

VATTENFALL READY TO INVEST FOR THE FUTURE

With continued profitable growth, Vattenfall can create the necessary resources for future-oriented investments within both electricity generation and improved security of supply. Major investments are also being made to improve customer service.

Strong set of annual accounts

2004 was a new record year for Vattenfall. Financial performance improved in all Vattenfall segments

- Net sales increased by 1.3 per cent to SEK 113,366 million
- Operating profit increased by 28.2 per cent to SEK 19,607 million
- Net profit after tax increased by 29.1 per cent to SEK 11,776 million

Lower electricity prices led to only a marginal increase in sales in 2004. The substantial increase in operating profit is explained in part by substantially increased electricity generation volumes and in part by advantageous hedging outcomes. Electricity generation in the Nordic countries went exceptionally well, with record levels in generation and availability in our nuclear power plants and greatly increased hydro power generation. The cost-cutting programme in German operations, the aim of which is to provide considerable annual savings, has proved successful. When the programme was completed at the end of 2004, the established goal had been exceeded and the annual savings amount to EUR 519 million (almost SEK 4.7 billion). Operations in Poland have continued to develop very positively. Highly streamlined operations and substantial cost-reductions have led to a considerable improvement in profit.

Growth creates resources

The strong set of annual accounts show that Vattenfall's strategy to grow in unison with development in the European market is the correct path to follow. This growth enables Vattenfall to make more effective use of resources and allows costs to be borne by a greater volume. This growth also provides a broader knowledge base for more efficient solutions, more efficient processes and improved customer offerings.

Through growth we create resources that can be used for future-oriented investments, which in turn can create

additional resources in the future. We have taken advantage of the new opportunities that the reformed European electricity market offers and have established a positive spiral that will provide good future conditions.

Major investment programmes are now underway in both electricity generation and electricity distribution and extensive efforts are being made to improve customer service. The company's financial position has improved considerably. It has been possible to use the strong cash flow to repay debt. The consolidation programme is near completion and Vattenfall can now take further steps towards the vision of becoming a leading European energy company that creates value through profitable growth. To be leading means that we shall be 'Number one' for the customer and for the environment, that growth will increase our ability to offer attractive solutions.

Act globally – think locally

Our operations are essentially local. Electricity and heating systems supply energy to millions of users. As markets have been opened up, solutions and environmental impact are no longer restricted by borders.

During the 1990s, we learnt that we must think globally and act locally. The three primary driving forces behind energy supply are all gaining an increasingly global dimension. Here I am referring to environmental impact, in particular the greenhouse effect, to the primary energy supply and to technological development. Together these three create the framework within which local needs and conditions can be balanced out with good solutions.

However, a viable energy company acting in an open market must know how to work this equation the other way around as well. We must act globally in order to create the resources, human capital and financing that are necessary and then use these to think locally.

Vattenfall has in several cases a strong local presence in areas with weak local economies, such as Norrbotten in Sweden, Lausitz in Germany and Silesia in Poland. Via

Vattenfall, conditions are created in these areas that enable them to compete in a European market. We think locally and act globally.

The greenhouse effect

The most overshadowing environmental problem of our time is the ongoing climate change. The climate problem is by its very nature global and long-term. If we do not take control of our emissions, we will be forced to make drastic changes to the conditions under which we – and more so our children and grandchildren – live. Economics, energy and the environment are intertwined and, in my opinion, it would be irresponsible not to take this problem most seriously. Ending the use of fossil fuels, however, is not a viable solution – neither globally nor on a European level. We must solve the problem with emissions from the combustion of fossil fuels both technically and economically. The emission-free coal-fired power plant must become a reality! The world is completely dependent on this form of energy and this will continue to be the case for a very long time. Fossil fuels are a prerequisite for growth in developing countries. Investments in research and development must be focused and greatly increased in order to develop new technologies and techniques. The climate issue will most likely bring to the table reassessment and further development of nuclear power. Gradually, the transport sector will make the transition to carbon dioxide-free engines, probably via hybrid vehicles to fuel cells using different energy sources. To create a global price for emissions is a prerequisite if we are to see positive development. Trading in emissions is an important step, but this alone is not enough to solve the problem.

Vattenfall works intensively with climate issues and our growth allows us to participate and influence development in Europe. We are pushing for the creation of sustainable pricing for carbon dioxide emissions. We are working with development. We are working with renewable energy. We are working to create the necessary conditions for our customers to use our products in an effective manner. One prerequisite for our success is that we have the resources and can continue to work along the positive spiral that we have established.

Electricity networks

Society has developed at a fast pace, and today all impor-



tant societal functions are dependent on the constant availability of electricity. Vulnerability has increased considerably faster than the reliability of electricity networks. At the beginning of January 2005, parts of Sweden were hit by a terrible storm. Even if this was the worst storm for 100 years, the consequences we witness when electricity networks are put out of operation are unacceptable. If we combine all the effects, the total costs are absurd. We must reconsider and make our networks significantly more robust.

The storms of recent winters have had much impact on how we at Vattenfall reason and act. We have initiated an extensive investment programme to rectify the problems and we have made a good deal of progress. At the same time, we have introduced a disruption guarantee to compensate our customers. We are doing what we can

within the current framework, but looking at existing and future requirements this will not be sufficient. We must ensure that the networks are upgraded throughout with a higher level of functionality based on a user perspective. And here too we have made good progress. At the beginning of 2004, Vattenfall decided to invest a further SEK 2 billion in improving operational reliability in its Swedish networks, bringing the total investment to SEK 10 billion over a five-year period. Moreover, compensation was increased to Swedish households losing power due to network disruptions. We invest almost all of Distribution Sweden's operating profit, that is, profit before financial expenses and tax, in our Swedish network operations.

The considerable expansion of wind power in Germany has led to the need for extensive development in the German electricity networks. Vattenfall has decided to expand the capacity of its high-voltage network by 3,000 MW with an investment of approximately EUR 260 million (approximately SEK 2.3 billion).

In Sweden, Finland and Germany, the authorities have introduced – or plan to introduce – new models for regulating network tariffs. New approaches and collaborative efforts are necessary if we are to reduce the vulnerability of our electricity networks. This places major demands on combining the local and global perspectives in a sensible fashion. It also places stringent demands on being able to mobilise sufficient resources.

Customised solutions

Vattenfall was the first Swedish electricity company to discontinue invoicing household customers in arrears for electricity consumed more than one year ago. We have also continued to invest in remote-readable meters in Sweden and Finland. We are moving forward forcibly with this work so that all of Vattenfall's 1.3 million Nordic network customers are provided with remote reading. In this way, advance charges can be abolished and replaced with invoicing of actual electricity consump-

tion. Open markets place stringent demands on both the upgrading of systems and the updating of knowledge.

Vattenfall is willing and able to invest for the future

Vattenfall's growth and development in tandem with market development is beginning to show results. Today Vattenfall is:

- An international company.
- A company with plentiful resources (considerably more than when incorporated in 1992) able to compete in the European arena.
- A leader in Sweden with regards to renewable energy. Vattenfall has broad expertise centered on electricity and heat.

Vattenfall plays an important role in opening up for competition and efficiency. Experience gained in Sweden has provided a solid foundation for considerable streamlining, which is reflected in the good profitability attained in the German market. By applying Vattenfall's knowledge to open markets in neighbouring countries, technical and market know-how has contributed to breaking old monopolies and to a more efficient electricity supply in Europe – completely in line with the intentions of the EU's internal market. Vattenfall represents innovative thinking in the European energy sector.

By taking advantage of the possibilities that an increasingly open European electricity market offers, Vattenfall is able to present a very strong set of annual accounts for 2004. Growth provides strength; strength that we use in lasting investments for the future.



Lars G Josefsson
President and Chief Executive Officer