Bulletin:

French Utility Veolia To Offset €3.4 Billion Stake Purchase In Suez With Remedy Measures

October 6, 2020

PARIS (S&P Global Ratings) Oct. 6, 2020--S&P Global Ratings today said that it expects French utility Veolia Environnement S.A. (BBB/Stable/A-2) will be able to restore its balance sheet after purchasing a 29.9% stake in Suez Environnement S.A. for €3.4 billion from Engie S.A. In light of Veolia's prudent financial policy, we believe it will implement remedy measures that offset the financial impact of this fully debt-financed acquisition, resulting in S&P Global Ratings-adjusted funds from operations (FFO) to debt returning to at least 20% in 2021, after dipping well below the 20% rating target level in 2020 due to the acquisition and challenging operating conditions amid the COIVD-19 pandemic. Should mitigation measure not materialize in the coming quarters, we will reconsider our assessment.

On Oct. 5, 2020, Veolia announced that Engie accepted its €3.4 billion offer to purchase a 29.9% stake in Suez. The price was higher than we initially anticipated, since Veolia increased its offer to €18.0 per share from €15.5 previously. That said, we expect Veolia will compensate for the additional cash outflow of about €500 million with further remedy measures. We understand the acquisition and cash outflow are imminent, given that they are not subject to any particular regulatory hurdle. In our base case, we now consolidate Suez as an affiliate of Veolia, with annual dividends to be received from Suez averaging €150 million-€200 million over 2021-2023.

Veolia confirmed its intention to file a voluntary public takeover bid on Suez's remaining shares to complete the merger of the companies. Should Veolia launch a full takeover offer, we would reassess our base-case scenario, evaluating the additional remedy measures. The offer price for the remaining stake should be €18 per share, in line with the price paid to Engie for the 29.9% stake. This would imply an additional €6.5 billion-€7.0 billion cash outflow for the full 70.1% stake, which would add to the debt already on Suez's balance sheet (about €12 billion). We understand Veolia aims to launch the full takeover bid after it receives the go-ahead from Suez's board of directors; Veolia aims to resume discussions today. Veolia reserves the right not to file a public tender offer in the event of major adverse circumstances impacting the Suez group, or if Suez divests any strategic assets, or takes any other measures that significantly affect these assets. These assets include its Spanish and Chilean water assets; Water Technologies & Solutions; its regulated water assets in the U.S; and its waste management assets in France, the U.K., and Australia. We also note that as of this morning Suez still defined the purchase of the 29.9% stake from Engie as hostile and under unprecedented and irregular conditions.

If successful, the transaction would create a global leader in the highly fragmented water and waste markets, with complementary businesses and geographies, potential for synergies, a combined EBITDA of about €7 billion, and over 200,000 employees. While we believe the

PRIMARY CREDIT ANALYST

Massimo Schiavo
Paris
+ 33 14 420 6718
Massimo.Schiavo
@spglobal.com

SECONDARY CONTACTS

Pierre Georges
Paris
(33) 1-4420-6735
pierre.georges
@spglobal.com

Claire Mauduit-Le Clercq
Paris
+ 33 14 420 7201
claire.mauduit
@spglobal.com

Emeline Vinot
Paris
(33) 1-4075-2569
emeline.vinot
@spglobal.com

ADDITIONAL CONTACT

Industrial Ratings Europe
Corporate_Admin_London
@spglobal.com

transaction will be broadly positive for Veolia's business risk profile, it is too early to assess its full impact, given significant uncertainties around the transaction at this stage, including its financing, the long time frame until completion, Veolia's final ownership in Suez, integration risks, the operating performance of each group amid the COVID-19 pandemic, and the likely evolving business perimeter. In particular, the acquisition would require the sale for competition reasons of a number of activities, including Suez's French water operations (already pre-agreed with French infrastructure fund Meridiam).

Taking into account the €3.4 billion cash outflow for the 29.9% stake in Suez and the more challenging operating conditions in 2020, we expect Veolia's 2020 S&P Global Ratings-adjusted FFO to debt will decline to well below 20% from 22.6% in 2019. In addition, we anticipate reported EBITDA of close to €3.6 billion, adjusted debt increasing to €15 billion-€16 billion, and adjusted debt to EBITDA increasing above 4.0x from 3.5x in 2019. In line with its financial policy and leverage targets, we expect Veolia will implement remedy measures in 2020 and 2021 and benefit from a rebound in operating performance in 2021. We now forecast reported EBITDA will increase to more than €4.0 billion in 2021. This would support improvement in credit metrics. In particular, in 2021, we anticipate adjusted FFO to debt improving to at least 20% (threshold for the rating) and adjusted debt to EBITDA declining to close to 4.0x.

Veolia -- Key Metrics

(Bil. €)	2019a	2020e	2021e	2022e	2023e
EBITDA reported	4	3.5-3.7	3.9-4.1	4.0-4.2	4.2-4.4
EBITDA*	3.7	3.3-3.6	3.8-4.1	4.0-4.3	4.2-4.4
Debt*	13	15.0-16.0	15.0-16.0	15.0-16.0	15.0-16.0
Capex*	1.9	1.9-2.3	2.2-2.7	1.5-2.0	1.5-2.0
Dividends*	0.7	0.4-0.5	0.7-0.8	0.8-0.9	0.8-0.9
FFO to debt* (%)	22.6	17.0-19.0	20.0-21.0	20.0-22.0	20.0-22.0
Debt to EBITDA* (x)	3.5	4.0-4.5	3.5-4.0	3.5-4.0	3.5-4.0

Capex--Capital expenditure. FFO--Funds from operations a--Actual. e—Estimate. *S&P Global Ratings' adjusted figures.

Related Research

- French Utility Veolia Environnement 'BBB' Rating Affirmed After €2.9 Billion Bid For 29.9% Stake In Suez; Otlk Stable, Sept. 1, 2020
- Veolia Environnement S.A., June 10, 2020
- French Utility Veolia Environnement S.A. Affirmed At 'BBB' Despite COVID-19 Operating Uncertainty; Outlook Stable, March 27, 2020

This report does not constitute a rating action.