

## Sector View

## Utilities

## TOP PICKS Q3 2016: VEOLIA

	1 M	3 M	6 M	31/12/15
Utilities	-0.2%	2.8%	-2.6%	-2.6%
DJ Stoxx 600	-5.1%	-2.3%	-9.8%	-9.8%

\*Stoxx Sector Indices

## Companies covered

Company	Recommendation	Target Price
<b>ALBIOMA</b>	<b>BUY</b>	<b>EUR16</b>
Last Price	EUR13.85	Market Cap. EUR413m
<b>AMOEBA</b>		
Last Price	EUR25.7	Market Cap. EUR154m
<b>E.ON</b>	<b>BUY</b>	<b>EUR10.2</b>
Last Price	EUR9.026	Market Cap. EUR18,061m
<b>EDF</b>	<b>BUY</b>	<b>EUR13.8</b>
Last Price	EUR10.97	Market Cap. EUR22,085m
<b>EDP RENOVAVEIS</b>	<b>NEUTRAL</b>	<b>EUR7.5</b>
Last Price	EUR6.78	Market Cap. EUR5,914m
<b>ENGIE</b>	<b>BUY</b>	<b>EUR16.8</b>
Last Price	EUR14.51	Market Cap. EUR35,336m
<b>PENNON GROUP</b>	<b>SELL</b>	<b>830p</b>
Last Price	945.5p	Market Cap. GBP3,901m
<b>RWE</b>	<b>NEUTRAL</b>	<b>EUR9.5</b>
Last Price	EUR14.19	Market Cap. EUR8,568m
<b>SUEZ</b>	<b>BUY</b>	<b>EUR17.5</b>
Last Price	EUR14.08	Market Cap. EUR7,665m
<b>VEOLIA</b>	<b>BUY</b>	<b>EUR23</b>
Last Price	EUR19.47	Market Cap. EUR10,969m
<b>VOLTALIA</b>	<b>BUY</b>	<b>EUR13</b>
Last Price	EUR9.6	Market Cap. EUR252m

## LOOKING BACK ON Q2 2016

The **Utilities sector** performed better than the **Stoxx 600** during Q2 2016 (2.8% for SX6P vs. -2.3% for the Stoxx 600). Since the beginning of the year, the Stoxx 600 Utilities has dropped 2.6% vs. a 9.8% decline for the Stoxx 600. Since our initiation of coverage in July 2014, we have recommended staying out of the sector as a whole and playing it safe through stocks offering strong earnings growth stories based on restructuring efforts. As a reminder, after having played Suez for Q1 2016, **we decided not to put any utilities stocks on the BG Top Picks List for Q2 2016 as we saw limited positive catalysts.** Inside the BG utilities universe (Albioma, EDF, EDPR, Engie, E.ON, Pennon, RWE, Suez, Veolia and Voltalia) the top performers were RWE (+24.7%) followed by Pennon (+16.6%) and Voltalia (+13.6%) while the worst performers were the two French environmental services companies we cover: Suez (-12.7%) and Veolia (-8.0%). Overall, integrated utilities outperformed environmental services companies. **Both the increase in power prices and positive newsflow (potential agreements on nuclear dismantling in Germany, potential carbon floor prices implementation in France) have contributed to this performance.** During the quarter, **European power prices (forward FY1 power prices for France, Germany, the UK and the Netherlands) surged by 26.7% on average (vs. a 20% drop in Q1-16) while gas (TTF) and coal prices increased by 23.5% (vs. -12% in Q1-16) and c.28% (vs. -4% in Q1-16) respectively over the period.**

## WHAT WE SEE FOR Q3 2016

As for Q2 2016, during the summer we expect no short term recovery in commodity prices in Europe. As a reminder our **models are marked-to-market** and therefore integrate no upside from any price recovery as yet. Except the traditional H2 earnings publications for almost all our stocks we do not **expect any precise catalysts.** All major events (*investor day, workshop session*) occurred during Q2-16 and affected positively Engie and RWE. **We remain cautious on the sector** given the lack of visibility on the macro and commodity prices environment, but have to admit that the sector could be played by investors as a defensive means of protecting against Brexit risks given that utilities remain poorly exposed to UK and the sector is not so cyclical.

**At this stage we remain Neutral.**

## CONCLUSIONS AND TOP PICKS

In our last reports, **we updated our models with our latest macro data assumptions (update on integrated utilities: [Potential upside from higher Brent for EDF & Engie](#) and report on environmental services companies: [Haste makes waste, it's upside time!](#))** which implies no further changes in our FV and estimates today.

**We have chosen to put Veolia (Buy, FV @ EUR23) on our BG Top Pick list for Q3 2016 as 1) the stock's derating over the past quarter (-8.0% in Q2-16 vs. 2.8% for the Stoxx 600 Utilities) now implies a 6.5x 2017e EV/EBITDA multiple - a 4% discount vs. its 6-year historical average – and a 5% discount vs. Suez on comparable basis. 2) Following Brexit, we believe Veolia's exposure to the UK is rather limited today (c. 9% of revenues of Group's revenues i.e. EUR2.3bn out of which 80% coming from the waste business) as GBP headwinds could be partly offset by USD tailwinds for an overall fairly limited FX impact. In addition, Veolia appears well-protected in case of a potential macro downturn in the UK as around one third of its UK waste revenues are generated by PFI contracts (around 50% EBITDA margin) whereas about 70-75% of volumes are guaranteed. 3) Despite, a potential weak sales performance in H1 2016 (due to FX headwinds, unsupportive weather as well as the downsizing of Veolia Water Technologies), we think Veolia will post a strong and resilient EBITDA performance in line with its 5% organic growth objective, notably thanks to its ability to deliver cost-savings measures (EUR600m over 2016/2017/2018 i.e. EUR200m per year). 4) Finally, we believe the Transdev's disposal – Transdev is 50% owned by Veolia – could be a positive catalyst in the upcoming quarter. More than the financial part of the disposal (EUR0.1 positive impact on our FV according to our estimates, assuming a mere 10% capital gain), we believe the disposal should be well received by investors as 1) this is a long-lasting story; and 2) proceeds could be used to fund future organic growth and contribute to ensuring the company's dividends target.**

[Click here to download](#)



**Analyst :**  
Xavier Caroen  
33(0) 1.56.68.75.18  
xcaroen@bryangarnier.com

**Sector Team :**  
Pierre-Antoine Chazal

# Bryan Garnier stock rating system

For the purposes of this Report, the Bryan Garnier stock rating system is defined as follows:

## Stock rating

BUY	Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
NEUTRAL	Opinion recommending not to trade in a stock short-term, neither as a BUYER or a SELLER, due to a specific set of factors. This view is intended to be temporary. It may reflect different situations, but in particular those where a fair value shows no significant potential or where an upcoming binary event constitutes a high-risk that is difficult to quantify. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

## Distribution of stock ratings

BUY ratings 56.8%

NEUTRAL ratings 33.8%

SELL ratings 9.5%

# Research Disclosure Legend

1	Bryan Garnier shareholding in Issuer	Bryan Garnier & Co Limited or another company in its group (together, the "Bryan Garnier Group") has a shareholding that, individually or combined, exceeds 5% of the paid up and issued share capital of a company that is the subject of this Report (the "Issuer").	No
2	Issuer shareholding in Bryan Garnier	The Issuer has a shareholding that exceeds 5% of the paid up and issued share capital of one or more members of the Bryan Garnier Group.	No
3	Financial interest	A member of the Bryan Garnier Group holds one or more financial interests in relation to the Issuer which are significant in relation to this report	No
4	Market maker or liquidity provider	A member of the Bryan Garnier Group is a market maker or liquidity provider in the securities of the Issuer or in any related derivatives.	No
5	Lead/co-lead manager	In the past twelve months, a member of the Bryan Garnier Group has been lead manager or co-lead manager of one or more publicly disclosed offers of securities of the Issuer or in any related derivatives.	No
6	Investment banking agreement	A member of the Bryan Garnier Group is or has in the past twelve months been party to an agreement with the Issuer relating to the provision of investment banking services, or has in that period received payment or been promised payment in respect of such services.	No
7	Research agreement	A member of the Bryan Garnier Group is party to an agreement with the Issuer relating to the production of this Report.	No
8	Analyst receipt or purchase of shares in Issuer	The investment analyst or another person involved in the preparation of this Report has received or purchased shares of the Issuer prior to a public offering of those shares.	No
9	Remuneration of analyst	The remuneration of the investment analyst or other persons involved in the preparation of this Report is tied to investment banking transactions performed by the Bryan Garnier Group.	No
10	Corporate finance client	In the past twelve months a member of the Bryan Garnier Group has been remunerated for providing corporate finance services to the issuer or may expect to receive or intend to seek remuneration for corporate finance services from the Issuer in the next six months.	No
11	Analyst has short position	The investment analyst or another person involved in the preparation of this Report has a short position in the securities or derivatives of the Issuer.	No
12	Analyst has long position	The investment analyst or another person involved in the preparation of this Report has a long position in the securities or derivatives of the Issuer.	No
13	Bryan Garnier executive is an officer	A partner, director, officer, employee or agent of the Bryan Garnier Group, or a member of such person's household, is a partner, director, officer or an employee of, or adviser to, the Issuer or one of its parents or subsidiaries. The name of such person or persons is disclosed above.	No
14	Analyst disclosure	The analyst hereby certifies that neither the views expressed in the research, nor the timing of the publication of the research has been influenced by any knowledge of clients positions and that the views expressed in the report accurately reflect his/her personal views about the investment and issuer to which the report relates and that no part of his/her remuneration was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in the report.	Yes
15	Other disclosures	Other specific disclosures: Report sent to Issuer to verify factual accuracy (with the recommendation/rating, price target/spread and summary of conclusions removed).	No

A copy of the Bryan Garnier & Co Limited conflicts policy in relation to the production of research is available at [www.bryangarnier.com](http://www.bryangarnier.com)

<b>London</b>	<b>Paris</b>	<b>New York</b>	<b>Munich</b>	<b>New Delhi</b>
Beaufort House	26 Avenue des Champs Elysées	750 Lexington Avenue	Widenmayerstrasse 29	The Imperial Hotel Janpath
15 St. Botolph Street	75008 Paris	New York, NY 10022	80538 Munich	New Delhi 110 001
London EC3A 7BB	Tel: +33 (0) 1 56 68 75 00	Tel: +1 (0) 212 337 7000	Germany	Tel +91 11 4132 6062
Tel: +44 (0) 207 332 2500	Fax: +33 (0) 1 56 68 75 01	Fax: +1 (0) 212 337 7002	+49 89 2422 62 11	+91 98 1111 5119
Fax: +44 (0) 207 332 2559	Regulated by the	FINRA and SIPC member		Fax +91 11 2621 9062
Authorised and regulated by the	Financial Conduct Authority (FCA) and the			<b>Geneva</b>
Financial Conduct Authority (FCA)	Autorité de Contrôle prudentiel et de			rue de Grenus 7
	resolution (ACPR)			CP 2113
				Genève 1, CH 1211
				Tel +4122 731 3263
				Fax+4122731 3243
				Regulated by the FINMA

#### **Important information**

This document is classified under the FCA Handbook as being investment research (independent research). Bryan Garnier & Co Limited has in place the measures and arrangements required for investment research as set out in the FCA's Conduct of Business Sourcebook.

This report is prepared by Bryan Garnier & Co Limited, registered in England Number 03034095 and its MIFID branch registered in France Number 452 605 512. Bryan Garnier & Co Limited is authorised and regulated by the Financial Conduct Authority (Firm Reference Number 178733) and is a member of the London Stock Exchange. Registered address: Beaufort House 15 St. Botolph Street, London EC3A 7BB, United Kingdom

This Report is provided for information purposes only and does not constitute an offer, or a solicitation of an offer, to buy or sell relevant securities, including securities mentioned in this Report and options, warrants or rights to or interests in any such securities. This Report is for general circulation to clients of the Firm and as such is not, and should not be construed as, investment advice or a personal recommendation. No account is taken of the investment objectives, financial situation or particular needs of any person.

The information and opinions contained in this Report have been compiled from and are based upon generally available information which the Firm believes to be reliable but the accuracy of which cannot be guaranteed. All components and estimates given are statements of the Firm, or an associated company's, opinion only and no express representation or warranty is given or should be implied from such statements. All opinions expressed in this Report are subject to change without notice. To the fullest extent permitted by law neither the Firm nor any associated company accept any liability whatsoever for any direct or consequential loss arising from the use of this Report. Information may be available to the Firm and/or associated companies which are not reflected in this Report. The Firm or an associated company may have a consulting relationship with a company which is the subject of this Report.

This Report may not be reproduced, distributed or published by you for any purpose except with the Firm's prior written permission. The Firm reserves all rights in relation to this Report.

Past performance information contained in this Report is not an indication of future performance. The information in this report has not been audited or verified by an independent party and should not be seen as an indication of returns which might be received by investors. Similarly, where projections, forecasts, targeted or illustrative returns or related statements or expressions of opinion are given ("Forward Looking Information") they should not be regarded as a guarantee, prediction or definitive statement of fact or probability. Actual events and circumstances are difficult or impossible to predict and will differ from assumptions. A number of factors, in addition to the risk factors stated in this Report, could cause actual results to differ materially from those in any Forward Looking Information.

Disclosures specific to clients in the United Kingdom

This Report has not been approved by Bryan Garnier & Co Limited for the purposes of section 21 of the Financial Services and Markets Act 2000 because it is being distributed in the United Kingdom only to persons who have been classified by Bryan Garnier & Co Limited as professional clients or eligible counterparties. Any recipient who is not such a person should return the Report to Bryan Garnier & Co Limited immediately and should not rely on it for any purposes whatsoever.

Notice to US investors

This research report (the "Report") was prepared by Bryan Garnier & Co Limited for information purposes only. The Report is intended for distribution in the United States to "Major US Institutional Investors" as defined in SEC Rule 15a-6 and may not be furnished to any other person in the United States. Each Major US Institutional Investor which receives a copy of this Report by its acceptance hereof represents and agrees that it shall not distribute or provide this Report to any other person. Any US person that desires to effect transactions in any security discussed in this Report should call or write to our US affiliated broker, Bryan Garnier Securities, LLC, 750 Lexington Avenue, New York NY 10022. Telephone: 1-212-337-7000.

This Report is based on information obtained from sources that Bryan Garnier & Co Limited believes to be reliable and, to the best of its knowledge, contains no misleading, untrue or false statements but which it has not independently verified. Neither Bryan Garnier & Co Limited and/or Bryan Garnier Securities LLC make no guarantee, representation or warranty as to its accuracy or completeness. Expressions of opinion herein are subject to change without notice. This Report is not an offer to buy or sell any security.

Bryan Garnier Securities, LLC and/or its affiliate, Bryan Garnier & Co Limited may own more than 1% of the securities of the company(ies) which is (are) the subject matter of this Report, may act as a market maker in the securities of the company(ies) discussed herein, may manage or co-manage a public offering of securities for the subject company(ies), may sell such securities to or buy them from customers on a principal basis and may also perform or seek to perform investment banking services for the company(ies).

Bryan Garnier Securities, LLC and/or Bryan Garnier & Co Limited are unaware of any actual, material conflict of interest of the research analyst who prepared this Report and are also not aware that the research analyst knew or had reason to know of any actual, material conflict of interest at the time this Report is distributed or made available..