

CREDIT OPINION

1 June 2017

Update

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RATINGS

Veolia Environnement S.A.

Domicile	Paris, France
Long Term Rating	Baa1
Type	LT Issuer Rating
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Analyst Contacts

Paul Marty 44-20-7772-1036
VP-Sr Credit Officer
paul.marty@moodys.com

Niel Bisset 44-20-7772-5344
Senior Vice President
niel.bisset@moodys.com

Stefanie Voelz 44-20-7772-5555
Senior Credit Officer
stefanie.voelz@moodys.com

Neil Griffiths-Lambeth 44-20-7772-5543
Associate Managing Director
neil.griffiths-lambeth@moodys.com

Veolia Environnement S.A.

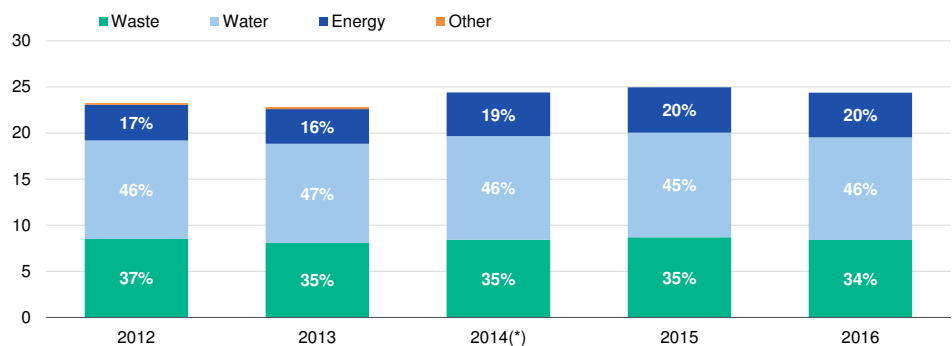
Update to Discussion of Key Credit Factors

Summary Rating Rationale

The Baa1/P-2 ratings of Veolia Environnement S.A. (Veolia) reflect (1) its size and position as one of the two largest groups active globally in environmental services, which benefit from positive structural dynamics; (2) the diversity of its revenue base by business, contract type and geography; and (3) the relatively low-risk profile of its water business, which is characterized by low volume volatility. These factors are balanced by (1) Veolia's exposure to the macroeconomic cycle through its waste business; and (2) the increasing proportion of shorter-term contracts with industrial clients in its revenue mix.

From the financial risk perspective, the Baa1 rating and stable outlook are based on our expectation that the company will continue to demonstrate credit metrics aligned with our guidance, which includes funds from operations (FFO)/net debt around 20% (this was 21.9% as of year-end 2016), retained cash flow (RCF)/net debt in the mid teens in percentage terms and FFO interest cover above 4.0x.

Exhibit 1
Veolia's scale and diversification by business supports earnings stability
(revenue split in € billion)



(*) Pro forma scope: excluding Dalkia France and with Dalkia International fully consolidated from January 1, 2014
Source: Veolia

Credit Strengths

- » Scale and diversification support cash flow stability
- » Supportive long-term industry dynamics
- » Low-risk water activities, albeit currently impacted in Europe (and notably in France) by weak indexation stemming from the low inflation environment
- » Improved financial profile primarily driven by cost saving programme

Credit Challenges

- » Exposure of waste business to cyclical – and currently sluggish – macroeconomic environment in Europe
- » Increasing share of the industrial sector in the company's client mix
- » Growing presence outside Western Europe, albeit mitigated by a balanced approach to capital deployment

Rating Outlook

The stable outlook reflects our expectation that Veolia's financial profile will remain aligned with our guidance for the Baa1 rating, which includes FFO/net debt around 20%, RCF/net debt at least in the mid-teens in percent terms and FFO interest cover above 4x. It also factors in that any potential deterioration in the company's business risk profile as a result of an increased exposure to industrial clients could be offset by a further improvement in credit metrics.

Factors that Could Lead to an Upgrade

Upward pressure on the ratings could develop over the medium term depending if Veolia were to achieve RCF/net debt approaching 20% on a sustainable basis. In this scenario, we would take into account management's future financial policy and use of the financial flexibility that could be developed in the medium term.

Factors that Could Lead to a Downgrade

Negative pressure on ratings could arise if metrics were to fall short of our guidance due to weaker-than-expected operating performance or increased investments.

Key Indicators

Exhibit 2

Veolia's key adjusted indicators

Veolia Environnement S.A. [1][2]

	12/31/2016	12/31/2015	12/31/2014	12/31/2013	12/31/2012
(FFO + Interest Expense) / Interest Expense	6.0x	5.5x	4.6x	4.2x	3.9x
FFO / Net Debt	21.9%	20.6%	20.2%	19.5%	17.3%
RCF / Net Debt	17.7%	16.4%	17.7%	18.0%	14.3%
FCF / Net Debt	0.7%	0.3%	-1.3%	-2.1%	-6.4%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's

[2] The 2015 and 2016 key indicators are adjusted for IFRIC 12.

For definitions of Moody's most common ratio terms please see the accompanying [User's Guide](#).

Source: Moody's Investors Service

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

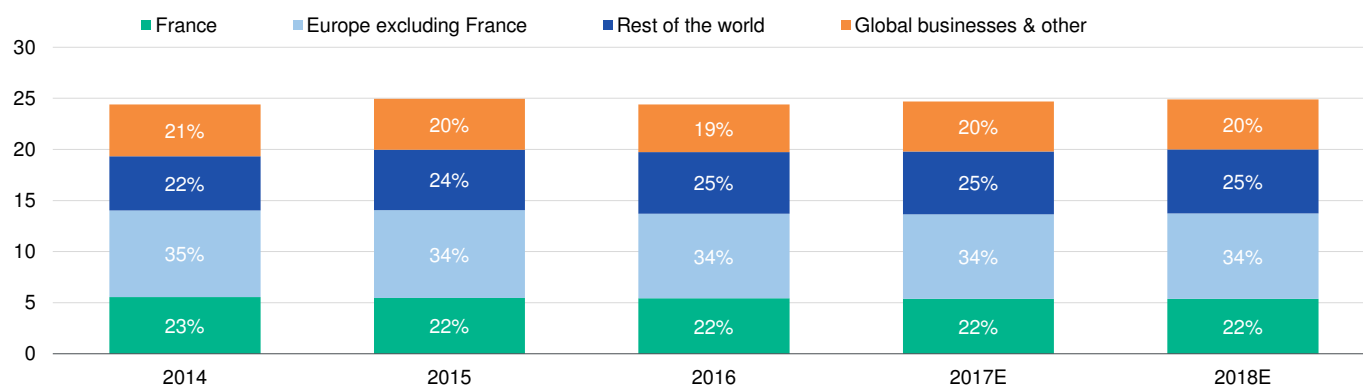
Detailed Rating Considerations

Scale and diversification support cash flow stability

Veolia is one of the world's largest provider of environmental services, with revenues of €24.4 billion in 2016. The Baa1 rating reflects its scale and diversity which have contributed to leading market positions in many different geographies across its three businesses of water, environmental and energy services. The diversity of its revenue base by business, contract type and geography (see exhibit below) helps mitigate the negative effect on earnings from deterioration in any one activity or region and supports the relative stability of its cash flows.

Exhibit 3

Veolia's diversification by geography underpins earnings stability (revenue split in € billion)



The 2017 and 2018 estimates represent Moody's forward view; not the view of the issuer.

Source: Veolia, Moody's Investors Service

Increasing share of industrial clients in revenue mix

Veolia's revenues are derived from a portfolio of thousands of multi-year contracts, which range from long-term concessions with low-risk counterparties in the public sector to shorter-term contracts with industrial and commercial (I&C) customers. Contracts vary by market and can either be capital intensive, requiring the group to invest in infrastructure in exchange for the right to provide services on a long-term basis, or structured as operating and maintenance or management contracts requiring little investment.

Public authorities currently account for 55% of Veolia's turnover and I&C customers for the remaining 45%, a proportion which we expect will continue to grow as the company's commercial pipeline includes a greater share of projects in the I&C sector. Veolia has identified six growth areas where it sees increasing demand from industrial clients to meet growing efficiency, environmental or regulatory requirements. This shift in client mix may over time raise Veolia's business risk profile as it entails greater reliance on shorter term, asset light contracts.

Supportive long-term industry dynamics, albeit in an increasingly competitive environment

Veolia operates within sectors that benefit from positive long-term underlying dynamics globally, although they are not immune from short-term economic pressures. These include population growth, the trend to urbanisation and industrialisation, and an expectation of rising living standards in emerging economies. Together with public concern over the impact of climate change on scarce resources and increasingly stricter environmental regulation, these positive underlying factors are combining (1) to increase demand for existing technologies for the provision of water, wastewater and waste management services; and (2) to extend demand into new services and technologies that, for example, facilitate water preservation, or the ongoing shift towards waste recovery. Against this backdrop, competition - notably from Asian players - is fierce, especially in the lower part of the value chain.

Low-risk water activities but exposure of waste business to cyclical macro-economic conditions

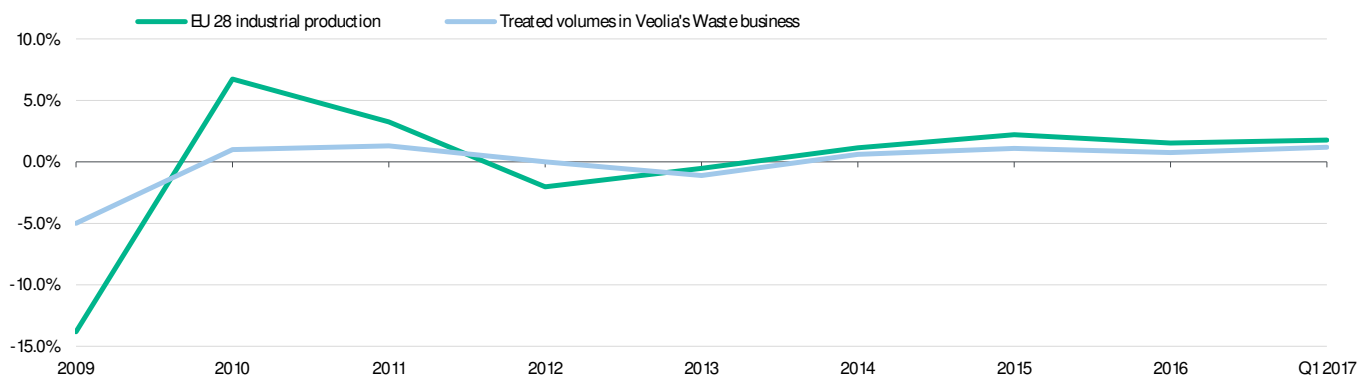
The Baa1 rating reflects the low risk profile of Veolia's water business, which provides essential water and wastewater services to individuals and businesses, often on behalf of local municipalities under long-term concession agreements. Although demand for water continues to experience a slow ongoing structural decline in advanced economies, especially in Europe because of a more

“resource-aware” population, variations in water consumption are mainly driven by weather. Typical renewal rates of around 90% in the municipal sector provide revenue visibility and stability.

The waste business is more exposed to cyclical macroeconomic conditions, reflecting (1) the higher proportion of I&C customers, (2) contract terms often linked to volumes collected or processed, which are in turn linked to industrial production (see exhibit below), and (3) the modest and residual exposure to paper and scrap metal prices of the recycling business. With barriers to entry low in the collecting and elimination of non-hazardous waste, Veolia continues to invest in higher value-added activities, which can include sorting, hazardous materials and recovery, which will in turn raise the group's exposure to materials and energy price fluctuations.

Exhibit 4

Veolia's waste business is exposed to the macroeconomic cycle (growth rate in %)



In 2010, waste volumes are from industrial clients only.

Source: Veolia, Moody's Analytics

In the energy business, around two thirds of its revenues come from the management of district heating and cooling networks. This activity typically demonstrates quasi-monopoly characteristics as it is underpinned by long-term contracts that include indexation and pass-through clauses covering variations in energy prices, although these can be subject to some regulatory risk. These features ensure relatively predictable cash flows, although this activity remains exposed to weather conditions, which drive seasonal demand for heating and cooling. In addition to networks, the company acts as a subcontractor for public and private customers to manage or maintain various energy installations, including decentralised electricity generation, such as biomass and CHP, which in turn can expose it to energy prices.

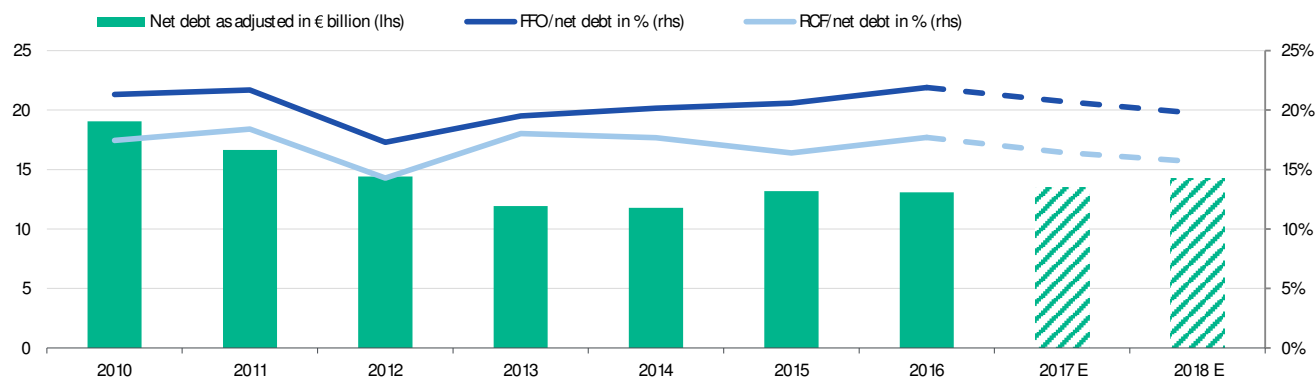
Growing presence outside Europe mitigated by a balanced approach to capital deployment

Veolia's strategy to shift progressively from mature economies to growth markets outside Europe implies incremental risks; thus, we expect that the group will remain cautious in its approach to capital deployment so as to limit the scale of the investment it takes on in any individual country.

Moderate financial leverage

The current ratings and stable outlook reflect our expectation that Veolia will maintain credit metrics well aligned with current levels, including FFO/net debt around 20%, RCF/net debt at least in the mid-teens in percentage terms and FFO interest cover above 4x. Our expectation is mostly predicated upon the continued successful execution of the company's cost-saving programme, which should more than offset the pressures stemming from weak price indexation and a subdued outlook for industrial production in Europe. The execution of this programme was the main driver behind the 4.3% EBITDA growth (at constant FX) reported in 2016. For 2017-18, Veolia targets another €550 million of cumulative gross cost savings vs. €245 million achieved in 2016.

Exhibit 5

Financial profile expected to remain resilient

The 2017 and 2018 estimates represent Moody's forward view; not the view of the issuer, and assume that the hybrids are refinanced with senior debt in 2018.

Source: Veolia, Moody's Investors Service

Liquidity Analysis

Veolia's liquidity profile is sound. We expect that the group will be broadly free cash flow neutral after dividend payment over the next 12 months. The group's funding needs as of December 2016 thus mostly comprise €5.0 billion of short term debt maturities and bank overdrafts. These funding needs are covered by (1) €5.3 billion of cash and cash equivalents (excluding restricted cash) on balance sheet and (2) undrawn credit lines of €3.9 billion in aggregate as of December 2016.

These credit lines mainly consist of (1) a syndicated facility of €3 billion maturing in 2021; and (2) undrawn bilateral facilities of €925 million maturing between 2018 and 2020. These facilities contain no triggers, covenants, material adverse changes or general restrictions. We also note positively that the group's average debt maturity was 9.3 years (excluding hybrids) as of December 2016.

Corporate Profile

Headquartered in Aubervilliers, France, Veolia Environnement S.A. (Baa1/P-2 stable), is one of two leading groups active globally in environmental services. It provides drinking water to 100 million people, wastewater treatment to 61 million people and waste management services to 40 million people. Veolia is listed on the Paris stock exchange with a market capitalisation of close to €10 billion.

Rating Methodology and Scorecard Factors

There is no single rating methodology for Veolia given the group's mix of businesses. We assess the water business in accordance with the rating methodology for [Regulated Water Utilities](#) published in December 2015, while we assess the waste activities in accordance with the rating methodology for [Environmental Services and Waste Management Companies](#) published in June 2014.

Ratings

Exhibit 6

Category	Moody's Rating
VEOLIA ENVIRONNEMENT S.A.	
Outlook	Stable
Issuer Rating	Baa1
Senior Unsecured	Baa1
Jr Subordinate	Baa3
Commercial Paper -Dom Curr	P-2

Source: Moody's Investors Service

Moody's Related Research

Rating Actions:

- » [Moody's assigns Baa1 rating to Veolia's convertible bonds, 10 March 2016 \(PR_345272\)](#)

Issuer Comment:

- » [Veolia Announces Credit-Positive Sale of Transdev Stake, 4 August 2016](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

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Analyst Contacts

Paul Marty <i>VP-Sr Credit Officer</i> paul.marty@moodys.com	44-20-7772-1036	Niel Bisset <i>Senior Vice President</i> niel.bisset@moodys.com	44-20-7772-5344
Stefanie Voelz <i>Senior Credit Officer</i> stefanie.voelz@moodys.com	44-20-7772-5555	Neil Griffiths-Lambeth <i>Associate Managing Director</i> neil.griffiths-lambeth@moodys.com	44-20-7772-5543

CLIENT SERVICES

Americas	1-212-553-1653
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