



Summary

KLM conducts a sustainability policy geared to creating economic, social and ecological value. By striking an equitable balance between these three pillars, the company wishes to realize its business objectives while respecting the opportunities for future generations to meet their own needs. This report has been written to inform KLM's stakeholders of the development and progress made with this policy and of the results achieved in fiscal year 2002/2003.

Airlines are being hit hard by the economic instability. Despite the uncertainty, KLM remains a firm believer in the sustainable growth of the company. Economic, social and ecological factors can complement each other and feed the creation of value. Anticipating the expectations of our stakeholders – customers, staff, local residents and local authorities in the municipalities around Schiphol Airport – helps the company take responsible decisions. The benefits will ultimately also be shared by our shareholders.

Our pursuit of sustainable growth does not yet seem to be a persuasive argument for the average customer to choose KLM. Fortunately, we do receive an occasional question on our sustainability policy, and we reply promptly. Greater interest, of course, would significantly accelerate the implementation of our sustainability policy.

In the social pillar, a new, less detailed CAO (collective labor agreement) was concluded in the past year, one that offers greater personal responsibility and more opportunity for consultation between line managers and staff. It does justice to the diversity of our employees and to the differing needs alive within the organization. A rigorous approach to absenteeism has reduced the rate of sick leave from 7.6% to 7.1%.

To improve KLM's environmental performance, staff must be aware of the organization's environmental impact and of the management system in place to implement, monitor and evaluate the company's environmental measures. We again worked hard on increasing staff awareness in the fiscal year. The environmental management system was re-verified by an external auditor. KLM has ISO 14001 certification and an EMAS Declaration (European Environmental Management and Audit Scheme).

KLM's environmental impact is determined chiefly by aircraft performance, load factors, aircraft maintenance and operational measures. These determine fuel consumption and emissions, and also noise levels. Through its efficient network and many savings, KLM's fuel efficiency is more than 25% higher than the European average.

The introduction of Schiphol's new Polder Runway is of great importance to KLM. It will facilitate further growth subject to new environmental standards that reduce local noise pollution. KLM takes part in the dialog with local residents and takes measures that lie within its span of control in order to enhance the quality of life around Schiphol.

With its hub-and-spoke model, KLM's ambition is to provide efficient transport, where appropriate by means of alternative modes of transport. The company has initiated several projects to encourage travel by train. Not all have met with success, which is determined by our customers' needs and our own commercial results.

Sustainable development will not lose any of its importance to the aviation industry. KLM itself can realize some of the changes it seeks; other improvements require international solutions. Examples of the latter include the improved efficiency of European airspace through the abolition of manmade borders in airspace and the establishment of an international system to trade CO₂ emissions. KLM actively supports these developments and in doing so continuously highlights the importance of an International level playing field.

Terms and Abbreviations

| | | | |
|-------------------|--|-----------------|---|
| AAS | Amsterdam Airport Schiphol | KCS | KLM Catering Services Schiphol bv |
| AEA | Association of European Airlines | Kyoto Treaty | The Kyoto Treaty was agreed in 1997 to reduce CO ₂ and other greenhouse gas emissions. The European Union has undertaken to reduce these gases by 8% in 2012 in comparison with 1990 |
| Aircraft movement | The takeoff or landing of an aircraft | | |
| APU | Auxiliary Power Unit; additional generator to provide power to aircraft on the ground | | |
| CAO | Collective labor agreement | Load factor | Revenue ton-kilometers as a percentage of available ton-kilometers |
| CDA | Continuous Descent Approach; aircraft approach on idle thrust to the landing | LTO cycle | Landing and takeoff cycle. The LTO cycle comprises four phases: taxiing, takeoff, climbing and descending |
| CFCs | Chlorofluorohydrocarbons | LVNL | Air Traffic Control The Netherlands |
| CGS | Schiphol Noise Pollution Commission | Mainport | A mainport is an airport that acts as a primary hub and optimizes the interaction between airport and location factors. A primary hub has a strong focus on intercontinental flights and cargo |
| CO | Carbon monoxide (damaging to health) | | |
| CO ₂ | Carbon dioxide (the most significant greenhouse gas) | | |
| CROS | Schiphol Regional Review Board | | |
| CxHy | General abbreviation for hydrocarbons | MIRA | KLM's Environmental Information and Reporting System |
| Deicing | The removal of ice from an aircraft's wings and fuselage and the prevention of ice formation | MYEA | Multiyear Energy Agreement |
| EEl | Energy Efficiency Index | NIDO | Dutch Initiative for Sustainable Development |
| EEMC | Environmental and Economic Management Committee. Consultative body comprising Amsterdam Airport Schiphol, Air Traffic Control The Netherlands and the airlines that operate at Schiphol. The consultation is designed to minimize the disruption of operations at Schiphol subject to applicable environmental limits. | NO _x | Nitrogen oxides, greenhouse gases that could deplete the ozone layer and contribute to local smog formation |
| ENTAF | Environmental Task Force (part of IATA) | NVLT | Netherlands Association of Aviation Technicians |
| GEs | Ground engineers | SO ₂ | Sulfur dioxide (causes acid rain) |
| GPU | Ground Power Unit. Mobile power unit for aircraft on the ground | VOCs | Volatile organic compounds |
| GRI | Global Reporting Initiative | Wvo license | License issued under the Surface Waters (Pollution) Act |
| Halons | Chemical compound used in fire extinguishers | | |
| HCFCs | Hydro-chlorofluorohydrocarbons with one or more hydrogen atom (cause less environmental harm than CFCs) | | |
| HSL | High-speed rail line | | |
| Hub and spoke | System in which a central airport ('hub') serves a network of direct and indirect destinations ('spokes') | | |
| IATA | International Air Transport Association | | |
| IPCC | Intergovernmental Panel on Climate Change. In its Special Report on Aviation and the Global Atmosphere (1999), the IPCC assessed the effects of flying on the climate and atmospheric ozone | | |

Content and Scope of this Report

Purpose and Target Groups

Step by step, KLM is making its business more sustainable. In this report, the company accounts for the results of its sustainability policy. A second important purpose of this report is to strengthen the dialog with stakeholders. KLM hopes the report will reach a wide readership. Its main target groups are customers, shareholders, staff, people living around Schiphol, politicians, public authorities, environmental organizations and other business relations.

Scope

The information in this report relates to the activities of the KLM corporation (KLM nv) and its wholly-owned holdings KLM city-hopper, KLM Luchtvaartschool, KLM Equipment Services, KLM Catering Services and KLM Arbo Services. References in this report to KLM are to KLM nv, excluding its holdings. Where the report refers to the holdings, this is explicitly stated. Further information on the holdings can be found on the Internet. The holdings conduct their own environmental policies.

As the largest customer and handling company, KLM has a very close working relationship with Amsterdam Airport Schiphol (AAS). The two parties regularly coordinate their environmental policies but retain individual accountability for their own activities and responsibilities. Schiphol Group publishes its own sustainability report on Amsterdam Airport Schiphol.

Reporting period

The information in this report relates to KLM's 83rd fiscal year, which ended on March 31, 2003. Data produced by external sources that report by calendar year relate to the 2002 calendar year. For the sake of clarity, all figures are accompanied by the exact reporting period. The fiscal year is referred to as 2002/2003 and the calendar year as 2002. This report has been verified by KPMG Sustainability. The verification report is included at the back of this report.

Additional Information

This report is intended to present an open and balanced picture of KLM's sustainability policy and its results. More detailed information on a number of subjects can be found on the Internet, as indicated at the end of each section. We hope the combination of this report and the additional information available on the Internet is an improvement. Our intention in using these two complementary and mutually-reinforcing media is to satisfy the information needs of our readers.

Global Reporting Initiative

KLM is a keen supporter of the development of the Global Reporting Initiative guidelines and has drawn up this report in accordance with them. For readers who are interested in the GRI, we have placed a matrix on the Internet explaining KLM's position with regard to the GRI indicators.

Feedback

Suggestions were received from several readers last fiscal year. We greatly appreciate their feedback. Most of the readers responded favorably to the content and presentation of the report. Suggested improvements included the presentation of the same indicators and targets each year, the consideration of certain subjects in greater detail and the broadening of the environmental program into a sustainability program. We have adopted the suggestions where possible. KLM wants to hear from its readers.

Please e-mail us at environmental.services@klm.com. KLM has filed this report with the Association for Environmental Accountancy (ACC) and having done so is a contender for the annual ACC Award, which it has already won twice.

@ Profile of KLM's holdings

@ Information on KLM's financial and commercial performance is available at www.klm.com

@ Schiphol Group's Annual Community Report can be read at www.schiphol.nl

@ The position with regard to the GRI indicators is set out in the KLM-GRI matrix at www.klm.com/sustainability

@ Information on the GRI can be found at www.globalreporting.org

KLM Royal Dutch Airlines

Sustainability Report 2002/2003

KLM Royal Dutch Airlines (KLM) is an international airline operating worldwide. Its home base is Amsterdam Airport Schiphol, one of the most modern airports in the world. KLM forms the core of KLM Group, other members being KLM cityhopper and Transavia.

Through its strong alliance with Northwest Airlines and close cooperation with European and intercontinental network and route partners, KLM Group offers passengers and airfreight shippers more than 125,000 city-pair connections throughout the world via one or more hubs.

KLM Group has four core activities: passenger transport, cargo transport, engineering and maintenance and the operation of charters and low cost / low fare scheduled flights. These activities are performed by the Passenger, Cargo, Engineering & Maintenance businesses and Transavia respectively. KLM Group and its partners serve more than 350 cities, in 73 countries on six continents.

In fiscal year 2002/2003, KLM Group carried more than 23.4 million passengers and 489,000 tons of cargo and provided engineering and maintenance services to more than 20 airlines. Measured by international revenue ton-kilometers, KLM ranks fifth among the 270-plus members of the International Air Transport Association (IATA). KLM Group operates a modern fleet of 219 aircraft, many configured for combined passenger / cargo flights. The number of KLM Group's employees as of March 31, 2003 was 37,487, of whom 31,638 were employed in The Netherlands and 5,849 abroad.

KLM is a key player in a global alliance that commands an important position in the world's three major trading areas: America, Europe and Asia. Its goal is to be the first choice passenger and cargo airline and provider of maintenance services, while consistently enhancing shareholder value, providing a stimulating and dynamic working environment for staff, and participating in mutually beneficial relationships with its partners.

KLM is aware of its influence on people, society and the environment and seeks to balance the company's interests with those of the broader society. The high profile of the aviation industry, the involvement of a large number of stakeholders and the political implications of local and global issues make it essential to strike the right balance. To KLM, sustainability is a pre-condition for it to create support to realize its business objectives. The controlled growth of Amsterdam Airport Schiphol is part of this objective.

Consolidated operating income for 2002/2003 amounted to EUR 133 million negative. Net loss including extraordinary items totaled EUR 416 million negative. Extraordinary items, after allowing for the net effect of taxes, amounted to EUR 230 million negative.

KLM shares are listed on the Amsterdam and New York stock exchanges.

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Letter from the President

I have the great pleasure of presenting you with our first Sustainability Report. It continues the course set last year to arrive at a comprehensive report on the sustainability of our company. The report has been written to inform our stakeholders of KLM's activities in this field and to explain how the company considers and serves their interests. To communicate our sustainability performance transparently and openly, we have prepared the report in accordance with the guidelines of the Global Reporting Initiative.

KLM recognizes the great importance of sustainable growth: the creation of financial, social and environmental value. Not least because it is in our own business interests. The economic, social and ecological aspects of our operations reinforce each other and help create value.

Value creation has proven difficult in the current turbulent economic and political circumstances. Stagnation in our main markets, increased fuel prices, the high cost of additional security measures, fierce competition and the lack of a level playing field in the aviation industry culminated in an operating loss for the year. In this respect, the past fiscal year was a disappointing one and one of the mainsprings of sustainable growth – realizing an operating income – was not achieved. At the beginning of the 2003/2004 fiscal year, we had no option but to announce measures to arrive at a structural reduction in costs and an improved earning capacity.

A great deal is expected of KLM's ability to adapt to rapidly changing circumstances. Precisely in such times, navigating on sustainability is a particularly dynamic and complex learning process. We are therefore pleased with our active participation in the Dutch Initiative for Sustainable Development (NIDO) in 2002, in which we studied the commercial motives for sustainability.

To our regret, this report contains not only successes. The absolute low point was the loss of three colleagues due to industrial accidents. This was a very painful blow for all of us, particularly because KLM puts safety above everything else.

Significant progress was made in transforming our human resources policy. Our aim is to create an environment that optimizes the staff's ability to apply their talents to serve our customers and develop themselves.

We ordered new aircraft during the year. KLM operates a modern fleet and we are continuing to work on reducing our environmental impact. The recertification audit carried out in accordance with international environmental management standards (ISO 14001) in December 2002 confirmed that the environmental policy was firmly anchored in our business.

Balancing the divergent interests of our stakeholders remains a great challenge. We must meet our customers' growing demand for efficient mobility without losing sight of the local inconvenience caused by the aviation industry. Schiphol Airport's new Polder Runway, for example, will be a source of noise pollution in areas that had previously experienced little if any inconvenience. But other areas will enjoy a reduction in noise levels. By talking with its 'neighbors', KLM remains aware of their experiences and can explain its own position.

We evidently cannot please everyone. Nonetheless, we hope all stakeholders will recognize our values in our actions, and trust that this report will help them do so.

Leo van Wijk
President & Chief Executive Officer

We cordially invite you to join us on our journey to sustainability by sharing your opinions with us about this report



*From left to right
Cees van Woudenberg
Peter Hartman
Rob Ruijter
Leo van Wijk*

KLM is working on a sustainability policy to create economic welfare, social value and environmental quality



KLM conducts an active dialog with its local environment.

By striking an equitable balance between these three pillars, KLM wishes to realize its business objectives while respecting the opportunities for future generations to meet their own needs, in particular the need for mobility, income, good working conditions, self-development and a high quality of life.

To serve the interests of its customers, staff and shareholders, KLM efficiently meets the demand for passenger and cargo mobility. Demand for mobility is growing. People want to travel, to push back frontiers, to keep in touch with family and to do business. Travel gives many people wonderful experiences and new opportunities for personal growth and development. In the words of Albert Plesman, the founder of KLM: 'Aviation unites all peoples'. In doing so, travel creates welfare and well-being.

As well as its positive effects, travel also has a negative side. Flying pollutes the environment, as does road, rail and water transport. KLM is keenly aware that local residents experience both the pleasure and the pain of the aviation industry.

The high profile of the aviation industry, the involvement of a large number of stakeholders and the political overtones of the local and global issues facing us make it difficult to balance the various interests. That is why dialog with stakeholders is so important: we cannot realize our business goals without taking their interests into account.

KLM therefore has a direct commercial interest in sustainable business. We can retain social support for our business objectives by showing that we take all reasonable measures to limit our environmental footprint.

Since economic, social and environmental interests often run parallel with each other, we can successfully strike an equitable balance on many fronts. This is illustrated by the construction of the new aircraft engine overhaul center that began last year. This investment is a fillip for high-quality employment in the Schiphol region and also for suppliers and aviation technology knowledge centers. Health, safety and environmental features were designed into the building at a very early stage.

Other parallels in the economic, social and environmental interests can be found in KLM's fleet replacement program and its policies on absenteeism and the transport of live animals. This report looks at these examples. In some cases, stakeholders indicate that an equitable balance has not yet been achieved. An example of this is the use of capacity at Schiphol Airport in the early morning. This capacity utilization is important to KLM, but KLM is aware of the public opposition to it. We will have to keep working on solutions that reduce opposition and increase support.

For KLM sustainable development is a continuous process without a fixed destination. Today's economic reality is making the process more challenging. Securing the continuity of the company remains the first requirement for creating social and ecological value.

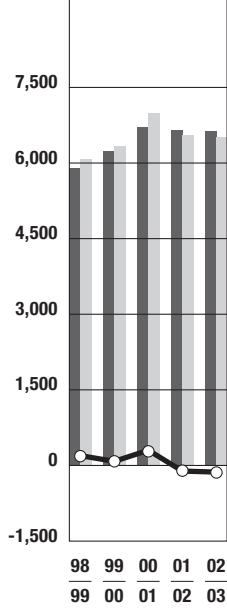
Our ambition is to generate added value for customers, staff and shareholders; the economic importance of the aviation industry is more far-reaching

International Economy The development of the international economy is a matter of concern and the aviation industry is certainly not escaping the consequences. KLM Group incurred a loss for the second year in succession. The financial statements explain in detail the development of our commercial results, the reasons for their being below target and the measures KLM is taking to restore earning capacity.

Many developments facing the aviation industry are not cyclical but structural in nature. We shall therefore have to continue working hard on the economic dimension of our company. This might raise questions about the feasibility of sustainable growth. In our opinion it is a realistic ambition, because economic, ecological and social interests are inseparable. Many environmental targets contribute to the company's commercial profitability. Being more efficient and cleaner, for example, modern aircraft produce both economic and ecological benefits. KLM has a modern fleet, one in which it again made substantial investments during the fiscal year.

National and Regional Economy

A strong aviation industry is important not only to create value for customers, staff and shareholders. It is also essential to the regional and national economy. The presence of a reliable international network of connections and destinations is a precondition for many companies to locate near to Schiphol. This is illustrated by the location of the flower auction, the distribution centers and many other companies that conduct international business from The Netherlands. The international network of flights operated by KLM and other airlines from Schiphol is a source of jobs for the Dutch economy. A report published by Nyfer (*Living on Air*, September 2002) calculated that an increase of one million passengers at a major European airport such as Schiphol creates, on average, 8,600 jobs in the region and raises the gross regional product by EUR 500 million.

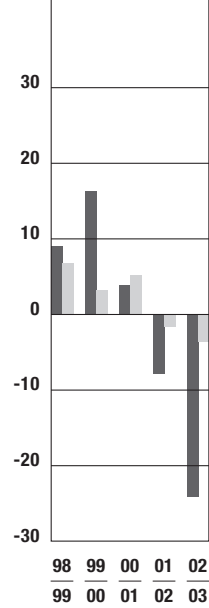


Operating revenues, expenses and result¹

Result in millions of euros
(02/03: -133)

Total expenses in millions of euros
(02/03: 6,618)

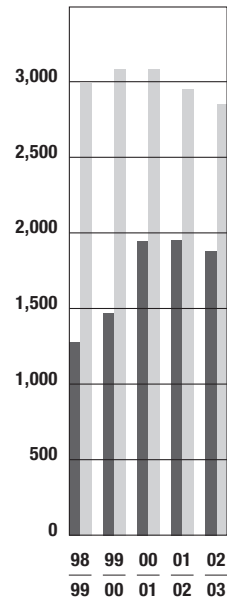
Revenues in millions of euros
(02/03: 6,485)



Return¹

Return on equity in %
(02/03: -24.1%)

Return on capital employed in %
(02/03: -3.5%)

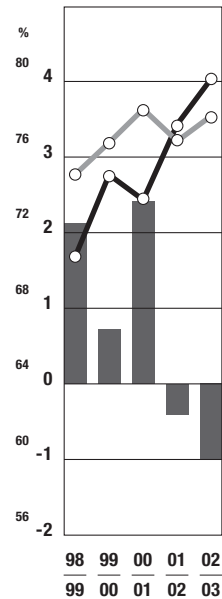


Product and service procurement from third parties¹

Products in millions of euros
(02/03: 1,869)

Services in millions of euros
(02/03: 2,842)

Products: Jet fuel + cost of materials consumption + depreciation
Services: All other items with the exception of salaries and social security costs

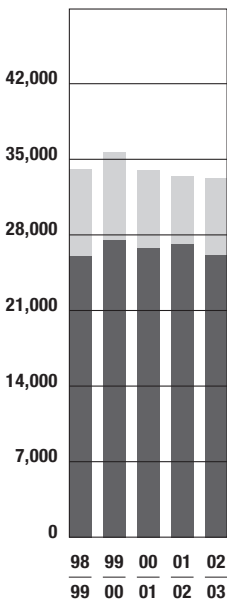


Margin and load factor¹

Break-even load factor in %
(02/03: 80.2%)

Load factor in %
(02/03: 78.2%)

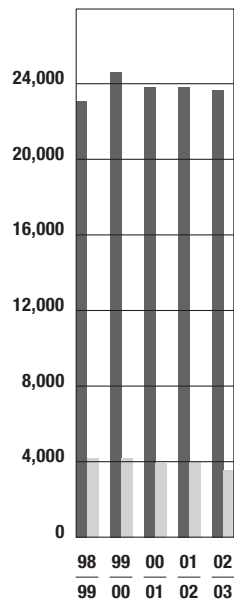
Margin per available ton-kilometer in cents
(02/03: -1.0 cents)



KLM Group staff

Other KLM in average full-time equivalents, including temporary staff
(02/03: 7,113)

KLM company in average full-time equivalents, including temporary staff
(02/03: 25,925)



KLM company staff in The Netherlands and abroad

Number of staff in The Netherlands
(02/03: 23,543)

Number of staff outside The Netherlands
(02/03: 3,532)

In average full-time equivalents including temporary and agency staff

The Importance of Transfer Passengers

Together with its partner Northwest Airlines, KLM is able to operate a worldwide network of more than 125,000 city-pair connections from the Schiphol mainport. A mainport is a central airport at which traffic flows (passengers and cargo) come together and are combined. The passengers are local (traveling between Amsterdam and a local destination) or transfer passengers (who transfer from one flight to another at Schiphol Airport). This concept is known as a hub-and-spoke system by analogy with a bicycle wheel. The central airport acts as the hub in the wheel and the surrounding smaller airports the feeder spokes.

The Schiphol mainport is the product of intensive cooperation between various players. The government is responsible for arranging international landing rights and regulating safety, environmental and orderly market conditions. The airport operator provides the infrastructure. Airlines such as KLM and its partners provide the worldwide network that allows people and businesses to travel from The Netherlands to many destinations throughout the world. It is this network that is so important to the national and regional economy, given the great reliance on imports and exports. Transfer passengers are essential to construct and maintain the worldwide network. They are also important to other hubs, such as Frankfurt and Paris, but particularly so to Schiphol because the Dutch home market is relatively small and the number of local passengers at Amsterdam is accordingly lower.

The smooth transfer of passengers and cargo is only possible if there are good connections between arriving and departing flights. This makes high demands on the airport's operational integrity. In other words, schedules must be carried out with the fewest disruptions in all weather conditions and delays and cancellations must be prevented. Preventing delays and cancellations is not only of economic importance. Fewer aircraft waiting to land saves fuel and reduces irritation among passengers and staff. KLM therefore works with the other players in the aviation industry to improve operational integrity.

Purchases from Third Parties Since about 68% of KLM Group's net revenues are applied to purchase goods and services from third parties, suppliers in The Netherlands and abroad also benefit from KLM's operations. With some 8% of its total operating expenses relating to fees paid to other states to fly through their airspace or to land at their airports, KLM also contributes to the economies of other countries. The work KLM creates for its staff and third parties both in The Netherlands and abroad has a significant economic value.

Reliable, punctual, caring and friendly. These are the KLM values that are at the heart of everything we do. They are the hallmarks of our service and our relationships with customers, staff and our surroundings. These values contribute to KLM's success.

Customers



To KLM, customer care means more than offering comfort and personal service onboard.

The public at large tends to think of KLM primarily as a passenger airline. Cargo transport and engineering and maintenance, however, are also important to the company. We therefore serve a highly divergent group of customers: not only passengers with their various needs, but also transport companies, international businesses and other airlines. Customers select KLM on clear criteria, for example the network, comfort, personal attention and reliability. For the average passenger, our sustainability activities are not yet sufficient reason to choose KLM. Greater recognition of their importance, however, might rapidly accelerate the implementation of the sustainability policy. For KLM, sustainability is an excellent complement to a reliable product and customer care. The care is particularly evident when circumstances disrupt scheduled operations or passengers have specific needs.

KLM offers unaccompanied children and passengers with limited mobility or specific dietary requirements special facilities. A helpdesk can be called free of charge from anywhere in the world for information on special facilities and assistance to make flights more enjoyable and safer. To encourage customers to travel healthily, KLM provides information and practical tips over the Internet and by means of in-flight videos. KLM has Travel Clinics at four locations in The Netherlands to provide customers with travel and health-related information, advice and facilities. The Travel Clinics are available by telephone 24 hours a day.

In response to the spread of SARS (Severe Acute Respiratory Syndrome) KLM has appointed a dedicated team of medical specialists. After careful consideration of the latest information from the World Health Organization and the Dutch Ministry of Health, Welfare and Sport, the team takes decisions on possible measures. Customer care led to ASSIST volunteers contacting all fellow passengers of a person suspected of having the SARS virus. The fellow passengers, from 33 countries, were contacted and told first about the suspected infection and then that the suspicion was unfounded. Both the passengers and the media greatly appreciated KLM's active provision of information.

KLM continuously and consistently monitors various aspects of passenger appreciation. KLM rates the overall appreciation of its service on the ground and in the air using a four-point scale (excellent, good, reasonable, poor). This intensive monitoring enables KLM to respond quickly to changes in passenger appreciation.

During the past fiscal year, KLM introduced a new complaints procedure. Despite our best efforts, there are times when we cannot live up to our customers' expectations. Complaints are dealt with by 80 customer relations departments worldwide. A central database processes the complaints into management reports for evaluation. The procedure is illustrated by the new catering product on European flights. Following a sharp increase in complaints about catering, the onboard meal was modified in the past fiscal year. At present, by far the majority of complaints relate to delayed or damaged baggage. Schiphol Group implemented a variety of projects to improve the automated baggage handling system at Schiphol in the past fiscal year. Since it was foreseen that the work would disrupt baggage handling, after consultation KLM had a temporary facility built, used additional equipment and hired extra staff. Despite these efforts, too many mistakes were made and there were many complaints about baggage handling.

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© Use the emissions calculator at www.klm.com/sustainability to work out the emissions produced by a KLM flight

Staff

For Cargo's customers, too, our sustainability activities are not a decisive argument. Nonetheless, interest is occasionally shown and when it is we respond promptly. On request, for example, we informed the Astra Zeneca pharmaceuticals group about our sustainability policy. As a result, the two parties are now working together to increase their profitability while reducing their environmental footprint.

Wherever possible, KLM considers all aspects of cargo transport. In the transport of live animals, one of KLM's specialties, for example, animal welfare comes first. Animals will only be carried if the entire chain from the animals' origin to their destination is transparent. KLM's quarantine station was set up in close consultation with the Government Meat and Livestock Inspectorate. The station is the only one at Schiphol Airport that complies with European regulations on the import and transit of live animals. KLM holds talks with various organizations, including The Netherlands Society for the Protection of Animals, on basic standards for the transport of animals in aircraft. Although these organizations are in principle opposed to transporting live animals, they recognize the care we take and therefore prefer KLM.

In certain cases, Engineering & Maintenance's customers also ask about KLM's working conditions and environmental policy or for a declaration that KLM complies with applicable legislation and regulations. This report is one of the media KLM uses to inform its customers of these issues.

KLM will continue to work hard on retaining its preferred position with passengers, cargo shippers and engineering and maintenance customers.

A Modern CAO Baggage handlers, pilots, engineers, stewardesses, animal carers, instructors, meteorologists and office staff. KLM has a highly diverse workforce. Its business units, moreover, have divergent characters: Passenger, for example, is fundamentally different from Engineering & Maintenance. Despite this unique staff complement, KLM's personnel policy has long been known for its rigid centralization and uniformity. The new CAO (collective labor agreement) agreed last year can be seen as a first step towards a new approach, one with fewer rules and more personal responsibility. KLM wants to create more opportunity to reach decisions through consultation between line managers and staff. KLM hopes the CAO will do justice to the diversity of our staff and the divergent needs within the organization. The new CAO is more appropriate to today's employees, who do not need to have every detail of their work laid down in procedures and rules but can make individual agreements with their line managers. At the same time, KLM hopes the new CAO will create more flexibility and increase productivity so that staff are better equipped to meet the challenges presented by the market.



KLM Catering Services Schiphol bv, an autonomous KLM subsidiary, works for 12 airlines. Every day KCS makes 40,000 meals and organizes drinks, newspapers and other requirements to make the flights as enjoyable as possible.

The multicultural society of KLM Catering Services Schiphol bv

Some 1,600 people with about 45 different nationalities work at KLM Catering Services Schiphol bv (KCS). Owing to the range of cultures, beliefs and backgrounds, KCS is known as a multicultural society, the world in miniature. The great diversity of ethnic groups has been part of KCS's identity for many years and has become a characteristic feature of the organization.

This cultural mix increases familiarity with and respect for each other's backgrounds. Employees from countries that are in conflict generally work harmoniously with each other. For colleagues, harmony is more important than conflict. Internal publications such as the staff magazine and KCS's annual staff report feature all the staff's backgrounds, experiences and outlooks in interviews and articles. Open communication, clear rules, respect and appreciation for each other are key concepts. Experience shows that this is a fruitful approach, as evidenced by the promotion of people from differing backgrounds to managerial and support positions.

Respect and support for people whose differing backgrounds exposed them to difficulties were particularly important in the aftermath of the attacks in the United States on September 11, 2001. Through clear communication – and care for staff – KCS paid additional attention to the position of various groups; its message was 'KCS stands for all its 1,600 employees, regardless of their backgrounds, beliefs and cultures'. Our staff display a high degree of solidarity precisely at such times.

KCS is a Dutch company subject to Dutch rules and standards. A staff complement from so many backgrounds is a strength for our organization, not an obstacle.

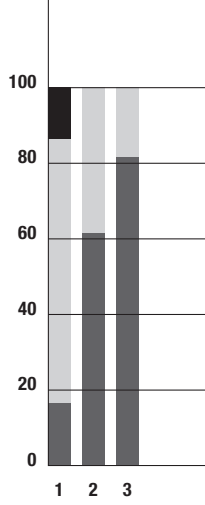
Through an active prevention and reintegration policy, the number of KLM employees becoming incapacitated for work fell by 24% in comparison with the previous calendar year. In comparison with the national fall in the number of new incapacity benefit claimants of 10%, this is a good result. Of the 450 KLM employees who applied for incapacity benefit during the calendar year, 31% were wholly incapacitated. The inflow of new claimants at KLM is still slightly higher than the national average. Nationally, the figure is 1.53%; at KLM it is 1.70%. Long-term sick leave at KLM declined from 7.6% to 7.1% during the calendar year. This decline testifies to the success of the targeted approach developed by KLM to tackle sick leave and incapacity for work, but both KLM and the Works Council think improvements can still be made. KLM will therefore continue to pursue an active policy to reduce the rate of sick leave even further. The well-being of our staff is very important to us. Furthermore, absenteeism costs the company a lot of money: the direct and indirect costs in the past fiscal year are estimated at approximately EUR 130 million.

The new Human Resources system is supported by various tools including an intranet site with information on the personnel system. Employees consult the site about 1,000 times a day.

Employment conditions are being modernized in dialog with eight trade unions and the Works Council. The ambition is to keep working on an environment that optimizes the employees' use of their talents to serve our customers. The divergent interests generally do not stand in the way of constructive cooperation, as evidenced by the agreement of the current CAO. The labor dispute with a group of ground engineers represented by the NVLT was an exception to the rule that harmed working relations within KLM and raised many questions outside the company. The agreement that was reached is a mark of mutual respect and teamwork. KLM is a company that overcomes differences of opinion in open dialog. It is in the interests of the staff, unions and management to rise to the challenges of our industry shoulder to shoulder. KLM is therefore working on a plan to improve relations with the aviation technicians, as requested by the Inspectorate for Transport, Public Works and Water Management.

Working Conditions, Safety and Health

The absolute low point of the past year was the accidental death of three members of staff in the course of their work. It was particularly harrowing in view of the very highest priority that KLM gives to safety. The traumatic events were extremely distressing, particularly to direct colleagues. The company medical officer and staff welfare officer were immediately engaged to provide aftercare. Together with KLM, the Health and Safety Inspectorate and the Royal Netherlands Military Constabulary started to investigate the causes of these regrettable events.



Staff diversity 2002/2003

1 Age structure in %

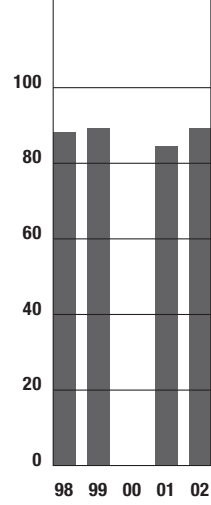
>50: 16%
30-50: 70%
<30: 14%

2 Male/female in %

vrouw: 39%
man: 61%

3 Native Dutch/Ethnic minorities in %

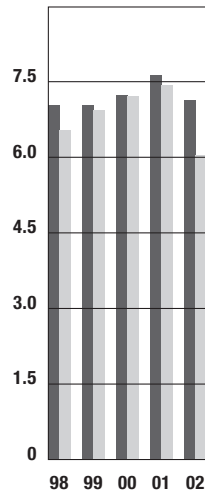
Ethnic minorities: 19%
Native Dutch: 81%



Cabin crew satisfaction

Percentage satisfied or very satisfied in %
(2002: 89%)

No survey held in 2000.

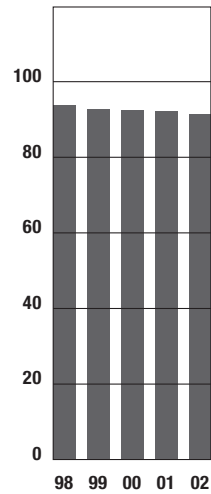


Absenteeism

Absenteeism at KLM in %
(2002: 7.1%)

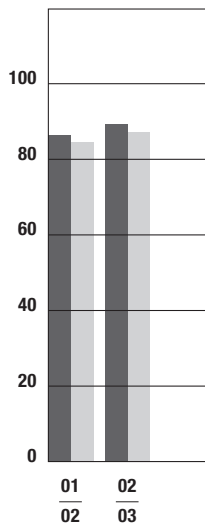
Absenteeism in The Netherlands* in %
(2002: 6.0%)

* At companies with more than 100 employees



Passenger appreciation good or excellent

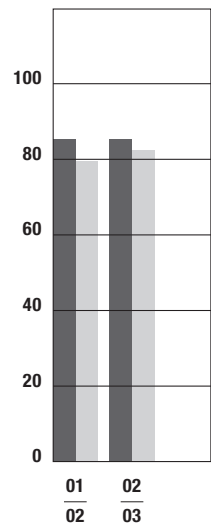
Passenger appreciation good or excellent in %
(2002: 91.0%)



Arrival punctuality Europe¹

Arrival Schiphol in %
(02/03: 89%)

Arrival network including Schiphol in %
(02/03: 87%)



Arrival punctuality intercontinental¹

Arrival Schiphol in %
(02/03: 85%)

Arrival network including Schiphol %
(02/03: 82%)

¹ According to the definitions used by the Association of European Airlines (AEA), a flight is on time if it arrives within 15 minutes of its scheduled time



Paul Elich,
Vice President Hub Operations, Schiphol

Reducing absenteeism is a shared priority

KLM Ground Services is responsible for handling KLM's and its partners' flights when they are on the ground. The services include not only check-in, baggage and loading but also push-back, refueling and cleaning. Much of this work is physically demanding and there is a high risk of physical strains leading to sickness. Last year, Ground Services devoted a great deal of attention to reducing absenteeism.

The 12-month moving average absenteeism rate fell from 10.1% in April 2002 to 9.1% in March 2003. It is still high but the improvement has been considerable and gives us confidence in the future.

The improvement is based on a series of organizational changes. The introduction of teams has reduced the span of control, placed responsibility lower down in the organization, clarified structures and removed anonymity. The weekly socio-medical meeting is also an important part of the absenteeism strategy. Since its entry into force on April 1, 2002, the Eligibility for Permanent Invalidation Benefit (Restrictions) Act has required us to adopt a structured absenteeism strategy. It is expressed in the regular contacts between employer and employees, shared responsibility for absenteeism and documenting the agreements we make.

The Human Resources department oversees, monitors and, where necessary, refines the process.

On the preventive side, we are tackling the problem at its source and looking for technical measures that reduce the physical strain. Ground Services, for example, will invest in a new loading machine, the Rampsnake, this year. It is a mobile and flexible conveyor belt with a lift platform on both sides to load and unload baggage. The Rampsnake will allow us to reduce lifting to virtually zero. The Rampsnake is the first and so far only technical aid in the world that relieves the physical burden when loading and unloading a small fleet. In the future, loading robots at Baggage Services may cut the physical demands even further.

Reducing absenteeism is a joint effort that will remain a top priority in our company!

Staff and Sustainable Business All ambitions and plans stand or fall on what they achieve. The same is true of sustainable business. All parts of KLM contribute to the goal of the sustainable business policy, namely to retain the license to grow. The pluriformity of the staff and the diversity of business processes make an individual approach essential. With Cabin Crew, for example, good communication is necessary to ensure that paper and newspapers are separated from other cabin waste after a flight. With Flight Operations, it is usually necessary to record changes in working practices in procedures or checklists. Examples of this include the development of measurable targets for taxiing with one engine shut down after landing and the evaluation of fuel consumption with pilots. At Engineering & Maintenance, staff present their own initiatives and ideas. They are all worked out but unfortunately not all of them are practicable. In the past year, for example, a study was made of whether the plastic parts of aircraft seats could be separated for recycling. On the initiative of staff, packaging materials are separated and used as filling material when packing shipments.

In KLM's operating environment, where the control of business processes is measured and registered and control mechanisms are highly developed for safety purposes, it is easier to manage by quantitative goals than by qualitative goals. Effective implementation of sustainable business therefore benefits from 'making soft values hard'. Since this is not always possible, managers must be made aware that such 'soft values' as reputation, transparency and public support underpin our commercial success. Our staff do not always recognize commercial initiatives as 'sustainable working practices'. They are just part of their work and they would not use those terms to describe them. But regularly highlighting sustainable developments and their benefits will increase staff awareness of them. This report is a means to increase that awareness.

Local Surroundings

It is important that we have good contacts with the local authorities and residents

The Schiphol region profits from the aviation industry as a creator of jobs and a stimulus for local economic activity. KLM is well aware the airport also has adverse consequences for the region. That is why we are constantly working on improving whatever lies in our sphere of influence. To this end we consult stakeholders, one being the Schiphol Regional Review Board (CROS). The environmental impact on the local surroundings is considered later in this report.

The New Civil Aviation Act During the fiscal year, parliament finally passed a new Schiphol chapter in the Civil Aviation Act and a new system of environmental and safety standards. The introduction of the Act separated policy, implementation and enforcement. The civil aviation industry is responsible for operating within the set environmental limits at Schiphol. This responsibility requires intensive cooperation between all airlines operating from Schiphol, the airport and air traffic controllers. Together, these parties must ensure that the strict rules on noise, emissions and external safety are not breached. To fulfill this responsibility, an Environmental and Economic Management Committee has been installed and agreements have been made between the various parties in the aviation industry. The government will evaluate the new system of standards in 2005. The aviation industry will closely monitor the practicability of the Act and will contribute its experience of the exercise of responsibility and the dialog on avoidable nuisance to the government's evaluation.



The new Polder Runway is very important to KLM.

Polder Runway The Polder Runway was taken into use at Schiphol in February 2003. This is a complicated operation that has been completed in stages. Air traffic controllers must become familiar with traffic handling in the new situation. Several construction issues also still have to be settled. 2003 is therefore a transitional year. The targeted reduction in noise pollution will gradually become apparent. The Polder Runway is very important to KLM. In addition to reducing noise pollution around the airport, the new runway system will enable more flight movements during peak hours. The handling capacity in poor weather will also be higher. There will therefore be fewer risks of disruption to KLM's schedule. This is very important for the quality of the network since delays may lead to customers missing connecting flights. The Polder Runway better guarantees the integrity of KLM's schedule.



Ada Wildekamp,
Acting Chairman Schiphol Regional Review
Board (CROS)

CROS must prove itself in a dialog on the responsible growth of the aviation industry

CROS is a consultative platform made up of representatives from the aviation industry, local residents and other stakeholders. The government has made us responsible for finding the best solutions subject to the noise contours set by the legislator. You could see CROS as a kind of 'polder model' for the aviation industry, taking decisions when we can reach consensus. We have to encourage a productive dialog, but in the end it's not words but deeds that count.

KLM's representatives in CROS, and before that in CGS (the Schiphol Noise Pollution Commission), are certainly constructive. The participants in our platform are building a kind of relationship with each other. They are creating understanding for each other's position and viewpoints. I have noticed that it's not always easy for the KLM representatives to turn their constructive attitude into concrete results within their own company. Other interests are sometimes at play. Things are definitely changing, though. Some adjustments to approach routes are the result of the former CGS.

What I am very pleased with is KLM's decision to provide more feedback on complaints. It is not often clear to the people concerned what happens to their complaints and whether anything comes of them. So there is room for improvement there. That KLM is taking it seriously is not only good for also local residents but KLM itself will benefit.

KLM's fleet is very modern and includes the most noise-friendly aircraft. Since KLM is the largest user of Schiphol, that's an advantage. The new Polder Runway should also have a positive effect on noise pollution. We in CROS will be measuring and evaluating the improvements. We have to measure to know the facts. The responsible growth of the aviation industry, in which the economic, social and ecological aspects are all relevant, is not possible without facts, the exchange of opinions and openness. CROS will have to prove itself in this field.

Dialog In accordance with the new Civil Aviation Act, the Schiphol Regional Review Board (CROS) was established to replace the Schiphol Noise Pollution Commission (CGS). Whereas the CGS had principally been a governmental advisory body, CROS is a consultative platform for regional dialog. Subject to conditions set by the government, the aviation industry agrees noise reduction measures in consultation with local bodies. Local authorities will determine what spatial planning measures will help improve the quality of life. CROS is made up of local representatives (provincial and municipal authorities and local residents' representatives) and the aviation industry (Amsterdam Airport Schiphol, air traffic controllers and airlines). Its primary task is to minimize avoidable nuisances for the local surroundings. Nuisance is avoidable if it can be reduced subject to the applicable legal framework without affecting capacity. It is a means to help improve environmental quality around Schiphol Airport. KLM is keenly aware of how important reducing avoidable nuisance is if local residents are to support the aviation industry.

Compliance with environmental standards and measures to reduce avoidable nuisance are matters that affect all airlines operating at Schiphol. In view of the large proportion of KLM's flight movements in the total number at Schiphol, it goes without saying that we have adopted a pro-active stance. In addition, CROS is responsible for receiving and dealing with complaints about the aviation industry. KLM plays a role in the Review Board, which meets every quarter. Items on the agenda are prepared by the Nuisance Reduction and Complaints working groups.

Schiphol Airport, Air Traffic Control The Netherlands and KLM invited delegations from all surrounding municipalities to a presentation on the new Polder Runway. Twenty-eight municipalities accepted the invitation. Intensive talks were held during the presentation about the balance between the economic, social and environmental aspects of the aviation industry. Departments within KLM also contact local authorities to share know-how and to obtain an understanding of each other's standpoints.

Social Commitment

Jan Post,
Managing Director of the Dutch Red Cross

I know KLM to be a socially committed company

KLM is a typically Dutch company with a fantastic history. Over the years we have often worked together and we are proud to associate ourselves with the KLM brand. I look upon KLM as a distributor of people, goods, health and wealth. It provides a platform for the Red Cross. We were immediately enthusiastic about KLM's initiative to publicize the Red Cross Red Crescent Society's Mother-and-Child Health project in Afghanistan through its AirCares program. There's no doubt the project deserves it: it's a topical and extremely important cause. We are committed to tackling deprivation and neglect among Afghan women and to making them full members of society again. The project will improve their own health and that of their children. Many children are dying from illnesses that are relatively easy to treat, such as diarrhea, respiratory infections and bronchitis. If the mothers are better informed about how to care for their children, the child mortality rate will fall.

KLM supports charity organizations through the AirCares program. Members of staff also take charitable actions on their own initiative.

AirCares Every three months KLM selects an aid organization that works for the development of children in The Netherlands and abroad. The organization selected can use the onboard video, the in-flight magazine, Holland Herald, and 19 other media to reach a large international public. Passengers are invited to donate money or Frequent Flyer points to the charity. KLM also provides financial support to good causes, although the available budgets are limited. Through the operation of the AirCares program, KLM nevertheless makes a highly appreciated contribution to the good causes.



The magazine Holland Herald featured an article on our project, a film was shown in the aircraft and passengers were invited to donate to the project. I think KLM is making clever use of its organization to help our good cause. KLM's ability to make donations is limited. The AirCares program, however, is an appealing and effective alternative. The direct income was not substantial but it gave us a fantastic communications channel to highlight the Red Cross organization. I am very pleased that more and more companies are using their core competences to realize social goals. Fewer sky boxes, less art and more meaning. This is also particularly appealing to young professionals. I know KLM to be a highly committed socially-aware company that offers a lot of help without blowing its own trumpet. As far as I'm concerned it should show more of its humanitarian side, both in word and in deed. I have got many ideas that would raise the profile of KLM's social commitment and make it an even stronger company!

KLM's staff travel the world and see wealth and poverty; their international experience confirms their commitment to AirCares and other social projects

Through our AirCares program, we supported the following initiatives in the past year:

- Warchild, an organization that helps children in regions affected by warfare;
- A project of the Nelson Mandela Children's Fund in South Africa to teach young children about the dangers of HIV and Aids;
- The Mother-and-Child Health project of the Red Cross Red Crescent Society in Afghanistan;
- The Esperanza educational organization for Brazilian street children.

KLM Managing Director Cees van Woudenberg visited several projects carried out by the Liliane Fund in Indonesia during the year. As AirCares ambassador, he wanted to demonstrate his personal commitment to projects supported by the AirCares program. The journey confirmed the importance of the Liliane Fund's work for the many people it helps.

Staff Initiatives On their own initiative KLM's staff organize many activities that demonstrate their social commitment. KLM has a great deal of respect for their charitable activities and voluntary work, of which we can give only a few brief examples here. Twice a year, a project week is organized in which KLM's staff in The Netherlands work for a civil organization for one day. The organizations have more 'hands' to help them carry out a variety of jobs. Last January, staff worked for the Salvation Army, the Dutch Refugee Council and the AAP sanctuary for exotic animals. Staff from Catering Inflight Services have for many years supported the Catholic Action for Street Children in Accra. This year they raised funds by organizing a Christmas high tea at which they sold homemade delicacies.

Wings of Support is an initiative by KLM's flight crews to provide housing and education for children in countries served by KLM. Owing to the nature of their work, flight crews visit many countries and can regularly visit the projects. In the past year, a bush camp was organized for deprived children from an orphanage in Kenya. The enthusiasm for such projects is infectious, as demonstrated by external initiatives that complement Wings of Support. A good example of this is a benefit concert organized in The Hague under the name Swings of Support.

The growth of the aviation industry is increasing the environmental pressure.

KLM continuously works on improving its environmental performance by investing in new aircraft, enhancing its business processes and pursuing an environmentally-aware procurement policy. In international dialog, we actively create support for environmental improvements.

In contrast to previous years, this is more a sustainability report than an environmental report. Nevertheless, we wish to maintain the high quality of our environmental reporting, for which we have already been twice honored with the Association of Environmental Accountancy Award. In this section we consider the spearheads of our environmental policy and the main results. Further information is available on the Internet to provide the complete picture you are accustomed to receiving from us.



KLM Cargo's new freighter has a 'nose door'. One of its advantages is the trouble-free loading of extremely long shipments. Improved customer service, cost savings and enhanced environmental performance often go hand-in-hand, as illustrated by KLM's new cargo aircraft.

Environmental Policy and Organization

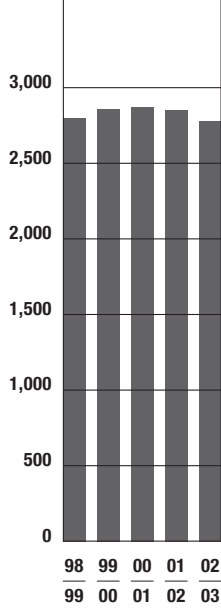
KLM's environmental ambition is to rank among the top airlines in the world. This ambition is laid down in the Environmental Policy Declaration endorsed by the Board of Managing Directors in 1999. An environmental program containing targets and concrete measures is drawn up each year. A summary of the current program is provided at the back of this report. The annual environmental program is an essential part of KLM's environmental management system, which is designed to continuously improve the company's environmental performance. KLM's environmental management system is ISO 14001 certified. Line managers are responsible for realizing the environmental targets. At the highest management level in our organization, a member of the Board of Managing Directors is responsible for environmental affairs. The Corporate Environmental Center supports management and the business units and flags internal and external developments. Environmental managers have been appointed within the business units to assist in the implementation of environmental policy. Active collaboration is sought with stakeholders, suppliers and other chain partners to achieve the environmental goals. Effective internal and external communication is essential. Consultation is held at least every six weeks for the en-

vironmental managers to discuss the environmental program's spearheads and progress. KLM operates the MIRA environmental reporting system to monitor and report upon its environmental impact. Since the past fiscal year, the system has been used to report to the Board of Managing Directors every six months on the current environmental impact. The performance of the environmental management system is verified by means of internal and external audits. During the fiscal year, KPMG Certification subjected the environmental management system to a follow-up ISO 14001 audit. The auditors concluded that KLM satisfied all the requirements of this international environmental management standard, including demonstrable and continuous improvement. Further to the audit, KLM formulated a series of improvement measures to enhance the system's efficiency. On the basis of its verification audit, KPMG Certification (RvA registration number C393) declared that KLM had implemented an environmental management system and reported to the public on its environmental performance in compliance with the EU Environmental Management and Audit System (EC no. 761/2001). This EMAS Declaration related to the Sustainability Report for 2002/2003 published on May 30, 2003.

Fuel Efficiency Fuel consumption during the fiscal year amounted to 2,771 million tons, 1% less than in the previous fiscal year. Total revenue ton-kilometers came to 9,852 million, an increase of 2.6%. Relative fuel consumption to carry 100 kg over 100 km was 3.5 liters, a decline of 3.4% on the previous year. These figures are the outcome of a higher load factor and the more efficient fleet. In comparison with average European fuel consumption, KLM is over 25% more efficient (source: AEA).

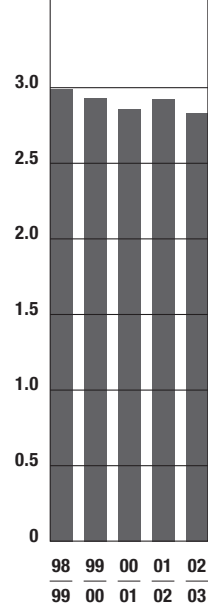
An aircraft's environmental qualities are determined principally by its age and maintenance status. The average age of KLM's fleet is 10.5 years, in comparison with a European average of 10.0 years and a worldwide average of 13.3 years. KLM's continued investment in new aircraft will further reduce the average age.

A new Boeing 747-400 was taken into service during the fiscal year. The first new Boeing 747-400ERF cargo aircraft and Boeing 777-200ER aircraft will be added to the fleet in the current year to replace the Boeing 747-300. The new aircraft are fitted with General Electric's most modern engines and consume 10% (747-400ERF) to 25% (777-200ER) less fuel than their predecessors. KLM will continue to invest in new fleet for the longer term. In the past year, for example, it ordered six Airbus A330-200 aircraft for delivery as from 2005. The Airbus A330-200 has a proven track record for its exceptional operational and commercial performances, its high degree of efficiency and flexibility and its high passenger appreciation. Furthermore, it will contribute to our policy of minimizing the impact on the environment and on residential areas around airports. In view of the narrow margins in the aviation industry, efficiency is not only ecologically but also economically relevant to our company. Efficiency is the first step to sustainability. KLM's sustainability goals are therefore an extension of its business activities.



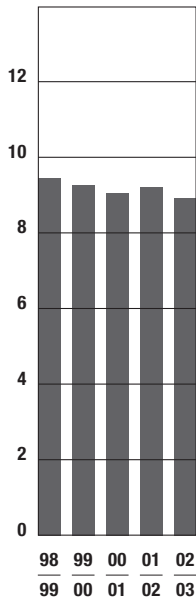
Absolute fuel consumption

Absolute fuel consumption in thousands of tons
(02/03: 2,771)



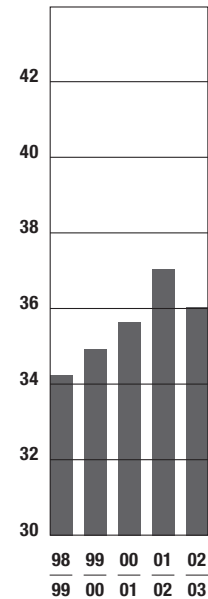
Fuel consumption to transport 100 kg a distance of 100 kg

Fuel consumption in kg
(02/03: 2.81 kg)



CO₂-emissions to transport 100 kg a distance of 100 km

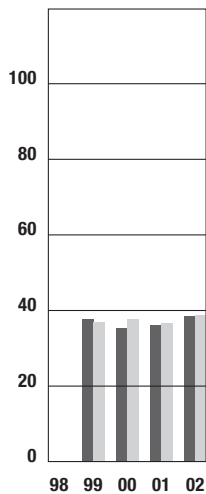
CO₂ in kg
(02/03: 8.88 kg)



NO_x-emissions to transport 100 kg a distance of 100 km

NO_x in gram
(02/03: 36.0 gram)

Wherever possible, KLM makes use of real-time flight data (such as pressure, temperature, fuel consumption for each flight phase) to calculate emissions. If this is not possible for one type of aircraft, emissions are calculated according to data from the manual

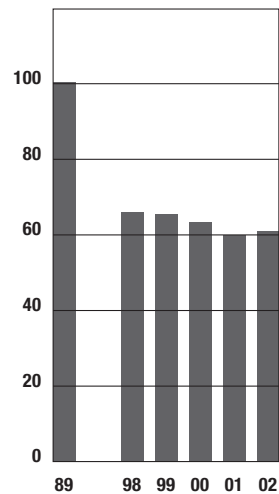


KLM noise nuisance at Schiphol in operations planning year Nov. 2001 - Nov. 2002

Flight movements in %
(2002: 37.9%)

Noise nuisance in %
(2002: 38.3%)

KLM's share in noise pollution at Schiphol Airport was calculated by Adecs bv in accordance with the enforcement method in the environmental legislation effective at Schiphol Airport



Energy-Efficiency Index (EEI)

EEI in %
(2002: 60.5%)



Alan Mulally,
Chief Executive Officer,
Boeing Commercial Airplanes

Manufacturers, suppliers, airlines and stakeholders all need to be involved in improving airplane environmental performance. KLM is an example of an airline that is very pro-active concerning the environmental performance of our airplanes. We work together on a regular basis on environmental issues. This kind of cooperation is very useful. It creates mutual opportunities for learning and it strengthens our relationship.

KLM and Boeing have been working together for a long time to improve the paints used to protect metal from corrosion. KLM is very interested in decreasing the solvents and other harmful chemicals, since this is a great way to ensure improvement for work environments for manufacturing and maintenance worldwide. We are very pleased by the way KLM and Boeing are teaming up.

Boeing cares about the environmental impacts of its products and services - in the air, in the factory or on the ground. We are looking forward to our future with KLM, one of our longstanding customers.

Boeing is a company that cares about the environment. We are actively supporting research that provides ecological benefits, modifying our manufacturing processes to minimize the environmental impact of our airplanes, using resources conscientiously and recycling. It is not only the right thing to do; it also makes good business sense.

Commercial aviation has made great advances during the last 40 years. The sound, emissions and fuel consumption of our airplanes have improved dramatically. In fact, our latest airplanes, like the Boeing 777, are 70% more fuel efficient than airplanes built 30 years ago. This obviously benefits the environment, but it also creates major economic benefits for our airline customers.

Our customers have to be very efficient to succeed in the extremely competitive commercial aviation industry. This means that the best airplanes have the best economic, as well as ecological performance. Our airline customers are very interested in the environmental characteristics of our airplanes and we are proud of the significant improvements we have made.

Greenhouse Gas Emissions The waste gases emitted by aircraft contribute to the greenhouse effect. According to the Intergovernmental Panel on Climate Change (IPCC), the aviation industry's contribution to the greenhouse effect will rise from 3.5% in 1990 to approximately 5% in 2050. The total transport industry produces about 28% of the worldwide emission of CO₂ (carbon dioxide). The aviation industry is responsible for about 11% of these emissions, in comparison with the road transport industry's 74%. Under the Kyoto protocol, the UN civil aviation organization (ICAO) is responsible for formulating aviation policy. KLM supports the developments within the ICAO to arrive at an open system to trade emission rights.

The volume of CO₂ emissions is proportional to the volume of fuel consumed. In the past year, 8.7 million tons of CO₂ were emitted. Flying at cruise altitude was responsible for approximately 93% of these emissions, the LTO cycle for approximately 6% and ground activities for approximately 1%. Increased fuel efficiency reduced relative CO₂ emissions by 3.3%. All Boeing 747-300 aircraft are

gradually being replaced with a combination of Boeing 777-200ER and Boeing 747-400ERF aircraft. The new aircraft are fitted with very clean and economical General Electric engines that produce 10% (747-400ERF) to 25% (777-200ER) less CO₂ but more NO_x. This is because lower fuel consumption and lower CO and C_xH_y emissions are achieved through the use of higher pressure ratios and temperatures, which increase NO_x emissions. The new General Electric engines that KLM will use on the new Boeing 777 aircraft are fitted with low NO_x combustor technology. Despite the use of the best technology available to limit NO_x emissions, the increase cannot be prevented. Minimizing NO_x emissions is important because the gas contributes to the greenhouse effect at high altitudes. KLM's relative emission of NO_x in the past year declined by 2.7%.

Local Environmental Impact

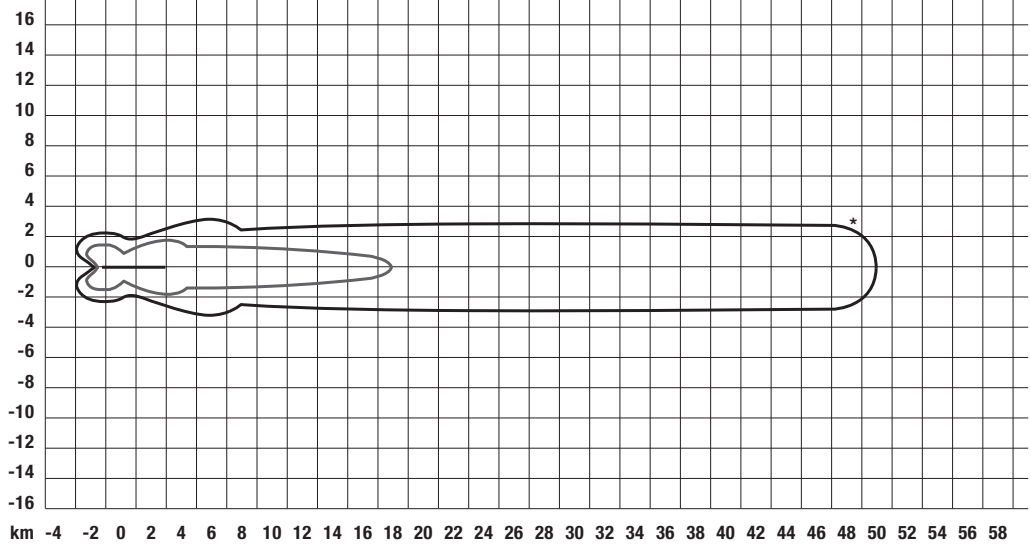
Of the aviation industry's total environmental impact, local residents are most directly affected by noise pollution; reducing noise pollution is one of the priorities in KLM's environmental policy

The total number of flight movements at Schiphol in the past operations planning year was 409,815, 1.6% fewer than in the previous operations planning year. The number of homes affected by noise during the operational planning year was well within the statutory limit and nearly 400 lower than in the 2001 operations planning year. The number of KLM's flight movements during the operations planning year was 155,170, equal to 37.9% of all flight movements. KLM Group as a whole was responsible for 64.3% of all flight movements at Schiphol. Both the number of KLM's flight movements and its contribution to the noise pollution were slightly higher. By modernizing its fleet, optimizing landing and takeoff procedures and optimizing the accuracy with which routes are flown, KLM is working on improving the impact within its span of control.

The cost of the Schiphol Noise Insulation Project is borne by the airlines that fly to the airport. As the biggest user of Schiphol Airport, KLM Group is also the biggest payer.

** The footprint represents the area subject to a particular noise level when an aircraft takes off or lands. New aircraft have a far smaller footprint than older ones, as shown by the 65 dB(A) footprint (the area within the 65 dB(A) contour) for Boeing 747-300 takeoffs (red) and Boeing 777-200ER takeoffs (blue)). With an area of 44 km², the latter is six times smaller than the former (area of more than 275 km²). N.B. the Boeing 747-300 contour line has been rounded on account of the size of the figure.*





Noise Nuisance Noise pollution in the 2002 operations planning year remained within the statutory limits, as they had in the previous year. The number of homes affected by noise also remained well within the maximum permitted number of 12,000, namely 9,287, nearly 400 lower than in the 2001 operations planning year (9,670).

This good result was attributable largely to the productive collaboration within the Environmental and Economic Management Committee (EMC), in which KLM is an active member. The trend is expected to continue in the current year. Use of the Polder Runway will reduce the number of flights over residential areas. In cooperation with the parties concerned, we shall closely monitor the new runway's effects.

KLM's landing and takeoff procedures are designed to limit local noise pollution, for example by routinely flying over the sea at night, Continuous Descent Approaches (CDA) and steeper climb-outs. The modernization of the KLM fleet will make a long-term contribution to reducing relative noise pollution in the coming years. The perceived noise level of a Boeing 777-200ER on takeoff is half that of the aircraft it is replacing, the Boeing 747-300.

The airlines that fly to Schiphol finance the Schiphol Noise Insulation Project through their landing fees. Given the high proportion of KLM's flights in the total, KLM is a major contributor. This two-phase project has been commissioned by the government. The first phase was completed in 1997, with the insulation of about 4,300 homes at a cost of approximately EUR 127 million. The second phase, in which about 14,000 houses will qualify for insulation, began in 1998. The total cost of the second phase is currently estimated at approximately EUR 540 million. It is thought that the actual cost will be considerably higher. The Dutch government's decision to insulate such a large number of houses makes the Schiphol Noise Insulation Project the largest of its kind in Europe. Comparison with other European airports shows that the largest investments in noise insulation are being made around Schiphol. The Netherlands is the only country in which the costs are borne by the airlines and not, as in other European countries, by the airports or governments.

Footprint

Boeing 747-300

Boeing 777-200ER

Runway

Despite our many efforts to reduce noise levels, we are a source of noise pollution. KLM has agreed with the CROS complaints desk that if ten or more complaints are received about one of its flights, the information will be passed on to KLM. This occurred in respect of 12 KLM flights last year. In nearly all cases, Air Traffic Control The Netherlands had instructed the pilot to depart from the prescribed flight route. The instructions lengthened the flight over residential areas. In one case, a KLM pilot had requested a longer runway, which also lengthened the flight over residential areas. Some 40 complaints were received about this flight.

Engine testing on the ground also causes noise pollution. Engine testing is necessary to check engines after, for example, maintenance work. During the fiscal year, KLM performed 1,865 engine tests, a decline on the previous year. Aircraft taxiing to and from the runways also causes noise pollution. Taxiing on fewer engines after landing, a procedure KLM applies wherever possible, makes a modest contribution to reducing this pollution.

Further information on noise pollution around Schiphol is available in Amsterdam Airport Schiphol's Annual Community Report.

Local Emissions Emissions at Schiphol Airport account for 5% to 10% of all air pollution in the vicinity of the airport. KLM's emissions are caused principally by the takeoff, landing and taxiing of aircraft. Furthermore, the vehicles on the platform necessary to load the aircraft, maintain them and supply them with energy also produce emissions. Platform emissions account for only a very limited part of KLM's local emissions, namely 2%. Nevertheless, KLM has made it its policy to reduce them. Working conditions and the environment were important factors in KLM Equipment Services' decision to replace vehicles with hybrid traction units that are both electric and diesel-driven. Their exhaust emissions on the platform are at least 50% lower than those of the vehicles they are replacing. This is helping to improve air quality in areas where many people work, such as on the platform. The type chosen has excellent ergonomic properties, including low vibration levels and noise reduction features.

C_xH_y (hydrocarbon) and CO (carbon monoxide) emissions stabilized after falling substantially in the previous year owing to the reduced use of Boeing 747-300s. Further fleet replacement will continue this downward trend. KLM reduces taxiing emissions wherever possible by shutting down one engine after landing. For the aircraft types on which this procedure is possible, it is applied on about 50% of all incoming flights at Schiphol. For safety reasons, it is not applicable on outgoing flights. Cutting emissions also reduces odors. At other airports, too, KLM applies the procedure of taxiing with one engine shut down after landing wherever possible, but monitoring currently takes place in Amsterdam only.

Aircraft painting and degreasing is a source of solvents (volatile organic compounds, VOCs). KLM is currently testing a new technique to reduce paint use and VOC emissions and also improve working conditions. Apart from this project, alternative methods to degrease aircraft before painting them are being studied. KLM process technicians are seeking alternatives and testing them on their functionality, cost and realizable emission reduction.

Internal Environmental Management

Energy Consumption in Buildings

KLM again participated in the government-sponsored Multiyear Energy Agreement (MJA2). The agreement lasts until 2012 and relates to improving energy efficiency. As part of MJA2, KLM will again review the energy efficiency of its buildings to identify potential energy savings. Opportunities will also be sought to apply sustainable energy sources such as heat/cold storage, thermal solar energy and wind energy.

Improvements can be realized by considering energy efficiency in investment decisions. The new engine overhaul center, for example, is being fitted with a heat/cold storage unit. Depending on the season, heat or cold will be stored underground and used for cooling in the summer and heating in the winter. Heat/cold storage is also expected to be applied in the overhaul center's offices in combination with a heat pump.

KLM is introducing the heat pump as a new energy saving technique within the company. Thanks to its use, the overhaul center's energy efficiency will be about 60% higher than required by law. Savings on the equipment in the building are also being sought. KLM expects the new overhaul center to be a building that its staff will be proud of. It will be environmentally friendly, architecturally attractive and efficient. In short, a building for the future.

Waste KLM's environmental policy also includes waste prevention and the separation of differing waste flows. The main waste flows are waste from aircraft, glass from catering, metals from aircraft maintenance, wood from pallets, foil from cargo handling, cardboard from packaging, and paper from offices and aircraft. A considerable proportion of the waste (more than 30%) is cabin and catering waste from the aircraft, nearly half of which consists of newspapers and magazines. Both waste from buildings and aircraft and hazardous waste are separated. To manage waste flows effectively and to create greater awareness among staff, waste separation tasks and responsibilities have been allocated to the business units.

Owing to the disappointing separation performance in 2001, we intensified the communication and introduced stricter controls. Nevertheless, we again failed to realize our target of 35% separation. New improvement measures have therefore been incorporated into the environmental program. KLM is a signatory to the Third Packaging Covenant. This covenant requires packaging that is imported or marketed to be at least 70% recyclable. Through its purchase of materials, KLM imports packaging. It encourages suppliers to comply with the covenant when supplying aircraft components. To this end, talks are being held with, amongst others, Boeing and General Electric.

The total volume of hazardous waste amounted to 1.3 million kg in 2002. In accordance with legislation and regulations, hazardous waste is supplied to the most suitable processors with a view to recycling it.

Environmental management is an integral part of KLM's operations. KLM applies strict procedures in its aircraft painting and deicing processes.



Water Total drinking water consumption amounted to 101,000 m³, a decrease of 21% on the previous calendar year. KLM samples the quality of its wastewater. Three departures from the discharge standards were detected in the effluent from the fat separators in the staff restaurants last year. The Rijnland water control corporation was informed of the excess levels by means of periodic reports.

Ozone-Depleting Substances The maintenance of cooling facilities and the refilling of fire extinguishers result in the emission of substances that are harmful to the ozone layer, such as halons. KLM's policy is to reduce the use of such substances. The halon fire extinguishers in the buildings and facilities were almost entirely phased out as of March 31, 2003. Both halons and conventional extinguishing agents are used in the aircraft. Their use is permitted under European regulations and no safe alternative is currently available. Despite intensive maintenance of the halon installation, the refilling of aircraft fire extinguishers is still far from perfect.

Environmental Management at Outstations

In the previous report, we announced that the proposal to start a second outstation program had been delayed by the general economic climate. The program was relaunched in the past fiscal year. In addition to presentations for managers, a pilot scheme reviewed a second outstation and GEPs (Good Environmental Practices with guidelines for the organization of environmental management at outstations) were introduced. The lessons learned will determine how the other outstations can be directed and their environmental management organized from The Netherlands in the current fiscal year.

Cooperation We also cooperate with our partners in the field of environmental management. At the end of August 2002, for example, talks were held with Boeing, General Electric, Northwest Airlines, Air France, Delta Airlines and Lufthansa. Each party informed the others of developments in American and European legislation. In addition, they undertook to assist each other wherever possible. KLM used the meeting to raise environmental subjects that are not yet an issue in the U.S. with Boeing and General Electric. The discussions considered, for example, the development of alternatives to halon fire extinguishers in aircraft and the search for alternative solvents to clean and degrease aircraft before repainting them. The European prohibition on the use of bromic fire-retardants in aircraft interiors as of 2004 was also discussed. Furthermore, the transport of hazardous substances by air and related problems were considered, as was the establishment of a consultative platform to reach agreements with suppliers on the delivery of suitable product safety information.

Towards an Efficient Mobility Chain

KLM works on improving not only its own sustainability performance but also that of the entire chain

The previous sections considered KLM's performance in its direct operations: cargo and passenger transport and related ground services. However, KLM's service to its customers requires an interplay with a large number of parties throughout the entire mobility chain. KLM is paying greater attention to the social and ecological dimensions of the services provided by third parties. KLM can influence these services in three areas:

- 1 Optimizing the transport network;
- 2 Procuring products and services;
- 3 Taking initiatives in the aviation industry.

Optimizing the Transport Network As a network carrier, KLM serves a large number of destinations through its hub-and-spoke system. Passengers and freight are carried from various locations to the hub and from the hub to their respective destinations. The choice of aircraft type and use of other transport modes can be optimized depending on the number of passengers, the volume of freight and the distance concerned. The hub-and-spoke system makes it easier to combine passenger and cargo flows and thus make better use of the available capacity and infrastructure. To give one example, KLM realizes a high load factor on the 11 flights it operates to South Africa each week. On four of the flights it uses combi aircraft that carry both passengers and cargo. If KLM flew only cargo or only passenger aircraft from Schiphol, more flights would be needed each week to accommodate the same demand for transport. But this would reduce the load factor per flight and thus be less efficient. If the traffic flows were carried directly to South Africa rather than via the Schiphol hub, the number of flight movements would be considerably higher. The high frequency of connections also enables perishable articles such as flowers and vegetables to be carried to sales markets with sufficient regularity. KLM is thus a link between South African businesses and Western customers.

Transport efficiency would be further enhanced if passengers took the train on short connections. To this end, KLM has taken various initiatives. Since the beginning of 2002, for example, passengers have been able to travel by the Thalys high-speed train between Schiphol and Antwerp in combination with a flight provided by KLM or its partners. In France, KLM and Northwest Airlines' passengers can use their KLM-coded tickets to travel with the TGV high-speed train to and from domestic destinations in France. The number of destinations covered by the contract was recently increased to 14 cities; the total network in France currently consists of 17 destinations. The most interesting development is KLM's involvement with Dutch Railways in the South High-Speed Line in The Netherlands. The line is expected to start operations in 2007 with a high frequency of connections between Amsterdam and Paris and intervening stations. Together with 25 other parties, KLM is involved in the European COACT (Combined Air Rail Cargo Transport) project to study the long-term carriage of freight by train in Europe. The first pilot study will be carried out between Schiphol and Frankfurt Airport.

Elfriek van Galen,
Director, KLM cityhopper bv

Although KLM expects train connections to grow in importance on shorter connections, not all initiatives have been successful. Nightly train connections between Schiphol and Milan have been stopped owing to lack of demand. The contract with Dutch Railways allowing KLM passengers to travel to and from Schiphol by train free of charge on presentation of their airline tickets was also recently terminated. The objective had been to encourage train travel and thus relieve some of the congestion on the roads around Schiphol and also reduce the overall environmental impact of the journey. Unfortunately, we had to conclude that our initiative had not increased the number of customers traveling to and from Schiphol by train. KLM therefore did not renew the contract with Dutch Railways.

KLM believes that the hub-and-spoke model will remain the mainstay of international aviation. Through further alliances, European and intercontinental networks will enhance their strength and efficiency. In current and future alliances, KLM will continue to promote efficient connections from Schiphol and hubs elsewhere in the world to the regions of Europe.

Within KLM's hub-and-spoke system, KLM cityhopper is a spoke: we carry passengers from various places in Europe so that they can transfer directly to the international network of connections. We play the same role for American and Asian passengers who travel with us from Schiphol to their final European destinations. We operate efficient aircraft and have a high load factor. We usually fly to smaller airports so that we are less affected by air congestion and don't have to taxi for as long. An efficient product for our customers often goes hand-in-hand with an environmentally-efficient operation. Our aircraft produce only a limited amount of noise. Last year we even won Schiphol Airport's award for the carrier with the quietest aircraft on European routes. We're quite proud of that.

The debate about regional airports flared up again recently. It goes without saying that they are important to KLM cityhopper. For the local economy and even for the environment, I think they offer advantages. We can carry passengers from Rotterdam to London, for example, with a high degree of energy efficiency. I don't think the high-speed train through the Channel Tunnel can compete with us. I have very clear views on the importance of regional airports, and I'm more than willing to share them.

The environment is a hot issue in our organization. Environmental aspects are integrated into our business processes. A clear example of this is the attention we pay to the environmental qualification of the goods we purchase. As an organization, we think that's very important.



Our staff also tell us they think it's important. The average age of our staff is low, just over 30. The people who work here quickly have to shoulder a lot of responsibility. I don't know whether that contributes to their environmental commitment, but I appreciate it very much. The commitment shown by the women, by the way, is even higher than that shown by the men.

Last year we devised a method to determine whether a business process had an environmental impact and whether it was significant. The results let us set effective priorities to improve our environmental performance. KLM cityhopper has not yet certified its environmental management system but we are working on it so that we comply with ISO standards wherever possible.

The highlight of the past year was the integration of KLM cityhopper uk into our quality organization. In a short period of time we included 21 aircraft from the KLM uk fleet (including their crews) in the program. The program currently consists of 54 aircraft. That's a lot! KLM cityhopper is a high performance airline with a high degree of customer satisfaction and a good return. We are ready for the future.



KLM offers its customers other transport modes to complement the airline network, including freight forwarding by road and rail, and passenger transport on high-speed rail lines.

Procuring Products and Services The aviation chain is made up of a wide range of players: aircraft manufacturers, leasing companies, airports, air traffic controllers, caterers, cargo handlers and, of course, the airlines themselves. The market forces in the chain are certainly not controlled by that last link. This is because of the various rules applicable to the players and the characteristics of their separate markets. Some players are monopolists or oligopolists (air traffic controllers and aircraft manufacturers); others have been through a process of consolidation (aircraft manufacturers and leasing companies). Many of them have raised their prices, yet the airlines' customers are demanding higher service at lower cost. The excellent margins realized by some players in a period when airlines are incurring losses indicate just how 'challenging' KLM's position is in the aviation chain.

Adaptability, flexibility and a professional approach are necessary to make the most of the limited opportunities. The anti-cyclical purchase of aircraft is one way in which KLM can rise to the challenge. The environmental aspects of purchasing aircraft and engines are considered elsewhere in this report. We also consider the environment in aircraft maintenance, although our freedom of choice is limited by strict regulations. Wherever possible, KLM opts for environmentally-friendly alternatives. The environment is included in the contracts we sign with our suppliers, such as cargo handlers and paper suppliers. In this time of economic weakness, the capacity available to evaluate the environmental performance of our suppliers, however, is limited. In the past year we carried out more than 50 evaluations.

Initiatives in the Aviation Industry KLM is represented in the ENTAF Environmental Task Force of the IATA (International Air Traffic Association). The IATA is struggling with a dilemma in the aviation industry: how can airlines improve their financial and economic situation while gradually raising their environmental performance? The industry is aware that the improvements expected in environmental performance, particularly with regard to greenhouse gas emissions, will be outstripped by the increased impact caused by the expected growth of the industry itself.

International consultation between aviation countries and airlines is a key mechanism for sustainability. Some essential improvements, such as the modernization of European airspace and the introduction of tradable emission rights, cannot be realized by carriers acting on their own. Both these issues are considered elsewhere in this report. Unilateral action by KLM would unacceptably weaken its competitive position and thus endanger its very existence. KLM is an active member of ENTAF because these improvements must be realized despite the current problems of individual airlines. Furthermore, ENTAF offers a platform for the exchange of best practices so that KLM can further improve its environmental performance and share its own progress with others.

Safety cannot be expressed as a simple number; it is the outcome of managing and continuously improving the entire chain. We recognize two aspects to safety: security and flight safety.

Security In 2003 KLM began implementation of additional security measures in accordance with the post-September 11, 2001 policy set out in the 'Positioning Paper Security'. They include investments in additional security personnel and tighter controls. Since January 1, 2003, baggage at nearly all airports has been subject to 100% x-ray examination. Security checks of the handling procedures, such as catering, cleaning and loading, have been stepped up. Cargo security measures have also been tightened up, with checks being made of the cargo supplier's integrity and the contents of the shipment. KLM is vigorously fitting reinforced cockpit doors in its aircraft. Refitting of the intercontinental fleet has already been realized and that of the European fleet is expected to be completed in 2003.

Level Playing Field KLM's security measures significantly influence its processes and entail significant costs. Despite the importance of effective security and the equal treatment of airlines by the authorities, there is no uniform international policy on what proportion of the costs should be borne by the authorities and what by airlines, airports and customers. KLM finds this difficult to accept and will continue to play an active role in international consultation. After all, sustainable aviation begins with safety.

For KLM, no single issue is more important than safety. Safety is a precondition for our operations

Flight Safety Flight safety is determined by the airworthiness of the aircraft, the processes on the ground and the way in which the flight is conducted. To ensure the safety of flight operations, cockpit and cabin crews continuously undergo intensive training programs using flight simulators so that they can prepare for unforeseen circumstances. Aircraft are maintained in accordance with maintenance programs approved by the aviation authorities. KLM has been certified by European and American aviation authorities to perform fleet maintenance. Various other airlines outsource their maintenance to KLM's specialists.

Aircraft are handled and maintained at all KLM destinations by qualified staff who are trained worldwide in flight safety awareness. All handling processes on the ground are inspected and audited every year. Any irregularities that might affect flight safety are recorded in a database and investigated in detail in order to identify opportunities to improve handling procedures. The database is also an important source for the exchange of information with other business units and handling companies. The opportunities for improvement are used as case studies in training courses to increase the ground staff's flight safety awareness and are shared with all staff by means of information bulletins.

Flight operations are constantly monitored during a flight. Departures from the normal pattern are immediately flagged and may lead to an evaluation with the crew or a further investigation. Furthermore, KLM Flight Operations registers all notifications of operational incidents in a database of Air Safety Reports. This database is used to analyze risks and generate trend information. In response to an Air Safety Report, it may be decided to carry out a further investigation. Specially trained staff in the department regularly carry out such investigations. KLM issues a quarterly magazine entitled 'In for Safety' to inform staff of how KLM can work even more safely. About 4,800 members of staff – pilots, engineers, pursers and others – receive the magazine. It is also circulated to other airlines because we like to share opportunities for improvement.

The integration of sustainability into the operations makes it difficult to analyze costs and benefits

Step by step, KLM's environmental policy is evolving into a sustainability policy. The change is prudent and controlled so that we do not overreach ourselves. We can thus remain on course and make sound progress. Organizationally, our company does not have an integrated sustainability structure. The environmental organization is firmly anchored by means of the environmental management system. Social aspects of sustainability are the responsibility principally of the Human Resources organization, but also of Corporate Communications and AirCares. It is difficult to present an exact statement of the sustainability costs and benefits because the activities have been integrated into the operations.

We do have an insight in certain areas. Environmental costs during the fiscal year amounted to approximately EUR 15.9 million. The main cost components were staff to an amount of EUR 2.5 million, aircraft modifications of EUR 1.3 million, fuel costs due to adapted flight routes for environmental reasons of EUR 3.4 million, additional maintenance costs due to the adapted flight routes of EUR 2.0 million, waste disposal of EUR 3.0 million and waste water of approximately EUR 1.7 million.

KLM is taking initiatives to gain more understanding of the financial benefits of sustainable business, in part through targeted studies such as the From Financial to Sustainable Performance project of the Dutch Initiative for Sustainable Development (NIDO). This study has provided us with an insight into the 'bridge' between sustainable business and financial value creation and reputation. Furthermore, its methodology enables concrete action points to be adopted so that line managers can influence our organization's sustainable performance in an economically sound manner. A decision has not yet been taken on our follow-up to this project.



Professor Jacqueline Cramer,
Dutch Initiative for Sustainable
Development, www.nido.nu

It is important to reveal the economic value added of sustainability

NIDO is the Dutch Initiative for Sustainable Development. NIDO brings companies, public authorities, civil organizations and scientific bodies together in programs that put sustainable development into practice.

The NIDO program From Financial to Sustainable Performance was recently completed. As part of this program, 19 companies, one of which was KLM, worked with each other and within their own organizations for two years on putting sustainable development into concrete terms. All the companies found that sustainability had to be customized. The participants underwent a steep learning curve that will help them realize their own sustainable operations.

KLM's project involved KLM Cargo. It looked at how the economic value added of sustainable business could be made transparent. The most important result was an initiative to translate the social and ecological aspects of sustainable business into financial and economic terms that could be used by KLM Cargo, in particular in the financial return on capital employed. This will make it easier for management to understand why sustainable development is on the business agenda and not a peripheral activity.

KLM Cargo's operations are closely related to the other parts of KLM. The financial angle to sustainable business will therefore also be relevant to those other parts of KLM. On the whole, the NIDO results will help flesh out a sustainability program.

It is widely known that KLM has already made progress in the field of the environment. Its environmental report has already won two awards. It therefore had solid foundations when it joined the NIDO program. I expect KLM to build actively on the program's findings and to give higher priority to the social pillar. In view of KLM's enthusiasm for both the program and the cooperation with other participants, I am certainly positive about that.

Sustainable development is a continuous process without a fixed destination; we make progress but are never finished

In dialog with our stakeholders, our ambition is to be even more sustainable 'tomorrow' than we are 'today'. In this section we look at certain aspects of sustainability that we are considering or believe will be important in the future. Sometimes we can bring about change by ourselves. At other times, we must apply our influence to encourage the international aviation industry or international authorities to take measures.

The main issue for KLM is continuity. The economic situation is forcing decisions and strict control of the cost base. Further cost control is possible and necessary but there is a point at which the network structure is in danger of being compromised and economy measures become counter-productive. Cooperation between airlines in the form of alliances or other partnerships is designed more to enlarge markets than to address this problem. A fundamental redesign of the network organization's cost structure will have to take place. Nevertheless, a further increase in scale will also be necessary in the longer term. International cooperation is therefore urgently being sought within the industry, not only by KLM. The global alliances Sky Team and OneWorld would gladly welcome KLM. Various issues must be considered, however, and KLM will not take such a fundamental decision hastily. The key issues in KLM's decision remain a stronger market position, the continuity of the company, the Schiphol hub and, not least, the development of KLM's proposition to customers, shareholders and staff.

Whatever alliance is established, it is clear that our company will undergo a change. Our staff are obviously following these developments with interest. We try to provide them with clear information on future developments. Line management has primary responsibility for this, but the in-house magazines, *Wolkenridder Actueel* and *Wolkenridder Magazine*, and other communication channels are also used to disseminate information. As a matter of course, the developments are discussed in detail with the Works Council.

KLM is following the international debate on codes of conduct with interest. Although the proponents claim such codes can help clarify standpoints and influence behavior, we do not think KLM is at a practical disadvantage by not having a written code. Internally, KLM pays a great deal of attention to the personal conduct and responsibility of our staff. In addition, we communicate with many stakeholders and are prepared to provide information on our positions and to enter into dialog about them. Furthermore, we judge our suppliers strictly on the high standards that are observed within the aviation industry. KLM's values – reliability, punctuality, friendliness and care – and our organization's rules and procedures give us a firm handhold for all our actions.

We attempt to introduce sustainability into our relationships with customers. We are increasingly testing the limits of our responsibilities. Our customers, too, of course, have their own responsibilities. The emission calculator provides them with an insight into the environmental impact of their journeys. It helps them take well-considered decisions.

We consider eco-tourism in the in-flight magazine and provide information via the onboard entertainment program. Sometimes we find that a subject is beyond our responsibilities. We were asked, for example, to accept a petition against child sex tourism from the Move Your World organization. Despite the sympathetic nature of the petition KLM, as an airline, did not think it was appropriate for it to accept it. KLM must not get involved in the reasons why its passengers travel. Moreover, we think it is a government duty and responsibility to inform the public about child sex tourism. Although this example took place in the past year, it illustrates the dilemmas KLM faces from time to time. In the future, too, we shall respect the limits of our responsibilities.

Governments have an indispensable part to play in enabling further environmental improvements. For many years, KLM has called for the introduction of a Single Sky in Europe. Every country in Europe still has its own air traffic control system, which is a source of inefficiency. Furthermore, parts of European airspace are not accessible to civil airlines owing to their military status. This inefficient situation leads to considerable delays for airlines and their customers. Furthermore, it leads to the rerouting of flights and thus to unnecessary environmental pollution. Modernizing European airspace might eventually reduce fuel consumption by about 10%. European transport ministers took a small step in the right direction in December 2002 by supporting a plan to modernize European airspace as from 2005. The Association of European Airlines believes the progress is too slow and is calling for safe, efficient and cost effective air traffic control in Europe. KLM supports its position.

To encourage sustainable mobility, KLM is in favor of including societal costs in the product price. However, they must be included in the same way by all transport modes. At present, cars, trains, ships and aircraft are treated differently. Through the payment of landing fees, airport fees, flyover fees and other taxes, airlines contribute to the cost of the infrastructure, air traffic control, noise insulation and the public purse. This is not the case for rail transport or shipping, where the government pays for the construction of infrastructure. KLM is in favor of the creation of a level playing field for all transport modes.

To reduce the aviation industry's contribution to the greenhouse effect, KLM is calling for an international and open system of tradable emission rights. Companies that work more efficiently than the set standard or within the maximum ceiling would retain emission rights that they could sell to companies that worked less efficiently or were in danger of exceeding the ceiling. Attaching a price to the emissions would encourage environmentally-friendly business. Furthermore, it would improve the cost/benefit ratio; in an open system, rights would be purchased from those companies that achieved the greatest emission reductions at the lowest price. Through international consultation within the aviation industry, KLM is promoting the introduction of an international system of tradable emission rights.

Since our sustainability policy explicitly includes the dimension of future generations, it goes without saying that we are increasingly benchmarking our activities for the future. This is a great challenge, one in which we shall bear our responsibilities for those issues that are within our span of control.

Summary of the Sustainability Program

| <i>Issue</i> | <i>Objectives</i> | <i>Measures in 2002/2003</i> | <i>Progress in 2002/2003</i> | <i>Measures in 2003/2004</i> |
|--|--|---|--|---|
| People | From industrial relations to human relations | | | Fewer detailed rules in the CAO and increased personal responsibility |
| | Higher staff satisfaction | | | Implementation of various measures in the new CAO |
| | Lower absenteeism | | | Continued dialog with the Works Council and the exchange of best practices |
| | Higher productivity and lower labor costs | | | Revision of rostering (over 2 years); Pension system study; Implementation of e-learning project |
| Planet – Continuous improvement in environmental management | Renew ISO 14001 certificate | Apply for ISO 14001 certificate | ISO 14001 certificate renewed | Continuous improvement in management system |
| | Roll out environmental management to the outstations | Gradual implementation of GEP at outstations | Presentations for various regional and service managers. Pilot conducted at second outstation | Continued implementation of GEP at outstations |
| | Benchmark KLM's environmental position within the aviation industry | Develop more (and better) environmental performance indicators | Various indicators developed. Benchmarking only feasible for fuel efficiency and flight emissions | Further development and implementation of indicators |
| Planet – Climate change | Reduce fuel consumption and emissions | Carry less additional fuel | Baseline measurements made | Reduction goal of 4% per aircraft type |
| | | Implementation of a pilot to reduce emissions and fuel consumption by means of additives | Effect on emissions could not be determined; no effect on fuel consumption | Determine whether the effect on emissions can be measured in an improved pilot |
| | | Reduce standard weight of catering load on inter-continental flights by 5% | Pilot successfully completed on limited number of flights | Further implementation on intercontinental flights |
| | Improve Energy Efficiency Index (EEI) to 59% in 2002 | Extra measures to raise EEI to 59% in accordance with KLM Energy Efficiency Program | EEI raised from 59.5% in 2001 to 60.5% in 2002 chiefly through lower production | Agree second MYEA with government and implement MYEA studies |

| <i>Issue</i> | <i>Objectives</i> | <i>Measures in 2002/2003</i> | <i>Progress in 2002/2003</i> | <i>Measures in 2003/2004</i> |
|--|--|--|---|--|
| Planet – Climate change, contd. | Phase out all ozone-depleting substances as required by law | Phase out remaining 50% of halon fire extinguishers for non-critical applications | All halon extinguishers for non-critical applications phased out according to plan | Replace halon bank |
| Planet – Local environmental impact | No increase in KLM's contribution to noise levels at Schiphol | Prepare implementation of fleet replacement | Implementation of fleet replacement started | Further implementation of fleet replacement |
| | | Increase number of flights with CDA procedure | CDA procedure dependant on air traffic control and weather | Where possible, continue requesting permission for CDA procedure |
| | | Evaluate noise complaints received | Talks with cockpit personnel to identify causes | Continue |
| | Reduce emissions caused by ground activities | Taxiing with one engine shut down where feasible; targets set per aircraft type | Some targets proved too high, others too low | Set more realistic targets |
| | | Consultation with airport on technical and financial feasibility of reducing APU use at Schiphol | Emission and financial variants set for Boeing 747-400 and Boeing 737-800 | Work out recommendations to increase GPU and PCA use and draw up implementation plan |
| | Increase industrial waste separation to 33% | Reintroduce checks of paper separation in onboard waste | Checks introduced; 32% separation achieved | Target set at 35%; continue checks of this separation |
| | Increase reuse of waste to 35% | Consultation with Boeing and General Electric on reducing packagings for aircraft components and possible preventative measures | Consultation held, greater insight into figures | Agree and implement measures where possible |
| | Reduce volume and pollution of wastewater discharges | Request new Wvo license for wastewater discharges | New Wvo license fully prepared | Water control corporation to issue Wvo license. Implementation of the license within the KLM organization |

Introduction The management of KLM asked us to verify its 'KLM Sustainability Report 2002/2003'. The sustainability report is the responsibility of KLM's management. Our responsibility is to issue a verifiers' report on this sustainability report.

Scope The report as a whole has been subject to verification, including text and figures. Our verification was focused on the question to what extent the management of KLM has drawn up the information included in the sustainability report with due care, as well as the review of the reliability of the information in the sustainability report.

Activities undertaken Our verification, planned and conducted by a multidisciplinary team, was based on the International Standard for Assurance Engagements of the International Federation of Accountants.

In the context of the verification we recognize that non-financial data are, in general, subject to more inherent limitations than financial data due to their nature and methods used for determining, calculating or estimating such data.

Our activities, aimed at providing a moderate level of assurance, included:

- a review of the underlying systems and procedures used to collect and process the reported information;
- a review of the underlying principles of management information and reporting used in drawing up the sustainability report;
- a review of the reliability of the reported information, including a review of important estimates, based on, among other things the Sustainability Reporting Guidelines of the Global Reporting Initiative (part B)
- an evaluation of the general picture presented in the sustainability report, based on underlying information and official external publications such as research reports, press releases and the audited annual accounts.

Opinion Based on our verification we conclude that the management of KLM has drawn up the information included in the sustainability report with due care. Nothing has come to our attention that causes us to believe that the information in the sustainability report is not reliable.

Amstelveen, May 2003
KPMG Sustainability B.V.

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Text

KLM Royal Dutch Airlines is responsible for the content of this Sustainability Report. Text consultation and compilation were handled by Triple Value Strategy Consulting, The Hague (www.triple-value.com).

Design

The Report was designed by UNA (Amsterdam) designers, The Netherlands

Photography

Vincent Mentzel, Rotterdam, The Netherlands, provided the photograph of the Board of Managing Directors. The other portraits were provided by Reinier Gerritsen (pages 13, 15, 17, 18, 30 and 35) and Lee Hol (page 6). Other photographs were provided by the KLM photo library (page 16), Boeing (page 23) and Henk Boom (pages 6, 11, 21, 24, 28 and 31), who also provided the cover photographs.

Lithography and Printing

Drukkerij Mart.Spruijt bv, Amsterdam, The Netherlands, handled the printing. The text was typeset in the typeface Scala, created by Martin Majoor in 1998. Tables and captions were typeset in the typeface Linotype Neue Helvetica, created by Max Miedinger in 1957.

Paper

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