



Press Release

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Swedish Electric Utility Vattenfall AB Placed on Watch Negative After German Merger Called Off

STOCKHOLM (Standard & Poor's) **Sept. 28, 2001**--In response to the cancellation, on Sept. 26, 2001, of the planned merger between Sweden-based electric utility Vattenfall AB's German holdings and Berlin-based utility Bewag, Standard & Poor's today placed all long-term ratings on Vattenfall and related entities on CreditWatch with negative implications. At the same time, all short-term ratings were affirmed. (See list below).

The rating actions reflect the potential negative impact on the future business and financial profiles of the Vattenfall group as a result of not having direct access to Bewag's base of 2.2 million customers, its stable monopoly operations, and the expected consolidation of its cash flows from 2003 onward. In view of this, a potential downgrade of Vattenfall by one notch cannot be ruled out.

In May 2001, Vattenfall agreed with the Mirant Corp. (BBB-/Stable/A-3) of the U.S. to form the third-largest electricity group in Germany (Neue Kraft). The group, which was to have been fully established by 2003, was to have included:

- Hamburgische Elektrizitäts-Werke AG (HEW; electricity and heating operations in Hamburg, owned 73.8% by Vattenfall);
- VEAG (generation and transmission operations in eastern Germany; 81.25% owned by HEW);
- Laubag (VEAG's lignite supplier; 92.5% owned by HEW); and
- Bewag (electricity and heating operations in Berlin; 44.8% owned by each HEW and Mirant Corp).

Following the cancellation of the merger plan, both Mirant Corp. and HEW have stated that they will maintain their respective holdings in Bewag. Vattenfall and HEW's 25.1% minority owner, the City of Hamburg, will continue the formation of Neue Kraft without the participation of Bewag. Vattenfall and HEW are open to the possibility of Bewag joining Neue Kraft at a later stage.

Overall, Standard & Poor's considers the cancellation of the merger to have negative implications for Vattenfall's credit profile. It increases the group's imbalance between electricity generation and supply operations in the German market, and reduces its access to Bewag's stable monopoly electricity distribution and heating operations. Furthermore, the cash flow contribution expected from the planned full consolidation of Bewag from 2003 will now not materialize, limiting cash flow from Bewag to dividends only (Bewag's funds from operations—FFO—for 1999/2000 was about €400 million). Adjusting Vattenfall's financial forecast for the 2001-2004 period according to the expected consequences of the abandoned merger, Standard & Poor's assesses at this stage that the average forecast FFO interest coverage could decrease from the 3.5 times (x) previously expected. Importantly, the financial

recovery expected for Vattenfall from 2003, including the reduction in the group's debt leverage, could be weaker than anticipated.

One factor partly mitigating the negative implications is that the absence of a minority owner enhances Vattenfall's direct control of the German operations and its cash flows, reducing execution risk in the integration process. In Standard & Poor's view, a deterioration in Vattenfall's business and financial profile might be offset by allowing additional partners to join the Neue Kraft group, or by making asset disposals to achieve a more balanced business portfolio. Furthermore, the Vattenfall group's debt levels could decrease if Bewag exercises its call option to obtain a 43.75% holding in VEAG and a 32.5% holding in Laubag (Bewag's current holdings are 6.25% and 2.5%, respectively). This could, however, again raise concerns regarding the actual control over operations and cash flows in the German operations.

Standard & Poor's expects to resolve the CreditWatch placement within the next month by further evaluating the business and financial implications of the cancelled merger and the strategic reaction of Vattenfall.

RATINGS PLACED ON CREDITWATCH WITH NEGATIVE IMPLICATIONS

| | Rating To | From |
|-----------------------------------|----------------|-----------|
| Vattenfall AB | | |
| Long-term corporate credit rating | A-/Watch Neg | A-/Stable |
| Senior unsecured ratings | A-/Watch Neg | A- |
| Subordinated debt rating | BBB+/Watch Neg | BBB+ |
| Vattenfall Treasury AB | | |
| Senior unsecured ratings* | A-/Watch Neg | A- |
| Subordinated debt rating* | BBB+/Watch Neg | BBB+ |

RATINGS AFFIRMED

Vattenfall AB
Short term corporate credit rating A-2

Vattenfall Treasury AB
Commercial paper rating* A-2
Swedish Commercial paper rating * K-1

Vattenfall Treasury Inc.
Commercial paper rating* A-2

*Guaranteed by Vattenfall AB.

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