

CREDIT OPINION

27 April 2022

New Issue

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RATINGS

SUEZ (former Sonate Bidco)

Domicile	Paris, France
Long Term Rating	Baa2
Type	LT Issuer Rating - Dom Curr
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.

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SUEZ (former Sonate Bidco)

Update following assignment of definitive rating

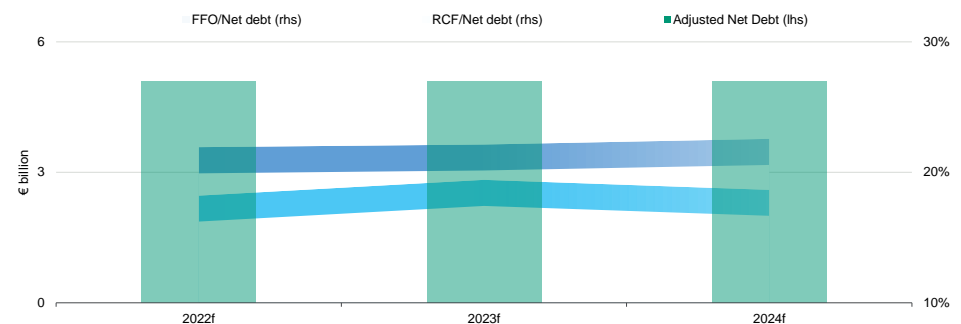
Summary

The credit quality of [SUEZ \(former Sonate Bidco\)](#) (Baa2 stable), the holding company that acquired a range of [SUEZ's](#) (Baa1, stable) water and waste assets from [Veolia Environnement SA](#) (Veolia, Baa1 stable), is underpinned by (1) the group's scale and positioning, with assets generating revenue in excess of €7.5 billion in 2021; (2) the low risk profile of its water business, which provides essential services to many low-risk counterparties in the public sector; (3) the diversification of its revenue base by business, contract type and somewhat by geography; (4) a strong integration across the value chain for water, sewage and waste treatments; and (5) underlying positive structural dynamics with tightening regulations on water and waste that will benefit from greater expertise and the rising sophistication in operations.

These positives factors are balanced by (1) the group's exposure to economic cycles through its waste activities in France given the prevalence of industrial clients in the segment and the paucity of regulated activities; (2) a fairly leveraged financial profile, as reflected by its expected Moody's-adjusted funds from operations (FFO)/net debt of 20%-21% in the first few years of operations, with no intention to reduce leverage in subsequent years; and (3) a dividend policy that appears to favour shareholders over creditors with a payout ratio potentially exceeding 100% over 2022-23, subject to shareholders' commitment to maintain an investment-grade rating.

Exhibit 1

Stabilisation of the financial metrics over 2022-24



The 2022-23 estimates represent our forward view, not the view of the issuer.
 Source: Moody's Financial Metrics™

Credit strengths

- » Scale, positioning and expertise of the group
- » Low risk profile of its water business and the strong integration across the value chain for water, sewage and waste treatments
- » Strategy focusing on the consolidation of existing positions, with a priority for organic growth and margin improvement resulting in higher cash flow
- » Supportive long-term industry trends

Credit challenges

- » Exposure to macroeconomic cycles through its waste business in France and to industrial customers
- » Leveraged profile, with no intention to reduce leverage in subsequent years
- » Dividend policy, which appears to favour shareholders over creditors
- » Operational turbulences induced by the carve-out and the new ownership

Rating outlook

The stable outlook reflects our expectation that the consolidated financial metrics for SUEZ (former Sonate Bidco) will be commensurate with a Baa2 rating, including FFO/net debt at least in the high teens in percentage terms. It further assumes successful execution of the strategic plan following the carve out, including the cost reduction programme.

Factors that could lead to an upgrade

A rating upgrade is unlikely in the next two years given the need for a new management team to build a track record. In the longer term, upward pressure on the ratings could develop if SUEZ (former Sonate Bidco) were to achieve FFO/net debt approaching the mid-20s in percentage terms on a sustained basis. Any potential upgrade would also take into consideration changes in the company's scale and diversity across geographies.

Factors that could lead to a downgrade

SUEZ's (former Sonate Bidco) ratings could be downgraded if credit metrics appear likely to remain persistently below the guidance for the Baa2 rating, which includes FFO/net debt in the high teens in percentage terms because, for example, of weaker-than-expected operating performance, a dividend policy resulting in payments exceeding the free cash flow before dividends over the period or a more aggressive financial policy than anticipated.

Key indicators

SUEZ (former Sonate Bidco)

	Dec-19	Dec-20	Moody's 12-18 Month Forward View
(FFO + Interest Expense) / Interest Expense	N/A	N/A	10x - 11x
FFO / Net Debt	N/A	N/A	20% - 21%
RCF / Net Debt	N/A	N/A	17% - 18%

All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Moody's forward view is Moody's opinion and does not represent the views of the issuer.

Source: Moody's Investors Service

Profile

Headquartered in Paris, SUEZ (former Sonate Bidco) provides environmental services to municipalities and industrial customers mainly in five countries and holds smaller positions in Asia and Africa. The group comprises two business lines:

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.

1. Water mostly covers municipal water activities under concession regimes, with strong positions in France, where the group is the second-largest group, and in Australia, with a 14% market share in the unregulated water market. SUEZ (former Sonate Bidco) also runs operations directly or indirectly in the Czech Republic, Morocco (whose closing is still subject to administrative authorisations expected by the summer 2022) and Italy. Water is the largest division, contributing around 48% of revenue in the first nine months of 2021.
2. Recycling and Recovery includes waste collection, elimination, sorting and recycling with operations in France, where SUEZ (former Sonate Bidco) is the largest group in this industry, as well as in Africa and China. The segment contributed around 47% to revenue in the first nine months of 2021.

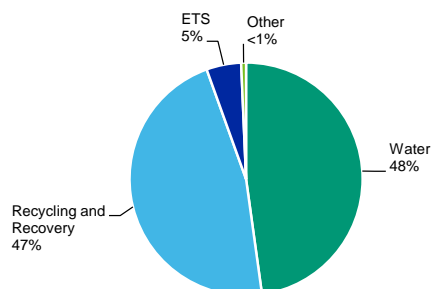
The group developed a technology division, Environmental Technology Solutions (ETS), which sells directly digital solutions associated with the contracts.

We expect the group to generate around €7.5 billion revenue and €1.5 billion EBITDA in 2021, with operations outside France to contribute around 40% of revenue in 2021.

SUEZ's (former Sonate Bidco) ultimate shareholders comprise a consortium led by the infrastructure funds Meridiam and GIP (holding 40% each), alongside the Caisse des Dépôts et Consignations and CNP Assurances (20%).

Exhibit 3

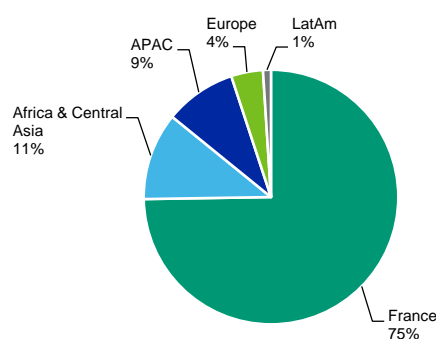
Revenue split by activity For the first nine months of 2021



Total over 100% due to rounding effects.
Source: Company's reports

Exhibit 4

Revenue split by geography For 2019



Financials of 2019 reflect a better view of the company's business profile because of the effect of the pandemic on the waste division in 2020.
Sources: Company's reports and Moody's Investors Service

Detailed credit considerations

SUEZ (former Sonate Bidco) has emerged from the Veolia-SUEZ merger and with high leverage

SUEZ (former Sonate Bidco) is the French holding company that acquired SUEZ's French water and waste assets, some of its unregulated municipal water operations outside France, and global digital and environmental activities from Veolia. SUEZ (former Sonate Bidco) bought related assets for €10.4 billion, including an earnout of around €300 million to be paid later in 2022. Acquisition of the assets was financed through an 18-month bridge loan of €2.25 billion and a four-year term loan of €2.25 billion. SUEZ (former Sonate Bidco) plans to refinance the bridge loan through bond issuance in the course of 2022, subject to market conditions.

SUEZ (former Sonate Bidco) has a fairly leveraged financial profile, as measured by reported net debt/EBITDA in excess of 3x, with no plan to reduce gearing in subsequent years. This financial profile results from the prevalence of two infrastructure funds in the shareholding structure. If cash flow is stronger than expected, then we expect additional capital spending, higher dividends or acquisitions, even if we assume that the strategy will focus on organic growth over the first two to three years of operations.

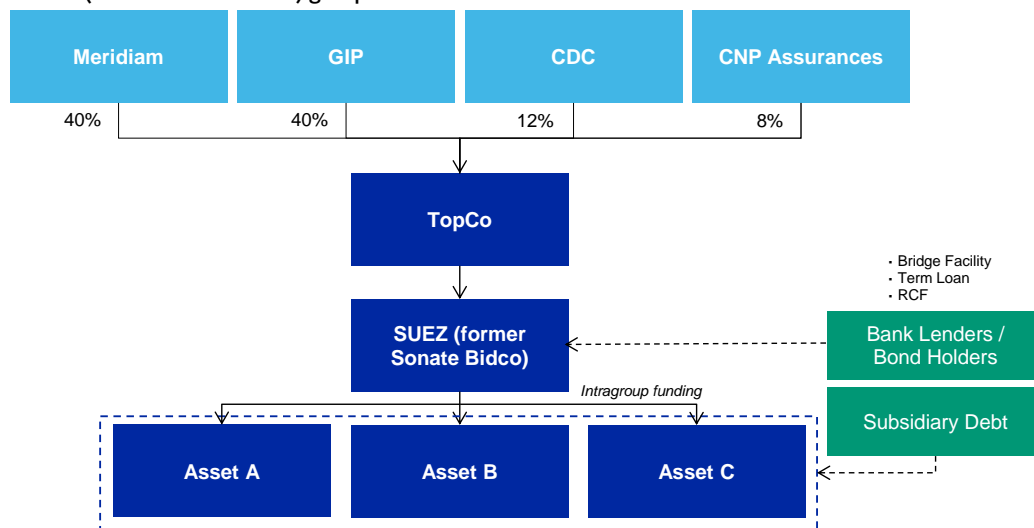
The consortium does not intend to increase the group's leverage and is committed to maintaining an investment-grade rating through a flexible dividend policy.

Supportive debt contractual features

Our assessment of SUEZ's (former Sonate Bidco) financial profile takes into account the terms and conditions of the debt and the existence of an undertaking agreement, which, in combination with the consortium's anticipated financial policy, provide a framework consistent with a Baa2 rating.

Exhibit 5

SUEZ's (former Sonate Bidco) group structure



Sources: Company and Moody's Investors Service

We take into account that the acquisition was partly financed by bonds mandatorily redeemable in shares (the ORA - Obligations Remboursables en Actions) due 2057, issued by Sonate TopCo whose sole asset is 100% of the shares issued by SUEZ (former Sonate Bidco). Without effective ring-fencing between the companies, any debt at Sonate TopCo is relevant to consideration of the credit quality of SUEZ (former Sonate Bidco). However, the ORA has equity-like characteristics given that conversion is mandatory at maturity, after 35 years, at a fixed ratio; coupons may be deferred on a cumulative basis; it is deeply subordinated; there is no provision for default, cross-default or acceleration; and payments to the ORA holders are subject to a financial lockup covenant. Given the terms and characteristics of the ORA and assuming that shareholders will maintain a prudent level of headroom against the lockup covenant, the presence of the instrument does not constrain the ratings.

Future noteholders will benefit from further protections, including events of default resulting from any changes to the subordination provisions, payment restrictions or mandatory conversion provisions of the ORA; or a breach or termination of, or a significant amendment to, the undertaking agreement — the main purpose of which is to mirror these terms and conditions — entered into by, inter alia, SUEZ (former Sonate Bidco), its parent and ultimate shareholders.

We consider these features supportive of SUEZ's (former Sonate Bidco) Baa2 rating because they will limit the calls on the company's cash flow; and the expected restrictions against changes in the ORA's terms and conditions and the notification requirements in the public notes and in the undertaking agreement should maintain the ORA's credit-supportive qualities with respect to the notes, notwithstanding the private nature of the instrument.

Long term public sector contracts and diversification support cash flow stability

SUEZ (former Sonate Bidco) is the largest waste management and the second-largest water treatment company in France, with revenue likely to exceed €7 billion in 2021. The group provides essential services to many low-risk counterparties in the public sector, with exposure to municipalities representing around 70% of revenue. The group's credit profile is supported by its diversification and leading market positions across its water and waste businesses, mainly in France. The diversification of its revenue base by business and

contract type helps mitigate the strain on its earnings from a deterioration in any one activity and supports the relative stability of its cash flow.

SUEZ's (former Sonate Bidco) portfolio consists of around 2,000 contracts, which range from long-term concessions with low-risk counterparties in the public sector to short-term contracts with industrial and commercial (I&C) customers. Contracts vary by market and can be either capital intensive, which require 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, which require little investment.

However, the group is exposed to the risk that concessions that are not renewed at maturity: contract losses for SUEZ (former Sonate Bidco) over 2022-23 will mainly concern the contracts concluded with the cities of Bordeaux, Saint Etienne, Cannes and Strasbourg. The loss will represent cumulative revenue close to 5% of consolidated revenue by 2023. In the absence of new contract gains, those losses will strain SUEZ's (former Sonate Bidco) cash generation.

Positive sector dynamics but also growing competition

SUEZ (former Sonate Bidco) operates in sectors that are inevitably exposed to short-term economic pressures but benefit from positive long-term underlying global dynamics. These include population growth, the trend towards urbanisation and industrialisation, modernisation of infrastructure and rising living standards in emerging economies.

Together with the public concern over the effect of climate change on scarce resources and tightening environmental regulations, these positive dynamics support increasing demand for existing technologies for the provision of water, wastewater and waste management services, and new services and technologies that, for example, facilitate water conservation and waste recovery. Against this backdrop, competition — notably from Asian companies — is intensifying, especially in the lower part of the value chain. However, our assessment of SUEZ's (former Sonate Bidco) credit profile factors in its scale and ability to provide a wide range of services and technologies across business lines as competitive advantages.

Low risk water activities but with volume exposure

SUEZ (former Sonate Bidco) benefits from the low risk profile of its water business, which provides essential water and wastewater services to individuals and businesses, often on behalf of local municipalities. There is volume exposure but volatility is mainly subject to weather conditions (temperature and rainfall) and potentially macroeconomic trends, as illustrated by the recent pandemic. Demand for water also continues to experience a slow structural decline in advanced economies, especially in Europe, because of a more resource aware population, which translates, for example, into an increasingly higher adoption of water-efficient appliances and rising water price.

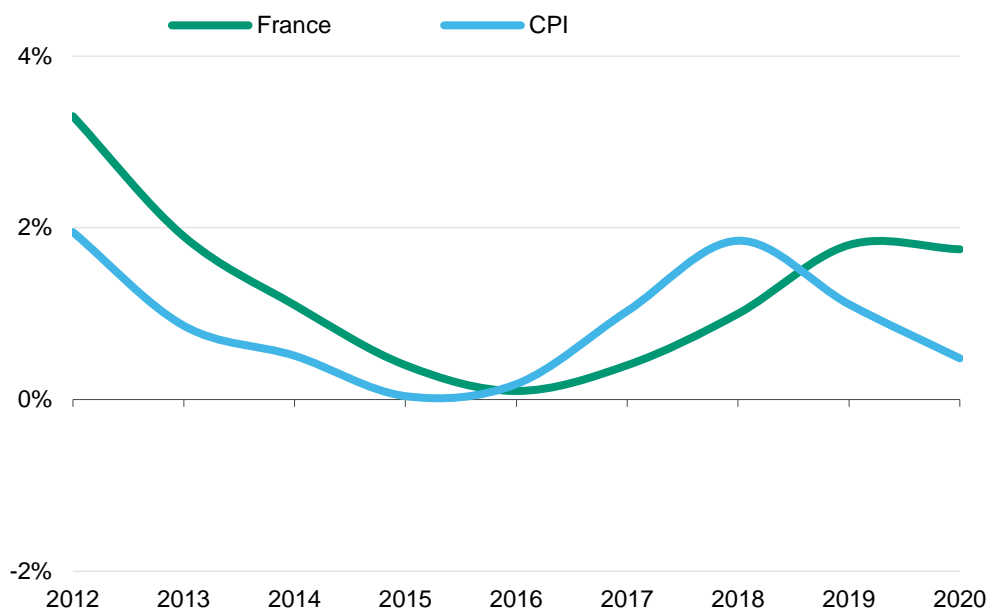
The market structure is, however, well established and the barriers to entry are high because of the entrenched knowledge of incumbent operators' assets under management, EU directives that resulted in complex operations because of laws and regulations on the quality of drinking water and the treatment of wastewater, and the benefits of critical mass.

In France, which represented around one-third of total revenue in 2021, SUEZ (former Sonate Bidco) has concession agreements, typically of 15 years, whereby it operates and maintains the local authority's infrastructure. The tariff paid by the consumer (usually the price per cubic metre) is increased based on a basket of indices. A typical renewal rate of around 75% provides revenue visibility and stability. The non-cyclical nature and stable structure of the French market for water and sanitation services provide a solid base of predictable earnings and cash flow. Water contracts are typically driven by inflation-linked indexation formulas and are designed to mirror the movements in the cost base (for example, wages and energy prices). Since 2014, inflation in France has been particularly weak but started to recover in 2017, rising above 1% for the first time since 2013 and stabilising at around +1.5% per year since 2019. The further rising inflation observed across Europe since the start of the energy crisis in Q4 2021, and exacerbated since the Ukraine invasion, will be credit positive, because it will allow for a full cost pass through to customers, although with a delay, with the group being committed to an efficiency gain programme up to €500 million by 2023.

Exhibit 6

Tariff indexation remains weak because of low inflation

SUEZ (former Sonate Bidco)'s water tariffs in France (annual percentage change)



Source: Company's reports

The waste business is exposed to cyclical macroeconomic conditions because of the prevalence of industrial customers and commodity prices

The waste business is more exposed to cyclical macroeconomic conditions than water, reflecting the higher proportion of I&C customers (around 30% of revenue), and contract terms that are more often linked to the volume collected or processed and, in turn, to industrial production. Changes in treated volume are typically correlated with industrial production in Europe.

The waste business is also exposed to raw material price volatility as a result of the rising contribution of recycled waste in the business mix, whereby SUEZ (former Sonate Bidco) purchases the collected waste to recycle at the fluctuating price of raw materials. Contract provisions include some pass-through mechanisms to share the volatility with industrial clients, although with a lag effect, which can weaken the segment's profitability when prices decline.

Earnings recovery from H2 2020 has continued in 2021, supported by the economic rebound

SUEZ (former Sonate Bidco) reported pro forma revenue of €5.5 billion in 9M 2021, up 17% from the previous year, driven by the Recycling and Recovery division in France, with the volume of treated waste back to the 2019 level and solid pricing dynamics supported by booming commodity prices. Volume in the Water France division is slightly up, but still below the 2019 level because of unfavourable weather conditions and a drop in demand associated to the pandemic-related measures. Pro forma EBITDA grew by 19% from €0.9 billion over the first nine months in 2020 to €1.1 billion over the same period in 2021, mainly resulting from increased volumes and reduction in expenses pertaining to maintenance for industrial assets, fees and external personnel costs.

We expect a continuation of the trends observed over the last 18 months, albeit to a lesser extent, with revenue growth supported by economic recovery, supplemented by tariffs revisions reflective of higher inflation and rising commodity prices, which will drive EBITDA up, in complement of the cost cutting programme. This supposes the absence of any escalation in the military conflict in Ukraine.

Over the next two to three years, we assume that SUEZ's (former Sonate Bidco) strategy will focus on consolidation of its existing positions, with priority given to organic growth including gains in market shares, and margin improvement through continuation of the substantial performance improvement and cost reduction plan initiated by SUEZ. Over a longer term, we also expect potential opportunistic small-to-medium-sized acquisitions in new geographies.

ESG considerations

In our assessment, environmental considerations include increasing environmental awareness and the regulatory push for reducing untreated water in the environment and increasing waste recycling. In this regard, climate change and governmental measures to mitigate it create business opportunities for SUEZ (former Sonate Bidco), acting in the exploitation of essential resources and treatment.

Social considerations are moderately material for SUEZ (former Sonate Bidco)'s credit profile. We recognise that SUEZ (former Sonate Bidco) benefits from [SUEZ's](#) (Baa1 stable) track record and expertise with regard to responsible operations, including technological shifts. Conversely, SUEZ (former Sonate Bidco) may face a higher employee turnover resulting from the carve out in the first year of implementation.

Governance considerations are material to SUEZ's (former Sonate Bidco) credit profile, given the group's shareholding structure with two infrastructure funds holding together 80% of the equity. The strategy will focus on, inter alia, growth, and the dividend policy appears to favour shareholders over creditors, although we recognise that the consortium's financial policy commits to maintain an investment-grade rating through a flexible dividend policy.

Liquidity analysis

SUEZ's (former Sonate Bidco) liquidity is solid in the next 18 months, underpinned by €840 million of available cash and undrawn committed credit facilities as of 31 January 2022. These include €610 million undrawn credit facilities maturing within six years. Together with strong cash generation, these sources are sufficient to cover the group's capital spending and expected dividend payments, without the debt maturities over the next 18 months.

Methodology and scorecard

The primary methodology used in rating SUEZ (former Sonate Bidco) is our [Environmental Services and Waste Management Companies](#) rating methodology, published in April 2018. The assigned Baa2 rating is one notch higher than the scorecard-indicated outcome of Baa3, which reflects the very broad diversification of its revenue base by sector and geography; and the low risk profile of its water business, which accounted for 52% of revenue in 2019, supervised by long-term concessions or regulations.

Exhibit 7

Rating factors

SUEZ (former Sonate Bidco)

Environmental Services and Waste Management Companies Industry Grid [1]	Moody's 12-18 Month Forward View As of April 2022 [2]	
	Measure	Score
Factor 1 : Business Profile (15%)		
a) Business Profile	A	A
Factor 2 : Scale (20%)		
a) Revenue (USD Billions)	Baa	Baa
Factor 3: Profitability and Efficiency (10%)		
a) EBIT Margin (%)	6% - 8%	Ba
Factor 4 : Leverage and Coverage (40%)		
a) FFO / Debt	18% - 20%	Ba
b) Debt / EBITDA	3.5x - 4.5x	Ba
c) EBIT / Interest Expense	5.0x - 6.0x	A
Factor 5: Financial Policy (15%)		
a) Financial Policy	Ba	Ba
Rating:		
a) Scorecard-Indicated Outcome		Baa3
b) Actual Rating Assigned		Baa2

[1] All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] This represents Moody's forward view, not the view of the issuer.

Source: Moody's Investors Service

Ratings

Exhibit 8

Category	Moody's Rating
SUEZ (FORMER SONATE BIDCO)	
Outlook	Stable
Issuer Rating -Dom Curr	Baa2
ST Issuer Rating -Dom Curr	P-2

Source: Moody's Investors Service

Moody's related publications

Press Release

- » [Moody's assigns definitive Baa2 rating to SUEZ \(former Sonate Bidco\); stable outlook](#), 6 April 2022
- » [Moody's assigns \(P\)Baa2 rating to Sonate Bidco; stable outlook](#), 2 November 2021

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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