BRYAN, GARNIER & CO

INDEPENDENT RESEARCH

28th March 2017

Suez

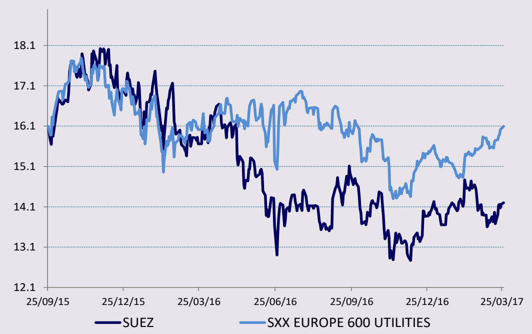
Checks and balances

Utilities

Fair Value EUR16.5 vs. EUR17.6 (price EUR14.16) **BUY**

Bloomberg	SEV FP
Reuters	SEVI.PA
12-month High / Low (EUR)	16.6 / 12.8
Market capitalisation (EURm)	8,009
Enterprise Value (BG estimates EURm)	21,229
Avg. 6m daily volume ('000 shares)	1 426
Free Float	56.8%
3y EPS CAGR	7.9%
Gearing (12/16)	112%
Dividend yields (12/17e)	4.59%

YE December	12/16	12/17e	12/18e	12/19e
Revenue (EURm)	15,322	16,547	18,125	18,584
EBIT(EURm)	1,282	1,391	1,602	1,702
Basic EPS (EUR)	0.77	0.78	0.90	0.98
Diluted EPS (EUR)	0.72	0.74	0.82	0.90
EV/Sales	1.26x	1.28x	1.19x	1.16x
EV/EBITDA	7.3x	7.4x	6.9x	6.6x
EV/EBIT	15.1x	15.3x	13.4x	12.7x
P/E	19.7x	19.2x	17.2x	15.7x
ROCE	6.9	7.8	8.9	9.4



We believe GE Water's acquisition is a smart move for Suez, which continues to build up a well-balanced business while strengthening its footprint in the industrial water market that is expected to grow faster than the still hesitant municipal market. Buy recommendation maintained, FV adjusted to EUR16.5.

- **On 8th March, Suez announced the acquisition, together with CDPQ, of GE Water for enterprise value of EUR3.2bn**. While confirming Suez's initial ambitions to grow both organically and via acquisitions, the move enables the company to significantly strengthen its presence in the **industrial water market** (85% of the EUR1.9bn in revenues posted by GE Water is generated in the industrial segment).
- The transaction should clearly **improve Suez's growth profile** (5% CAGR expected by the group in the mid-term in this EUR95bn market) and, in our view, is likely to offset the **challenging and hesitant European municipal water environment showing low inflation and a poor trend in volumes** (which partly led us to revise downwards our EBITDA and EBIT estimates, excluding GE Water's contribution, by **5%** and **6%** on average per year over 2017e-2020e).
- **We believe this acquisition is a smart move for Suez:** it confirms the company's strategy to build up **a well-balanced business with increased presence in the industrial segment** (from 34% to 40% of revenues) **and abroad** (40% of revenues now generated outside Europe vs. 32% before). **Synergy** targets look challenging but the apparently **strong complementary fit** of both companies and Suez's solid track record in terms of cost savings make us **optimistic in the company's ability to manage these potential integration risks.**
- **We expect the acquisition to generate double-digit accretion in EPS by 2020** (completion of expected cost synergies) while the **impact on debt ratios should be rather limited** given the acquisition funding scheme unveiled (incl. EUR600m in hybrid bonds and a EUR750m capital increase).
- **Buy recommendation maintained**: In all, we believe the potential increase in cyclicity comes with a stronger growth profile, likely to offset the situation in Water Europe, while the yield remains attractive at 4.6% with the current DPS level (EUR0.65) still considered as a floor. For all these reasons, **we maintain our Buy recommendation**. Our **FV**, still derived from our SOTP valuation, stands at **EUR16.5** per share implying 16% upside vs. the current share price.

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Company description

As a former subsidiary of Lyonnaise des Eaux, which merged with Suez in 1997, Suez was listed in 2008, as part of the merger process of GDF with Suez. The group is the number 2 player in the environmental services sector. Its revenues are derived from water (31%), waste (41%) and International (28%) activities. Major shareholders are GDF-Suez (33.7%) and La Caixa (5.67%). The implementation of the cost reduction programme became the group's DNA earlier than at Veolia (2010 for Suez vs. 2012 for Veolia) allowing Suez to better face the European economic slowdown observed since 2008. The group has less earnings growth potential and return to shareholders to offer to investors compared with Veolia yet benefits from a solid track record over the past few years and is therefore seen by the market as one of the best in class stocks in the sector. Investment case now relies on external growth given the limited organic growth the group is able to generate.

Income Statement (EURm)	**2014**	**2015**	**2016**	**2017e**	**2018e**	**2019e**
Revenues	14,223	15,135	15,322	16,547	18,125	18,584
Change (%)	*-2.9%*	*6.4%*	*1.2%*	*8.0%*	*9.5%*	*2.5%*
EBITDA	2,643	2,751	2,651	2,850	3,126	3,253
EBIT	1,255	1,381	1,282	1,391	1,602	1,702
Change (%)	*6.0%*	*10.1%*	*-7.2%*	*8.5%*	*15.2%*	*6.3%*
Financial results	(406)	(422)	(424)	(441)	(459)	(480)
Pre-Tax profits	768	786	867	920	1,118	1,212
Exceptionals	(81.2)	(174)	8.0	(30.0)	(25.0)	(10.0)
Tax	(173)	(173)	(244)	(215)	(274)	(301)
Profits from associates	5.8	0.0	0.0	0.0	0.0	0.0
Minority interests	(183)	(206)	(203)	(241)	(273)	(289)
Net profit	417	407	421	464	572	622
Restated net profit	321	560	393	436	520	570
Change (%)	*-3.8%*	*74.4%*	*-29.9%*	*11.1%*	*19.2%*	*9.7%*
Cash flow Statement (EURm)						
Operating cash flows	1,610	1,673	1,596	1,382	1,740	1,825
Change in working capital	(124)	(13.7)	(68.0)	(100)	75.8	26.1
Income tax paid	0.0	0.0	0.0	0.0	0.0	0.0
Capex, net	(1,076)	(1,277)	(1,087)	(1,168)	(1,231)	(1,255)
Financial investments, net	216	(402)	253	(2,450)	0.0	0.0
Dividends	(548)	(550)	(602)	(543)	(552)	(606)
Other	(344)	391	685	2,422	(52.0)	(52.0)
Net debt	7,186	8,083	8,042	9,219	9,043	8,907
Free Cash flow	534	255	314	214	509	569
Balance sheet (EURm)						
Tangible fixed assets	8,009	8,275	8,280	10,725	10,725	10,727
Intangibles assets	4,276	4,214	4,223	4,223	4,223	4,223
Cash & equivalents	2,249	2,079	2,925	2,568	2,473	2,383
current assets	7,863	8,039	9,086	9,033	9,552	9,637
Total assets	26,855	27,632	29,284	31,803	32,408	32,521
L & ST Debt	9,648	10,355	11,165	12,265	12,265	12,265
Others liabilities	10,210	10,471	10,753	10,769	11,268	11,274
Other assets	4,458	5,025	4,770	5,254	5,436	5,550
Shareholders' funds	5,478	5,420	5,496	6,846	6,846	6,846
Total Balance sheet	26,855	27,632	29,284	31,734	32,294	32,360
Capital employed	14,283	15,008	15,086	15,005	14,979	14,956
Financial Ratios						
Operating margin	8.82	9.12	8.37	8.41	8.84	9.16
Tax rate	26.85	26.34	33.02	30.00	30.00	30.00
Net margin	2.26	3.70	2.56	2.64	2.87	3.07
ROE (after tax)	4.59	8.23	5.33	5.01	5.93	6.47
ROCE (after tax)	6.67	8.05	6.88	7.84	8.87	9.37
Gearing	106	122	112	111	112	112
Pay out ratio	105	62.50	90.64	65.00	65.00	65.00
Number of shares, diluted	518	538	547	592	633	633
Per share data (EUR)						
EPS	0.81	0.76	0.77	0.78	0.90	0.98
Restated EPS	0.62	1.04	0.72	0.74	0.82	0.90
% change	*-5.4%*	*67.9%*	*-31.0%*	*2.6%*	*11.6%*	*9.7%*
BVPS	10.57	10.07	10.08	12.16	12.27	12.38
Operating cash flows	3.11	3.11	2.92	2.33	2.75	2.88
FCF	1.03	0.47	0.57	0.36	0.80	0.90
Net dividend	0.65	0.65	0.65	0.65	0.65	0.65

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

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1. Investment Case

Why the interest now?

The reason for writing now

On 8th March, Suez announced the **acquisition of GE Water for an EV of c. EUR3.2bn**. With this acquisition, Suez is substantially strengthening its **international footprint** and rebalancing its customer portfolio with **more industrial clients**. **Synergies** between GE Water and Suez's existing industrial water business appear ambitious but achievable while the company's **growth profile** should clearly be enhanced (industrial water is a **EUR95bn** addressable market with an expected **5% growth per year** in the mid-term).

Cheap or Expensive?

Valuation

We value Suez via an **SOTP model**. Our FV stands at **EUR16.5** per share still implying c. **16% upside** vs. the company's current share price. The stock trades at **7.4x** its FY-17 EV/EBITDA multiple broadly in line with historical levels. With a near **4.6% implied dividend yield** (based on a **EUR0.65** DPS for FY-17), Suez is in line with sector's standards.

When will I start making money?

Catalysts

In our view, **catalysts will mainly be related to Suez's ability to integrate GE Water**. The transaction is expected to be closed at the beginning of **Q3 2017**. The group should launch a **EUR750m capital increase** to partly fund the acquisition. However, **no information has been provided regarding this capital increase** (rights issue or ABB?). **Other catalysts** could be the current improvement observed in European industrial production given **the strong correlation it has with organic growth in the waste business.**

What's the value added?

Difference from consensus

We believe **only a small part of the consensus has already integrated the acquisition of GE Water**. When compared with estimates which already include GE Water, our forecasts for **2017e-2018e** are **0.4%** above expectations for EBITDA and **0.3%** above expectations for EBIT, while our bottom line forecasts c. **4.0%** below expectations, both over the same 2017e-2018e period.

Could I lose money?

Risks to our investment case

Potential **risks** include: **1/**integration risks inherent in the acquisition of GE Water (different activities, different cultures); **2/**further pressure on traditional municipal water margins (low inflation, weak volumes, further unpaid bills); **3/**changes in regulations for Suez's Chilean regulated water activities

2. Checks and balances

After 2016 results broadly in line with expectations and the company's initial guidance, **the group unveiled a rather tepid outlook for 2017** with "slight growth" expected in both revenues and EBIT. The near **EUR155m** in cost savings we expect for 2017 as well as the full-year contribution of recent energy-from-waste commissioning in the UK and in Poland will be offset by a **very challenging current market environment in the group's Water Europe division** on the back of low inflation, which triggers negative tariff indexation in France in 2017, weak volumes and challenging comparable bases in Spain and Chile (particularly for H2 2017 vs. H2 2016).

A few days after this release (on 8th March 2017), **Suez announced the acquisition of GE Water** for enterprise value of c. **EUR3.2bn**. Suez will create a 70%/30% joint venture along with Caisse de Dépôt et de Placement du Québec (CDPQ), which will include newly acquired GE Water and Suez's existing assets in the industrial water segment and which should have pro-forma revenues to the tune of **EUR2.5bn**. The acquisition of GE Water is Suez's bet on the **EUR95bn industrial water segment** which is expected to grow at an annual pace of a **5%** in the mid-term and is likely to offset the poor short-term trend and outlook of the municipal water segment in mature European markets. With this acquisition, we expect Suez to benefit from a **higher growth profile,** which should be triggered by GE Water's current exposure (**85%** to industrial customers and **80%** to non-European areas, including **30%** in emerging areas).

Moreover, the acquisition of GE Water enables Suez to tick three out of the four boxes the group set in the past with a stronger international footprint, a more integrated offer to industrial customers and a significantly enhanced digital platform. In all, **Suez's overall portfolio will be rebalanced** with industrial customers to represent about **40%** of revenues of the new aggregated structure (vs. 34% before the acquisition). Similarly, around **40%** of the company's revenues will be generated outside Europe vs. about 32.5% today, on our estimates.

Suez expects the acquisition of GE Water to be **EPS accretive from year one and to generate a double-digit EPS accretion by year five** based on run-rate synergies. **Our approach is slightly more conservative in the short-term** as we expect the acquisition to be **slightly dilutive in FY 2017e** to the tune of -0.4%, but we agree with the potential double-digit accretion in EPS by 2021. Note Suez's computation does not include implementation costs, roughly equal to one-year of cost synergies digressively spread over 2017/2018/2019, whereas we do include them in our accretion/dilution analysis.

On our estimates, **Suez's financial ratios should not be hurt by the operation given the unveiled funding scheme:** EUR600m in hybrid bonds (not included in the group's net debt calculation), EUR1.1bn in long-term senior bonds, a EUR750m capital increase and EUR700m in equity provided by CDPQ. In all, we expect Suez's net debt/EBITDA multiple to reach **3.3x** in 2017 (based on a five-month consolidation of GE Water) but to return to **more standard net debt/EBITDA ratios as soon as 2018** (3.1x in 2018e and 3.0x in 2019e, according to our estimates). As a reminder, the group's net debt to EBITDA target remains at 3.0x (objective set before the acquisition of GE Water).

As for the transaction's multiples, they do look high at first sight vs. Suez and rival Veolia's current trading multiples (acquisition at 12.5x EV/EBITDA excluding synergies and at 10.0x EV/EBITDA including synergies). **After considering the low capital intensity and high cash conversion ratio (70%+) of GE Water's business, they nevertheless appear 1/** broadly in line with company's peers at the EV/EBITDA level and even **2/**in line with Suez and Veolia's EV/EBIT current metrics. As a consequence, and in our view, **the transaction prices does not specifically imply an overpriced deal.**

For all these reasons, **we believe the acquisition of GE Water is a smart move for Suez**. The group's initial aim to report **EUR3bn in EBITDA** including roughly EUR200m from acquisitions **should finally be reached one year behind the initial schedule,** in 2018 vs. 2017.

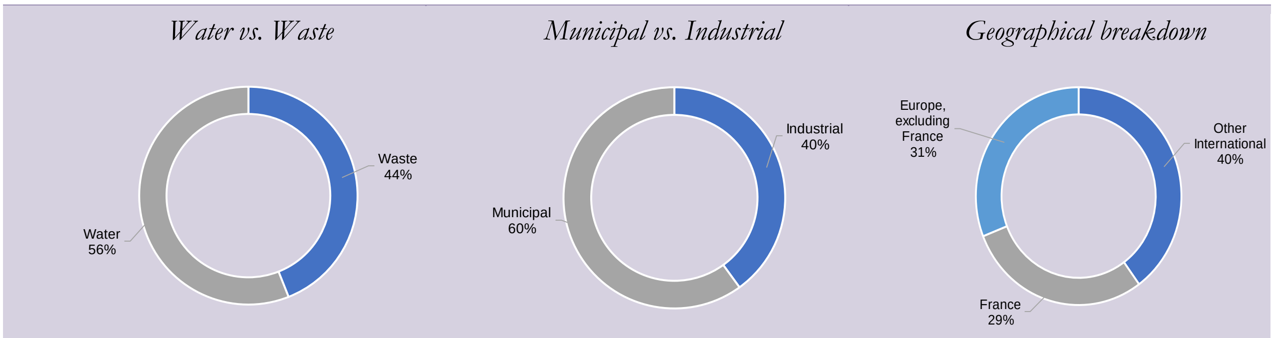
Some **execution risks clearly exist** with fresh exposure to the oil & gas segment, a slowdown in GE Water's activity over the past couple of years, integration risks, a further increase in minorities, but **we believe the risk/reward profile could be attractive in the end.** Additionally, **oil & gas exposure is somewhat mitigated by the downstream bias**, which implies a **more limited volatility** than in the upstream sub-segment, while **we remain confident in Suez's ability to deliver its synergy targets** (the company's track record in terms of cost savings remains solid).

Excluding the contribution from GE Water, **we have revised significantly downwards both our EBITDA and EBIT estimates for the 2017e-2020e period: -5% and -6%, respectively, on average per year over the period**. As mentioned previously, this was mainly due to lower-than-expected growth expected in the Water Europe business division (mainly in France and in Spain) and the more cautious approach we adopted in the International segment.

After including the contribution from GE Water (five months for 2017e, the full-year contribution in 2018e and beyond), **we expect Suez's EPS pre-hybrid coupons to grow c. 10.5% on average per year over 2017e-2020e.** Similarly, Suez's EPS post-hybrid coupons is expected to grow c. 10.0% on average per year over 2017e-2020e. We still expect dividend per share to reach **EUR0.65** in both FY-17e and FY-18e as this level remains **a floor** in our view (confirmed by the company) and still implies a rather attractive **4.6% yield**.

In all, the GE Water transaction confirms Suez's strategy to build up a **well-balanced business** between: **1/**France/Europe/International; **2/**Water & Waste; **and 3/**Municipal & Industrial customers.

Fig. 1: A well-balanced portfolio following GE Water transaction (revenues, EURm)



Source: Bryan, Garnier & Co ests.

Potentially higher cyclicity comes with a stronger growth profile, likely to offset the hesitant situation in Europe in our view, while the yield remains attractive. For all these reasons, **we are maintaining our Buy recommendation. Our FV,** still derived from our SOTP valuation, stands at **EUR16.5 per share**, which still implies upside of around **16%** vs. the current share price.

We would still favour Suez over Veolia (Neutral, FV @ EUR18.5) for now as we believe **business momentum remains rather unsupportive for Veolia notably in H1 2017** as the company should bear the brunt of **a disadvantageous comparison basis** (with notably the end of the Vilnius contract i.e. a EUR40m headwind on a full-year basis broadly equally split between Q1 and Q4) with Q1 2017 and Q2 2017 EBITDA very likely to be down year-on-year. For both companies, **the apparent improvements in European industrial production would remain one of the key short-to-mid-term catalysts** given the strong correlation historically observed between European PMI and organic growth in their respective waste businesses. As a reminder, **we estimate a 100bp increase in volumes treated triggers a tailwind of EUR30-35m for the group's EBITDA**.

3. GE Water is Suez's bet on the industrial water segment

3.1. A few words on the deal

3.1.1. Implicitly back to the EUR3bn EBITDA objective

On 8th March, **Suez announced the acquisition of GE Water,** a former subsidiary of General Electric. Suez acquired alongside Caisse de Dépôt et de Placement du Québec (CDPQ), in a 70/30 joint-venture, 100% of GE Water for **enterprise value of c. EUR3.2bn.** Suez will then contribute to the newly dedicated Industrial Water business unit by bringing its own existing assets. The deal will be financed in two steps, firstly with bridge financing which will then be refinanced through: 1/a near **EUR750 capital increase**; 2/a **EUR1.1bn long-term senior bond**; 3/around **EUR600m in hybrid bonds** and 4/a c. **EUR700m** equity contribution provided by CDPQ. The transaction is expected to be closed at the **beginning of Q3 2017**.

This transaction confirms Suez's initial strategy to grow through both organic and external growth. Note that back in 2015, the company unveiled a **EUR3bn EBITDA 'objective' by 2017,** of which roughly EUR200m was supposed to come from M&A. **In June 2016** *(Environmental Services: haste makes waste, it's upside time!)***, we highlighted that this objective was unlikely to be reached by the company as the timing appeared too short to fully integrate the potential c. EUR200m contribution by 2017**. In July 2016, Suez did not confirm this EUR3bn objective, which finally validated our initial view.

With the acquisition of GE Water, the group should finally reach the initial EUR3bn target should in 2018, according to our estimates.

Suez expects to generate both **cost and revenue synergies** from the acquisition whose full benefit should be completed by year five. These synergies include:

- **A EUR65m** net impact on EBITDA from **already identified cost synergies**, of which 80% achieved over the first three years. Synergies should mainly come from manufacturing costs, engineering costs, purchasing streamlining and SG&A;

- **EUR200m** in **revenue synergies** per year. Significant revenue synergies are expected from **cross-selling** industrial water activities on Suez geographical footprint. **Additional cross-selling opportunities could be achieved from recycling and recovery activities but are not included by the group in previously mentioned synergies**. **Note we have adopted a conservative view as these revenue synergies are not included in our model.**

With these synergies, Suez expects the deal to be **EPS accretive from year one** and to generate **double-digit accretion in EPS** based on run-rate cost synergies

Implementation costs will be equal to one year of cost synergies and are likely to be digressively spread over 2017-2019.

With these synergies, Suez expects the deal to be **EPS accretive from year one** and to generate a **double-digit accretion** in EPS based on run-rate cost synergies (i.e. **double-digit EPS accretion is expected by year five**).

3.1.2. What about implied multiples?

The EUR3.2bn enterprise value implies a c. **10.0x EV/EBITDA** multiple including cost synergies and a c. **12.5x EV/EBITDA** multiple without these synergies. We therefore deduce that GE Water has a normative EBITDA to the tune of **EUR255-260m**. It is also interesting to note that the 10.0x EV/EBITDA multiple is broadly in line with the implied one for Suez's acquisition of **Nalco** – a company also specialised in chemical water treatment and industrial process water - back in 1999.

These multiples clearly seem high compared to Suez's current trading multiples at **7.4x.** They nevertheless stand at the mid-range of GE Water's peers' multiples with **Ecolab, Xylem, Kemira and Pentair currently trading at respectively 14.2x, 12.5x, 7.2x and 15.3x.** The standard deviation between these metrics is mainly explained by different end-markets, a different products & services mix and inherent **different EBITDA margins,** which range from 15-20% for Pentair and Ecolab and 10-15% for Kemira, Xylem and GE Water.

Fig. 2: Key peers' services & products mix

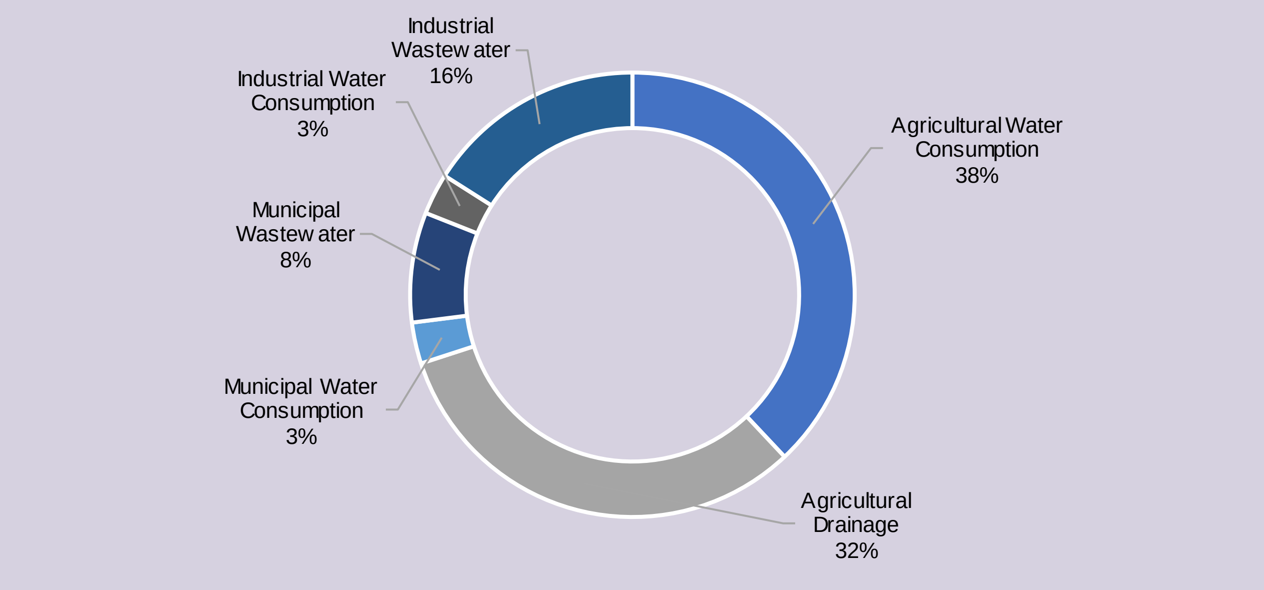
	Instrumentation	Equipment & Systems	Engineering Procurement & Construction	Operations & Maintenance	Chemical Water Treatment & Related Services	Monitoring, analytics & Digital Services
Suez & GE Water	++++	++++	++++	++++	++++	++++
Ecolab	++++	+	-	+	++++	++
Xylem	++++	++++	-	-	-	++
Kemira	-	-	-	-	++++	++
Veolia	-	++++	++++	++++	+	++
Pentair	++++	++++	-	-	-	++++

Source: Company Data

In all, **we believe these high multiples – compared to Suez and Veolia - can be explained by various factors** including:

- A supposedly **higher growth profile and booming addressable market** with the industrial segment being mainly driven by harsher regulations today. According to Suez, **industrial water consumption represents between 15% and 20% of global water consumption** vs. c. 5-10% only for individual and city water consumption in which both Suez and Veolia are historically present;

Fig. 3: Global consumption & wastewater production by major water use sector

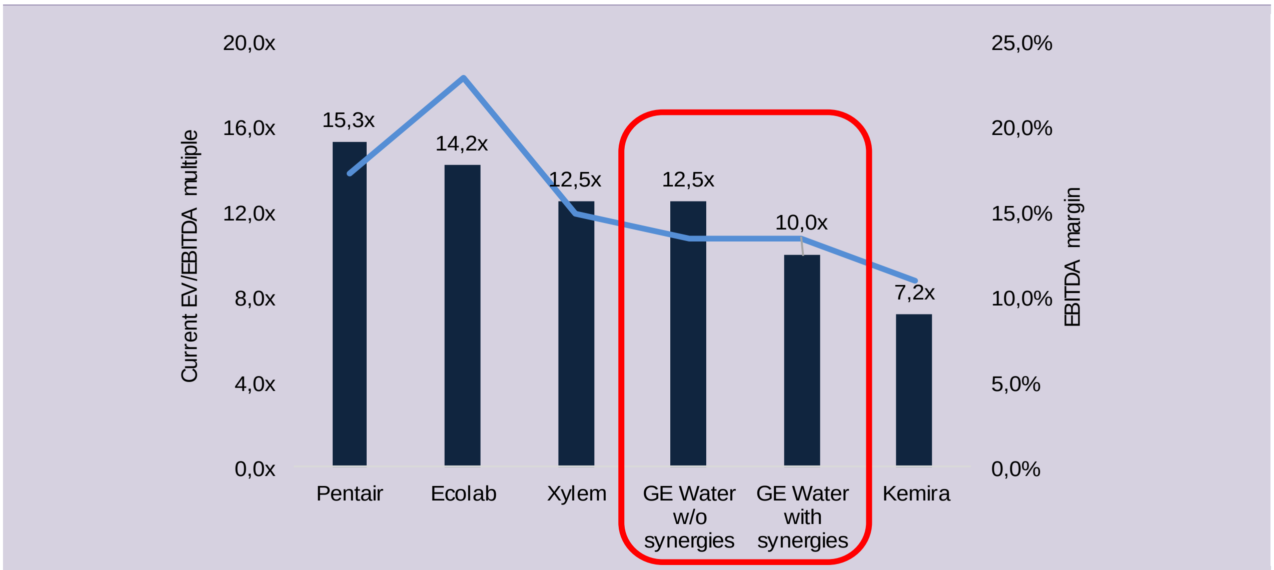


Source: United Nations

- The **recurrence** of a large part of these businesses on the back of high renewal rates and strong customer dependency on services provided by industrial water companies;

- **Strong cash conversion** ratios mainly given the low-capital intensity of the business. Suez indicated GE Water has a 70%+ cash conversion ratio (vs. a **ratio slightly below 60% for Suez**). The company mentioned that **GE Water's capital expenditure only represents about 4% of its sales** vs. between 7% and 8%, on an historical basis for Suez.

Fig. 4: GE Water's transaction vs. current peers' trading multiples



Source: Bloomberg; Bryan, Garnier & Co ests.

In our view, **the price-tag does not specifically imply an overpriced deal when compared to existing peers' multiples** and the growth prospects mentioned

Consequently, in our view, **the price-tag does not specifically imply an overpriced deal** when compared to existing peers' multiples and the previously mentioned growth perspectives.

Moreover, given GE Water's intrinsic characteristics (low-capital intensity), it may seem more relevant to compare GE Water's implied **EV/EBIT** valuation with those of Suez and Veolia. As the EUR65m in cost synergies will mainly be pass-through to EBIT and considering a normative 75% EBIT/EBITDA ratio (management indications), we estimate GE Water's normative EBIT including costs synergies at around **EUR240m**. **This would imply a c. 13.3x EV/EBIT multiple which looks slightly lower than multiples at both Suez** (trading at 14.8x its FY-17 EV/EBIT multiple) **and Veolia** (trading at 13.9x).

Similarly, notably due to the low-capital intensity of GE Water's business model, **we estimate the acquisition will generate a ROIC/WACC equal/higher than 1.0x by 2020e** on the back of the previously mentioned synergies and solid cash generation. **Integrating the EUR200m in revenue synergies as well as the contribution of these synergies to EBITDA would imply ROIC/WACC higher than 1.0x as soon as 2019e.**

Note that we assume Suez's WACC will remain broadly stable at 6.3%.

Fig. 5: ROIC/WACC > 1.0x by 2020e

Year	**2017e**	**2018e**	**2019e**	**2020e**	**2021e**
Fixed Assets (+)	3,203	3,206	3,209	3,212	3,215
Cash (-)	107	123	148	154	164
FCF	*134*	*151*	*180*	*190*	*200*
Financial interests	*(17)*	*(17)*	*(17)*	*(17)*	*(17)*
Hybrid coupons	*(24)*	*(24)*	*(24)*	*(24)*	*(24)*
Tax adjustments	*14*	*12*	*8*	*5*	*5*
Invested Capital	**3,096**	**3,083**	**3,061**	**3,057**	**3,050**
NOPAT	137	154	183	193	203
ROIC	**4.4%**	**5.0%**	**6.0%**	**6.3%**	**6.7%**
WACC Group	6.3%	6.3%	6.3%	6.3%	6.3%
ROIC/WACC	**0.70x**	**0.79x**	**0.95x**	**1.00x**	**1.06x**

Source: Bryan, Garnier & Co ests.

3.2. What is GE Water?

As previously mentioned, GE Water is specialised in the **industrial water segment**. The group notably provides integrated chemical treatment solutions as well as equipment and technology solutions for water and wastewater treatment. In FY 2016, GE Water reported revenues of c. **EUR1.9bn,** with two-thirds of these revenues generated in **services,** while the remaining third was generated in **systems**.

About 65% of GE Water's revenues are considered as recurrent by Suez given the very high renewal rate of services' contracts by Suez given the very high renewal rate of services' contracts

Historically, **GE Water has been built on an 'aggressive' external growth policy at the beginning of the 2000's**. **BetzDearborn** (water treatment services business, acquired for **USD1.8bn**), **Osmonics** (leader in water purification and filtration, acquired for c. **USD250m**), **Ionics** (leader in desalination, water reuse and recycling as well as in industrial ultrapure water services, acquired for c. **USD1.1bn**) and **ZENON Environmental** (leader in advanced membranes for water purification, wastewater treatment and water reuse to municipalities and industries worldwide, acquired for c. **USD690m)** had respectively be acquired and integrated by General Electric in 2002, 2003, 2005 and 2006.

About 65% of GE Water's revenues are considered as recurrent by Suez given the very high renewal rate of services contracts (c. **95%**, according to management), much higher than for equipment contracts (renewal rate of only around **35%**, according to Suez's management, mainly on the back of BOO – Build, Own, Operate - and mobile contracts).

Fig. 6: GE Water's businesses

Source: Company Data

Fig. 7: Selected solutions provided by GE Water by end-market

POWER	- Water outsourcing solutions - Mobile water fleet - Alternative fuel solutions - Dust control programs - Metals removal - Membrane bioreactor systems - Zero Liquid Discharge systems - Chemical & Monitoring solutions - Utility water solutions
MUNICIPAL WATER & WASTEWATER	- Membrane bioreactor systems - Ultrafiltration systems - Electro dialysis reversal - Reverse osmosis systems - Membrane cleaning chemicals
REFINING	- Phase separation - Corrosion inhibitors - Advanced boiler and cooling chemicals - Integrated wastewater management and water reuse - Clarification and filtration - Portfolio of membrane clarification and water purification technologies - Zero Liquid Discharge Systems
MINING	- Discharge water management and reuse - Dust control programs - Membrane & Filtration Technologies - Zero Liquid Discharge Systems - Metals removal - Corrosion and deposit control
CHEMICAL PROCESSING	- Antifoulants - Corrosion inhibitors - Membrane clarification and water purification - Mobile water fleet - Oxygen scavengers
UNCONVENTIONAL GAS	- Produced water treatment technology - Salt removal and recovery - Brine concentrators and crystallisers - Membrane and filtration technologies - Metals Removal
OIL SANDS	- Zero Liquid Discharge systems - Emulsion breakers - Mobile Water - Membrane
FOOD & BEVERAGE	- Ingredient water solutions - Membrane cleaning chemicals - Food process chemistries - Wastewater management and water reuse - Sterilisers and pasteurisers

Source: Company Data

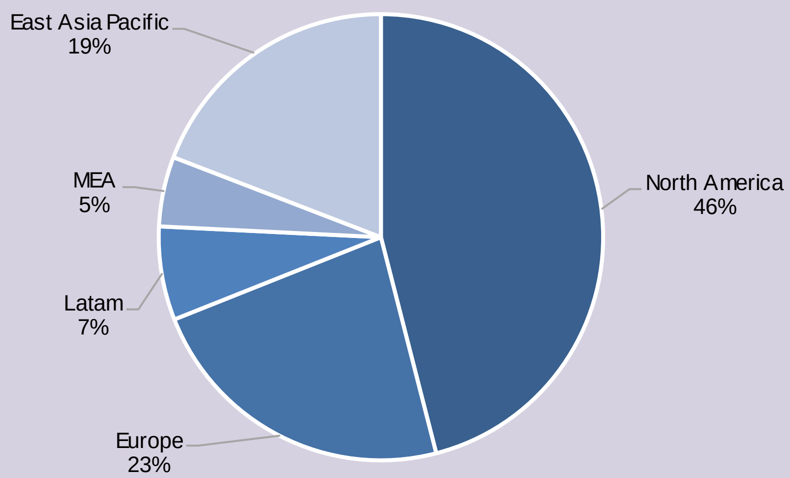
According to our estimates, **more than 85% of GE Water's business is geared towards industrial customers**. Main end-market exposures are the **oil & gas sector** (23% of GE Water's 2016 revenues with the main exposure being in the downstream/refinery sub-segment), the **power sector** (15% of reported revenues) and the **chemical industry** (15% of reported revenues). Other sectors covered by GE Water include particularly **Pharma**, **Mining** or **Food & Beverages**. GE Water's customer base notably includes various giant players in the previously mentioned sectors such as Shell or Exxon Mobil (Oil & Gas), BASF (Chemicals), Sanofi and Pfizer (Pharmaceuticals) or Coca-Cola and Nestlé (Food & Beverages). **As GE Water's businesses are mainly based on rather small size contracts** (around EUR10-20m), **the company has a limited dependence on any of these particular customers**.

About 80% of GE Water's revenues are generated outside Europe

About 80% of GE Water's revenues are generated outside Europe with a strong exposure to **North American markets** (50% of the company's revenues incl. about 40% in the US) **and to Asia** (c. EUR400m of revenues o/w about EUR100m in China). Remaining exposures are to Latin America (c. EUR120m of revenues), Europe (c. EUR400m of revenues) and the Middle East and Africa (c. EUR120m of revenues).

Once combined with Suez's existing industrial water businesses, **the new division will have around EUR2.5bn** in revenues with **strong international exposure** as the new entity will generate only 23% of its aggregated revenues in Europe.

Fig. 8: Suez's new industrial water division: geographical breakdown of revenues



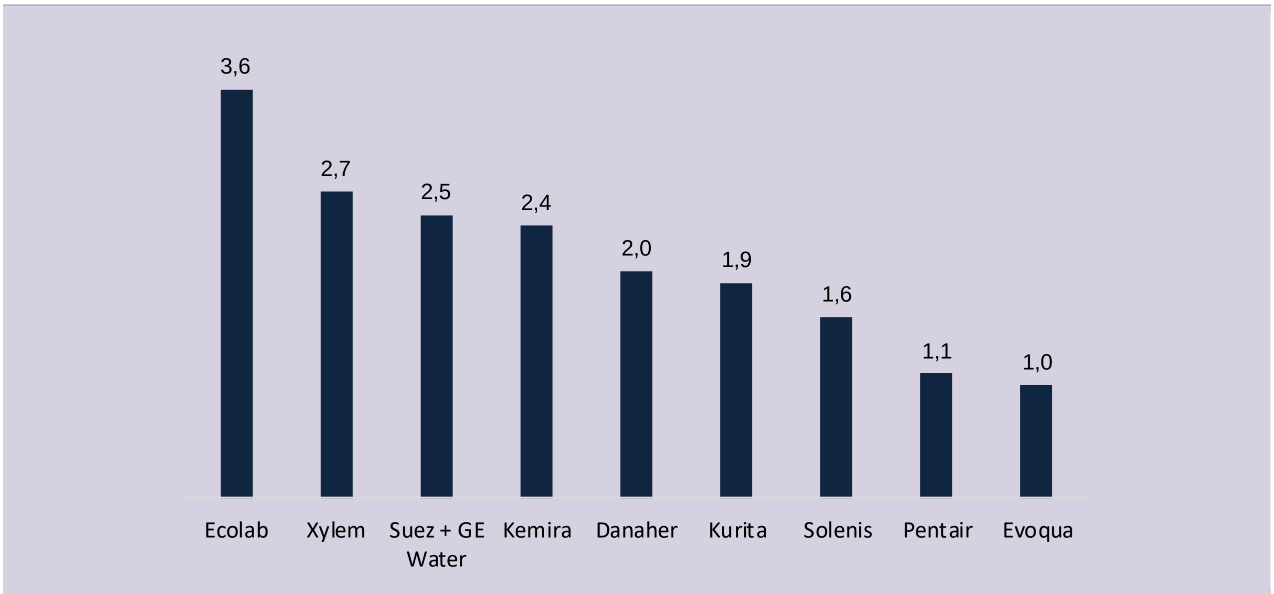
Source: Company Data; Bryan, Garnier & Co ests.

With this acquisition, Suez will become the **third-largest player in the industrial water market**

With this acquisition, **Suez will become the third-largest player in the industrial water market**, behind US companies Ecolab and Xylem, while being **present across the entire industrial water value chain** (instrumentation, equipment & systems, engineering, procurement, construction, operation & maintenance, chemical water treatment and related services, monitoring/analytics/digital services). Suez will also benefit from **GE Water's digital platform** (2,500 patents and applications and 12R&D centres across four continents) with the group's expertise ranging from asset monitoring to developed digital customer service capabilities and digital sales.

Note that **Veolia does not explicitly communicate on its industrial water revenues.** However, we estimate these revenues could amount to **EUR1.1-1.2bn** especially following last year's acquisition of Chemours' assets (c. EUR230m of revenues) and the EUR130m/year contract awarded in 2016 by Chinese company Sinopec. This actually excludes the contribution from construction works and Veolia Water Technologies (about 60% of VWT revenues is generated in the industrial segment). Integrating this contribution, **we estimate Veolia's overall revenues in the industrial water segment should total around EUR2.5-2.6bn.**

Fig. 9: Suez becomes the no. 3 player in the industrial water market



Source: Company Data; Bryan, Garnier & Co ests. Note that Veolia's revenues in the industrial water segment are not publicly available but we estimate the company has industrial water revenues to the tune of EUR1.1-1.2bn excluding construction works and VWT (and c. EUR2.5-2.6bn once included them).

3.3. Why does this deal makes sense for Suez?

3.3.1. Lagging trend in European municipal water businesses

Just like Veolia, Suez bears the brunt of an **unsupportive macro environment in its traditional municipal water business**

As a reminder, back in 2013, Suez plotted out a **new strategic road-map** based on four pillars:

1- **Speeding-up the group's international footprint** with the aim of growing international revenues by **6-8%** over the mid-term;

2- **Speeding-up integrated offers to industrials**. Back in 2015, Suez reported around **EUR1.7bn** in revenues in the industrial segment with around EUR1.2bn generated in the waste segment and c. EUR0.5bn in the water segment. The group initially aimed at increasing its revenues from big industrial customers by around 10% per year on average by 2020 to EUR2.9bn (EUR1.9bn in the waste segment and EUR1.0bn in the water segment);

3- **Speeding-up innovative offers in water services** notably through smart metering and new monitoring services;

4- **Speeding-up momentum in waste recovery** with the aim of focusing on value-added segments such as hazardous waste or alternative fuels.

In our view, **the acquisition of GE Water therefore enables Suez to tick the first three boxes** as GE Water's key investment highlights mainly rely on its international industrial customer portfolio and its digital platform.

It also enables the company to offset the poor short-term trend and outlook of its municipal water business, which bears the brunt – just like Veolia's - of a **rather unsupportive market environment.**

Among the main **headwinds:**

- **Inflation remains low** in Europe and this negatively impacts the tariff indexation formula. In 2017, **tariff indexations will be negative** due to the low inflation environment in 2016 and depressed energy prices (which are part of indexation formulas);

- **Volume trends (also) remain negative** from a medium-to-long-term perspective, at around -1/-1.5% per year – due to the development of smart water devices and new behaviour in terms of water consumption, mainly in mature markets;

- In France, **the Brottes law** (which in a nutshell prevents companies like Suez or Veolia from cutting off water supply even in the case of unpaid bills) has led to a **sharp increase in unpaid bills** which are said to represent around 1.5-2% of overall French water bills vs. c. 0.5% historically. This trend has mainly been highlighted by Veolia while **Suez's position is more nuanced.**

- Finally, the Olivet decree (which limits public delegation services contracts to a maximum of 20 years) has led to **unfavourable contract renegotiations** with downward pressure on prices. Every year, both Veolia and Suez renegotiate between 5% and 10% of their contract portfolio. **The renewal rate remains high** (c. 95%) **despite downward pressure on tariffs**. As for Suez, main contract about to expire in the short-term is that in Bordeaux (maturity in 2017 with aggregate revenues of c. EUR40m). Veolia's main challenges will be to renew contracts in Toulouse (maturity 2020 with aggregated revenues of c. EUR95m) and in Toulon (maturity 2019 with revenues of c. EUR20m).

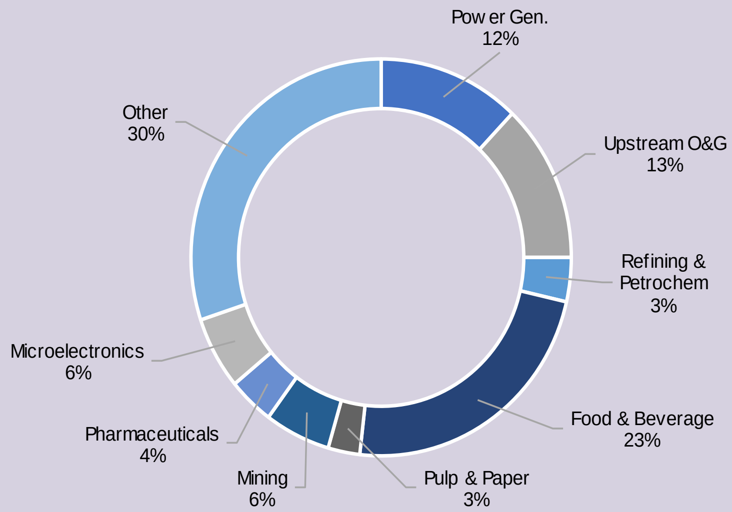
3.3.2. Growth profile set to be improve with GE Water

The **global addressable industrial water market** is thought to total around **EUR95bn**

According to *Global Water Intelligence* (GWI), **the global addressable industrial water market is thought to total around EUR95bn** (both operational expenditure and capital expenditure).

In 2016, **industrial water capital expenditure was expected to reach USD20.3bn**, according to data published by GWI back in April 2016.

Fig. 10: 2016 industrial water capex breakdown



Source: Global Water Intelligence, April 2016

Suez expects the global industrial water market to grow at **5% per year on average in the mid-term**

Based on GWI data, Suez expects the global industrial water market to grow at 5% per year, on average, in the mid-term, with this trend mainly driven by global industrial growth, harsher regulations, increasing need for water reuse solutions and increasing industrial need for outsourcing solutions in order to minimize costs.

Note additionally that this mid-single digit growth appears in line with Veolia's initial expectations, unveiled by the company during its last Investor Day in December 2015, to grow its industrial businesses (note this included water, waste and energy activities) by c. 5% on average in the mid-term.

Fig. 11: Expected 2016-2020e growth by end-market

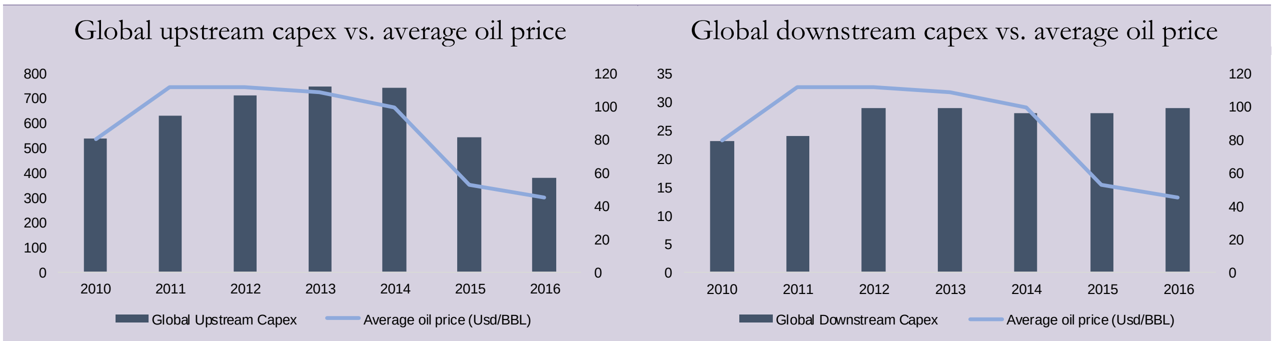
	Food & Beverage	O&G Upstream	Power	Mining	O&G Downstream	Micro Electronics	Pharma & Cosmetics
Expected average annual growth 2016-2020	4.3%	12.3%	3.4%	5.9%	2.2%	5.6%	6.9%

Source: Company Data based on GWI data. Microelectronics and Pharma & Cosmetics data are based on total capex spent only (vs. opex and capex for other sectors).

GE Water's strong exposure to the oil & gas segment (about a quarter of the company's business) **raised some concerns given the generally high volatility in the sector**. In 2016, Veolia suffered from this exposure, especially in the US where industrial services activity with oil & gas clients contributed to the organic decline in revenues of the company's US branch (up 0.6% at constant FX but this included a positive contribution of around EUR110m from the acquisition of Chemours' assets back in June 2016).

We believe these concerns are not fully justified as GE Water's exposure to the O&G sector is mainly effective in the downstream sub-segment with downstream capital expenditure generally **less volatile** than upstream spending and generally less dependent on barrel price variations. Indeed, **while upstream capex fell by around 6% on average per year over 2010-2016**, with a sharper decrease between 2013 and 2016 of around. 20% on average per year, **downstream capex increased by c. 4% on average per year between 2010 and 2016 and has been broadly stable since 2013**.

Fig. 12: Downstream capital expenditure less volatile than upstream



Source: Bloomberg, Bryan, Garnier & Co ests.

3.3.3. A rebalanced customer portfolio

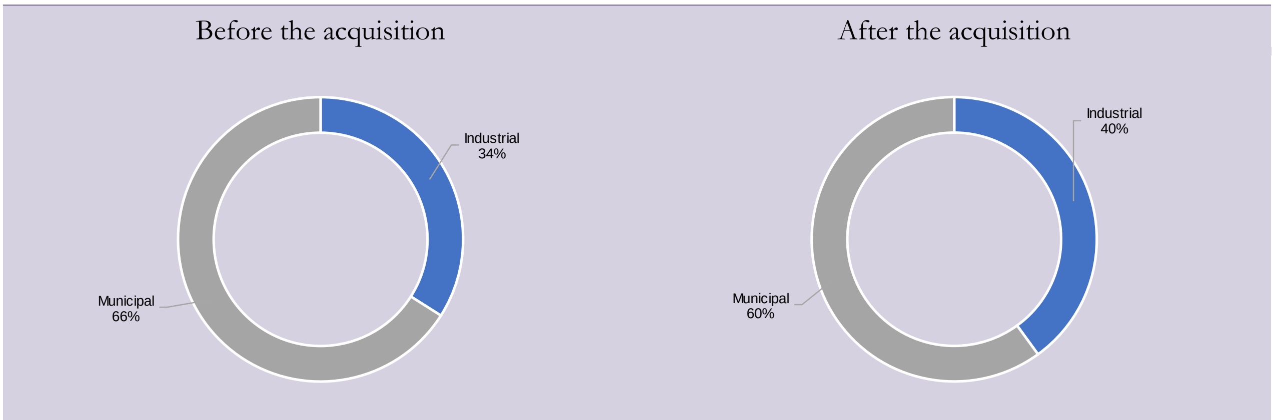
The GE Water transaction should help Suez **rebalance its customer portfolio both in terms of businesses and geographies**

On top of this improved growth profile, the GE Water transaction should help Suez **rebalance its customer portfolio both in terms of businesses and geographies.**

Following the acquisition of GE Water, Suez will derive:

- **about 40% of its revenues from industrial customers,** which compares with "only" **34%** before the acquisition. This implies that around **EUR7bn** of Suez's revenues will be generated with industrial customers.

Fig. 13: c. 40% of Suez's revenues set to stem from industrial customers



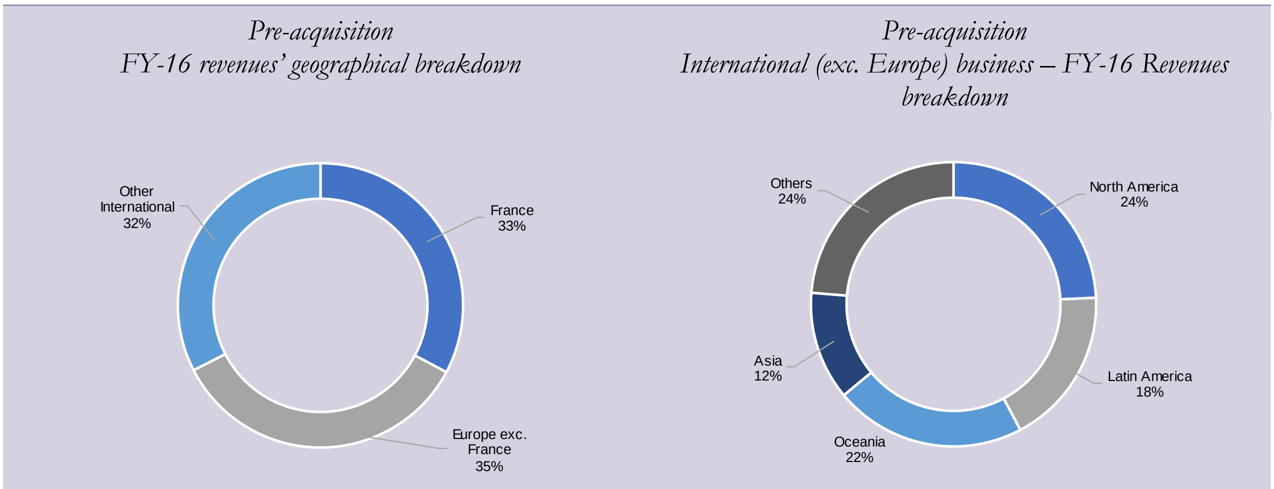
Source: Company data

Note nevertheless that this is still **below Veolia's levels**, as about **45%** of the company's revenues came from industrial customers in 2016. Moreover, Veolia recently unveiled **54%** of its 700-strong project pipeline is geared towards industrial customers.

- about **40% of its revenues from outside Europe**.

As of today, Suez's revenues are quite equally split between France (about a third of the company's revenues), **Europe exc. France** (c. 35% of the company's revenues) **and outside Europe** (c. 32.5% of the company's revenues). At the international level, the main contributors are North America (c. EUR1.2bn in revenues mainly from Suez's regulated water subsidiary), Oceania (c. EUR1.1bn of revenues) and South America (c. EUR900m of revenues). The remaining international revenues mainly stem from China, Morocco and India.

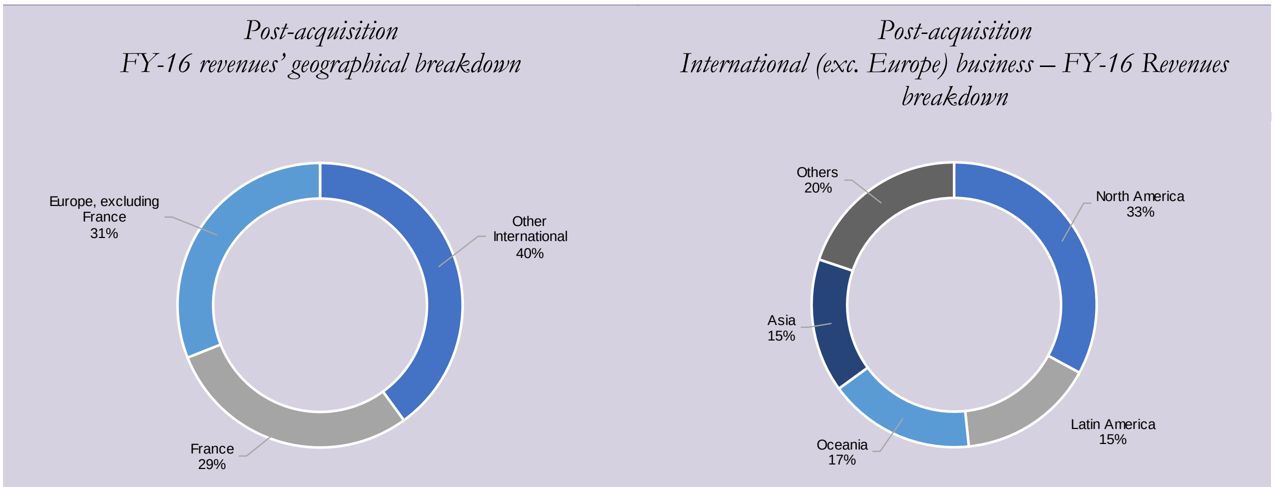
Fig. 14: Before the acquisition, revenues were fairly equally split on a geographic basis



Source: Company data

Following the acquisition, **Suez's exposure to lagging French businesses will be diluted from around 33% to about 29% while booming international businesses** (exc. Europe) **will see their shares rise from around 32% to around 40%.**

Fig. 15: After the acquisition: revenues generated outside Europe should represent about 40% of Suez's overall top line



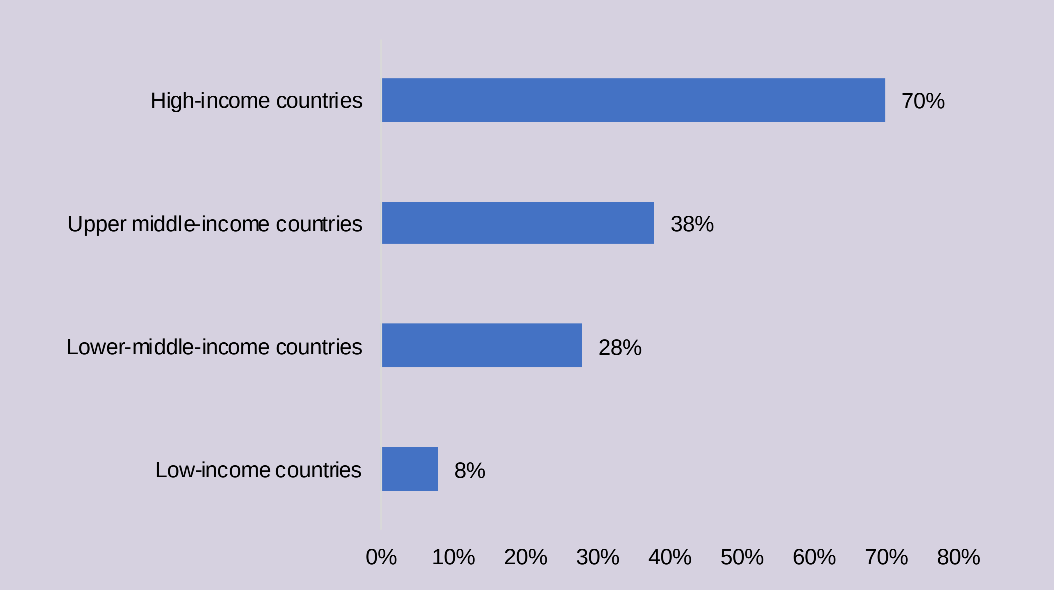
Source: Company data; Bryan, Garnier & Co ests. Note that we assumed revenues reported by GE Water in Europe are generated outside France.

We also estimate Suez generates a slight more than 20% of its overall revenues in emerging areas, a presence which is strengthened by the acquisition of GE Water, which generates c. 30% of its revenues in emerging markets.

In low-income nations, **only 8% of its industrial and municipal wastewater undergoes treatment of any kind**

Last week's new report from the United Nations (United Nations World Water Development Report) gave even more meaning to Suez's international and industrial strategy. **The report highlights that, globally, more than 80% of wastewater is released into rivers and lakes without treatment with a negative impact on both health and the environment**. High-income nations treat about 70% of the wastewater they generate, a figure that sharply drops to 38% for upper-middle income countries. **In** low-income nations, only 8% of industrial and municipal wastewater undergoes treatment of any kind.

Fig. 16: % of wastewater treated in 2015 with different income levels



Source: United Nations

3.4. Various challenges & risks to be managed

As is often the case, transformative acquisitions such as this come with risks and can raise various uncertainties. Obviously, **tepid past experiences by both Suez** (acquisition of US company Nalco back in 1999 for USD4.1bn and disposal in 2003 for USD4.35bn with an EUR700m impairment due to unfavourable forex variations), **and Veolia** (acquisition of US Filter also in 1999 for about USD6.2bn and disposal of the company in tranches in 2002 and 2004 with a c.EUR4.8bn impairment) **in the US, means caution is needed**.

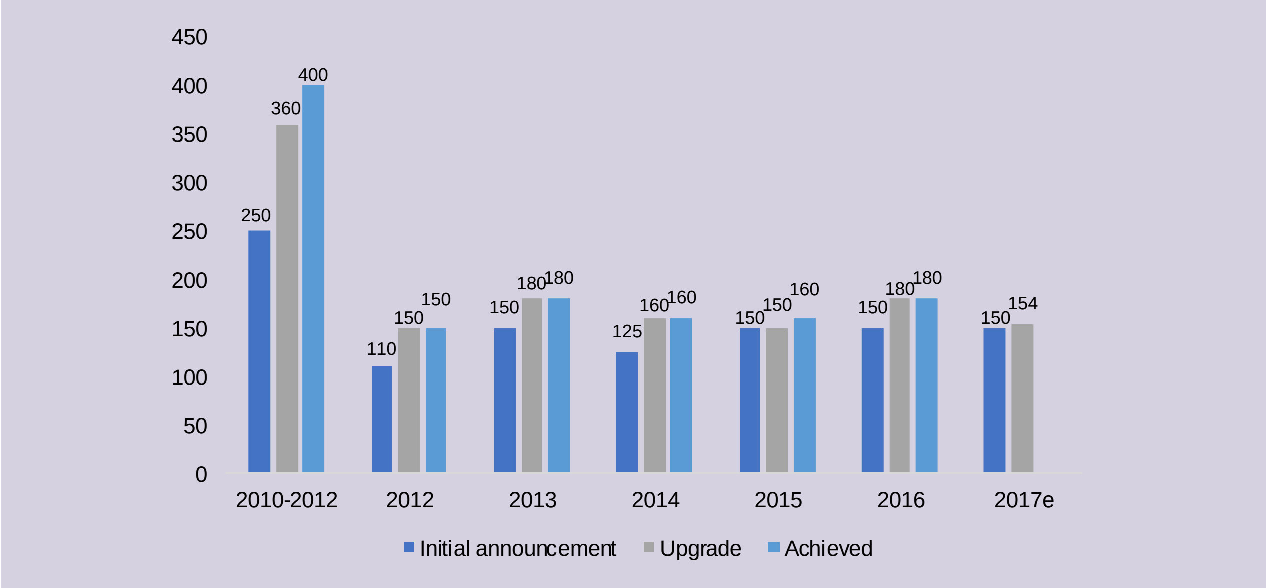
In our view, some of these uncertainties can be justified (Suez's minorities' policy appears unclear in our view). Other ones need to be identified but come along with an inherent attractive reward (new oil and gas exposure for Suez, particularly).

- **Suez will now be exposed to the oil & gas segment** (as a reminder, about a quarter of GE Water's revenues), which was not really the case before (we estimate the company generated about a hundred million in revenues in this sector before the transaction). In 2016, Veolia bore the brunt its exposure to the sector, mainly in the US, which negatively impacted the group's organic growth all over the year. **However**, and as previously mentioned, **GE Water's exposure to the sector is mainly geared towards the downstream sub-segment, which appears to be less volatile than the upstream one and hence less dependent on barrel price variations. Suez indicated that the upstream activity only represented c. 7% of GE Water's revenues vs. c. 16% for the downstream sub-segment**.

- **GE Water has seen its EBITDA decline over the past couple of years** after reporting years of double-digit EBITDA growth between 2011 and 2014. Despite the pretended low volatility of GE water's business in the oil & gas sector, the company bore the brunt of a challenging market environment in the segment (downstream activity was resilient while upstream business suffered from volatile capital spending, as explained above). Note that **2016 metrics were also affected by one-off items** principally linked with Alberta Wildfire in 2016. **Suez has not provided any business outlook for GE Water for 2017** (except for the 5% expected mid-term CAGR). **Comments from US company Ecolab, one of GE Water's main peers, are however rather reinsuring for 2017.** Ecolab unveiled a brighter than initially expected outlook for 2017 notably on the back of expected improvements in its Global Industrial and Global Energy business divisions.

- **Integration risks**. Integrating about 7,500 new employees (vs. about 80,000 for Suez as of today) is clearly not an easy task. This seems even more true when considering the **strong General Electric corporate culture.** We however believe **GE Water was likely to be somewhat strapped into General Electric's "machine" as the subsidiary only represented a very small share in its parent company's earnings** (less than 2% of General Electric's cumulated revenues and EBITDA). In all, Suez appears inclined to form a standalone industrial water business unit, with potentially high independence, while **Heiner Markhoff, current CEO of GE Water, will be head of the brand-new division**. As for synergies, we estimate the expected **EUR65m** in cost synergies represent about **1.4%** of the expected 2021e combined cost base ,which could appear **challenging but which is not so far from Suez' general objective to save about 1% of its cost base each year**. Historically, **Suez has a solid track record in delivering cost-savings.** For each of the last seven years, Suez has upgraded its initial cost-savings target and/or has exceeded it with an **average 28.5% beat over the period**.

Fig. 17: Suez cost-savings track record between 2010 and 2017e (EURm)



Source: Bryan, Garnier & Co ests.

It also worth mentioning that **over the past few years** (from 2010 to 2016, which therefore excludes the 'Nalco period' previously mentioned), **Suez's track record in M&A operations appear solid**. The company booked **only EUR10.7m in goodwill impairment over the period while financial investments have exceeded EUR2bn**.

Fig. 18: Goodwill impairment vs. financial investments since 2010

	2016	2015	2014	2013	2012	2011	2010	Total
Goodwill impairment	0.0	0.0	0.0	1.0	1,7	0.0	8.0	**10,7**
Financial investments	404	472	498	37	127	262	587	**2,387**

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

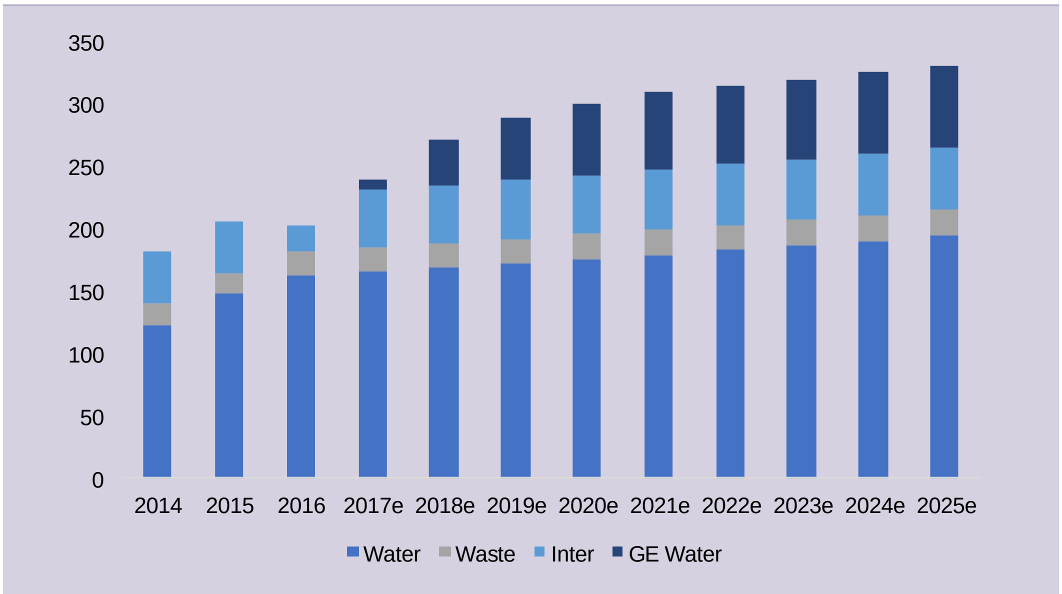
- **Suez's minorities policy appears unclear in our view**. Back in Q3 2015, we believed Suez could foster EPS accretion via minority buy-back operations. We notably highlighted that the group could buy back minorities from Australian company Sembsita Pacific (which was then 60% owned by Suez), Moroccan company Lydec (51% owned by Suez) and Chilean company Aguas Andinas (c. 28% owned by Suez). **In September 2015, Suez confirmed our initial view with the buy-out of Sembcorp's minority interests in Sembsita Pacific for about AUD485m** (EUR310m)**. But Suez's recent operations appear more inclined to an increase in minorities:**

    - In November 2016, **Suez announced that it had reached an agreement with NWH holding** for the restructuring of their 50/50 JV in the water business. Under this agreement, NWS and Suez grouped together their respective waste and wastewater businesses. Following the operation, Suez owns a 58% stake in the new structure with the remaining 42% being held by NWS. **The operation should add a near EUR30m contribution to Suez's EBIT on a yearly basis as the new structure is now fully consolidated by the group. However, the impact on the group's bottom line is said to be very marginal given the inherent increase in minorities.**

- **The Caisse de Dépôt et Placement de Québec (CDPQ) will have a 30% stake in Suez's new Industrial Water business unit** which will group together, as a reminder, GE Water and Suez's existing assets in the segment. **We estimate this operation will increase Suez's minorities by EUR35m on a full-year basis.**

In all, we **expect minorities to increase by around 5.5% on average per year between 2016 and 2026.**

Fig. 19: Expected increase in minorities (2014-2025e)



Source: Bryan, Garnier & Co ests.

4. Integrating a tepid outlook into our estimates

On 1st March, Suez reported its 2016 results and unveiled a rather **tepid 2017 outlook**, in our view. The group only expects **slight organic growth in both revenues and EBIT** whereas we believed it could have benefitted from various positive elements including the full-year contribution from new waste commissioning, the company's cost-savings programme, as well as the positive scope effect inherent in the group's reorganisation in China.

No real surprise however for other group targets with FCF expected to reach around **EUR1bn**, net debt to EBITDA at c. **3.0x** (bearing in mind that this target was set before the EUR3.2bn acquisition of GE Water) and DPS at least equal to **EUR0.65 per share** (which can clearly be seen as **a floor**, in our view, which was confirmed by the company).

Following these results and the new outlook unveiled, we made various adjustments to our model. Note that for now we consider GE Water as a new business division while in the future the company is likely to be integrated in a brand unit dedicated to industrial water solutions and to be combined with Suez's existing assets in the segment. As a consequence, we model separately four business divisions: Water Europe, Recycling & Recovery Europe, International and GE Water.

4.1. Still challenging market conditions in Water Europe

We expect EBITDA and EBIT in the Water Europe division to respectively decrease by 2.2% and 3.4% in 2017 on an organic basis.

In our view, Suez will bear the brunt of **various headwinds** including:

- **A negative tariff indexation in France** (we expect a -0.5% indexation for FY 2017 before rebounding to a positive 0.5% in 2018 on the back of higher inflation and higher energy prices yoy);

- **Similar pressure on tariffs in Spain** which is likely to take a toll on Aguas de Barcelona's margins;

- Note that we still integrate a c. **EUR10m** negative impact from the **Brottes law** and the inherent increase in **unpaid bills** in the company's French Water segment;

- **A still unsupportive volume impact** with a volume trend of -1% expected in France. In all, we expect combined French, Spanish and Chilean volumes to decrease by 0.3% on average over the 2017-2020 period. Recent floods in Chile should negatively impact Aguas Andinas' performance in Q1 2017 while H2 2017 could suffer from a challenging comparison basis on a year-on-year basis.

These identified headwinds should be partly offset by the implementation of **cost-savings**, a positive **scope effect** following Suez's higher stake in Italian environmental services company **ACEA** (from 12.5% to 23.33%, which could bring an additional EUR15m to both Suez's EBITDA and EBIT) and a **positive currency effect** with the Chilean peso.

Fig. 20: Water Europe – Key metrics (2015A-2018e)

Water	2015A	2016A	2017e	2018e
Revenues	4,677	4,703	4,719	4,718
YoY change	-	0,5%	0.3%	0.0%
Organic growth	-	(1,3%)	(0.9%)	0.0%
EBITDA	**1,320**	**1,277**	**1,273**	**1,281**
EBITDA margin	28.2%	27,2%	27.0%	27.1%
YoY change	-	(3,2%)	(0.3%)	0.7%
Organic growth	-	(3,4%)	(2.2%)	0.7%
EBIT	**636**	**611**	**607**	**612**
EBIT margin	13.6%	13,0%	12.9%	13.0%
YoY change	-	(3,9%)	(0.7%)	0.8%
Organic growth	-	(3,5%)	(3.4%)	0.8%

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

<u>**Main upside to our estimates:**</u>

- **Increase in inflation in Europe,** which would imply a potential positive impact on our estimates in 2018 and beyond.

Fig. 21: HICP - Annual rate of change (%)

	2011	2012	2013	2014	2015	2016	2017e	2018e
European Union	3.1%	2.7%	1.5%	0.6%	0.0%	0.3%	1.4%	1.4%
France	2.3%	2.2%	1.0%	0.6%	0.1%	0.3%	1.2%	1.4%
Spain	3.0%	2.4%	1.5%	(0.2%)	(0.6%)	(0.4%)	1.6%	1.4%

Source: Bloomberg for consensus' forecasts; Eurostat for historical data.

- **Higher temperatures** than average, which would imply stronger water volumes.

<u>**Main risks to our estimates:**</u>

- At the end of 2016, a bill was passed by Chilean MPs with the aim of **revising downward the remuneration of Chilean regulated water activities** (end of the current 7% remuneration floor and potential decrease in the risk premium used for the remuneration formula). **Suez's management nevertheless appears confident regarding this potential measure** as: **1/**the MP's vote is just a first step and the bill now has to be voted by the Senate; **2/**the Chilean government has publicly opposed this reform; **and 3/**Aguas Andinas is immunised against any change in law by 2021 following recent tariff renegotiations. Recently, Japanese company INCJ was said to have put on hold the sale process of its 50% stake in Chilean water company Aguas Nuevas as a consequence of the previously mentioned uncertainties. **As a reminder, Aguas Andinas, Suez's subsidiary in the Chilean regulated water activity, represents about 14-15% of Suez's EBITDA and about 23-24% of Suez's EBIT**.

- **Lower temperatures** than average which would imply weaker water volumes.

4.2. Recycling & Recovery Europe: light at the end of the tunnel?

We expect EBITDA and EBIT in the Recycling & Recovery division to respectively increase by 9.5% and 3.1% in 2017 on an organic basis.

We notably expect volumes treated to rise by 3.6% in FY 2017 on the back of **1/**organic growth in Suez's existing capacities inherent in the slight rebound observed in European industrial production (re. below); **and 2/**the full-year impact of recent commissioning (Poznan in Poland, West London and Merseyside in the UK in Q4-16) and future commissioning in 2017 (Surrey and Cornwall in the UK).

The company's management is fairly reassuring in our view as it stated for the first time in about three years, that the month of January was in line with budget.

In all, this should strongly spur the division's EBITDA growth on top of the **solid contribution expected from Suez's cost-savings programme** (we estimate 40% of overall savings to be implemented by the group this year will be completed in the R&V division). The negative impact of last year's electricity prices (EUR27m EBIT headwind) should not be renewed in 2017 with Suez being 75% hedged.

EBIT organic growth should however be more limited (at 3.1% though above the 2% reached in FY-16) **due to provision reversals booked in 2016** for c. EUR70m **net**).

On a reported basis, we expect the division's EBIT to be broadly flat yoy on the back of a slight negative impact from the EUR/GBP exchange rate and the **expected deconsolidation of the Finnish waste subsidiary** (Suez indicated the subsidiary generated around EUR70m in revenues, we assumed a 10% EBITDA margin hence a mere EUR7m scope headwind).

Fig. 22: Recycling & Recovery Europe – Key metrics (2015-2018e)

Waste	**2015A**	**2016A**	**2017e**	**2018e**
Revenues	6,357	6,302	6,314	6,410
YoY change	-	*(0,9%)*	*0.2%*	*1.5%*
Organic growth	-	*0,6%*	*1.9%*	*1.5%*
EBITDA	**767**	**748**	**809**	**848**
EBITDA margin	*12,1%*	*11,9%*	*12.8%*	*13.2%*
YoY change	-	*(2,4%)*	*8.2%*	*4.7%*
Organic growth	-	*(2,0%)*	*9.5%*	*4.7%*
EBIT	**306**	**310**	**311**	**341**
EBIT margin	*4,8%*	*4,9%*	*4.9%*	*5.3%*
YoY change	-	*1,5%*	*0.3%*	*9.6%*
Organic growth	-	*2,0%*	*3.1%*	*9.7%*

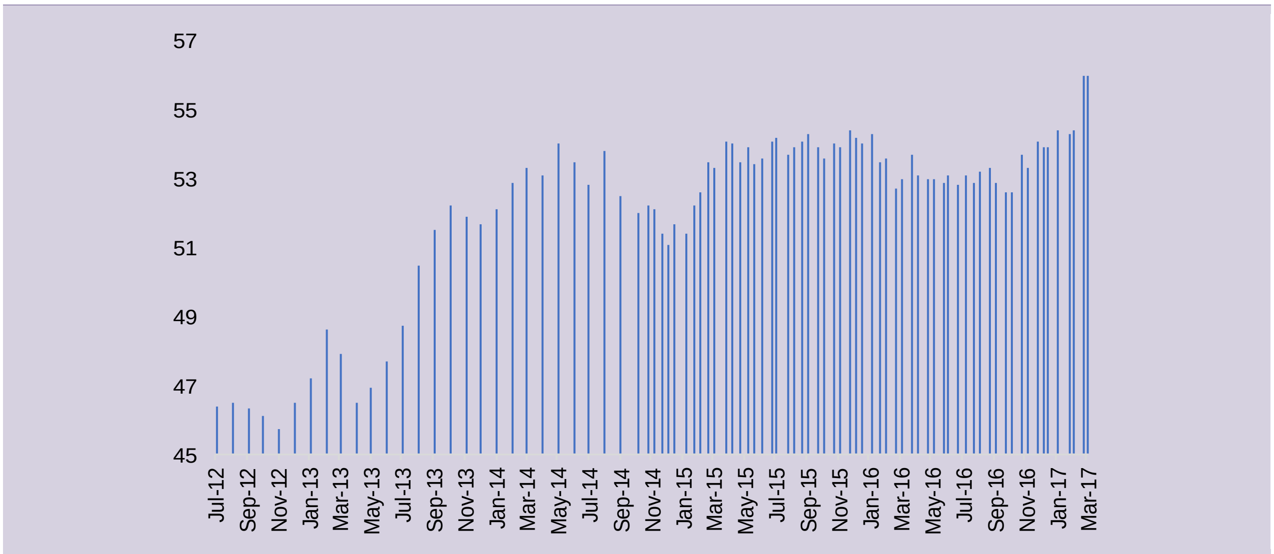
Source: Company Data; Bryan, Garnier & Co ests.

Main upside to our estimates:

- **Rebound in raw material prices** (notably plastic and scrap metal whose price variations negatively impacted Suez's metrics in 2016);

- **Higher-than-expected impact of the European industrial production recovery**: the **Europe Markit PMI** stood at 56.0 for February 2017 vs. 54.4 the month before, representing the **highest level seen for about six years**. This appears to be the **main short-term catalyst** in our view given the historically high correlation observed between Eurozone PMI and organic growth in the waste business. As a reminder, **we previously highlighted that a 1% increase in treated volumes would have a near EUR30-35m positive impact on EBITDA and a 4-5% positive impact on EPS.**

Fig. 23: Strong increase in Eurozone PMI – highest level for about six years



Source: Markit; Bryan, Garnier & Co ests.

__Main risk to our estimates:__

- **Slowdown in the recovery of European industrial production,** which could bear the brunt of a potential unsupportive political context, particularly in H2 2017 (French presidential and legislative elections in April/May and June 2017 and German elections in September 2017).

4.3. International: still the main organic growth engine

We expect EBITDA and EBIT in the International division to respectively increase by 6.8% and 7.2% in 2017 on an organic basis.

Note that **we integrated the contribution from the recent operation with NWS Holding** (c. EUR70m positive impact on revenues, c. EUR40m positive impact on EBITDA, c. EUR30m positive impact on EBIT, marginal impact on the group's bottom line). Despite this operation, we expect the scope effect at the EBIT level to be slightly negative given the EUR36m Derun-linked provision reversal booked by the group in 2016.

Note also that our EBIT organic growth is somewhat helped by provisions booked in 2016 (EUR18m negative impact on EBIT in 2016 despite the previously mentioned EUR36m provision reversal). Consequently, **we expect EBIT organic growth to reach 7.2%, bang in the middle of the**

company's objective (6-8%, broadly in line with the group's revenue objectives for the international division).

Fig. 24: International – Key metrics (2015-2018e)

International	2015A	2016A	2017e	2018e
Revenues	3,998	4,217	4608	4851
YoY change	*-*	*5,5%*	*9.3%*	*5.3%*
Organic growth	*-*	*4,7%*	*5.3%*	*5.3%*
EBITDA	**772**	**745**	**796**	**846**
EBITDA margin	*19,3%*	*17,7%*	*17.3%*	*17.4%*
YoY change	*-*	*(3,5%)*	*6.8%*	*6.4%*
Organic growth	*-*	*9,0%*	*4.7%*	*6.4%*
EBIT	**566**	**496**	**538**	**576**
EBIT margin	*14,2%*	*11,8%*	*11.7%*	*11.9%*
YoY change	*-*	*(12,4%)*	*8.5%*	*7.1%*
Organic growth	*-*	*5,5%*	*7.2%*	*7.1%*

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

Main upside to our estimates:

- **Donald Trump's potential infrastructure programme**. During his first address to Congress, Mr Trump said he will ask "*the Congress to approve legislation that produces a USD1 trillion investment in the infrastructure of the USA financed through both public and private capital*". **No information has however been unveiled regarding both the timing and the financing**. We believe Suez could be in a good position to benefit from such a plan notably thanks to its **solid presence in the regulated water segment**. As a reminder, in 2016, Suez's regulated water subsidiary in the US generated revenues of c. **EUR508m**, EBITDA of c. **EUR235m** and EBIT of c. **EUR173m**.

Main risk to our estimates:

- **A slower than expected recovery in the US equipment market**;

- Uncertainties over the current **political context in the USA** with the recent election of Donald Trump

4.4. Integration of GE Water

4.4.1. Main assumptions

We have assumed GE Water contributes to Suez's 2017 earnings from August 2017. Our estimates are based on the following:

- GE Water has a normative **EUR255m** EBITDA in line with the transaction's implied multiples;

- In line with Suez's indications, we have assumed about **80% of the EUR65m** in cost synergies will be achieved by year three with no synergies achieved in year one;

- **We have adopted a conservative view on revenue synergies as we do not include any of them**;

- We have assumed **2%** organic growth at the EBITDA level for 2017 and **3.5**% organic growth for 2018e-2021e, which highlights a more **conservative view** than Suez given the company's indications of a 5% mid-term CAGR;

- We have assumed a **75% normative EBIT/EBITDA ratio** (management indications) for 2016 implying 2016 EBIT of around **EUR190m** for GE Water. We then plugged a normative **3%** annual increase in D&A;

- Contrary to Suez's assumptions, **we do integrate implementation costs** in our computation (equal to one year of costs synergies digressively over 2017-2019);

- We have assumed the **EUR1.1bn** long-term bond will be funded with a **1.5%** interest rate implying an annual EUR17m in additional financial expenses;

- We have assumed the **EUR600m** hybrid bond will be funded with a **4.0%** interest rate implying a yearly EUR24m coupon. As we expect the first hybrid coupon payment to occur in 2018, we have assumed **no hybrid charge booked in Suez's P&L for FY-17**;

- We have assumed a **20.0%** discount to TERP for Suez's **EUR750m** capital increase leading to the creation of about **69m** new shares. No information has been unveiled by the group regarding the terms of this capital increase (rights issue? ABB?). Note that in accordance with IFRS rules, we have used a monthly average number of shares for FY-17.

- Finally we have used a **30%** normative tax rate and a **30%** minorities' stake, which will be held by Caisse de Dépôt et de Placement du Québec (CDPQ). **Theoretically, CDPQ will also hold a 30% stake in Suez's existing industrial water business.** We have however assumed Suez's existing bottom line in this business is marginal given the company was still looking for critical mass (only EUR500m in revenues until now).

4.4.2. Accretion/Dilution analysis

As a result, we calculate that **the acquisition of GE Water would be c. 0.4% dilutive in 2017e** for Suez given the EUR30m in implementation costs we expect, and the fact that the creation of new shares inherent to the EUR750m capital increase will be unlikely to be offset by the **five months of EBITDA contribution to the company.**

2018e will be the first full-year contribution of GE Water and we expect a c. 2.5% EPS accretion.

After completion of expected cost and revenue synergies in 2021e, we estimate that the acquisition should be accretive to the tune of 11.0% for Suez.

Fig. 25: Accretion/Dilution analysis (% change)

P&L GE Water	2017e	2018e	2019e	2020e	2021e
EBITDA GE Water	**108**	**287**	**331**	**347**	**363**
D&A	(27)	(68)	(70)	(72)	(74)
EBIT GE Water	81	219	261	275	290
Implementation costs	(30)	(25)	(10)	0	0
Financial expenses	(7)	(17)	(17)	(17)	(17)
Pre-tax income	44	177	234	259	273
Taxes	(13)	(53)	(70)	(78)	(82)
Net income	31	124	164	181	191
Minorities	(9)	(37)	(49)	(54)	(57)
Net Income, Group Share	22	87	115	127	134
Hybrid coupon	0	(24)	(24)	(24)	(24)
Net income post-hybrid coupon GE Water	22	63	91	103	110
Net income Suez	414	457	479	515	520
Cumulated net income post-hybrid coupon	**436**	**519**	**570**	**618**	**630**
New # of shares (weighted average)	592.4	632.7	632.7	632.7	632.7
New EPS	0.74	0.82	0.90	0.98	1.00
Old EPS	0.74	0.80	0.85	0.89	0.90
EPS Accretion/Dilution (%)	**(0.4%)**	**2.4%**	**6.5%**	**9.6%**	**11.0%**

Source: Bryan, Garnier & Co ests.

4.4.3. Sensitivity analysis

Below we present **two sensitivity analyses on our FY-21e EPS accretion figure with**:

- FY-21e accretion depending on FY-18e-21e EBITDA organic growth and % of cost synergies completed by Suez;

- FY-21e accretion depending on the LT bond interest rate and the capital increase's discount to TERP

Fig. 26: FY-21e accretion depending on FY18e-21e EBITDA organic growth and % of cost synergies achieved by Suez

		EBITDA organic growth 2018e-2021e						
		2,0%	2,5%	3,0%	3,5%	4,0%	4,5%	5.0%
Percentage Of Cost Synergies Achieved	60%	7.3%	7.8%	8.3%	8.8%	9.3%	9.8%	10.3%
	70%	7.9%	8.4%	8.9%	9.4%	9.9%	10.4%	10.9%
	80%	8.5%	8.9%	9.4%	9.9%	10.4%	10.9%	11.4%
	90%	9.0%	9.5%	10.0%	10.5%	11.0%	11.5%	12.0%
	100%	9.6%	10.1%	10.5%	11.0%	11.5%	12.1%	12.6%
	110%	10.1%	10.6%	11.1%	11.6%	12.1%	12.6%	13.1%

Source: Bryan, Garnier & Co ests.

Fig. 27: FY-21 accretion depending on LT bond interest rate and capital increase's discount to TERP

		LT bond interest rate %				
		1.0%	1.5%	2.0%	2.5%	3.0%
Discount To TERP	10%	13.0%	12.5%	12.1%	11.6%	11.1%
	15%	12.3%	11.8%	11.4%	10.9%	10.4%
	20%	11.5%	11.0%	10.6%	10.1%	9.6%
	25%	10.6%	10.1%	9.7%	9.2%	8.7%
	30%	9.6%	9.1%	8.6%	8.2%	7.7%

Source: Bryan, Garnier & Co ests.

We deduce from our analysis that:

- Every **+/- 5%** change in our discount to TERP assumptions implies an average **+/- 100bps** impact on our FY-21e EPS accretion figure;

- Every **+/- 50bps** change in our LT bond interest rate assumption implies a c. **+/- 50bps** impact on our FY-21e EPS accretion figure;

- Every **+/- 10%** change in our assumption of costs synergies completion implies a c. **+/- 60bps** impact on our FY-21e EPS accretion figure;

- Every **+/- 50bps** change in our EBITDA organic growth assumption over the 2018e-2021e period implies a c. **+/- 50bps** impact on our FY-21e EPS accretion figure.

Note also that if we add the EUR200m in revenue synergies from the operation targeted by Suez, we estimate the FY-21e accretion figure will stand at around 14.0%.

4.4.4. Impact on debt ratios set to be limited

The impact of the acquisition of GE Water on Suez's financial ratios should remain limited in our view due to the funding scheme, which will be used by the company (EUR600m hybrid bond, EUR750m capital increase, EUR700m equity provided by Caisse de Dépôt et Placement du Québec). **We estimate Suez should exceed its target of a 3.0x net debt/EBITDA ratio in 2017** (at c. 3.3x) **but only due to the phasing of the integration of GE Water (five-month consolidation in 2017).**

The company should be back to more standard ratios as soon as 2018 (3.1x in 2018, 3.0x in 2019 and 2.9x in 2020). As a reminder, Suez has a **3.0x** net debt to EBITDA ratio **target**, which was set up before the acquisition of GE Water.

Fig. 28: Back to standard net debt/EBITDA ratios as soon as 2018

Solvency ratios	2015	2016	2017e	2018e	2019e	2020e
Net debt	8 083	8 042	9 223	9 051	8 913	8 721
EBITDA	2,751	2,651	2,850	3,134	3,270	3,380
Net financial debt/ EBITDA	**2,94x**	**3,03x**	**3,33x**	**3,06x**	**2,96x**	**2,88x**

Source: Bryan, Garnier & Co ests.

5. Estimates summary

5.1.1. Key estimates

Excluding the integration of GE Water, our estimates are significantly revised downward at both the EBITDA and EBIT levels by c. 5% and 6%, respectively, on average over the 2017e-2020e period mainly due to lower-than-expected growth in the water segment while we adopt more cautious assumptions in the company's international division.

Fig. 29: Change in estimates – pro-forma (2017e-2019e)

	New			Old			Var %		
	2017e	**2018e**	**2019e**	**2017e**	**2018e**	**2019e**	**2017e**	**2018e**	**2019e**
Revenues	15,740	16,079	16,428	15,949	16,422	16,893	(1,3%)	(2,1%)	(2,8%)
EBITDA	**2,742**	**2,839**	**2,923**	**2,864**	**2,980**	**3,083**	**(4,3%)**	**(4,7%)**	**(5,2%)**
EBIT	1,310	1,382	1,441	1,391	1,470	1,536	(5,8%)	(6,0%)	(6,2%)

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

In all, we expect Suez's EPS pre-hybrid coupons to grow c.**10.5%** on average per year over the same period. Similarly, EPS post-hybrid coupons is expected to grow c. **10.0%** on average per year over the same period.

Despite the acquisition of GE Water and the expected slight EPS dilution we forecast for 2017e (including implementation costs), **we still consider** – in line with company's comments - **the EUR0.65 dividend per share Suez paid for FY-2016 as a floor**. We expect this level to be broadly stable until 2019 and to pick up from 2020 once a large part of the expected synergies coming from the acquisition of GE Water will be completed by the Group.

As a reminder, we assume GE Water will be consolidated from 1st August 2017e implying **our 2017e figures only integrated a five-month consolidation of GE Water.**

Fig. 30: Key P&L reported estimates (2017e-2020e)

P&L	2016A	2017e	2018e	2019e	2020e
Revenues	15,322	16 547	18 125	18 584	19 087
EBITDA	**2 651**	**2 850**	**3 126**	**3 253**	**3 355**
Margin %	17.3%	17,2%	17,2%	17,5%	17,6%
o/w Water Europe	*1,277*	*1 273*	*1 281*	*1 296*	*1 307*
o/w Recycling & Recovery Europe	*748*	*809*	*848*	*883*	*921*
o/w International	*745*	*796*	*846*	*880*	*916*
o/w GE Water	*0*	*108*	*287*	*331*	*347*
EBIT	**1,282**	**1,391**	**1,602**	**1,702**	**1,774**
o/w Water Europe	*611*	*607*	*612*	*623*	*630*
o/w Recycling & Recovery Europe	*310*	*311*	*341*	*367*	*394*
o/w International	*496*	*538*	*576*	*597*	*620*
o/w GE Water	*0*	*81*	*220*	*262*	*276*
Implementation costs	0	(30)	(25)	(10)	0
EBIT Adjusted	**1,290**	**1,361**	**1,577**	**1,692**	**1,774**
Net Financials	(424)	(441)	(459)	(481)	(483)
Pre-tax results	867	920	1,118	1,212	1,291
Taxes	(244)	(215)	(274)	(301)	(324)
Minorities	(203)	(241)	(273)	(289)	(298)
Net Income, Group Share	**420**	**464**	**571**	**622**	**669**
Hybrid coupons	(28)	(28)	(52)	(52)	(52)
Net Income post hybrid	**393**	**436**	**519**	**570**	**618**
# of shares	547	592	633	633	633
EPS pre-hybrid coupons	**0.77**	**0.78**	**0.90**	**0.98**	**1.06**
EPS post-hybrid coupons	**0.72**	**0.74**	**0.82**	**0.90**	**0.98**

Source: Bryan, Garnier & Co ests.

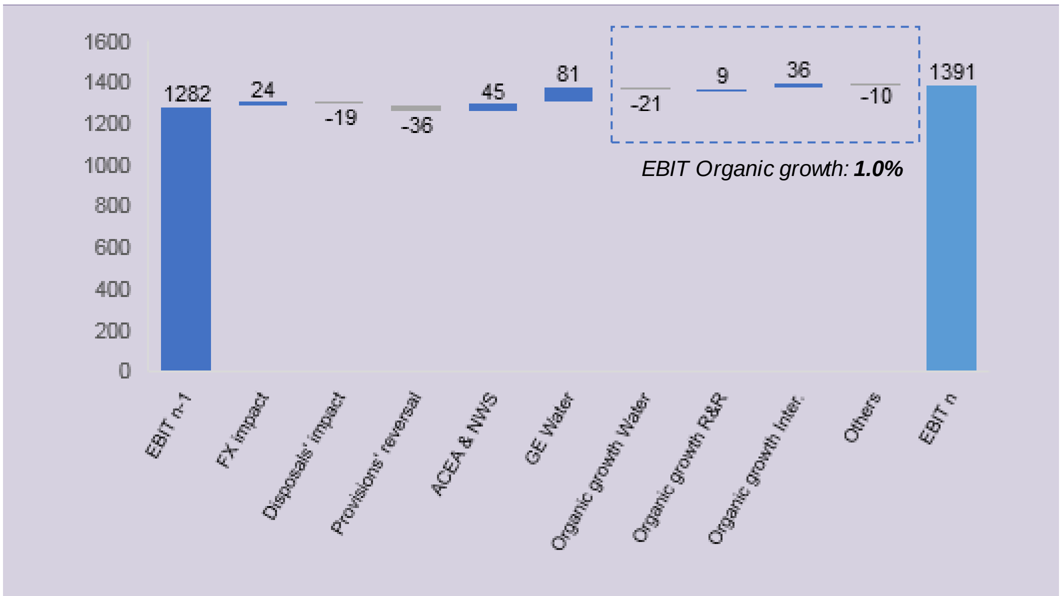
5.1.2. We expect 1% EBIT organic growth for 2017

In all, we expect 1.0% organic growth at the EBIT level, in line with Suez's guidance for "slight organic growth".

As for **FX and scope impacts**, we notably expect:

- A **EUR24m** positive FX impact mainly on the back of a positive EUR/CLP evolution;
- A **EUR19m** negative impact stemming from the deconsolidation of Suez's Finnish activities and from the disposal of the company's participation in Bristol Water;
- We expect this negative impact to be more than offset by the positive scope impact stemming from the transaction with ACEA and NWS Holding (**EUR45m** positive impact)

Fig. 31: EBIT bridge 2016A-2017e



Source: Bryan, Garnier & Co ests..

6. Valuation

As a reminder, we value Suez via a **sum-of-the parts** valuation.

Our weighted average **WACC** and our weighted average **beta** came out at **6.1%** and **1.05**, respectively.

Fig. 32: BG Assumptions

	Weighted Average WACC	Weighted Average LT growth	Weighted Average Beta
Water Europe	5.9%	1.0%	1.05
Recycling & Recovery Europe	5.9%	1.0%	1.00
International	6.1%	2.0%	1.05
GE Water	6.7%	2.0%	1.10
Suez	**6.1%**	**1.1%**	**1.05**

Source: Bryan, Garnier & Co ests.

We have integrated GE Water into our SOTP with an estimated c. **EUR3.8bn** Enterprise Value above the EUR3.2bn EV Suez and CDPQ paid for the acquisition. Note we have also used an unchanged **9.5x** EV/EBITDA multiple for the company's regulated water assets in the US and a revised downward **9.0x** EV/EBITDA multiple for the company's regulated water assets in Chile (vs. 9.5x initially on the back of the previously mentioned regulatory uncertainties).

In all, **our SOTP leads us to a EUR16.5 Fair Value** (FV) per share implying a c. **16% upside** vs. Suez's current share price.

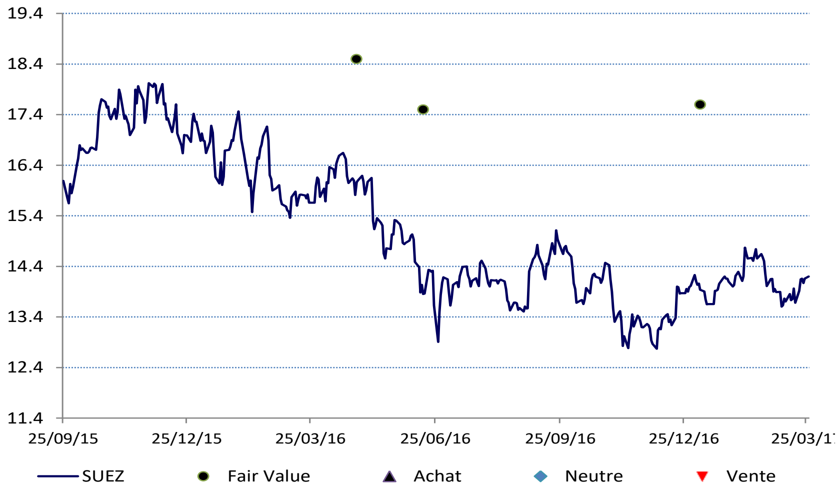
Fig. 33: Suez - Sum-of-the parts (SOTP)

SEV SOTP valuation	Value (EURm)	Method	Value per share
Water Europe - Non regulated	5,667	Discounted CF	9.0
Aguas Andinas – Regulated water Chile	3,735	9.0x FY-17e EV/EBITDA multiple	5.9
Recycling & Recovery Europe	6,196	Discounted CF	9.8
International - Excluding United Water Regulated	4,813	Discounted CF	7.6
United Water – Regulated Water US	2,316	9.5x FY-17e EV/EBITDA multiple	3.7
Others	(816)	6.0x FY-17e EV/EBITDA multiple	(1.3)
GE Water	3,772	Discounted CF	6.0
Implied Enterprise Value (EV)	**25,682**	**-**	**40.6**
Net debt at end 2017e	(9,223)	-	(14.6)
Integration of hybrid debt @ 100%	(1,600)	-	(2.5)
Provisions	(2,062)	Book Value	(3.3)
Minority interest	(3,147)	14x P/E for non-regulated assets 17x P/E for regulated assets	(5.0)
New minorities inherent to GE Water's transaction	(1,131)	30% of GEW EV	(1.8)
Financial assets	(1,900)	Book Value	3.0
o/w Associates (exc. ACEA, already integrated in our EV)	*785*	*Book Value*	*1.2*
o/w other financial assets	*1,115*	*Book Value*	*1.8*
Total implied Equity value	**10,419**	**-**	**16.5**
Number of shares	633	-	
Equity value per share (rounded)	**16.5**	-	
Current share price	*14.2*	-	
Up/Downside	*16.2%*	-	

Source: Bryan, Garnier & Co ests.

Price Chart and Rating History

Suez



Ratings

Date	Ratings	Price
08/09/15	BUY	EUR15.96
30/09/14	NEUTRAL	EUR13.155

Target Price

Date	Target price
09/03/17	Under review
06/01/17	EUR17.6
16/06/16	EUR17.5
28/04/16	EUR18.5
28/04/16	EUR18.5
17/07/15	EUR19
02/04/15	EUR18
13/03/15	EUR17
09/12/14	EUR16
30/09/14	EUR14

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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 48,2% NEUTRAL ratings 36,6% SELL ratings 15,2%

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