

CEO's message

A SUSTAINABLE ENERGY COMPANY FOR A SUSTAINABLE SOCIETY

Looking back at Vattenfall's development in recent years, we can view it from two entirely different perspectives.

On the one hand, Vattenfall can look back at a number of years filled with major successes. Year after year we have presented record earnings, we have expanded into new markets, and we have successfully integrated acquired companies. Profitable growth has been our guiding principle – to focus on value creation as a platform on which to meet the challenges presented by a deregulated, common European energy market.

Parallel with this, Vattenfall has carried out a number of aggressive moves. Major investments have been made in the electricity network to ensure improved security of supply delivery reliability for our customers. Investments in new technology in our existing power plants have resulted in improved efficiency, at the same time that emissions of carbon dioxide and other harmful compounds have been reduced.

On the other hand, success is a subjective experience. For many in our operating environment – society, customers and other interest organisations – Vattenfall's development has not been equated with success in all respects.

On the contrary, many people still regard Vattenfall as part of an ineffective energy market in which the market mechanisms are not creating efficiency and competitive prices. Instead, say the critics, energy trading is taking place in an oligopolistic market in which a handful of large energy companies are maintaining price levels that are too high and detrimental for energy consumers.

This criticism must not be brushed aside as off-target and mistaken. We cannot let ourselves be satisfied with the tangible successes that we have achieved in terms of delivered terawatt hours, or in dollars and cents. We must acknowledge that these reactions are real and worth taking seriously. Therefore, one of our absolute most important tasks is to continue the work on showing that we are a company that stands by a well-functioning market and constantly strives to deliver competitive energy solutions to society and to the customers we work for. It is not until our customers are satisfied that we can be satisfied ourselves with the services and products that we deliver.

Building up this trust is a duty fitting for a company that has a long-term horizon such as Vattenfall's. We must take advantage of every opportunity to show that our company, our products and our knowledge truly support sustainable development and correspond to our customers' needs and preferences. We do this by offering modern technological solutions of the highest calibre as well as products and advice at prices that meet the high demands made by our customers.

Customers' success is Vattenfall's success

Sustained profitable growth is the centrepiece for meeting the demands that are placed on Vattenfall. Being a strong partner to our customers and to the society that we work for requires a profitable Vattenfall. A strong balance sheet and strong cash flow are prerequisites for the major investments and risk-taking that are required to manage our part of the necessary changeover to a sustainable energy system that does not contribute to climate change.

On a platform of this financial strength, we are constantly taking new strides to offer an even better partnership for our customers. At Vattenfall we regard the society in which we work as our principal. A successful society is one in which investment is made; accordingly, success for our customers also means success for Vattenfall.

2006 was a year of high electricity prices throughout Europe and especially in the Nordic countries. Representatives of Sweden's basic industry have expressed their concerns and have also questioned the energy companies' ability to offer competitive terms. For large companies in the forest industry, steel industry and other energy-intensive industries, for example, it is critical for long-term investment to be able to foresee electricity costs in production for several years into the future. This is why Vattenfall's relationships with basic industries are based on long-term partnership.

During the past year, Vattenfall has also been able to offer a long-term partnership to our private customers in Sweden. Last summer we introduced "Trygghetsavtalet", which briefly entails a fixed electricity price for three years, but with the right to renegotiate the agreement if wholesale electricity prices should fall during the term of the agreement.

"Trygghetsavtalet" has met a positive reception from both "old" and new customers. The response was so high at times that our customer service unit had problems taking care of all the new customers who contacted us. The warm reception given to "Trygghetsavtalet" shows the confidence with which retail customers in Sweden regard Vattenfall. The introduction of this price model is an important step in our work on further strengthening our relationships with our customers.

Major initiative in curbing CO₂ emissions

Another way of measuring Vattenfall's success is to see how well we succeed in combining financial success and increased energy generation with our simultaneous effort to reduce environmental impact. It is now entirely clear that major emissions of carbon dioxide and other greenhouse

gases are posing a major threat that risks irreparably changing the climate on our entire planet.

The climate issue is a challenge of such huge dimensions that everyone – nations, states, organisations and individuals – must take an involvement. At the same time, we know that all of the energy sources that we use today will continue to be needed in the foreseeable future. Consequently, we are forced to make long-term choices and use the energy sources that are available in an efficient and responsible manner.

Vattenfall approaches its climate work on contributing to sustainable development through technological development and suggests solutions and contributes to opinion-shaping. In the important work on finding new technological solutions to the environmental problem, Vattenfall is far advanced. We have a long record of experience in both increasing the efficiency of our electricity and heat generation plants and in minimising emissions of harmful greenhouse gases. Especially with respect to the integration of the Polish power plants, these are undergoing a technical upgrading that is bringing them up to an environmental level that is well in line with the rest of the Group's facilities. In Sweden and Finland, a number of thermal energy plants have been rebuilt in order to be able to change over from fossil fuels to biofuels.

In spring 2006 Vattenfall presented a plan to further increase investment in renewable energy sources in the Nordic countries. Our ambition is to increase our generation of renewable energy by 10 TWh per year in Sweden by 2016. A key part of this initiative involves a massive expansion in wind power, which will be conducted at Lillgrund in the Oresund Strait and at the Kriegers Flak site in the southern Baltic Sea, among other places.

However, our most pioneering and progressive investment involves the construction of the world's first coal-fired power plant that does not emit any CO₂ gas. In May 2006 the planning work began on the pilot plant at Schwarze Pumpe in eastern Germany. Through this investment we



are leading the global development in a technology area that will be absolutely necessary in the efforts to solve the climate issue.

Leading role in opinion-shaping

Vattenfall has taken a leading role in the opinion-shaping work surrounding our shared responsibility for the future. In our "Curbing Climate Change" report, which we published in January 2006, Vattenfall outlined a proposal for handling

climate change on the global level. Vattenfall has set forth a global model that is based on the principle that all countries should participate in relation to their share of global GDP, without slowing economic development or allowing the changeover in energy sources to present a threat to prosperity. Vattenfall's proposal combines trade mechanisms with measures for accelerating technological development.

Vattenfall's responsible approach and constructive attitude toward handling this important and difficult issue has been met with interest and respect around the world, and I have personally presented our proposal at several international environmental conferences and discussed it with several of the world's political leaders. Since December 2006 I have had the honour to serve as German Chancellor Angela Merkel's adviser on climate issues. During the current year, Germany is serving as chair in both the EU and G8 and sees this as a key opportunity to further direct focus to the climate issue.

In early 2007 Vattenfall took two more steps in its work on reducing greenhouse gas emissions. Together with the leaders of a number of international corporations, we launched the global 3C initiative – Combating Climate

Change. Detailed information on this initiative can be found at the 3C website: www.combatclimatechange.org.

In our extensive Global Climate Impact Abatement Map, Vattenfall has compiled the measures that are needed and possibly can be done around the world to curb climate change. If these measures are realised it will be possible to stabilise emissions of greenhouse gases at a level making it possible to limit the long-term temperature rise to 2°C. For more information on this, visit our website: www.vattenfall.com/climate.

A central part of Vattenfall's proposal involves developing a global system for trading in emission allowances. Vattenfall therefore supports the system for trading in emission allowances for greenhouse gases that has been used in the European Union during the past two years.

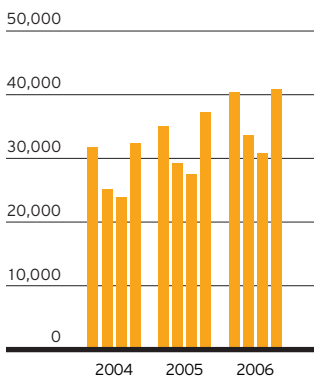
Record earnings also in 2006

Vattenfall is thus facing a number of major challenges – ranging from the decisive climate issues to issues involving customer confidence and price levels. Allow me therefore to once again stress that continued profitable growth is a

Sales rose 12.9% to SEK 145,815 million (129,158)

Net sales, quarterly

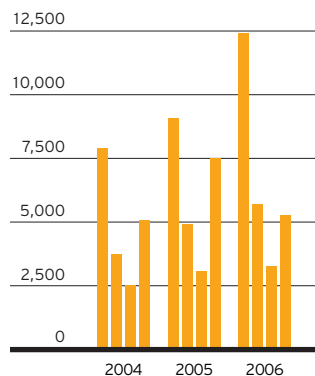
SEK million



Operating profit excluding items affecting comparability rose 8.5% to SEK 26,676 million (24,585)

Operating profit, quarterly

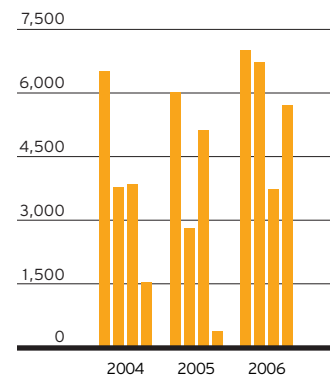
SEK million



Free cash flow totalled SEK 23,178 million (14,341)

Free cash flow¹, quarterly

SEK million



¹) Cash flow from operating activities less maintenance investments.

prerequisite for our success in handling future issues. Stable long-term earnings are a necessity if Vattenfall is to be a stable and long-term player that can guarantee energy supply in the future.

I am pleased to note that the Group's earnings for 2006 were strong, despite a weak fourth quarter. Operating profit excluding items affecting comparability rose 8.5% to SEK 26,676 million, and net sales rose 12.9% to SEK 145,815 million. The improvement can be credited primarily to stronger earnings from our German operations as a result of higher wholesale electricity prices and slightly higher generation volumes. In the Nordic countries, however, sales as well as earnings were down from the preceding year due to a significant drop in generation. This decline is mainly attributable to a weak hydrological balance – water levels in reservoirs hit their lowest levels since 1996 – and to problems at the Forsmark nuclear power plant during the second half of the year. These problems, which were caused by a short circuit in a switchyard outside the Forsmark facility in late July, resulted in a standstill for both reactors for a couple of months. The disruption resulted in a loss of approximately SEK 900 million in

income. The Nordic operations were also burdened by higher generation taxes of approximately SEK 1.7 billion.

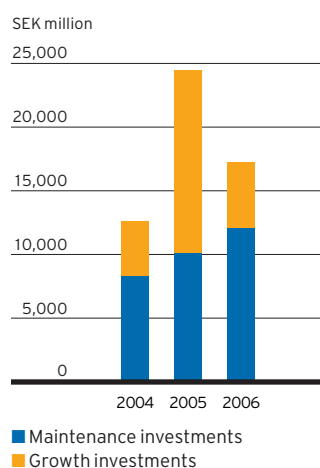
To meet tomorrow's challenges, Vattenfall must also succeed in attracting the competence needed to be a leading energy company in Europe. To our pleasure, we can see that the energy industry is regarded as a future segment by many young people, and vacant positions in our organisation attract many applicants.

It is with the knowledge of strong contributions from all of our employees during the past year and knowing that we are well equipped for the future that I look forward with confidence to the many major challenges that await us – in 2007 and the years that follow.

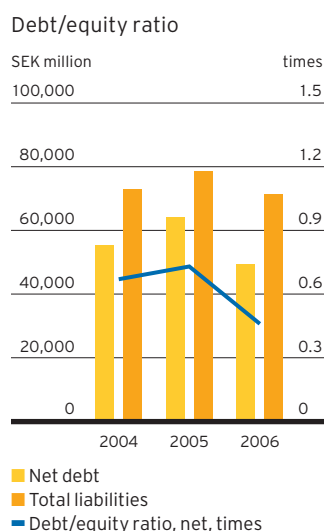


Lars G. Josefsson
President and CEO

Investments



Net debt decreased by SEK 14.9 billion, to SEK 49.4 billion



Net debt, quarterly

