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Research Update:

Sweden-Based Truck And Bus Producer Scania (publ.) AB Assigned 'zaAA+' South Africa National Scale Rating; On Watch Neg

Primary Credit Analyst:
Werner Staeblein, Frankfurt (49) 69-33-999-130;werner_staeblein@standardandpoors.com

Secondary Credit Analyst:
Maria Bissinger, Frankfurt (49) 69-33-999-120;maria_bissinger@standardandpoors.com

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Overview

- Scania has requested the release of our long-term national scale rating on its South Africa-based operations.
- We are assigning our 'zaAA+' long-term South Africa national scale rating to Scania and placing it on CreditWatch.
- The negative implications of the CreditWatch reflect the possibility that we could lower our 'A-' global scale rating on Scania as a result of Volkswagen AG's group restructuring.

Rating Action

On July 23, 2009, Standard & Poor's Ratings Services assigned its 'zaAA+' long-term South Africa national scale rating to Sweden-based truck and bus manufacturer Scania (publ.) AB. At the same time, the rating was placed on CreditWatch with negative implications.

The 'A-' long-term corporate credit rating on Scania remains on CreditWatch, where it was placed with negative implications on May 8, 2009, because of our concern about the potential impact on Scania's credit quality from the group restructuring of Volkswagen AG (A-/Watch Neg/A-2). VW owns 46% of Scania's capital and 71% of the voting shares.

Rationale

The ratings on Scania reflect our view of the group's strong business profile and modest financial risk. The ratings are supported by Scania's outstanding profitability in the global truck industry, which we do not expect to fall below an operating margin of 4%-5% at the bottom of the cycle. The group's truck and bus businesses benefit from leading market positions, up-to-date product lines, and the highest degree of component commonality in the global truck industry.

Scania's results for the first quarter of 2009 showed a sharp decline in profitability, owing to a considerable drop in unit sales. EBIT was down drastically compared with peak-of-the-cycle margins in 2006-2008, although Scania's industrial unit managed to achieve a positive EBIT margin of 3.2%, mainly supported by the service business. Free operating cash flow (FOCF) at Scania's industrial operations was positive at Swedish krona (SEK) 0.8 billion, owing to a reduction of working capital, notably inventory. The outlook for Scania's markets continues to be bleak. We expect that Scania's operating profit will contract sharply in 2009 compared with 2008, although the group's industrial unit will likely show slightly positive EBIT and positive FOCF in 2009.

In 2008, Scania's credit protection measures, such as funds from operations to debt of 46% and debt to EBITDA of 0.9x, were commensurate with the rating. However, rapidly weakening business conditions have made Scania vulnerable to the global economic downturn.

Short-term credit factors

The short-term rating on Scania is 'A-2'. Standard & Poor's considers Scania's liquidity and financial flexibility to be adequate. They are enhanced by two committed revolving credit facilities (RCF) of €1 billion each. In early 2008, Scania upsized its old €500 million RCF to €1 billion. This new facility is due in January 2013 and carries a two-year renewal option. The second RCF is due in May 2012.

As of March 2009, Scania reported access to unutilized credit facilities of SEK27 billion, although some of these facilities are not committed. Scania has committed facilities with a broad variety of banks. We understand that, for its financial services unit, Scania pursues a policy of dedicated financing that covers the estimated demand for funding during the subsequent year.

Scania's bank lines are not subject to financial covenants or rating triggers.

Scania's liquidity position is underpinned by access to medium-term note and commercial paper programs. In addition, its industrial unit reported cash and short-term investments of SEK5.9 billion as of March 31, 2009. Short-term maturities at the industrial unit are covered with existing financial flexibility. We expect Scania to report positive FOCF in 2009.

CreditWatch

VW owns 46% of Scania's capital and 71% of the voting shares. The CreditWatch placement is based on our parent-subsidiary rating criteria and reflects the possibility that we could lower our assessment of Scania's credit quality, owing to VW's group restructuring. A negative rating action could result from a change in Scania's financial or business profile if it becomes directly involved in the VW group's restructuring. We could also downgrade Scania if we perceive, under our parent-subsidiary rating criteria, that Scania will remain subject to group risk through VW's exercise of its voting power or through other means of influence, in the absence of offsetting protective measures and incentives. At this stage, we expect that, in the event of a downgrade, our rating on Scania will not likely be higher than that on VW.

Related Research

For details on our parent-subsidiary rating methodology, please see the chapter "Parent/Subsidiary Links" in the 2006 edition of our corporate criteria book "Corporate Ratings Criteria 2006" on RatingsDirect. Go to the

"Criteria" tab at the top, select "Corporates" in the drop-down menu, then "Criteria Books."

Ratings List

New Rating

Scania (publ.) AB	
Long-Term South Africa National Scale Rating	zaAA+/Watch Neg

Ratings Unchanged

Scania (publ.) AB	
Corporate Credit Rating	A-/Watch Neg/A-2
Short-Term South Africa National Scale Rating	zaA-1

Additional Contact:
Industrial Ratings Europe;CorporateFinanceEurope@standardandpoors.com

Ratings information is available to RatingsDirect subscribers at www.ratingsdirect.com. It can also be found on Standard & Poor's public Web site at www.standardandpoors.com; select your preferred country or region, then Ratings in the left navigation bar, followed by Find a Rating. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow (7) 495-783-4011.