

DRAFT: Syctom

July 6, 2022

This report does not constitute a rating action.

Credit Highlights

Overview

Credit context and assumptions

We expect Syctom to weather the shock of increased inflation and energy and transportation costs, and continue to report sound credit metrics, thanks to increased energy sales and its disciplined pursuit of financial stability and expenditure control.

Its budgetary trajectory remains subject to risks arising from the Russia-Ukraine conflict, which is pressuring Syctom's expenditure through high inflation and transportation costs.

But rising energy and material prices are also positively affecting Syctom's revenues (notably through energy sales and waste recovery).

The increase in construction material prices is inflating capital expenditure (capex) and supply chain disruptions may also delay the company's investment program.

Base-case expectations

Strong budget controls and good management of private-sector operator contracts should allow Syctom to maintain a strong operating balance despite increasing operating expenditure (opex).

The widespread impact of geopolitical conflicts on the syndicate's activities, increased waste treatment costs, and a large investment program will result in deep deficits after capital accounts and hike its debt accumulation.

The syndicate's sound debt and liquidity management, good budgetary control, and prudent long-term planning will help soften the impact on budgetary results.

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From 2022, in addition to the impact of rising inflation and energy and transportation costs on Syctom's activity and waste treatment expenses, the syndicate will be penalized by a sizable increase in the tax on polluting activities (TGAP). We expect it to take measures to partly offset these increased costs, including a waste-treatment-tariffs increase; tight control over opex, particularly when renewing contracts with operators; and the optimization of energy sales.

The syndicate has an ambitious investment program, with plans to invest €900 million in 2022-2029. Syctom will pursue its major modernization projects, with an expected €220 million in capex this year. It will continue borrowing to finance this capex to the tune of over €221 million over 2022-2024. This will keep the debt burden comparatively high.

Liquidity remains very comfortable with a large cash buffer and liquidity lines and a sizable envelope of contracted long-term funding.

Outlook

The stable outlook reflects our expectation that the syndicate's budgetary and liquidity positions are strong enough to withstand pandemic- and geopolitical-conflict-related headwinds, although increased waste treatment costs will weaken its budgetary performance. We assume Syctom will continue to implement its sizable investment program through 2024, which will result in large deficits and a substantial increase in its debt burden.

Downside scenario

We could lower the rating if the pandemic and Russia-Ukraine conflict's effects are protracted, or if Syctom experiences difficulties in materially increasing tariffs, or it invests substantially more than we expect. Under this scenario, the syndicate would record a materially weaker budgetary performance than we envisage in our base-case scenario. A lower likelihood of joint and several extraordinary support from members, including Paris, could also result in a downgrade, for example if Syctom's governing bodies showed less capacity for consensus-based decision-making.

Upside scenario

We could raise our ratings if the syndicate significantly improved its operating performance thanks to timely adjustment of tariffs while delivering adequately on its investment plan, and the City of Paris performed in line with our base-case scenario.

Rationale

The syndicate covers almost 10% of the country's population. Syctom is France's largest municipal syndicate for the treatment and recovery of household waste, operating in and around Paris, the economic engine of the country. Its owners are 11 local and regional governments (LRGs), namely the City of Paris (AA/Stable/A-1+), and 10 special intercity structures ("Etablissements Publics Territoriaux"). Syctom covers almost 50% of the population of Ile-de-France, which benefits from a very wealthy and diversified economy, with GDP per capita more than 1.5x the national average.

As a municipal syndicate, Syctom is subject to the same laws ("Code Général des Collectivités Territoriales") as French LRGs, including those governing budgets and accounting. We therefore view it as operating under a predictable and supportive institutional framework, similarly to the one for French cities. Syctom's governing body, appointed after the June 2020 local elections, consists of representatives from the 11 French LRG members and is pursuing a consistent budgetary strategy of ambitious capex for 2022-2029 (the program amounts to almost €900 million over the period). We expect Syctom to maintain a strong capacity for consensus-based decision-making, including on budget strategy and financial planning. In our view, this will strongly support Syctom as it implements

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its investment program, which we expect will account for almost one-third of total expenditure in 2022-2024, while controlling debt increases.

We expect Syctom to weather the shock of increased inflation and energy costs and continue to report sound credit metrics, thanks to its disciplined expenditure control. Debt will continue to finance the capex program. The widespread impact of the pandemic and Russia-Ukraine conflict on its activity and waste treatment costs; the sharp increase in tax on polluting activities; and its large investment project will weaken the syndicate's budgetary performance and hike its debt accumulation.

Our forecasts factor in an overall decrease of 1.7% of combined waste tonnage for 2022–2024, excluding glass, and in particular a 3.6% decrease in household waste. The government's efforts and law of Feb. 10, 2020, related to achieving a circular economy encourage waste reduction, and promote waste recycling and high-energy-efficiency incineration. The trend for products sale made from recovered waste is upward though (sales of energy and materials) mitigating revenue pressure. In 2022, the economic recovery and Russia-Ukraine conflict led to a surge in energy prices and a shortage of secondary raw materials, which resulted in price increases, and Syctom saw a big increase in revenues from energy and materials sales. We therefore anticipate revenue will pick up in 2022, before eroding from 2023 onward as a result of reduced garbage collection and waste treatment.

Syctom is taking measures to partly offset this revenue pressure, including strong opex control, especially through the tight management of private-sector operator contracts, optimization of energy sales, and an increase in waste treatment tariffs. Syctom's governing bodies increased fees (64% of operating revenue in 2021) by 6% in 2021, and a further increase is expected for 2022. This aims to self-finance part of the investment program and compensate for higher payments related to TGAP. The central government increased TGAP in the 2019 state finance budget. The cumulative additional cost for 2022-2024 is almost €68 million. Syctom's mitigating budgetary measures should allow it to maintain a strong operating balance of more than 19% of operating revenue on average in 2022-2024, helping to contain debt growth.

In line with its long-term investment cycle, the capex program for 2022-2029 remains ambitious, with a cumulative forecast investment of around €450 million over 2022-2024. This will hike Syctom's debt accumulation. We anticipate debt will peak at 237% of operating revenue in 2024. Despite its high indebtedness, the effect of recent interest-rate increases on its cost of debt is limited because Syctom's debt is primarily long-term and fixed-rate. From 2025, the debt burden should decrease gradually once the new investments in waste treatment and recovery plants are completed and the syndicate progressively shifts focus to maintenance only.

We view Syctom's liquidity as favorable. Although we expect funding needs will remain large through 2024, the syndicate has good access to external liquidity. It tested this satisfactorily during the pandemic-related market turbulence. Syctom has secured its liquidity through multiyear loans and liquidity lines, allowing a strong debt service coverage ratio. The syndicate also regularly accesses financial markets through green bond issuances (€60 million green bonds issued or 46% of total borrowing in 2021). We understand that Syctom is willing to continue to issue under its euro medium-term note program to diversify its sources of funding and benefit from attractive yields earned on the financial markets. It will continue to favor the use of green financing.

Our long-term rating on Syctom is one notch above its stand-alone credit profile because we see a high likelihood that syndicate members would provide timely and sufficient joint and several extraordinary support to Syctom if it were in financial distress.

Our view of support is based on our assessment of the syndicate's:

- Critical role for its members, given its essential public policy mandate. Waste treatment and recovery is a core responsibility of the member LRGs, which they delegate to Syctom. Its role is also essential for the sustainable development goals enshrined in French law ("Loi de transition énergétique pour la croissance verte"), where France has set ambitious targets for the transition to a circular economy. Published on April 2018, this roadmap was the basis for the recent anti-waste law for a circular economy issued in February 2020. Moreover, the syndicate plays a key role in providing energy to Paris'

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minority-owned heating utility (Compagnie Parisienne de Chauffage Urbain) via the steam produced by its waste incinerators; and

- Strong link with its members. Because Syctom is an administrative public agency, its members are, by law, ultimately responsible for its assets and liabilities. Members' oversight is through political representatives that are part of the syndicate's governing bodies. Syctom's administration is independent from its members and makes its own decisions, including those related to finance.

Syctom Selected Indicators

Mil. EUR	2019	2020	2021	2022bc	2023bc	2024bc
Operating revenue	391	380	403	422	390	398
Operating expenditure	345	311	332	345	315	317
Operating balance	46	69	71	77	75	81
Operating balance (% of operating revenue)	11.8	18.2	17.6	18.3	19.2	20.4
Capital revenue	9	14	51	37	29	29
Capital expenditure	201	200	226	220	113	114
Balance after capital accounts	(147)	(116)	(104)	(106)	(10)	(4)
Balance after capital accounts (% of total revenue)	(36.6)	(29.5)	(23.0)	(23.1)	(2.3)	(1.0)
Debt repaid	64	30	33	33	33	36
Gross borrowings	243	155	130	139	42	40
Balance after borrowings	32	9	(7)	0	0	0
Direct debt (outstanding at year-end)	604	729	826	932	941	945
Direct debt (% of operating revenue)	154.4	191.7	205.0	220.9	241.3	237.4
Tax-supported debt (outstanding at year-end)	604	729	826	932	941	945
Tax-supported debt (% of consolidated operating revenue)	154.4	191.7	205.0	220.9	241.3	237.4
Interest (% of operating revenue)	3.6	3.6	3.5	3.3	3.5	3.6
Local GDP per capita (\$)	--	--	--	--	--	--
National GDP per capita (\$)	40,555.7	38,966.7	43,465.8	42,799.4	45,640.3	48,533.4

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. EUR--euro. \$--U.S. dollar.

Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	1
Financial management	3
Budgetary performance	4
Liquidity	2
Debt burden	4
Stand-alone credit profile	a
Issuer credit rating	A+

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "**Methodology For Rating Local And Regional Governments Outside Of The U.S.**," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

France, Jul 05, 2022

https://www.capitaliq.com/CIQDotNet/CreditResearch/SPResearch.aspx?DocumentId=52013987&From=SNP_CRS

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria | Environmental Social And Governance Principles In Credit Ratings, Oct. 10, 2021

Related Research

- Institutional Framework Assessments For International Local And Regional Governments, May 18, 2022
- Local Government Debt 2022: French LRGs Drive The Investment-Led Recovery While Reducing Debt Intake, March 22, 2022
- French Local And Regional Governments' Wage Bill Increase Could Weigh On Operating Balances And Investment Capacity, March 17, 2022
- City of Paris Outlook Revised To Stable From Negative On Expected Stronger Budgetary Performance; Affirmed At 'AA/A-1+' Oct 08, 2021

Ratings Detail (as of July 06, 2022)*

Syctom

Issuer Credit Rating	A+/Stable/A-1
Senior Unsecured	A+

Issuer Credit Ratings History

24-Jul-2020	A+/Stable/A-1
05-Nov-2019	A+/Positive/A-1
05-Nov-2018	A+/Stable/A-1

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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