounts for 34.8% of all outstanding loans and consists of three loans. NEFCO is exposed to a rouble-related foreign exchange risk not hedged in respect of exchange rate fluctuations during the repayment term. The foreign exchange rate risk in respect of other activities is insignificant.

- *Credit risk*

The credit risk associated with NEFCO's lending is subjected to thorough examination before presentation to NEFCO's Board for a lending decision. The maximum credit risk exposure at the balance sheet date consists of the amounts outstanding for loans totalling EUR 23.6 million as at 31 December 2012. The cumulative risk reserves protect the Corporation's authorised capital against losses.

Credit risk is NEFCO's main financial risk. It involves the risk that the Corporation's borrowers or other counterparties fail to fulfil their contractual undertakings and that the collateral provided as security does not cover the Corporation's claims. In accordance with NEFCO's mandate, all of the Corporation's lending can be classified as high risk. The main risk consists of lending to companies in the target countries, which accounts for 20.8% of the paid-in authorised capital. Collateral for the loans consists of local authority guarantees (28.1%) or guarantees given by a parent company or bank (23.0%) while various types of liens and charges account for 26.6%. Negative pledge or other financial covenants represent 22.4% of the total.

- *Interest rate risk*

Interest rate risk refers to the effect of market rate fluctuations on the Corporation's interest-bearing assets and related interest income.

Of the loans outstanding, 92.3% are floating-rate and 7.7% fixed-rate loans on which interest accrues up until the final repayment date. The distribution of loans outstanding according to the length of the interest rate fixing period is indicated in Note 11. The liquidity reserve of approximately EUR 112 million is primarily placed in one-year bank deposits. As the maturity dates are spread across the year, the interest rate risk is distributed in such a way that any change in interest rate levels resulting from a fall in market interest rates is not immediately fully reflected in the financial result. A 0.5% fall in the annual interest rate would result in a reduction in earnings of around EUR 0.6 million. Conversely, an increase in interest rates would have a positive impact on financial performance.

- *Price risk*

The price risk associated with NEFCO's equity investments is subjected to thorough examination before presentation to NEFCO's Board for an investment decision. The maximum price risk exposure at the balance sheet date consists of the investment assets totalling EUR 16.5 million as at 31 December 2012. The cumulative risk reserves protect the Corporation's authorised capital against losses. Equity investments account for 14.5% of the authorised capital.

An indirect price risk may be associated with placements in the NEFCO Carbon Fund (NeCF) and the emission reductions received. During 2012, the market price fell sharply (EUR 0.18/CER and EUR 0.12/ERU as at 31 December 2012) and market volatility diminished. A large proportion of NeCF's agreements on emission reductions were signed with project developers before the prices fell. As the prices specified in the agreements exceed the current market prices by a wide margin, NEFCO's investments in NeCF will be loss-making to the extent the funds have been invested in projects. Additionally, all the projects may not generate all the emission reductions foreseen in the agreements. NEFCO is involved in projects that are expected to deliver the last emission reductions in 2013. NEFCO's investments are expected to generate a total of 83,883 CERs. In the assessment of NEFCO's investments in NeCF, the CERs expected to be generated by the agreements have been recognised at current market price. However, a substantial percentage of the fund's reserves remain unused.

Liquidity risk

The effective management of liquidity risk ensures that NEFCO can fulfil all its payment obligations as they mature. In total, 95.7% of the liquid funds and other placements with credit institutions (accounting for 98.9% of the authorised capital) consist of euro-denominated deposits with Nordic banks placed for a period of one year or less. The deposits mature at regular intervals, guaranteeing access to liquid funds when necessary. Status reports regarding the liquid funds are regularly presented to NEFCO's Board of Directors. NEFCO is not burdened by any substantial financial liabilities.

Operational risk

Operational risk is the risk of financial loss or loss of reputation through shortcomings or failings relating to technology, the Corporation's employees or physical circumstances. Legal risk is also considered an operational risk. NEFCO's management of operational risk focuses on proactive measures designed to ensure business continuity as well as the accuracy and appropriateness of internal and external information. The main responsibility of Internal Audit is to evaluate the in-house controls, risk management and governance processes in NEFCO. Internal Audit reports to NEFCO's Board of Directors while keeping the Managing Director informed of the developments on a regular basis. The annual internal audit activity plan is submitted to the Board of Directors for approval.

Capital management

NEFCO is not governed by any national or international regulations. The Corporation maintains an adequate capital base to cover the risks inherent in its lending and investment activities.

(1) NET RESULT OF FINANCIAL OPERATIONS

(Amounts in EUR 1,000)	**2012**	**2011**
Investment assets, realised gains and losses	-	876
Other placements, realised gains and losses	-1,513	-1,845
Other realised gains and losses	1	20
Total, realised gains and losses	**-1,512**	**-950**
Investment assets, unrealised gains and losses	-	1,500
Other placements, unrealised gains and losses	-95	-1,100
Total, unrealised gains and losses	**-95**	**400**
Net result of financial operations	**-1,607**	**-550**

(2) ADMINISTRATIVE EXPENSES

(Amounts in EUR 1,000)	**2012**	**2011**
Staff costs	3,019	2,723
Pension premiums in accordance with the Finnish state pension system	590	513
Other pension premiums	116	105
Office premises expenses	279	255
Other administrative expenses	2,172	2,382
Miscellaneous administrative income	-6	-6
Total, administrative expenses [1)]	**6,169**	**5,972**
Host country reimbursement according to agreement with Finnish government	-704	-592
Net administrative expenses	**5,466**	**5,380**

1) The Corporation's administrative expenses include the administrative expenses for NeCF, TGF, NMF and NCF. Income from administration amounting to EUR 2,616,238 (2011: EUR 2,637,512) for NeCF; EUR 371,046 (2011: EUR 500,245) for TGF; EUR 846,659 (2011: EUR 817,178) for NMF; and EUR 274,680 (2011: EUR 210,532) for NCF are included in the statement of comprehensive income under 'Other income'.

In 2012 the average number of employees was 29 (27 in 2011).

NEFCO is renting an office with a floor area of 729.5 m2 from NIB in Helsinki. Additionally, the Corporation is renting a 54.5 m2 office in Kiev.

(3) COMPENSATION AND BENEFITS

Compensation paid to the Board of Directors, Control Committee and Managing Director
The compensation paid to the Board of Directors and the Control Committee is determined by the Nordic Council of Ministers. The members of the Board of Directors and Control Committee are also entitled to reimbursement of the cost of travel and accommodation and daily allowance in accordance with the Corporation's travel regulations. The compensation paid to the Managing Director of the Corporation as determined annually by the Board of Directors consists of a base salary and customary taxable benefits.

The Managing Director's pension benefits are based on the terms of the Finnish state pension with certain supplements.

The remuneration of the Board of Directors, Control Committee and Managing Director was as follows:

(Amounts in EUR)	2012 Compensation / taxable income	2011 Compensation / taxable income
Chairman of the Board	3,364	3,364
Other Directors and Alternates	17,498	17,498
Managing Director	395,026	394,396
Control Committee	4,241	4,003

Pension obligations
NEFCO is responsible for providing pension security for its employees. The current pension arrangement consists of pensions based on the Finnish state pension system (VaEL Pension) as the basis for the pension benefits. The VaEL Pension is calculated on the basis of the employee's annual pensionable income and the applicable age-linked pension accrual rate.

In 2012 the employer's pension contribution was 17.89% of the pensionable income used as basis for determining the amount of pension. The employee's pension contribution in 2012 was either 5.15% or 6.5%, depending on the employee's age. This contribution paid by NEFCO for the permanent staff based in Helsinki is a taxable benefit for the employees.

In addition to the VaEL Pension, the Corporation has taken out a supplementary group pension insurance policy for its permanent staff and the Managing Director. This pension insurance is based on a defined contribution plan. The insurance premium (6.5%) is calculated on the basis of the employee's taxable income and paid by NEFCO until the employee reaches the age of 63.

In 2012 NEFCO paid a total of EUR 98,270 (2011 EUR 96,400) in pension insurance premiums for the Managing Director.

Staff loans
Staff loans can be granted on the Corporation's recommendation to permanent staff members based in Helsinki who have been employed by NEFCO for a minimum period of one year. The Managing Director is extended staff loans subject to a recommendation from NEFCO's Board. Staff loans are granted by a commercial bank.

The total amount of loans may not exceed EUR 200,000. The employee pays interest on the loan in accordance with the official base rate established by the Ministry of Finance of Finland (1.5% in July–December 2012). The same interest rates, terms and conditions are applied to all permanent staff members of the Corporation, including the Managing Director. The total amount of staff loans extended to employees in key positions was EUR 62,365 (2011: EUR 79,415).

Additional benefits to expatriates
Professional staff (including the Managing Director) who move to Finland for the sole purpose of taking up employment with the Corporation, are entitled to certain expatriate benefits, such as an expatriate allowance and a spouse allowance. In addition, NEFCO assists the expatriates in finding a residence and with other practical arrangements. Such staff members are required to pay the Corporation a part of the rent, which equals to at least the tax value of the accommodation benefit received. The tax value is determined annually by the Finnish tax authorities.

(4) RELATED PARTY DISCLOSURES

The Nordic Investment Bank (NIB), which has for the most part the same owners as NEFCO, is considered a related party of NEFCO. NEFCO acquires services from and enters into transactions with NIB. The table below shows the outstanding balance of NEFCO's receivables from and amounts owed to NIB and the amount of interest received during the year. The interest received is equal to normal commercial rates. NEFCO's key individuals are also considered related parties. Information regarding key individuals is presented in Note 3.

(Amounts in EUR 1000)	Interest income	Amounts owed by NEFCO to NIB	Amounts owed by NIB to NEFCO	Rents paid to NIB
2012	317	17	-	209
2011	1,101	81	109,046	197

(5) CASH AND CASH EQUIVALENTS AND PLACEMENTS WITH CREDIT INSTITUTIONS

(Amounts in EUR 1,000)			**2012**			**2011**
	Book value	**Fair value**	**Change in fair value**	**Book value**	**Fair value**	**Change in fair value**
Cash and cash equivalents						
Cash and balances with banks	4,839	4,839	-	7,904	7,904	-
Placements with credit institutions, held-to-maturity	-	-		30,021	30,021	-
Total, cash and cash equivalents	**4,839**	**4,839**	**-**	**37,925**	**37,925**	**-**
Placements with credit institutions						
Placements with credit institutions, held-to-maturity	107,350	107,350	-	78,747	78,747	-
Total, placements with credit institutions	**107,350**	**107,350**		**78,747**	**78,747**	
Total, cash and cash equivalents and placements with credit institutions	**112,189**	**112,189**	**-**	**116,672**	**116,672**	**-**

The remaining maturity of cash and cash equivalents and placements, counted from the balance sheet date to maturity, is as follows:

Maturity (Amounts in EUR 1,000)	**2012**	**2011**
Up to and including 3 months	24,838	77,650
3–6 months	22,000	26,235
6–12 months	65,000	12,440
Undefined	350	348
Total, cash and cash equivalents and placements with credit institutions	**112,189**	**116,672**

(6) LENDING

The following tables show net lending after deductions for impairment losses totalling EUR 1,131,386 (EUR 1,527,574 in 2011).

Loans outstanding by country as at 31 December:

Country (Amounts in EUR 1,000)	**2012**	**2011**
Estonia	546	682
Finland	2,892	2,612
Latvia	3,306	3,421
Lithuania	737	737
Poland	-	381
Russia	10,029	5,872
Ukraine	6,069	4,590
Total, loans outstanding	**23,579**	**18,296**

As at 31 December 2012, the loans signed but not yet disbursed totalled EUR 18.39 million (2011: EUR 15.44 million).

Impairment of loans, accrued interest on loans and other loan receivables

NEFCO's loans outstanding, accrued interest and other loan receivables under 'Other receivables' have been reduced by a total of EUR 1.31 million (EUR 1.76 million in 2011) in impairment losses. The following changes were recognised in the statement of financial position in respect of impairment losses.

Impairment, loans outstanding (Amounts in EUR 1,000)	**2012**	**2011**
Impairment losses 1 January	1,528	1,063
Impairment losses recognised during the year	-	531
Reversals of previously recognised impairment losses	-396	-67
Impairment losses 31 December	**1,131**	**1,528**

Impairment, accrued interest (Amounts in EUR 1,000)	**2012**	**2011**
Impairment losses 1 January	5	6
Impairment losses recognised during the year	-	-
Reversals of previously recognised impairment losses	-4	-1
Impairment losses 31 December	**1**	**5**

Impairment, other receivables (Amounts in EUR 1,000)	2012	2011
Impairment losses 1 January	227	627
Impairment losses recognised during the year	88	104
Reversals of previously recognised impairment losses	-139	-504
Impairment losses 31 December	**176**	**227**

A realised credit loss of EUR 481,127 (EUR 0 in 2011) was recognised in the statement of comprehensive income under the item 'Impairment of loans'.

Default loan repayments totalled EUR 1,257,096 (EUR 1,657,096 in 2011).

The maturity profile for loans outstanding as at 31 December:

Maturity (Amounts in EUR 1,000)	**2012**	**2011**
Up to and including 3 months	573	720
3–6 months	758	221
6–12 months	3,912	3,488
1–2 years	4,055	3,069
2–3 years	3,725	3,502
3–4 years	2,655	3,068
4–5 years	2,518	1,893
5–10 years	5,383	2,308
Total, loans outstanding	**23,579**	**18,296**

Loans outstanding by currency:

Currency (Amounts in EUR 1,000)	**2012**	**2011**
EUR	15,376	14,424
RUB	8,203	3,872
Total, loans outstanding	**23,579**	**18,296**

As at 31 December, the guarantee commitments with a maturity of less than 1 year totalled EUR 773,196 (EUR 706,595 in 2011). Any extensions to the commitments are approved annually for 1 year ahead.

Loans outstanding by type of security:

As at 31 December 2012 (Amounts in EUR 1,000)	**Amount**	**Total amount**	**Share %**
Loans guaranteed by governments		-	0.0%
Loans to or guaranteed by local authorities		6,617	28.1%
Loans guaranteed by banks		682	2.9%
Other loans		16,280	69.0%
with mortgage on immovable property	4,220		
with mortgage on movable property	-		
with pledge on shares	1,500		
with floating charge	546		
with a guarantee from the parent company	4,741		
with a negative pledge clause and other covenants	5,273		
Total, loans outstanding		**23,579**	**100.0**

As at 31 December 2012 (Amounts in EUR 1,000)	**Amount**	**Total amount**	**Share %**
Loans guaranteed by governments		117	0.6
Loans to or guaranteed by local authorities		5,101	27.9
Loans guaranteed by banks		250	1.4
Other loans		12,828	70.1
with mortgage on immovable property	4,971		
with mortgage on movable property	-		
with pledge on shares	2,612		
with floating charge	682		
with a guarantee from the parent company	-		
with a negative pledge clause and other covenants	4,563		
Total, loans outstanding		**18,296**	**100.0**

The maturities of the loans extended by the Corporation vary from 1 to 12 years. Of all outstanding loans, 65% are denominated in euros and 35% in roubles. Of the total of 16 loans, 13 are floating-rate loans pegged to the 3-month or 6-month Euribor or Euro Libor rate (Mosprime for RUB) plus margin. Such loans account for 88% of the total. The other 3 loans accounting for 12% of the total have fixed interest rates. Repayment on floating-rate loans are made in equal half-year or quarterly instalments.

(7) INVESTMENT ASSETS

The Corporation's portfolio comprised the following holdings as at 31 December 2012:

Holding	**Country / region**	**% of total capital**
Vardar Eurus AS	Baltic	10.0
4E Biofond OÜ	Estonia	30.1
International Pork Investments AS	Latvia	3.4
DGE Baltic Soil & Environment UAB	Lithuania	34.7
Foster Wheeler Energy Fakop Sp.zo.o	Poland	21.3
Rindipol S.A.	Poland	35.0
Ekovod LLC	Russia	22.0
LTM OOO	Russia	22.8
Halychyna-Zahid LLC	Ukraine	5.6
Dolle Ukraine ApS	Ukraine	33.3
Eskaro Ukraine AS	Ukraine	20.0
Rindibel JC JSC	Belarus	35.0

The acquisition cost of the investment assets was EUR 19,907,394 (EUR 19,207,394 in 2011) while the fair value was EUR 16,453,827 (EUR 15,753,827 in 2011).

FAIR VALUE OF INVESTMENT ASSETS AS AT YEAR END

The following table provides an analysis of the fair value of investment assets at the end of the year broken down by the applicable level in the fair value hierarchy.

(Amounts in EUR 1,000)	**2012**	**2011**
Level 1	-	-
Level 2	1,769	1,769
Level 3	14,685	13,985
Total	**16,454**	**15,754**

Level 1 refers to market prices quoted in an active marketplace.
Level 2 refers to observable data other than Level 1 market prices.
Level 3 refers to information not based on observable data.

The following table provides an analysis of the change in the fair value of Level 3 investment assets.

(Amounts in EUR 1,000)	2012	2011
1 January	**13,985**	**4,012**
Investments during the year	700	1,861
Divestments during the year	-	-2,005
Change in value	-	1,500
Reassignment from Level 2	-	8,617
31 December	**14,685**	**13,985**

(8) OTHER PLACEMENTS

The following table provides an overview of other placements measured at fair value at the end of the year.

(Amounts in EUR 1,000)	2012	2011
NEFCO Carbon Fund	3,742	3,703
Emission reductions	9	219
NMF	-	-
Total	**3,751**	**3,922**

NEFCO's share of NeCF's authorised capital is 2.7% (2.9% in 2011).

The following table provides an analysis of other placements according to the fair value hierarchy.

(Amounts in EUR 1,000)	2012	2011
Level 1	9	219
Level 2	-	-
Level 3	3,742	3,703
Total	**3,751**	**3,922**

Level 1 refers to market prices quoted in an active marketplace.
Level 2 refers to observable data other than Level 1 market prices.
Level 3 refers to information not based on observable data.

NEFCO Carbon Fund and emission reductions

NEFCO has invested EUR 5 million in the NEFCO Carbon Fund (NeCF). 5% of the investment is earmarked as 'Technical Assistance Provision' of which half is committed. The second delivery of emission reductions by the fund took place during 2012 when NEFCO received reductions worth EUR 183,625 (accrued value EUR 802,358). The management fee for NEFCO's investments is paid out of interest income and through reduction in capital. In the valuation of the investment in NeCF, due consideration is also given to the indirect price risk. The investment in NeCF falls in the Level 3 category in the fair value hierarchy. The change in fair value is due to the valuation of the investment in NeCF and the emission reductions received by NEFCO in 2012.

The investment in NeCF has generated 67,523 emission reduction units (CER and ERU) with a total value of EUR 9,154 based on the market price (respective 53,398 and EUR 218,747 in 2011). The investment in emission reductions falls in the Level 1 category in the fair value hierarchy.

Other commitments

NEFCO is committed to invest in the Nordic Environmental Development Fund (NMF) a maximum amount equivalent to DKK 43 million (approx. EUR 5.75 million) during 2011–2013. Of this amount, EUR 1.51 million has been recognised in the 2012 financial statements (EUR 1.92 million in 2011), as a result of which NEFCO has fulfilled its commitment. While the investment in NMF does not yield any financial profit, it contributes to NEFCO's investment activities. As at 31 December 2012, the amount of EUR 1.51 million is recognised as realised loss under 'Net result of financial operations'. The investment in NMF falls in the Level 3 category in the fair value hierarchy.

(9) INTANGIBLE AND TANGIBLE ASSETS

(Amounts in EUR)	2012	2011
Intangible assets	**Computer software, development costs**	**Computer software, development costs**
Acquisition value 1 January	93,503	75,014
Acquisitions during the year	11,301	18,489
Acquisition value 31 December	104,804	93,503
Accumulated amortisation 1 January	63,492	55,967
Amortisation according to plan	12,637	7,524
Accumulated amortisation 31 December	76,128	63,492
Net book value	28,676	30,011

Tangible assets	**Office inventories**	**Office inventories**
Acquisition value 1 January	48,019	44,243
Acquisitions during the year	2,823	3,776
Acquisition value 31 December	50,842	48,019
Accumulated depreciation 1 January	34,206	22,558
Depreciation according to plan	10,410	11,648
Accumulated depreciation 31 December	44,616	34,206
Net book value	6,226	13,813

(10) EQUITY

NEFCO's paid-in authorised capital reached its full amount of EUR 113,406,560 in 2007. The breakdown of the authorised capital is as follows:

(Amounts in EUR)		Share %
Denmark	21,561,320	19.0
Finland	22,264,600	19.6
Iceland	1,319,560	1.2
Norway	24,191,560	21.3
Sweden	44,069,520	38.9
Total, authorised capital	**113,406,560**	**100.0**

(11) INTEREST RATE RISK

Interest rate risk describes how the fluctuations in market interest rates affect the value of NEFCO's interest-bearing assets and liabilities, as well as interest income and expenses. The table below shows the interest rate profile for loans outstanding. Loans outstanding are broken down by maturity or interest adjustment date.

Loans outstanding (Amounts in EUR 1,000)	**2012**	**2011**
Up to and including 3 months	10,735	11,088
3–6 months	10,992	4,916
6–12 months	-	381
1–5 years	546	682
5–10 years	1,306	1,229
Total, loans outstanding	**23,579**	**18,296**

(12) EXCHANGE RATES

The following exchange rates were used to convert monetary assets and liabilities into foreign currency:

		EUR rate 31 December 2012	**EUR rate 30 December 2011**
DKK	Danish krone	7.46100	7.43420
GBP	British pound	0.81610	0.83530
NOK	Norwegian krone	7.34830	7.75400
PLN	Polish zloty	4.07400	4.45800
RUB	Russian rouble	40.32950	41.76500
SEK	Swedish krona	8.58200	8.91200
UAH	Ukrainian hryvnia	10.537171[1)]	-
USD	US dollar	1.31940	1.29390

1) Ukrainian Central Bank as per 31 December 2012

Independent Auditors' Report

In our capacity as auditors appointed by the Control Committee of the Nordic Environment Finance Corporation we have audited the accompanying financial statements of the Corporation, which comprise the statement of financial position as at 31 December 2012, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

The Board of Directors' and the Managing Director's responsibility for the financial statements

The Board of Directors and the Managing Director are responsible for the preparation of the financial statements that give a true and fair view in accordance with International Financial Reporting Standards, and for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Nordic Environment Finance Corporation as of 31 December 2012, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Report on the other requirements

In accordance with the Terms of Engagement our audit also included a review of whether the Board of Directors' and the Managing Director's administration have complied with the Statutes of the Corporation. It is our opinion that the administration of the Board of Directors and the Managing Director complied with the Statutes of the Corporation.

Helsinki, 7 March 2013

Sixten Nyman
Authorised Public Accountant
KPMG Oy Ab

Per Gunslev
State Authorised Public Accountant
KPMG Statsautoriseret
Revisionspartnerselskab

Statement by the Control Committee

In accordance with section 9 of the statutes of the Nordic Environment Finance Corporation, we have been appointed to ensure that the operations of the Corporation are conducted in accordance with the Statutes and to bear responsibility for the audit of the Corporation. Having completed our assignment for the year 2012, we hereby submit the following report.

The Control Committee met during the financial year as well as after the Corporation's financial statements had been prepared, whereupon the necessary control and examination measures were performed. The Corporation's Annual Report was examined at a meeting in Helsinki on 7 March 2013, at which time we also received the Auditor's Report submitted on 7 March 2013 by the authorised public accountants appointed by the Control Committee.

Following the audit performed,
we note that:

- the Corporation's operations during the financial year have been conducted in accordance with the Statutes, and that
- the financial statements give a true and fair view of the financial position of the Corporation as at 31 December 2012 and of its results and cash flows in 2012. The Statement of Comprehensive Income shows a profit of EUR 27 499,73.

We recommend to the Nordic Council of Ministers that:

- the profit for the financial year be treated as proposed by the Board of Directors,
- the Statement of Comprehensive Income and the Statement of Financial Position be adopted, and
- the Board of Directors and Managing Director be discharged from liability for the administration of the Corporation's operations during the accounting period examined by us.

Helsinki, 7 March 2013

Bill Fransson
Thomas Jensen
Hans Frode Kielland Asmyhr
Åsa Torstensson
Tuula Peltonen
Ragnheiður Rikhardsdóttir

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