

Veolia Environnement

Price EUR19.89

Strong commercial developments and accretive acquisitions to boost H2-16 earnings
Fair Value EUR23.5 vs. EUR23 (+18%)
BUY-Top Picks

Bloomberg	VIE.FP
Reuters	VIE.PA
12-month High / Low (EUR)	22.9 / 18.1
Market Cap (EURm)	11,205
Ev (BG Estimates) (EURm)	18,626
Avg. 6m daily volume (000)	1,926
3y EPS CAGR	27.0%

Following yesterday's H1 2016 results, we have updated our model on Veolia and adjusted some of our figures. While the macro environment remains challenging, notably in France, we were pretty impressed by the company's solid commercial development over the past six months. This should spur robust growth in H2 on top of the extensive cost-reduction measures already implemented. This leads us to maintain our Buy recommendation and slightly increase our FV to EUR23.5 (vs. EUR23) implying upside of c. 18% vs. last closing price.

	1 M	3 M	6 M	31/12/15
Absolute perf.	2.6%	-7.3%	-12.3%	-9.0%
Utilities	0.5%	0.3%	-0.9%	-2.1%
DJ Stoxx 600	2.3%	-0.5%	-0.5%	-7.1%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	24,965	25,080	26,116	26,801
% change		0.5%	4.1%	2.6%
EBITDA	2,997	3,147	3,386	3,554
EBIT	1,060	1,404	1,584	1,713
% change		32.5%	12.8%	8.1%
Net income	378.7	528.1	696.1	784.9
% change		39.4%	31.8%	12.8%

	2015	2016e	2017e	2018e
Operating margin	4.5	5.6	6.1	6.4
Net margin	1.8	2.4	2.9	3.2
ROE	4.0	6.3	7.1	7.8
ROCE	6.4	6.4	7.0	7.4
Gearing	82.6	79.8	77.8	74.0

(EUR)	2015	2016e	2017e	2018e
EPS	0.68	0.93	1.23	1.39
% change	-	37.9%	31.8%	12.8%
P/E	29.4x	21.3x	16.2x	14.3x
FCF yield (%)	9.5%	1.8%	7.8%	8.9%
Dividends (EUR)	0.73	0.85	0.84	0.97
Div yield (%)	3.7%	4.3%	4.2%	4.9%
EV/Sales	0.7x	0.7x	0.7x	0.7x
EV/EBITDA	6.0x	5.9x	5.4x	5.2x
EV/EBIT	17.1x	13.3x	11.6x	10.7x

ANALYSIS

- As expected, Veolia posted rather **weak H1 revenues** yesterday at **EUR11.956bn**, down **1.0%** at constant exchange rates despite the improvement in Q2 (+0.1% vs. -2.1% in Q1-16). We nevertheless believe that Veolia will **benefit from new revenue sources in H2 and beyond**, which should more than offset headwinds in France. We estimate the five key international developments highlighted by the group (Prague district heating network, Pedreira landfill in Brazil, giant contract with Chinese Sinopec and acquisitions of Kurion and Chemours' sulfuric acid division) should generate **additional revenues of EUR536m on a full-year basis** i.e. c. **2.0% of the company's 2017e revenues**. Management indicated these contracts and acquisitions will generate EBITDA margin at least equal to the group's average margin, which would imply an **additional contribution of at least EUR65m per year**. We consider this fairly **conservative** as we expect Kurion and Chemours' asset acquisitions to generate respectively **EUR20m and EUR40m of additional EBITDA per year**. As we already integrated Kurion and Chemours' asset acquisitions into our previous estimates, we have "only" **increased our revenues' estimates by 0.6% and 1.1% for 2016e and 2017e respectively**. We also believe higher than expected growth in the rest of Europe and global businesses divisions would be partly offset by lower than expected growth in France, which still bears the brunt of low inflation and an unsupportive climate.
- We have also included the **upcoming disposal of Veolia's 20% stake in Transdev for EUR220m**. This has a **positive impact of EURO.2 per share** on our estimates and assuming the disposal is completed by the end of the year as **1/** the company's net debt is reduced by **EUR220m** and **2/** the remaining 30% stake in Transdev is now valued at **EUR330m** vs. the initial EUR280m at book value implying a c. **18% premium**. Note that **an option to sell the remaining 30% stake is exercisable in two years under the same valuation**. Additionally, Veolia announced it has ended the divestment process of its construction subsidiary SADE as no satisfying bids have been received. **We believe further cost-cutting could be implemented within the subsidiary**, which would imply a similar gradual downsizing as for Veolia Water Technologies.
- The group generated EUR121m in cost-savings in H1, which seems rather impressive in our view** – despite the fairly high inherent EUR100m restructuring charges – as we expected this figure to reach EUR100m. **We remain however cautious** for now and **keep our EUR200m assumption** for cost-savings achieved, per year, between 2016 and 2018, in line with Veolia's objective.
- In all, **we have increased our EBITDA estimates by 0.4%, 1.5% and 1.1% for 2016e, 2017e and 2018e** respectively. We now stand at EUR3,147m for 2016 implying a 12.5% EBITDA margin (50bps up yoy). **As for 2016 adjusted net income** (company definition), we now expect Veolia to reach **EUR635m** (up 2.4% vs. our previous estimates) - on the back of higher than expected capital gains – and therefore **to beat its EUR600m guidance** (which includes a capital gain of just EUR10m).
- This leads us to maintain our **Buy recommendation** and to slightly **increase our Fair Value by 2.2% to EUR23.5** (vs. EUR23) implying upside of c. 18% vs. yesterday's closing price.

VALUATION

- At the current share price, **Veolia is trading at 5.9x its 2016e EV/EBITDA multiple**.
- Buy, FV @ EUR23.5**



NEXT CATALYSTS

3rd November 2016: Q3 2016 results

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Table 1: Main changes in estimates (2016e-2018e)

	2016e			2017e			2018e		
	New	Old	Estimates change (%)	New	Old	Estimates change (%)	New	Old	Estimates change (%)
Revenues	25,080	24,927	0.6%	26,116	25,821	1.1%	26,801	26,471	1.2%
EBITDA	3,147	3,135	0.4%	3,386	3,336	1.5%	3,554	3,516	1.1%
EBITDA margin	12.5%	12.6%	-	13.0%	12.9%	-	13.3%	13.3%	-
Net income adjusted Veolia def.	635	620	2.4%	733	730	0.4%	835	820	1.9%
EPS adjusted - Veolia def.	1.12	1.10	1.9%	1.29	1.30	-0.5%	1.48	1.46	1.0%

Source : Company Data; Bryan Garnier & Co. ests.

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