STANDARD & POOR'S

RATINGSDIRECT®

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ENECO Holding N.V.

Primary Credit Analyst:
Karin Erlander, London (44) 20-7176-3584; karin_erlander@standardandpoors.com

Secondary Credit Analyst:
Hugues De La Presle, Paris (33) 1-4420-6666; hugues_delapresle@standardandpoors.com

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ENECO Holding N.V.

Major Rating Factors

Corporate Credit Rating
A/Watch Neg/A-1

Strengths:

- Bulk of operating earnings derived from regulated distribution business
- Monopoly operations within licensed area
- Weaker financial risk profile, although still satisfactory

Weaknesses:

- Enforced unbundling of supply assets and trading activities from distribution networks
- Exposure to potentially volatile wholesale electricity prices as a result of short power supply position

Rationale

The ratings on Netherlands-based utilities ENECO Holding N.V. and N.V. ENECO (collectively known as Eneco) reflect the stable and substantial earnings contribution of the group's monopoly energy distribution businesses and its satisfactory financial risk profile.

These strengths are offset by Eneco's exposure to volatile wholesale power prices, given its short power supply position, and the risks stemming from the forced unbundling of its regulated distribution networks from the rest of its operations. Standard & Poor's Ratings Services placed all ratings on Eneco, including the 'A' long-term corporate credit rating, on CreditWatch with negative implications on July 18, 2008.

The CreditWatch placement, which also applies to Dutch utilities N.V. NUON, Essent N.V., and Delta N.V., is driven by the risks linked to the forced ownership unbundling of regulated distribution operations from unregulated businesses at the latest by Dec. 31, 2010.

Given that the ratings on Eneco factor in its vertically integrated business model and its significant share of regulated earnings, the unbundling will have negative credit consequences for the company. Eneco's monopoly energy distribution businesses accounted for 71% of the group's reported operating income in 2007.

Short-term credit factors

The short-term rating is 'A-1'. Eneco's sound liquidity is underpinned by limited debt maturities before 2012, available cash and securities of €113 million (at end-December 2007), and an undrawn €1.5 billion credit facility maturing in 2013. The facility is a backup for the €750 million commercial paper program, and also provides collateral support for letters of credit (LOCs) issued in connection with the company's cross-border leases (CBLs).

Eneco's net exposure to the costs of early termination of the CBLs, amounting to $948 million at year-end 2007, is a negative credit factor. The group's risk in this respect could heighten as a result of the upcoming unbundling. The exposure is partly covered by LOCs of about $1.0 billion, but the portion of costs that must be covered by LOCs depends on the corporate credit rating; a downgrade would require an increase of the drawing amounts.

CreditWatch

We aim to resolve the CreditWatch placement by the end of the year and will focus on the following main points:

- The strategy of Eneco's municipality shareholders regarding the unregulated business, as the regulated business has to remain in public hands.
- The financial policy of the regulated businesses. The regulator is considering putting in place minimum credit metrics for the regulated businesses. We will meet with the regulator to gain a better understanding of how these metrics might affect the financial risk profiles of the regulated businesses.
- The allocation of debt between the unregulated and regulated businesses.
- The consequences of unbundling for Eneco's CBL exposure.
- Any one-time costs and/or liabilities resulting from the unbundling.

Business Description

Eneco is the third-largest energy utility in The Netherlands. Its operations primarily span distribution (71% of 2007 consolidated EBIT) and supply (24%). It serves about two million customers and has retail market shares of 21% in electricity and 22% in gas. The group is also the largest supplier and distributor of district heating.

Eneco's shareholders are public authorities, including the municipalities of Rotterdam (31.3%), The Hague (16.6%), Dordrecht (9.1%), and other smaller local authorities, each with less than 5.0%.

Business Risk Profile: Low-Risk Monopoly Network Operations Are Key Strength

Eneco's business risk profile is currently underpinned by its monopoly position and the predictable revenues generated by its regulated network operations. These strengths are partially offset by exposure to potentially volatile wholesale electricity prices as a result of the group's short power supply position. The upcoming unbundling of supply assets and trading activities from the distribution networks is expected to result in a different business structure, which will affect the risk profile of the emerging entities.

Strategy: Focus on sustainable energy generation and supply

Currently, the high operational risk associated with Eneco's energy trading and supply activities is largely offset by its low-risk network operations. Like the other Dutch publicly owned utilities, however, Eneco will have to split into separate distribution and supply and generation companies by Dec. 31, 2010. In that respect, Eneco's infrastructure activities were divided into two separate companies in 2008. Infra is a commercial entity, focusing on network maintenance. Stedin remains fully regulated and is responsible for the management, enhancement, and expansion of the networks.

Last year, Eneco adopted a strategy focusing on sustainable energy supply, and launched a number of biomass and wind energy initiatives. By actively seeking partners to facilitate and accelerate the process, Eneco foresees that its entire power supply will be generated from sustainable energy sources or clean fossil fuels by 2020. An example is the Princess Amalia wind farm on the North Sea, which is a joint project between Econcern, a holding company specializing in sustainable energy supply, investment company Energy Investments Holding, and Eneco. Eneco wants to continue the development of wind farms, and to construct a second wind farm off the Dutch coast. Eneco could also acquire wind farms, as exemplified in the 85% stake it holds in the Belgian wind farm developer, Air Energy, or purchase energy generated by wind farms. The company's €2 billion investment program over 2008-2012 is mainly aimed at the northwest European region.

Regulation: Stable and transparent regulatory regime supports distribution operations

Eneco's distribution operations benefit from a stable and transparent regulatory regime. The regulator--Energiekamer, which is part of the Netherlands Competition Authority (NMa)--sets price caps based on an annual adjustment of the consumer price index less an efficiency factor (X). All Dutch utilities were required to transfer the management of the high-voltage electricity grids (110 kilovolts and higher) to the national transmission system operator, TenneT, in 2008. The supply operations are not regulated.

Markets: Stable market position and mixed customer base

Eneco is the third-largest utility in The Netherlands, serving about two million business and retail customers nationwide and with retail market shares of 21% in electricity and 22% in gas. Growth in the Dutch utility market has remained stable, roughly mirroring that of the country's GDP.

The group's distribution networks are primarily concentrated in the southwestern region of The Netherlands, with some gas distribution in the north. Nearly 60% of Eneco's electricity revenues stems from commercial and industrial customers, with the remainder from the residential sector. The majority of its gas revenues come from residential customers, who generate more stable revenues.

Operations: Group seeks to become more vertically integrated

Even when factoring in the PPA set up in late 2004 with the Rijnmond power station, and a smaller 15-year PPA set up with Air Liquide, Eneco remains significantly short of power supply resources. The PPAs and the group's own generation account for less than one-half of its power needs.

Eneco remains exposed to substantial commodity price risk. Volumes not covered under PPA contracts are hedged in the over-the-counter (OTC) market and energy exchanges. All fixed-price risks of industrial and commercial customers are hedged back to back at the moment of customer signing, thereby limiting the price exposure. All sourcing for retail customers is done well in advance of delivery and only weather-related exposures are traded through the power exchange.

The group is seeking to become more vertically integrated in order to be less dependent on the wholesale market. Its aim is to cover 50%-70% (2,000 MW–2,800 MW) of its electricity requirements via its own power stations and long-term purchase contracts. The Rijnmond and PerGen power plants generate 850 MW and 250 MW, respectively, corresponding to about 28% of Eneco's electricity needs. The 120 MW offshore Princess Amalia wind farm in the North Sea became operational this year, and more wind farm projects are planned. Eneco is also aiming to construct a 840 MW gas fired combined heat and power plant in Rotterdam, in a joint venture with International Power PLC (BB-/Stable/--).

In gas, Eneco wants to become less dependent on GasTerra B.V. (AA+/Stable/A-1+). To that end, Eneco is investing in gas storage capacity and has agreed with StatoilHydro ASA on the delivery of 500 million cubic meters of natural gas annually over three years, starting in October 2008.

Competitive position/profitability: Monopoly distribution and good quality of assets

The distribution operations are essentially a monopoly. Direct competition in this area is unlikely to arise, owing to the capital-intensive nature of network infrastructure and the limited returns allowed on investments by the regulator. The networks require limited capital expenditure, owing to the good quality of the assets and the high proportion of the network that is underground.

Electricity supply is not regulated and all customers are free to choose their suppliers. The Dutch energy markets are experiencing some competition on prices, especially in the business segment.

Financial Risk Profile: Satisfactory Financial Profile Reflects Solid Cash Flows

We expect Eneco's financial risk profile to weaken due to large investments, as indicated by the company's €2 billion investment program over 2008-2012. However, the deterioration comes from a strong position and Eneco's financial risk profile should remain satisfactory.

Accounting: Adjustments of operating leases and PPAs

Eneco reports under International Financial Reporting Standards (IFRS). We adjust Eneco's reported figures:

- Operating lease commitments are capitalized using a 6% discount rate and are added to debt.
- The annual capacity payments relative to the Rijnmond and PerGen PPAs are capitalized, reflecting our view that long-term electricity utility PPAs are debt-like.

Table 1

Reconciliation Of ENECO Holding N.V. Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)*

	--Fiscal year ended Dec. 31, 2007--							
ENECO Holding N.V. reported amounts								
	Debt	**Operating income (before D&A)**	**Operating income (before D&A)**	**Operating income (after D&A)**	**Interest expense**	**Cash flow from operations**	**Cash flow from operations**	**Capital expenditures**
Reported	1,346.0	690.0	690.0	474.0	80.0	725.0	725.0	370.0
Standard & Poor's adjustments								
Operating leases	99.8	37.5	5.2	5.2	5.2	32.3	32.3	58.2
Postretirement benefit obligations	24.6	--	--	--	--	--	--	--
Surplus cash and near cash investments	(113.0)	--	--	--	--	--	--	--
Power purchase agreements	456.4	27.4	27.4	27.4	27.4	--	--	--
Reclassification of nonoperating income (expenses)	--	--	--	40.0	--	--	--	--
Reclassification of working-capital cash flow changes	--	--	--	--	--	--	(284.0)	--
Total adjustments	467.8	64.9	32.6	72.6	32.6	32.3	(251.7)	58.2

Table 1

Reconciliation Of ENECO Holding N.V. Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)*(cont.)

Standard & Poor's adjusted amounts

	Debt	Operating income (before D&A)	EBITDA	EBIT	Interest expense	Cash flow from operations	Funds from operations	Capital expenditures
Adjusted	1,813.8	754.9	722.6	546.6	112.6	757.3	473.3	428.2

*Please note that two reported amounts (operating income before D&A and cash flow from operations) are used to derive more than one Standard & Poor's-adjusted amount (operating income before D&A and EBITDA, and cash flow from operations and funds from operations, respectively). Consequently, the first section in some tables may feature duplicate descriptions and amounts.

Corporate governance/Risk tolerance/Financial policies

In view of Eneco's strategy to accelerate into sustainable energy, we expect Eneco's financial risk profile to become less conservative, although the strategy to enter projects together with partners is a mitigating factor.

Eneco is exposed to substantial commodity price risk, but have in place specific control measures, as well as risk management and a risk committee overseeing the trading activities. Also, prudent financial and risk management policies govern Eneco's exposure to interest rate, liquidity, and credit risk. Currency risk is virtually zero as all results, trading transactions, and cash flows are realized within the eurozone.

Eneco's dividend payout is set at a minimum of 50% of net income and was 55% for the year 2007.

Cash flow adequacy: Strong, owing to robust cash flows from regulated distribution activities

In 2007, Eneco reported a 14% decrease in operating profit and funds from operations fell by 33% to €441 million, mainly due to lower revenues and high costs relating to the takeover of ONS Energie. One-off items, including favorable tax items, boosted earnings, without which the net profit was similar to 2006. With adjusted debt largely unchanged, adjusted FFO to debt and FFO interest coverage fell to 26% and 4.9x, respectively, from 37% and 7.9x in 2006.

We expect Eneco's cash flow generation to remain solid, however, owing to its robust cash flows from regulated distribution activities. However, we expect capital expenditures to rise over the next three years, which could result in negative free operating cash flows.

Capital structure/Asset protection

We expect Eneco's adjusted debt to increase, given the large investment program. Although Eneco's adjusted debt to capital was 37% in 2007, down from 40% in 2006, we expect this ratio to rise above 40% this year or next.

Eneco has limited debt maturities before 2012. In 2007, Eneco made a number of private placements with U.S. investors, borrowing a total of €775 million for terms between seven and 20 years. Using the funds to repay a bridge facility, Eneco extended its maturity profile significantly. The company has access to an undrawn €1.5 billion credit facility maturing in 2013. The facility is a backup for the €750 million commercial paper program, and also provides collateral support for LOCs issued in connection with the company's CBLs.

Cross-border leases

Between 1997 and 2000, Eneco entered into 38 tax-driven long-term lease and lease-back transactions with U.S. investors. The transactions total $6.2 billion and pertain to large parts of Eneco's electricity, gas, and heating networks. As the legal and economic ownership of these assets has remained with Eneco, these assets still appear on its balance sheet. As these transactions mature between 2016 and 2028, the risk for U.S. investors of the cost of premature cancellation, which represented $2.4 billion at year-end 2007, is covered by:

- Investments worth $1.43 billion, which correspond to some of the proceeds of the transactions that are invested in U.S. government bonds and bonds of similar creditworthiness.
- LOCs for $1.02 billion.

Eneco's net exposure to the costs of early termination of the CBLs, amounting to $948 million at year-end 2007, is a negative credit factor. The group's risk in this respect could heighten as a result of the upcoming unbundling, as the portion of costs that must contractually be covered by LOCs would increase following a downgrade. Structural subordination does not apply to Eneco, although the net exposure is secured by mortgages and liens on part of the networks. This reflects that the $948 million constitutes, in our view, Eneco's only priority liability compared with assets of €6.3 billion.

Table 2

ENECO Holding N.V.--Peer Comparison*

	--Fiscal year ended Dec. 31, 2007--			
(Mil. €)	**ENECO Holding N.V.**	**Delta N.V.¶§**	**Essent N.V.**	**N.V. NUON**
Rating as of Sept. 10, 2008	A/Watch Neg/A-1	A-/Watch Neg/--	A+/Watch Neg/A-1	A+/Watch Neg/A-1
Revenues	4,789.0	1,813.2	7,377.5	5,650.0
Net income from cont. oper.	424.0	114.5	799.7	864.0
Funds from operations (FFO)	473.3	285.4	1,276.5	1,167.6
Capital expenditures	428.2	240.1	778.2	439.1
Cash and short-term investments	0.0	61.2	0.0	0.0
Debt	1,813.8	844.0	580.0	103.3
Preferred stock	0.0	0.0	0.0	0.0
Equity	3,040.0	1,742.3	5,161.7	5,658.0
Debt and equity	4,853.8	2,586.4	5,741.7	5,761.3
Adjusted ratios				
EBIT interest coverage (x)	4.9	4.1	9.2	12.0
FFO int. cov. (X)	4.9	8.9	11.8	12.5
FFO/debt (%)	26.1	33.8	220.1	1,129.8
Discretionary cash flow/debt (%)	8.7	0.4	(190.5)	391.4
Net cash flow/capex (%)	70.6	90.1	(5.5)	183.5
Total debt/debt plus equity (%)	37.4	32.6	10.1	1.8
Return on common equity (%)	14.7	8.7	19.8	16.0
Common dividend payout ratio (un-adj.) (%)	0.0	50.0	162.2	47.8

*Fully adjusted (including postretirement obligations). Excess cash and investments netted against debt. ¶Fully adjusted. §Excess cash and investments not netted against debt. N.M.--Not meaningful.

Table 3

ENECO Holding N.V.--Financial Summary*

	--Fiscal year ended Dec. 31--			
(Mil. €)	**2007**	**2006**	**2005**	**2004**
Rating history	A/Negative/A-1	A/Negative/A-1	A/Negative/A-1	A+/Watch Neg/A-1
Revenues	4,789.0	4,287.0	3,692.0	3,544.4
Net income from continuing operations	424.0	311.0	302.0	218.2
Funds from operations (FFO)	473.3	687.5	525.8	464.7
Capital expenditures	428.2	353.9	321.1	211.1
Cash and short-term investments	0.0	0.0	0.0	0.0
Debt	1,813.8	1,838.3	1,520.7	1,377.9
Preferred stock	0.0	0.0	0.0	0.0
Equity	3,040.0	2,738.0	2,601.9	2,396.8
Debt and equity	4,853.8	4,576.3	4,122.6	3,774.7
Adjusted ratios				
EBIT interest coverage (x)	4.9	6.1	6.2	3.6
FFO int. cov. (x)	4.9	7.9	6.7	4.1
FFO/debt (%)	26.1	37.4	34.6	33.7
Discretionary cash flow/debt (%)	8.7	(9.7)	6.8	23.3
Net Cash Flow/Capex (%)	70.6	147.4	132.4	220.1
Debt/debt and equity (%)	37.4	40.2	36.9	36.5
Return on common equity (%)	14.7	11.6	12.1	9.1
Common dividend payout ratio (un-adj.) (%)	0.0	0.0	0.0	0.0

*Fully adjusted (including postretirement obligations). Excess cash and investments netted against debt. N.M.--Not meaningful.

Ratings Detail (As Of September 11, 2008)*

ENECO Holding N.V.	
Corporate Credit Rating	A/Watch Neg/A-1
Commercial Paper	
Local Currency	A-1/Watch Neg
Senior Unsecured (2 Issues)	A/Watch Neg
Corporate Credit Ratings History	
18-Jul-2008	A/Watch Neg/A-1
04-Dec-2006	A/Negative/A-1
28-Apr-2006	A/Watch Neg/A-1
13-Jul-2005	A/Negative/A-1
19-Aug-2004	A+/Watch Neg/A-1
01-Apr-2004	A+/Negative/A-1
Business Risk Profile	1 2 3 4 $\boxed{5}$ 6 7 8 9 10
Financial Risk Profile	Satisfactory

Ratings Detail (As Of September 11, 2008)***(cont.)**	
Debt Maturities	
At Dec. 31, 2007 2008: €168 million 2009: €66 million 2010: €158 million 2011: €30 million 2012: €31 million Thereafter: €893 million	
Related Entities	
N.V. ENECO	
Issuer Credit Rating	A/Watch Neg/A-1

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

Additional Contact:
Infrastructure Finance Ratings Europe; InfrastructureEurope@standardandpoors.com

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Infrastructure Finance Ratings Europe; InfrastructureEurope@standardandpoors.com