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**Summary:**  
**Veolia Environnement S.A.**

**Primary Credit Analyst:**

Hugues De La Presle, Paris (33) 1-4420-6666; hugues\_delapresle@standardandpoors.com

**Secondary Credit Analyst:**

Beatrice de Taisne, London (44) 20-7176-3938; beatrice\_de\_taisne@standardandpoors.com

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## Summary:

# Veolia Environnement S.A.

**Credit Rating:** BBB+/Stable/A-2

## Rationale

The ratings on France-based environmental services group Veolia Environnement S.A. (VE) are underpinned by its leading positions worldwide in water utility and waste management activities, and its strong European presence in energy services. VE benefits from diversified and recurring revenues under long-term municipal concessions and shorter term industrial outsourcing contracts.

As a result of its focus on operating service contracts rather than on owning assets, VE is, however, exposed to a degree of price competition at renewal time and renewal risk at contract maturity. Furthermore, VE is not immune to the current economic downturn: Given the slowdown since the summer in its waste activities and to a lesser extent in water, the group has further revised its guidance and now only targets flat EBITDA in 2008 compared with 2007. In response, the group is further scaling down its net investments to €4 billion in 2008 from €6.1 billion in 2007. It moreover plans to be free cash flow positive in 2009 (after investments, disposals, and dividends), which is a very substantial shift, the group having been systematically free cash flow negative in recent years because of substantial growth investments and a generous dividend policy. In addition, VE has announced a disposal program of at least €1.5 billion to be completed in 2008/2009.

From an operational perspective, VE intends to focus in the near term on delivering its €400 million cost-cutting program to be completed by 2010. It will also seek to further integrate recent lower margin acquisitions.

The group remains broadly diversified by contract and by business. It has leading positions in water (41% of first-half 2008 consolidated EBITDA before central costs of €46 million), waste (32%), energy services (20%), and transport (7%). It is also highly diversified geographically, with 58% of sales generated outside France in first-half 2008, notably in the rest of Europe as well as the U.S. and the Asia-Pacific region.

VE's financial profile is moderate, reflecting the group's focus in recent years on growth and shareholder value. It was, however, significantly boosted by the substantial €2.6 billion capital increase completed in 2007 to refinance acquisitions. The group's financial profile is currently in line with our expectations for the ratings--with funds from operations (FFO) coverage of adjusted net debt in the 12 months to June 2008 of about 18.5%--and is expected to remain so, with the shortfall in earnings and cash flows being offset by reduced investments and some disposals.

### Short-term credit factors

The 'A-2' short-term rating is supported by VE's satisfactory liquidity, its recent strategic shift (in particular its aim to be free cash flow positive in 2009, which will entail a substantial reduction in investments), and the visibility provided by its contractual revenues.

VE currently has about €3.2 billion of immediately available cash, as well as a €4 billion backup line maturing in 2012 (of which €1,150 million is currently drawn), and €1,025 million of undrawn committed bilateral lines (of which €175 million matures in 2008), which VE is currently seeking to renew, €350 million in 2009, and €500

million in 2010. None of VE's bank lines contain financial covenants. VE has recently drawn, for the first time since its inception, on its €4 billion backup line to refinance its Polish operations (€350 million) and to make €800 million available in cash to cover the bulk of its outstanding commercial paper (CP).

Factoring in VE's reduced investments in 2008 and its objective of slightly reducing debt in 2009, the group has substantial liquidity to cover its short-term debt. In June 2008, VE's debt maturing over the next 18 months, i.e. until the end of 2009, stood at €3.4 billion, of which:

- €0.7 billion of overdrafts;
- €302 million of bonds, €200 million of which was repaid in August 2008;
- €285 million of CP, which has since grown to €850 million;
- €430 million of receivable securitizations;
- €166 million of accrued interest; and
- €143 million corresponding to a put option by minorities on a waste business that is majority owned by VE.

The balance of €1.2 billion corresponds to bank debt at the level of operating companies and is spread over a large number of companies. Except as stated for the bonds and the CP, these amounts have remained broadly stable since June 2008. Beyond 2009, VE has €1.6 billion of debt in total maturing over 2010 and 2011; this is essentially bank debt, which the group aims to roll over.

## Outlook

The stable outlook is underpinned by the resilience of VE's contractual revenues--despite the recent profit warnings--and the group's credit-supportive strategic shift of reducing investments. It also reflects our expectation that the group will maintain a financial profile in line with current ratings, i.e. FFO coverage of adjusted net debt at the upper end of the 15%-20% range. The ratings will come under pressure if VE's financial profile stays at or falls below the lower end of this range.

Given VE's recent operating performance and its financial profile, the ratings offer limited upside.

### **Additional Contact:**

Infrastructure Finance Ratings Europe; InfrastructureEurope@standardandpoors.com

### **Additional Contact:**

Infrastructure Finance Ratings Europe; InfrastructureEurope@standardandpoors.com

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