



28th April 2016

Utilities

Suez

Price EUR16.10

Q1 metrics: flat LfL EBIT growth, as expected. 2016 guidance confirmed despite poor year start

Fair Value EUR18,5 vs. EUR19 (+15%)

BUY

Bloomberg	SEV FP
Reuters	SEVI.PA
12-month High / Low (EUR)	19.0 / 15.1
Market Cap (EURm)	8,762
Ev (BG Estimates) (EURm)	20,808
Avg. 6m daily volume (000)	1 258
3y EPS CAGR	4.1%

This morning Suez posted poor Q1 sales and operating performance as expected. Sales were up +0.5% YoY thanks to the International division while EBIT came out at -4.6% to EUR253m whereas we were forecasting EUR258m. As expected, the start of the year is difficult for the group, especially compared with Veolia. We expect a growth recovery over the next nine months. 2016 guidance was confirmed as well as the 2017 EBITDA target. We anticipate a negative share price reaction this morning but still see upside to the 2016-18 consensus. Buy, FV @ EUR18.5 unchanged.

	1 M	3 M	6 M	31/12/15
Absolute perf.	2.8%	-4.0%	-8.8%	-6.7%
Utilities	3.4%	0.8%	-6.5%	-2.8%
DJ Stoxx 600	3.6%	2.4%	-7.6%	-5.1%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	15,135	15,444	16,031	16,459
% change		2.0%	3.8%	2.7%
EBITDA	2,751	2,690	2,907	3,092
EBIT	1,381	1,315	1,477	1,590
% change		-4.8%	12.3%	7.6%
Net income	559.8	435.7	557.4	631.5
% change		-22.2%	27.9%	13.3%

	2015	2016e	2017e	2018e
Operating margin	9.1	8.5	9.2	9.7
Net margin	3.7	2.8	3.5	3.8
ROE	8.2	6.5	8.2	9.2
ROCE	8.0	7.3	8.0	8.6
Gearing	121.6	133.7	138.3	137.0

(EUR)	2015	2016e	2017e	2018e
EPS	1.04	0.81	1.04	1.17
% change		-22.2%	27.9%	13.3%
P/E	15.5x	19.9x	15.5x	13.7x
FCF yield (%)	2.9%	0.5%	2.8%	7.0%
Dividends (EUR)	0.65	0.65	0.70	0.79
Div yield (%)	4.0%	4.0%	4.3%	4.9%
EV/Sales	1.3x	1.3x	1.3x	1.3x
EV/EBITDA	7.4x	7.7x	7.3x	6.9x
EV/EBIT	14.7x	15.8x	14.4x	13.5x

ANALYSIS

- Main Q1 metrics:** Total Q1 sales came out at **EUR3.55bn**, up **0.5%** YoY and up **1.5%** LfL with most of the sales growth coming from International business (+9.5% LfL) while the Water Europe division reported flat LfL growth (+0.3%) helped by positive sales growth in Spain and in Chile (+1.7% LfL) despite a decline in water volumes compared with Q1 2015 due to highly unfavourable weather conditions in the summer period. As expected, the Waste Europe business (renamed *Recycling and Recovery Europe*) incurred a negative sales performance (-1.9% LfL and -2.4% YoY) due to the negative effect from the secondary raw materials prices drop. Most of the sales decline in this business came from French activities (-5.4% LfL) while the UK and Benelux/Germany posted positive LfL sales growth. In such a poor growth environment, the group posted **Q1 EBITDA of EUR574m** down 3.9% YoY and **flat on a LfL basis** below both our figures and consensus expectations (respectively *EUR591m* and *EUR587m*) and EBIT of **EUR253m** down **4.6% YoY** and up **0.6% organically** leading to a **40bp EBIT** margin decline to **7.1%** compared with last year.
- 2016 and 2017 targets confirmed:** Despite this poor expected performance, management is confident in its ability to generate higher earnings growth during the rest of the year than during Q1. 2016 guidance to post organic sales growth greater than or equal to **2%** and organic EBIT growth greater than organic revenue growth was confirmed. Cash flow and net debt targets were also confirmed for 2016. The group's target to generate **EBITDA of EUR3bn** thanks to M&A (at 50%) by 2017 was also confirmed even if management did not give additional indications on any deals in its press release. If 2017 numbers need to be revised down, we assume this will be done during the H1 2016 earnings presentation.
- Conclusion:** This is a poor start to the year for the group as expected, and Veolia is likely to report higher EBITDA and EBIT LfL growth thanks to the contribution from cost-cutting notably. As such, we expect the share price to react negatively this morning but still see upside on 2016-18 consensus thanks notably to M&A. Buy, **FV @ EUR18.5** unchanged.

VALUATION

- At the current share price Suez is trading at 7.7x its 2016e EBITDA and offers a 4% yield
- Buy, FV @ EUR18.5

NEXT CATALYSTS

- Conference call at 08.30am CET (UK: +44(0)20 3427 1919)

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