

Veolia Environnement

Price EUR19.86

Preview Q3-16: tepid performance expected amid difficulties in the US and in French water

Fair Value EUR23.5 (+18%)

BUY

Bloomberg	VIE.FP
Reuters	VIE.PA
12-month High / Low (EUR)	22.9 / 18.1
Market Cap (EUR)	11,186
Ev (BG Estimates) (EUR)	18,606
Avg. 6m daily volume (000)	1 776
3y EPS CAGR	27.0%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-1.8%	1.2%	-5.9%	-9.2%
Utilities	-0.8%	-7.0%	-4.7%	-7.4%
DJ Stoxx 600	0.5%	0.1%	-1.6%	-6.6%

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	5.1x
EV/EBIT	17.1x	13.2x	11.6x	10.7x



Veolia is set to report its Q3-16 results on November 3rd. We expect the company to still bear the brunt of an unsupportive environment in both its US industrial activities and in its French water business. However, we forecast a 3.3% increase in Q3-16 EBITDA yoy as we expect cost-savings, positive scope impact (acquisition of Chemours' sulfuric assets, back in June 2016) and recent contracts awarded to more than offset the double-digit EUR/GBP expected headwind. We expect Q3-16 current EBIT and current net income to be flat and down, respectively, on a reported basis (*exc. capital gains*), but up 6.5% and 8% once adjusted from the EUR15m provision reversal in Q3-15. Despite this tepid quarterly performance, we believe Veolia will confirm its FY-16 guidance which notably includes EBITDA growth and EUR600m of current net income, both at constant exchange rates. Buy rating maintained and FV unchanged at EUR23.5.

ANALYSIS

- What to expect from Veolia's Q3-16 publication?** We expect Veolia to post a **Q3-16 EBITDA at EUR638m** up 3.3% yoy which would bring company's 9-month EBITDA to **EUR2,218m** up 3.2% yoy. We forecast a **4.5%** organic growth at the Q3-16 EBITDA level, down 90bps vs. H1-16 performance as we believe the company notably suffered from **1/a still-weak performance in industrial waste in the US; and 2/an unsupportive environment in its French water business** with both climate and regulatory headwinds (Brottes law for which we estimate an EUR6m headwind over the quarter). The EUR3.3bn contract with Sinopec as well as the recent acquisition of **Chemours' sulfuric assets** should contribute about **EUR10m** at the EBITDA level. This should, however, be more than offset by an EUR15m FX headwind (GBP mainly) over the quarter. The main driver of the growth in EBITDA should remain the **company's cost-cutting programme** for which we expect a **EUR50m** positive impact over the quarter. **We therefore expect Veolia to confirm its advance on its annual savings' target** (EUR600m over a 3-year period hence EUR200m per year) as the company would have completed about **EUR170m of savings** after the first 9 months of the year.
- We expect company's Q3-16 current EBIT to reach **EUR229m** (**EUR978m** for 9-month current EBIT) flat yoy on a reported basis, but up 6.5% once **excluding the EUR15m provision reversal in Q3-15**. Finally, we expect Q3-16 current net income to reach **EUR68m** (**EUR409m** for 9-month) down c. 13% yoy on a reported basis (*exc. capital gains*). Adjusted from the provision reversal, we expect net income to be **up 8% yoy** notably on the back of a lower cost of debt. As a reminder, **the contribution from Transdev is not included in the company's current net income so as the expected capital gain** related to the 20% disposal announced during H1-16 results.
- Despite this tepid performance, **we believe Veolia will confirm its FY-16 guidance** which includes **1/generation of growth** at both revenues and EBITDA levels (at constant FX); **2/EUR650m of FCF** (before divestments & acquisitions) and **3/current net income** of at least EUR600m (at constant FX and including no more than EUR10m of capital gains). **We notably expect Q4-16 performance to be positively impacted** by **1/a** full-quarter contribution from the contract with Sinopec (c. EUR3m at the EBITDA level); **2/the** first contribution coming from the Prague district heating network (EUR5-7m expected quarterly contribution to Veolia's EBITDA); **3/the** deconsolidation of Bartin Recycling and the inherent reducing exposure to scrap metals (+/- 10% in scrap metals price implied a +/-EUR4m impact on EBITDA); **and 4/the** cost-cutting programme which should bring its usual **EUR50m** positive contribution.

VALUATION

- At current share price, Veolia is trading at **5.9x** its 2016e EV/EBITDA multiple and **5.4x** its 2017e EV/EBITDA multiple
- Buy, FV @ EUR23.5**

NEXT CATALYSTS

- 3rd November 2016:** Q3-16 results

Table 1: Q3-16 EBITDA Bridge (BG estimates)

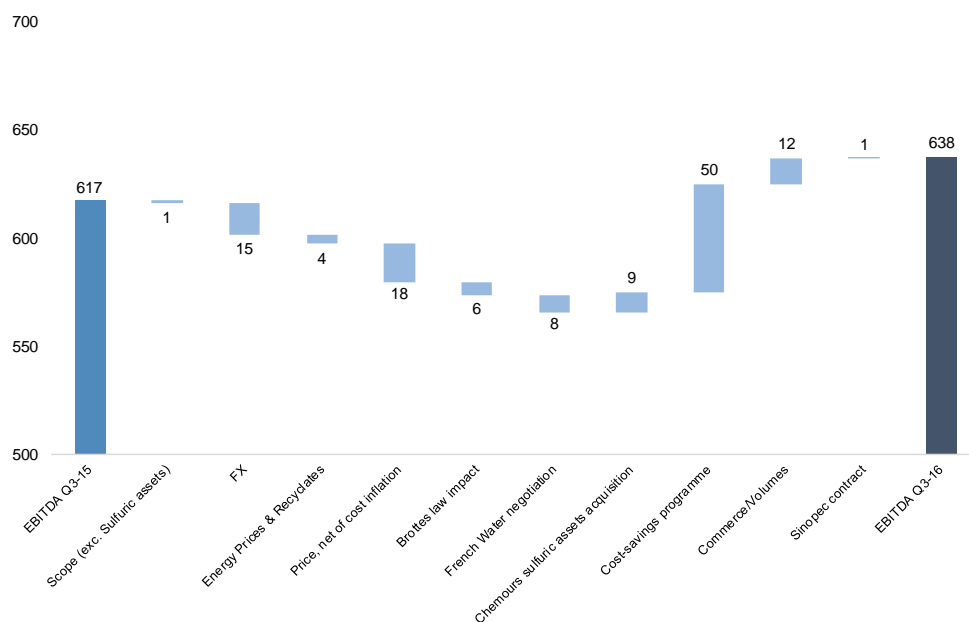


Table 2: Q3-16 and 9-month EBIT (BG estimates)

Veolia - Key metrics	Q3 2016e	9-month 2016e
EBITDA	638	2,218
<i>Renewal expenses</i>	(65)	(201)
<i>D&A</i>	(332)	(1,013)
<i>Reimbursement OFAs</i>	(37)	(141)
<i>Provisions, fair value adjustment & other</i>	0	47
<i>Share of current NI of JV & associates</i>	25	68
Current EBIT	229	978
<i>Cost of financial debt</i>	(97)	(306)
<i>Other financial income & expense</i>	(12)	(40)
<i>Capital gains on financial divestments</i>	0	41
<i>Income tax expenses</i>	(32)	(169)
<i>Non-controlling interests</i>	(20)	(95)
Current net income Group Share	68	409

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