

Research Update:

# French Waste Treatment Syndicate Syctom Outlook Revised To Stable On COVID-19 And National Strikes; Affirmed At 'A+/A-1'

July 24, 2020

## Overview

- The widespread impact of national strikes in France in the first quarter of 2020 and COVID-19 on Syctom's activity, coupled with important investment needs, will result in deep deficits after capital accounts and a high debt burden.
- Nevertheless, we expect the syndicate's sound debt and liquidity management, good budgetary control, and prudent long-term planning will help soften the impact on its budgetary results.
- We are revising our outlook on Syctom to stable from positive, and affirming our 'A+/A-1' ratings.
- The stable outlook reflects our expectation that, despite the syndicate's revenue contraction in 2020, activity will begin to recover in 2021.

## Rating Action

On July 24, 2020, S&P Global Ratings revised its outlook on France-based metropolitan waste treatment and recovery authority Syctom to stable from positive. At the same time, we affirmed the 'A+' long-term and 'A-1' short-term issuer credit ratings on Syctom.

## Outlook

The stable outlook reflects our expectation that Syctom's liquidity position is strong enough to withstand the impact of the COVID-19 outbreak and of the strikes earlier in the year in 2020, even though the reduced revenue will weaken its budgetary performance. In our current assumptions, Syctom will continue to implement its sizable investment program until 2023, which will result in large deficits and a substantial increase in the debt burden.

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## Downside scenario

We could lower the rating if the effects of the pandemic are protracted or tariff adjustment is delayed. Under this scenario, Syctom would record a materially weaker budgetary performance than we currently envisage in our base-case scenario. A lower likelihood of joint and several extraordinary support from members, including Paris, could also potentially result in a downgrade, for example if Syctom's governing bodies elected in the June 2020 municipal elections showed less capacity for consensus-based decision-making.

## Upside scenario

Alternatively, we could raise our ratings if Syctom was able to significantly improve 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

We revised the outlook on Syctom to stable from positive because we believe that the COVID-19 pandemic and the impact of strikes in the first quarter of 2020 may delay the recovery of Syctom's financial performance and deleveraging after it implements its ambitious investment program. Most recently, the operations of Syctom's waste treatment plants were disrupted during the lockdown, resulting in a loss of revenue. At this point we expect the cost of the pandemic to remain manageable. We expect Syctom to take some measures to partly offset the cost of the crisis, including delaying and downsizing its large investment program, while controlling debt increases. Moreover, liquidity remains very comfortable with a large buffer, which underpins our stable outlook.

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. Syctom's owners are 12 local and regional governments (LRGs), namely the City of Paris (AA/Negative/A-1+), 10 special intercity structures ("Etablissements Publics Territoriaux"), and the intercity of Versailles Grand Parc. Syctom covers almost 50% of the population of Ile-de-France, which benefits from a very wealthy and diversified economy, with GDP per capita above €60,100, which is 1.7x the 2018 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 believe Syctom operates under a predictable and supportive institutional framework, similarly to the one for French cities.

The outcome of the June 2020 municipal elections will affect Syctom's governing body, because it consists of representatives from the 12 French LRG members. However, 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 its large investment program, which will account for about 40% of total expenditure during 2020-2022, while controlling debt increases.

The cost of strikes in the first quarter, the pandemic, and a large investment project will substantially weaken Syctom's budgetary performance and hike its debt accumulation before the reduction of capital spending and higher tariffs lead to a robust recovery in financial indicators after 2022.

In line with the long-term investment cycle, after eight years of deleveraging, Syctom's debt started to increase in 2018. We anticipate debt will peak at 231% of operating revenue in 2022 once the new investments in waste treatment and recovery plants are complete and Syctom shifts focus to maintenance only. From 2023, the debt burden should then decrease gradually.

Strong budget controls and good management of private-sector operator contracts should allow Syctom to maintain a strong operating balance of nearly 15% of operating revenue during 2020-2022, helping contain debt growth. Moreover, we understand Syctom's governing bodies will increase tariffs on fees (62% of operating revenue in 2019) from 2021, in order to self-finance part of the investment program and compensate for higher payments related to the general tax on polluting activities (TGAP). The central government has decided to increase TGAP in the state finance bill from 2019.

We view Syctom's liquidity as favorable. Although we expect funding needs will remain large through 2022, the syndicate has strong access to external liquidity that was satisfactorily tested during the market turbulence provoked by COVID-19. Syctom has secured its liquidity through multiyear loans and liquidity lines, therefore allowing a strong debt service coverage ratio. We also understand that Syctom is willing to access financial markets to diversify its sources of funding.

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 is in financial distress.

Our view of support is based on our assessment of Syctom'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"). More specifically, Syctom plays a key role in providing energy to Paris' 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 Syctom's governing bodies. Syctom's administration is independent from its members and it makes its own decisions, including those related to finance.

#### Environmental, social, and governance (ESG) credit factors for this credit rating change:

- Health and safety

## Key Statistics

Table 1

### Syctom Selected Indicators

	--Fiscal year ended Dec. 31--				
	2018	2019	2020bc	2021bc	2022bc
Operating revenues	381	391	365	413	424
Operating expenditures	317	345	311	356	359
Operating balance	64	46	54	57	65

Table 1

## Syctom Selected Indicators (cont.)

	--Fiscal year ended Dec. 31--				
	2018	2019	2020bc	2021bc	2022bc
Operating balance (% of operating revenues)	16.8	11.8	14.8	13.8	15.3
Capital revenues	8	9	29	39	42
Capital expenditures	173	201	220	210	230
Balance after capital accounts	(101)	(147)	(137)	(114)	(123)
Balance after capital accounts (% of total revenues)	(25.8)	(36.6)	(34.7)	(25.2)	(26.4)
Debt repaid	46	64	30	33	50
Gross borrowings	62	243	167	147	173
Balance after borrowings	(85)	32	0	0	0
Direct debt (outstanding at year-end)	425	604	741	855	978
Direct debt (% of operating revenues)	111.5	154.4	203.0	207.0	230.7
Tax-supported debt (outstanding at year-end)	425	604	741	855	978
Tax-supported debt (% of consolidated operating revenues)	111.5	154.4	203.0	207.0	230.7
Interest (% of operating revenues)	4.3	3.6	3.7	4.4	4.5
Local GDP per capita (single units)	60,222	62,275	55,212	61,035	64,263
National GDP per capita (single units)	35,303	36,217	33,151	35,709	37,261

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.

## Ratings Score Snapshot

Table 2

### Syctom 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

Table 2

**Syctom Ratings Score Snapshot (cont.)**

Key rating factors	Scores
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.

**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: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

**Related Research**

- Sovereign Risk Indicators, July 14, 2020. An interactive version is also available at <http://spratings.com/sri>.
- COVID-19: Fiscal Response Will Lift Local And Regional Government Borrowing To Record High, June 9, 2020
- COVID-19: French Departments Face Marked Revenue Losses, While Regions Swerve Near-Term Fallout, May 28, 2020

**Ratings List****Ratings Affirmed; Outlook Action**

	To	From
<b>Syctom</b>		
Issuer Credit Rating	A+/Stable/A-1	A+/Positive/A-1

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at [https://www.standardandpoors.com/en\\_US/web/guest/article/-/view/sourceId/504352](https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352) Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search

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