

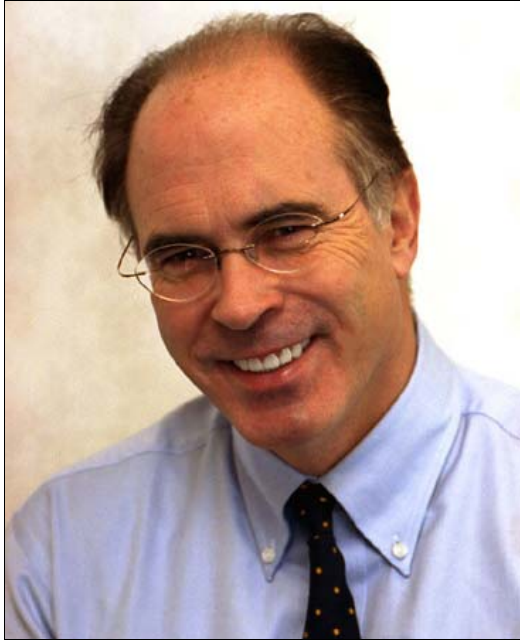


The importance of the Finance Function from a CEO perspective

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4th Annual Finance Directors Strategy Meeting, London
June 14, 2004



Rob Routs has been a managing director of Royal Dutch Petroleum Company and a Group managing director of the Royal Dutch/Shell Group since 2003.

He is CEO of the Group's Oil Products and Chemicals businesses. As a managing director he is also responsible for the Consumer, Renewables and Hydrogen businesses, for Group Research, and for Europe and Africa (excluding Nigeria).

Rob was born in Australia and graduated in Chemical Engineering from the Technical University of Eindhoven in the Netherlands, where he also obtained a Ph.D. in Technical Sciences.

He joined Shell in the Netherlands in 1976 and worked for Shell Canada from 1978 until 1999, finally as President of Oil Products. He then led Shell Global Solutions – the Group's research and technical services group – before becoming CEO of the Equilon refining and marketing joint venture in the United States. Following the Group's acquisition of Texaco's interests, he became the CEO of Shell Oil Products US and President of Shell Oil Company.

Rob and his wife, Janicke, have one son and five daughters.

The Finance Function plays a crucial role in enabling the business to achieve competitive performance and make strategic progress, as well as in providing assurance about the state of the business to shareholders and regulators. It must provide the consistent financial information, risk management and controls that enable managers to drive performance improvement, evaluate investments, and meet external reporting obligations. The relationship between the CEO and CFO is crucial, particularly in challenging business performance and proposals, and in communicating effectively with the finance community.

In an increasingly demanding business environment – where companies must respond to relentless competitive pressures as well as intensifying external scrutiny – the role of the Finance Function has never been more important.

I believe Finance has two critical roles:

- to help the business achieve competitive performance and make strategic progress, which includes providing first rate operational finance support, and
- to provide assurance about the state of the business to shareholders and regulators.

As you would expect, the second is something we are thinking very hard about at present in Shell. I don't intend to discuss the reserves recategorisation or the events surrounding it. But I will mention some the changes we are making in our organisation and control framework as a result.

A global business delivering locally

As the title says, I approach this not as a finance specialist – my background is as a chemical engineer – but from the perspective of a CEO.

I am CEO of the Group's oil products business – on which I will focus much of what I say – as well as of our petrochemicals business. I am accountable for the performance of these businesses. I am also a Group managing director and take part in wider decision making – in the Committee of Managing Directors and as a parent company director.

Let me start by giving you a brief description of our downstream oil

business and the challenges it faces.

Shell Oil Products companies manufacture and market transport fuels, heating oils, lubricants, bitumen and liquefied petroleum gas.

Collectively we are the largest fuels marketer and operate the world's largest branded retail network – with over 50,000 service stations serving some 25 million customers a day. We also have a flourishing global technical services business.

We operate in 140 countries – the most diverse and geographically balanced portfolio in the industry – and employ over 80,000 people around the world. Our net proceeds last year were \$166 billion. We had operating expenses of nearly \$15 billion and earned nearly \$2.9 billion.

The downstream oil industry is increasingly competitive. There has been significant consolidation since 1997 – which left ExxonMobil and Shell as the two leading players.

In the United States, we acquired downstream assets from Texaco – making us the largest fuel retailer in the world's largest market – as well as the Pennzoil Quaker State lubricants business. We also bought DEA in Germany, enhancing our position in this important market.

New competitors have emerged to challenge the integrated majors, including:

- niche players specialising in particular parts of the value chain,
- hypermarkets who bundle fuel retailing with their core businesses, and
- national companies from oil producing countries.

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Extensive overcapacity in many markets has led to widespread closures and disposals of refineries and retail sites. We have been very active in this drive.

Downstream margins are unusually strong at present. But they have been volatile in recent years – with prolonged periods of very low refining margins in Europe and Asia.

We have consistently been an industry leader in earnings per barrel.

In the mid-1990s, our business was fragmented – with individual national operating companies working independently and often in isolation.

Five years ago, we restructured our core manufacturing and fuels marketing operations into transnational organisations – for example in Europe we now operate seamlessly across more than 30 countries. And we created global organisations for specialised business-to-business units, such as aviation and marine refuelling.

We are now taking this process of globalisation forward so that our worldwide operations are run in five lines of business – manufacturing, supply and distribution, retail, business-to-business and lubricants.

These will be supported by strong global functions – including Finance – which will have their own global organisations rather than being dispersed throughout the businesses.

We believe this change will provide

- clearer line of sight, accountability and direction,
- more cost-effective and efficient use of resources, and
- global standardisation of business processes and systems.

Most importantly it will help us put even greater focus on serving our customers, and make us easier to do business with.

We are already working very hard on this standardisation, through a structured process called ‘Streamline’. We believe this has the potential to provide significant savings – as well as further improvements in our efficiency and service to customers.

Finance is at the centre of these changes. So let me start by looking at its role in raising business performance.

Supporting business delivery

For me, Finance supports our performance in three main ways:

- providing the information to manage our business and the insights to take it forward,
- challenging our performance and proposals, and
- delivering operational excellence in finance services.

Getting information on how your business is performing – quickly, accurately and clearly – is vital for management. Delivering this – in such a large, complex, dispersed and fast-moving business – is clearly a challenge.

We have made significant improvements in the information flow – but still have more to do. It is one of the areas targeted in the global standardisation drive I mentioned.

Good information is vital for the improvement targets that drive our business forward – such as those for 3% annual reduction in unit costs and the delivery of synergies from our acquisitions. We need to choose the right measures, monitor our performance accurately, and benchmark it against that of our competitors.

As well as being essential for managing the business, these results are also an important component of the scorecards that focus people’s efforts and determine their reward.

Another key area where accurate information is essential is in evaluating our investment proposals. The downstream oil business is not as capital intensive as the upstream – but we invested \$2.4 billion last year. We need to make sure we spend our shareholders’ money wisely, on things that deliver long-term value for them.

Finance has an essential role in evaluating proposals, ensuring they are executed efficiently, and reviewing the outcome.

That brings me to the vital question of providing challenge. As a CEO, I rely

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on my Finance Director to help me challenge the performance, plans and proposals of our line colleagues. Having a Finance Director whose judgement I trust is fundamental to my ability to do my job.

Effective challenge is a difficult art. It must be rigorous and clear sighted. But it must also be constructive, helping the business to achieve its goals.

Of course, it doesn't only take place at the top. We can't argue everything out around the executive table. We have to get things right from the start.

So this challenge has to be a part of the interaction of finance specialists with their business colleagues throughout the organisation. This means they must be trusted – for their skills, judgement and commitment to business goals.

Providing excellent operational finance support to the businesses is the starting point for gaining this trust. Finance processes require the same challenge and improvement drive as any other part of the business.

Let me mention two areas where the quality of financial support is particularly important in the Oil Products business.

First mergers and acquisitions, I mentioned three major OP acquisitions, for which we paid \$8.7 billion including debt. But that is not the end of our portfolio action by any means. Over the past three years, we have also divested assets worth over \$2 billion.

We see portfolio management as a fundamental part of our business – constantly upgrading our portfolio, responding to market changes and recycling capital. It is essential that we make the right decisions, carry them out efficiently – not least because they involve people's jobs – and ensure we gain the value from them. The Finance M&A specialists have a vital role in making this happen.

Let me give an example of good practice. As part of our acquisition of DEA in Germany the competition authorities required us to dispose of some retail sites there. We could have just put them on the market. Instead, we arranged a swap that gave us sites in

growing East European markets where we wanted to expand.

The second very important area is taxation, for a business that – as well as taxes on our own income – collects over \$60 billion in sales taxes for governments around the world. Our tax specialists have an essential role in maintaining relationships with the tax authorities in 140 countries and ensuring that our operations are structured and run tax efficiently.

Earning trust

Let me turn to the essential task of providing assurance about the state of the business to shareholders and regulators.

I think this has four key elements

- following clear business principles and standards of governance,
- having effective internal controls and risk management processes,
- being scrupulous in reporting and complying with regulatory requirements, and
- earning the trust of shareholders in the company's management and plans.

The Group has established business principles and standards of governance. We have put a lot of effort into ensuring they are understood and followed throughout our businesses – including a comprehensive, worldwide annual assurance process. Making sure that these systems meet both our business needs and external expectations is clearly a priority.

We are also looking very hard at our framework and philosophy of controls. I say philosophy because – since the mid-1990s – we have emphasised bringing Finance and other staff functions into the line organisation to ensure a shared focus on achieving business goals.

This shared focus remains vital. But we now recognise there is equal need for independent lines of reporting and functional standards.

Our Oil Products CFO remains an essential member of the OP executive team. But he now reports – together with the CFOs of our other businesses –

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directly to the Group's Director of Finance, and is accountable as a member of the Finance leadership team.

We have also strengthened the role of the Chief Internal Auditor who now also reports to the Director of Finance – and, of course, continues to have direct access to the non-executive directors in the Group Audit Committee.

The Group has an established Risk and Internal Control policy, which requires each business:

- to identify and evaluate the risks that might jeopardise the achievement of their objectives,
- and have strategies and controls for managing them.

Assessments of the impact and likelihood of these risks – and of how they are being managed – must be reported quarterly to the Group Controller for consideration by the Group Managing Directors and Group Audit Committee.

The controls must also ensure that external reporting is scrupulously accurate. Like other companies listed in the US, we are required by Sarbanes-Oxley 404 to be able to report on the effectiveness of these controls in our annual report from 2005.

This, of course, comes at the same time as the change to International Financial Reporting Standards – which will become our primary accounting and reporting standard from 2005. Achieving these vital changes will be very challenging for all the Finance staff involved. We rely on their professionalism.

Excellent reporting is at the heart of the relationship with our shareholders and others in the financial community. But this requires much more. We have to earn their trust that their company is

being managed in a way that will deliver the returns they have a right to expect.

As in all forms of communication, I believe the starting point must be to listen to their views and understand their expectations. We can improve confidence and credibility through clear, straightforward and consistent communication, and by building stronger relationships with the investment community.

We need to set out a coherent and compelling strategy for achieving our goals – and demonstrate that we are sticking to it. That doesn't, of course, mean following it blindly if there is a fundamental change in conditions. But it does mean not being blown off course by every change of wind.

Above all, it means delivering what we say we will – which has the corollary of not promising more than we can deliver.

All these things are, of course, much easier to say than to achieve in an uncertain – and increasingly competitive – world. As a CEO, I know that my ability to achieve them depends to a great extent on the quality of my Finance Director and his staff.

I suspect all Finance people have had to put up at some time or another with the taunt that they are just bean counters. But all thinking managers understand that counting your beans properly – with financial accuracy, acumen and intuition – is the foundation on which business rests.

Without it you can have no idea of what you are doing or where you are going, let alone the ability to influence either.

The skills of Finance professionals will always be at the heart of business.

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