This section provides an overview of the progress we’re making on our strategy and gives details about our value creation during 2018.

<table>
<thead>
<tr>
<th>Our strategy</th>
<th>18</th>
</tr>
</thead>
<tbody>
<tr>
<td>How we created value in 2018</td>
<td>22</td>
</tr>
</tbody>
</table>

Taking color-matching to the next level

A new standard in quick and reliable advanced color-matching is available to vehicle bodyshops after we combined two of our most innovative tools into a single system.

We’ve hooked up our Automatchic hand-held spectrophotometer with our MIXIT digital color retrieval technology. Now known as Automatchic in MIXIT, the system creates a single, seamless workflow which allows customers to precisely identify any color from an ever-expanding database of more than two million.

It means customers can now measure and match color with superior accuracy even faster. Tailor-made to streamline operations, Automatchic in MIXIT’s ability to improve both accuracy and speed helps to increase profitability and throughput, while reducing waste.

www.colorvation.com
OUR STRATEGY

OUR WINNING TOGETHER: 15 BY 20 STRATEGY

We’re now a focused paints and coatings company with strong global brands, leading market positions and a balanced geographic exposure across all regions, with 50% of revenue from emerging markets. Our ambition is to be the reference in paints and coatings. We’re building our future on solid foundations – our long and proud heritage of more than 200 years, our core principles and our values. Our success will be driven by our passion for paint, our precise processes, our powerful performance and our proud people.

Our Winning together: 15 by 20 strategy is driving a major transformation to accelerate growth and profitability. We’re adopting a laser sharp focus to deliver 15% return on sales1 (ROS) and more than 25% return on investment2 (ROI) by 2020. We’re creating a fit-for-purpose organization with clearer customer focus, continued cost discipline, and a performance-driven culture with simplified ways of working. All our businesses and functions are working together to achieve our ambition. We’re reigniting our passion for making and selling paint by gaining a deeper understanding of our customers’ needs and stepping up our innovation to develop more sustainable products and solutions in the most efficient way.

MORE EFFICIENT AND STREAMLINED ORGANIZATION

Our new organization structure is designed to drive operational synergies and deliver standardization while leveraging expertise across the business. Since the beginning of 2018, we have a faster and more efficient way of working, with two clear focus areas – making and selling paint. Our commercial activities are organized into business units, reporting to the Chief Operating Officer. Meanwhile, all our supply chain activities are led by the Chief Supply Chain Officer. The commercial organization is focused on our customers and leverages product development across our businesses. For the first time, the sales and marketing teams from all business units are aligning their capabilities and processes. For example, rolling out standardized pricing methodology, sales force effectiveness initiatives, margin and portfolio management. Each business unit has a clear mandate to deliver on our 15 by 20 ambition.

The centralization of all supply chain activities – including manufacturing and procurement – into a single global Integrated Supply Chain organization (ISC), with dedicated experts, has been a major change which is already delivering improvements. We’re leveraging scale and expertise across our business units, as well as accelerating continuous improvement through our AkzoNobel Leading Performance System (known as ALPS),

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1 Excluding unallocated corporate center costs; assumes no significant market disruption.
2 Excluding unallocated corporate center costs and invested capital; assumes no significant market disruption.
We can achieve faster standardization, drive improvement in safety, quality, service, cost and capital management as we continue to anticipate current and future needs.

**Simplifying Our Processes**

To ensure these organizations can efficiently collaborate, we’re investing in precise processes, reliable information (master data) and aligned systems. Integrated Business Planning (IBP) helps to connect teams and drive delivery. IBP involves a formal monthly decision-making process led by senior management, with projections for portfolio, demand and supply, resulting in financial forecasts and a single operating plan. This common way of working is fundamental to our new operating model. We expect IBP to drive further efficiencies and enable the achievement of top quartile performance, including increased forecast accuracy, higher service levels and reduced inventories.

During 2018, we also put more focus on getting the waste out of our key end-to-end processes and using reliable, real-time information for decision-making. This will drive further efficiency, improve transparency and enable us to lower the cost of getting products to customers. The deployment of one common ERP (enterprise resource planning) system across all businesses is also in progress, enabling further cost savings and more powerful management of operations and performance.

Our Transformation Office is tracking all initiatives to ensure accountability of different teams to deliver on the cost savings and implement the new ways of working in the organization. In addition to the initiatives already mentioned, we will also achieve significant cost savings through innovation excellence, making our sales force more effective and by streamlining our support functions, for example by transferring some activities to Global Business Services.

We believe in fostering a trusted workforce with strong values, respect for our core principles and a winning mindset. We intend to accelerate opportunities for the talented people we have around the world. We’re building a single, strong and diverse global team for a high performing paints and coatings company. In order to generate stronger collaboration, we’re investing in dedicated, high performing team training throughout the company.

We also conduct regular employee surveys to measure our organizational health. This feedback enables us to take appropriate measures to improve engagement and ensure that team priorities are fully aligned with our Winning together: 15 by 20 strategy.

**Acquisitions and Innovation Contributing to Profitable Growth**

Our strategy is to build on our existing position by focusing on our strong brands, leading market positions, customer intimacy and innovation capabilities. In addition to organic growth, we’re targeting acquisitions to boost our presence in key markets, generate synergies and give us access to new technologies. The acquisitions we made in 2018 demonstrate the success of this strategy. We added Fabryo in Romania, Xylazel in Spain, Colourland Paints in Malaysia, four distributors in the UK (to enhance our network of Dulux Decorator Centres), and acquired the minority interest share to obtain full ownership of the AkzoNobel Swire Paints joint venture in China, reinforcing our positions in all these key markets. We’ve developed a precise process to integrate our bolt-on acquisitions in an efficient and controlled manner.
Our products and technologies already set the industry standard in many markets – and we continue to drive new developments that will keep us ahead of the competition. Our new innovation group is led by our Chief Technology Officer and brings together the combined know-how of experts who now work on one, unified innovation road map. This team includes the AkzoNobel Incubator, which looks for disruptive opportunities, businesses and/or services that go beyond what we do today.

Digital innovation is also a key component of our innovation portfolio. It involves the innovation team partnering with our businesses to develop new solutions closer to our customers’ needs. For example, we use digital innovation to help make choosing the right color easy – from precise color-matching tools such as Automatchic Vision for auto bodyshops, to popular decorating apps like our hugely successful Visualizer, which lets you play (via augmented reality) with color ideas before applying any paint to the wall. Collaboration is the future of innovation, and the announcement of our Paint the Future startup challenge (see page 14) reflects this open, collaborative way of working – and winning – together, both inside and outside the company.

SUSTAINABILITY DRIVING BUSINESS SUCCESS

Sustainability is an integral part of our strategy. Over the last 15 years, our pragmatic approach to business sustainability has enabled us to differentiate ourselves from our competitors. Our commitment to generating more value from fewer resources – and turning environmental challenges and societal concerns into product innovations for customers – is helping to establish us as the reference in paints and coatings. Our value proposition for many stakeholders, including employees and business partners, has also been enhanced by making sustainability an explicit differentiator – part of the AkzoNobel brand. Our main focus areas are value selling and resource productivity.

We continue to develop business opportunities aligned with the most relevant UN Sustainable Development Goals (SDGs). Our agenda is built on core principles of sustainability, safety and integrity, including respect for human rights. We set sustainability targets that contribute to our ROS target, in line with our focus areas of resource productivity and value selling.

By prioritizing our innovation towards developing eco-performer and eco-premium solutions, we enhance our value proposition and give customers choice and competitive advantage through our sustainable product portfolios. We believe we can drive growth by understanding how to build a better business, with solutions for environmental and social needs, as outlined by the SDGs (see page 158).

DELIVERING ON OUR COMMITMENTS

In 2018, we showed that we deliver on our promises. We have created a focused paints and coatings company through the successful sale of our Specialty Chemicals business to The Carlyle Group and GIC. We have increased our regular dividend and confirmed we will return to shareholders the vast majority of the net proceeds from the sale of the Specialty Chemicals business. Our cost discipline has delivered significant savings, while pricing initiatives are in place to compensate for challenges including significant raw material headwinds. By creating a high performing, customer-focused organization, with a clear commitment to deliver on our Winning together: 15 by 20 strategy, we intend to accelerate our growth momentum and enhance profitability. We are committed to increasing returns to shareholders while investing in innovation, sustainable solutions, organic growth and bolt-on acquisitions, creating long-term value for all our stakeholders and becoming the reference in paints and coatings.
The future of fouling prevention has never really had a place in the pages of science fiction. Which is interesting, because we’re working on an exciting innovation which is on the verge of becoming science fact – and wouldn’t look out of place in certain comic book adventures.

Since early 2018, we’ve been developing revolutionary technology designed to eliminate fouling growth from the underwater surface of ocean-going vessels. The secret weapon? Ultraviolet light-emitting diodes (UV-LEDs).

The pioneering solution obtains its superpowers by combining our cutting-edge surface protection and adhesion know-how with underlying technology developed by Royal Philips. The intention is to integrate UV-LEDs in a protective coating and laminate scheme which will allow for UV light to be emitted from the vessel’s surface – providing total prevention of biofouling accumulation on the surface of the protected area.

Recent sea trials have produced impressive results, and with stage two vessel trials already underway, the project is on course to deliver a first commercially viable solution by around 2023.

The implications are huge, because biocidal-free total control of biofouling would represent a substantial economic and environmental benefit for ship owners and operators – not to mention the positive impact on our planet. All of which are inherent in our sustainable approach to doing business.

“This is an exciting project which is fully aligned with our continuous focus on innovation,” explains Klaas Kruthof, AkzoNobel’s Chief Technology Officer. “Combining our capabilities with Royal Philips’ technology will enable us to accelerate the realization of this transformative innovation, which has the potential to completely revolutionize the fouling control industry.”

Initially, the focus will be on applications for ships, yachts and offshore assets, but the project will be extended to include other surfaces and areas challenged by biofouling issues. More partners will also be joining to add essential capabilities and accelerate the development.
How we created value in 2018

By bringing more value to our customers, investors, employees and society in general, we can better position ourselves for growth while accelerating profitability.

**Summary of financial outcomes**

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2018</th>
<th>Δ%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>9,612</td>
<td>9,256</td>
<td>(4)</td>
</tr>
<tr>
<td>Adjusted operating income</td>
<td>905</td>
<td>798</td>
<td>(12)</td>
</tr>
<tr>
<td>Operating income</td>
<td>825</td>
<td>605</td>
<td>(27)</td>
</tr>
<tr>
<td>ROS%</td>
<td>9.4</td>
<td>8.6</td>
<td></td>
</tr>
<tr>
<td>ROS%, excluding unallocated costs</td>
<td>10.6</td>
<td>10.6</td>
<td></td>
</tr>
<tr>
<td>OPI margin %</td>
<td>8.6</td>
<td>6.5</td>
<td></td>
</tr>
<tr>
<td>Average invested capital</td>
<td>6,494</td>
<td>6,340</td>
<td></td>
</tr>
<tr>
<td>ROI%</td>
<td>13.9</td>
<td>12.6</td>
<td></td>
</tr>
<tr>
<td>Capital expenditures</td>
<td>250</td>
<td>160</td>
<td>(36)</td>
</tr>
<tr>
<td>Net debt</td>
<td>1,961</td>
<td>(5,861)</td>
<td></td>
</tr>
<tr>
<td>Number of employees</td>
<td>35,700</td>
<td>34,500</td>
<td>(3)</td>
</tr>
<tr>
<td>Net income from continuing operations</td>
<td>439</td>
<td>410</td>
<td>(7)</td>
</tr>
<tr>
<td>Net income from discontinued operations</td>
<td>393</td>
<td>6,264</td>
<td></td>
</tr>
<tr>
<td>Net income attributable to shareholders</td>
<td>832</td>
<td>6,674</td>
<td></td>
</tr>
<tr>
<td>Earnings per share from total operations (in €)</td>
<td>3,31</td>
<td>26.19</td>
<td></td>
</tr>
<tr>
<td>Adjusted earnings per share from continuing operations (in €)</td>
<td>2.35</td>
<td>1.91</td>
<td>(19)</td>
</tr>
<tr>
<td>Adjusted earnings per share from total operations (in €)</td>
<td>4.06</td>
<td>3.78</td>
<td>(7)</td>
</tr>
<tr>
<td>Net cash from operating activities</td>
<td>278</td>
<td>162</td>
<td>(42)</td>
</tr>
</tbody>
</table>

1 ROS% = Adjusted operating income/revenue.
2 ROI% = 12 months adjusted operating income/12 months average invested capital.
3 Represented for the new adjusted earnings per share definition, which no longer excludes post-tax amortization charges.

**Economic Value**

**Financial overview**

Revenue was 4% lower, although up 1% in constant currencies, with positive price/mix partly offset by lower volumes. Adjusted operating income of €798 million (2017: €905 million) was impacted by adverse currencies, higher raw material costs and lower volumes, not yet fully offset by positive price/mix and cost savings. Operating income was €605 million (2017: €825 million) and includes the adverse impact of identified items of €193 million (mainly related to transformation costs of €130 million) and one-off non-cash pension costs (€57 million). ROS excluding unallocated costs was 10.6% (2017: 10.6%). ROS was at 8.6% (2017: 9.4%) and ROI at 12.6% (2017: 13.9%).

**Revenue**

Revenue was 4% lower, although up 1% in constant currencies. Volumes were 5% lower versus an exceptionally strong last year in China and driven by our value over volume strategy.

**Revenue development in % versus 2017**

- Increase
- Decrease

<table>
<thead>
<tr>
<th>Volume</th>
<th>Price/ mix</th>
<th>Acquisitions/ divestments</th>
<th>Exchange rates</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>-5%</td>
<td>6%</td>
<td>0%</td>
<td>-5%</td>
<td>-4%</td>
</tr>
</tbody>
</table>

**Revenue by destination in %**

- A Mature Europe: 34
- B Asia Pacific: 31
- C North America: 12
- D South America: 9
- E Emerging Europe: 9
- F Other regions: 5
• In Decorative Paints, revenue was up 1% in constant currencies. Price/mix was 4% positive. Pricing initiatives offset lower volumes.
• In Performance Coatings, revenue was up 1% in constant currencies. Price/mix effect was 7% positive, while volumes were lower.

Acquisitions
• The acquisitions of Xylazel in Spain and Doves Decorating Supplies in the UK were completed in September 2018.
• The acquisition of Fabryo Corporation S.R.L. was completed on October 1, 2018.
• The acquisition of Colourland Paints Sdn Bhd and Colourland Paints (Marketing) Sdn Bhd in Malaysia was completed in November 2018.
• The acquisition of the minority interest share to obtain full ownership of the AkzoNobel Swire Paints joint venture in China was completed in December 2018.

Raw material price development
Raw material prices in 2018 were higher compared with the previous year. Robust pricing initiatives continue being implemented to deal with these higher raw material costs. In the latter part of the year, inflation continued, although at a slower rate than during the start of the year.

Adjusted operating income
Adjusted operating income at €798 million (2017: €905 million), was impacted by adverse currencies, higher raw material costs and lower volumes, partly compensated by pricing initiatives.

Savings from continuous improvement were €165 million, while creating a fit-for-purpose organization fully delivered on the €110 million planned for 2018.
• Decorative Paints was impacted by higher raw material costs and adverse currency effects, partly compensated by higher selling prices and cost savings. ROS was 9.4% (2017: 9.0%).
• Performance Coatings was also impacted by foreign currencies and higher raw material costs, as well as lower volumes. ROS was 11.3% (2017: 11.6%).
• Other activities/eliminations decreased by €62 million. 2017 was impacted by one-off items as well as lower pension and insurance related costs.

Operating income
Operating income was negatively impacted by identified items totaling €193 million, mainly related to restructuring costs for the transformation of the Paints and Coatings organization (€130 million) and a one-off non-cash pension cost (€57 million) for the Guaranteed Minimum Pensions equalization regulations, based on a UK precedent set in October 2018.

Net financing income and expenses
Net financing expenses decreased by €26 million, mainly due to a one-off interest benefit on a tax settlement and a lower interest on discounted provisions driven by discount rate developments.

Income tax paid

<table>
<thead>
<tr>
<th>Year</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income tax paid in € millions</td>
<td>229</td>
<td>266</td>
<td>164</td>
</tr>
</tbody>
</table>

Income tax
The effective tax rate decreased to 20.6% (2017: 33.1%), mainly as a result of a re-recognition of certain deferred tax assets and a tax settlement. Excluding these, the 2018 effective tax rate was 28%.

Cash flows and net debt
Operating activities in 2018 resulted in an inflow of €162 million (2017: €278 million). This was mainly caused by lower profitability and related non-cash items, as well as higher working capital, partly offset by lower payments from provisions.

Investing activities resulted in an outflow of €5,668 million, mainly driven by investment of the cash proceeds from the sale of the Specialty Chemicals business in short-term investments.

At December 31, 2018, net debt was €5,861 million negative versus €1,951 million positive at year-end 2017. The decrease was mainly driven by the receipt of the cash proceeds from the sale of the Specialty Chemicals business.

Invested capital
Invested capital of continuing operations at December 31, 2018, totaled €6.2 billion, up €0.2 billion from year-end 2017. Operating working capital as percentage of revenue increased to 12.3% at year-end 2018 (2017: 10.2%), mainly due to higher trade receivables and increased inventories, driven by higher raw material costs.

Allocation of 2018 capital expenditures of €160 million (1.7% of revenue)
Innovation investments
research and development expenses
in € millions

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>257</td>
<td>270</td>
<td>264</td>
</tr>
</tbody>
</table>

Dividend in €

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1.65</td>
<td>2.50</td>
<td>1.80</td>
</tr>
</tbody>
</table>

1 1 2016 is represented to present the Specialty Chemicals business as discontinued operations.

1 1 Excludes special cash dividend of €4.00 per share paid as advance proceeds related to the separation of Specialty Chemicals.

1 1 Proposed.

Innovation
We continue to invest in research, development and innovation to help us fulfill future customer needs and fuel our targeted growth in revenue share of eco-premium solutions with customer benefits.

Eco-premium solutions
We achieved 22% of total sales from eco-premium solutions with customer benefits, ahead of our 2020 target of 20%. Eco-premium solutions are a moving target as they need to exceed the sustainability performance of the constantly evolving market reference. Initial assessments indicate that another estimated 20% of sales were from eco-performers, which have clear sustainability features, and are overall on a par with mainstream alternatives. Total sales of sustainable solutions was around 42%.

For more details, see Note 1 of the Sustainability statements.

Dividend
Our dividend policy is to pay a stable to rising dividend. In 2018, an interim dividend of €0.37 per share (2017: €0.56) was paid.

Earnings per share total operations in €

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3.87</td>
<td>3.31</td>
<td>26.19</td>
</tr>
</tbody>
</table>

Adjusted earnings per share in €

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3.80</td>
<td>4.06</td>
<td>3.78</td>
</tr>
</tbody>
</table>

1 1 Represented for the new adjusted earnings per share definition, which no longer excludes post-tax amortization charges.

In line with our announcement on April 19, 2017, we intend to return the vast majority of net proceeds from the sale of Specialty Chemicals to our shareholders.

The Extraordinary General Meeting of November 13, 2018, approved the return of €2.0 billion to shareholders by means of a capital repayment and share consolidation, which was executed in January 2019. A share consolidation ratio of 9:8 was applied.

We will distribute €1.0 billion by means of a special cash dividend of €4.50 per common share (post consolidation) on February 25, 2019.

A share buyback program to repurchase common shares up to the value of €2.5 billion is due to be completed at the end of 2019. We intend to cancel these shares after repurchase.

We propose a 2018 final dividend of €1.43 per share (post consolidation), which would equal a total 2018 dividend of €1.80 (2017: €2.50, including €0.85 related to the Specialty Chemicals business) per share.

We are continuing with our transformation to deliver the next €200 million cost savings by 2020, incurring one-off costs in 2019 and 2020.

We target a leverage ratio of between 1.0-2.0 times net debt/EBITDA by the end of 2020 and commit to retain a strong investment grade credit rating.

ENVIRONMENTAL VALUE

We manage the environmental impact of our sites through our Resource Productivity program. We focus on three key indicators – waste, energy and VOC emissions – for which targets are in place.

Waste
Effective raw material management helps to eliminate waste in our manufacturing operations, while reducing both our environmental footprint and costs. Our target is to drive towards “zero waste to landfill”, with our first priority being to eliminate hazardous waste to landfill.

Total waste volume and waste per ton of production generated were down by 12% and 8% respectively in 2018, which meets the reduction target of 5% per ton of production from 2017. Hazardous waste per ton of production decreased by 6%.
For more details, see Note 3 of the Sustainability statements.

Energy and greenhouse gas emissions
In 2018, energy use per ton of production remained flat, while absolute energy consumption was down 3% compared with last year. Our total share of renewable energy was 31%.

Electricity consumption and fuel for heating are the main drivers for greenhouse gas (GHG) emissions from our facilities. GHG emissions per ton of product increased 1%, with absolute emissions decreasing 4%.

For more details, see Note 3 of the Sustainability statements.

VOC emissions
Most of the air emissions generated from our operations are volatile organic compounds (VOC). We aim to reduce emissions through product design, good management practices, and environmental controls at our sites.

VOC emissions per ton of product and our total VOC emissions decreased by 4% and 8% respectively.

For more details, see Note 3 of the Sustainability statements.

Cradle-to-grave carbon footprint
As a focused paints and coatings company, more than 98% of our emissions come from our suppliers and customers. Applying the principles of circular economy across the value chain will be our biggest contributor to the Paris climate agreement. We continue to work with suppliers so we can source material with a low carbon footprint, such as renewable raw materials or materials generated with renewable energy. We also continue to offer our customers technologies and solutions to help reduce their emissions and material use.

Our value chain emissions were 5% lower than in 2017.

For more details, see Note 5 of the Sustainability statements.

SOCIAL VALUE

Employees
We use a quarterly company-wide employee survey, which goes beyond only measuring people engagement and focuses on measuring our wider organizational health. In 2018, our organizational health score was 58. The outcomes of the survey are reflected in action plans. We aim to be in the top quartile in 2020 (currently 77).

At year-end 2018, the number of employees decreased by 3% to 34,500 people (year-end 2017: 35,700 people).

For more details, see Note 6 of the Consolidated financial statements.

Safety
AkzoNobel strives to deliver leading performance in health, safety, environment and security (HSE&S) with a vision to deliver zero injuries, waste and harm through operational excellence.

The number of reportable injuries reduced by 5% compared with last year, while the injury rate is already at the target level set for 2020 (0.20 per 200,000 hours worked).

For more details, see Note 7 of the Sustainability statements.

Programs
During 2018, we carried out 49 Community Program projects and 65 “Let’s Colour” projects.

For more details, see Note 9 of the Sustainability statements.