Summary: ISS A/S

Credit Rating:
B+/Stable/B

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Rationale

The ratings on FS Funding A/S, ISS A/S, and ISS Global A/S, the entities of Denmark-based facilities services provider ISS, reflect the group's highly leveraged financial profile and weak credit measures. This is mitigated by the group's strong business profile, underpinned by a solid business position in an attractive—albeit fragmented and competitive—industry.

At Sept. 30, 2006 adjusted group debt was about Danish krone (DKK) 29.2 billion (€3.9 billion; including unfunded postretirement liabilities).

With sales of DKK46.4 billion in 2005, ISS benefits from a strong business position, particularly in Northern Europe, where it is a market leader in most of its operations. The group benefits from good geographic diversity in Europe, and a highly diversified customer base. Standard & Poor's Ratings Services regards ISS' business sector as attractive, as it is resilient to downside, and will likely benefit from increasing outsourcing. Although there are few barriers to entry and pricing is competitive in this sector, the group has a good record of contract retention, and is large enough to benefit from economies of scale.

Acquisitions have been, and will likely remain, part of ISS' strategy to add competencies and build critical mass and geographic presence. Although its acquisition strategy adds some risk to the business, ISS' track record is good in this regard, the group having successfully integrated acquired companies. In light of the competitive nature of the facilities services business, operating profit margins are relatively low, with EBITDA margin of about 7% (unadjusted for operating leases) for the 12 months to Sept. 30, 2006.

The group's financial profile is highly leveraged, following the buy out in May 2005 by a private equity consortium comprising EQT III, EQT IV and Goldman Sachs Capital Partners. This resulted in weak credit measures, with adjusted debt to EBITDA likely to be about 7.5x (not lease adjusted) in the near term, and EBITDA cash interest at about 2x. We do not expect material improvements in these ratios in the medium term, in view of the company's acquisitive growth strategy. Acquisition spending is discretionary and flexible, however, and acquisitions are normally immediately cash flow enhancing. Furthermore, the group's highly flexible cost base (primarily related to staff) and low capital expenditure needs provide additional downside resilience.

Liquidity

ISS' liquidity is adequate, with likely modest annual debt maturities until 2010. At Sept. 30, 2006, short-term debt was DKK968 million. Most of this was represented by drawings under the group's major liquidity resource, a DKK1.75 billion committed revolving credit facility. ISS also has a DKK750 million uncommitted revolving credit facility. In addition, the group has a LOC/guarantee facility of DKK500 million, and separate acquisition facilities totaling DKK4.9 billion (of which DKK2.5 billion was drawn at Sept. 30, 2006). These facilities mature in 2012 and 2013, respectively, and include financial covenants. Headroom under the covenants should be sufficient. We also expect the group to continue to post positive free operating cash flow (before acquisitions, and adjusted for seasonal working-capital swings).

Recovery analysis

The €1.3 billion (DKK9.7 billion) senior subordinated notes, issued by FS Funding, have been rated two notches below the corporate credit rating, as the notes are contractually and structurally subordinated to substantial priority liabilities within the group, including drawings under credit facilities and noninterest-bearing liabilities at the operating subsidiary level. For similar reasons, the two existing bonds totaling €1.35 billion, maturing in 2010 and 2014, and issued by ISS Global under the group's EMTN program, continue to be rated two notches below the corporate credit rating, although the €1.3 billion senior subordinated notes are structurally subordinated to the EMTN bonds. The full recovery analysis can be found in the article entitled "ISS Group", published on April 24, 2006, on RatingsDirect, Standard & Poor's Web-based credit analysis system.

Outlook

The stable outlook reflects our expectation that ISS' operating performance should remain steady, and is underpinned by the group's ability to generate strong cash flows. We do not incorporate material improvements in ISS' credit measures, reflecting the expected continued acquisition strategy, which limits ratings upside potential. Furthermore, we do not expect any material deterioration in credit measures. Any such deterioration could result in an outlook revision to negative, or a downgrade.