Final Transcript

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Corporate Participants

Barbara Jensen

ISS – Group Treasurer

Jacob Stausholm

ISS -Group CFO

Jeff Gravenhorst

ISS - Group CEO

Presentation

Operator

Welcome to the ISS Conference Call. At this time, all participants are in a listen-only mode. Later we will conduct a question and answer session. Please note that this conference is being recorded. Your conference will begin momentarily. A short introduction will now be played before the presentation begins, and after the introduction the call will be turned over to Group Treasurer Barbara Jensen.

Barbara Jensen – *ISS Group Treasurer*

Ladies and gentlemen, welcome to the Investor call and presentation of the ISS third quarter results released earlier today. Please be aware that our announcement, the report as well as the slides used for this call can be found on our website, where the webcast will also be available following the call. Please be aware that on slide two you will be able to see the forward-looking statements prior to our presentation.

With me today I have Group CEO Jeff Gravenhorst and Group CFO Jacob Stausholm, and if you turn to slide number three, you will be able to see the agenda of today. Jeff will go through the first two points, Jacob will then go through the financials and I will end the presentation by going through the capital structure. In the end of our presentation, the lines will be open for questions, and now I'd like to hand over the presentation to Group CEO, Jeff Gravenhorst.

Jeff Gravenhorst - *ISS – Group CEO*

Thank you Barbara, and welcome from my part as well. First and foremost on the slide four I would like to draw your attention to a change in our senior management team in ISF. In connection with the ( ) and ISS combination which was terminated, Jacob Stausholm also looked at other opportunities outside the group of ISS, and in that connection made an agreement with me that he will stop with ISS.

In connection with that, we have appointed a new CFO for ISS on group level, and that is Henrik Andersen, coming from our UK operations. Henrik has an 11 year history with ISF, good operational experience as well as strong financial exposure to, or experience from our UK operation, as well as Group Treasurer experience from our group management back in 2003. So basically, a very strong individual, a person who I've worked with for many years, and a person who both has an operational and a financial knowledge about the company, but also from general banking background. I do really look forward to working together with Henrik for the coming future. So a welcome to Henrik of course, and from the 1st of December Henrik will be taking over, and of course also be part of these investor calls from January onwards.

So if I can draw your attention to the business update, which is... starts on page number six, overall, the key features of ISF are the same. We've gone through, over the last couple of times, more details of the strategy of ISF, but I just want to highlight here some of the key features of the group. Number one is that we are actually a global leader of a unique service offering. Today ISS is present in more than 50 countries. We have more than 540,000 employees, and we are capable to deliver a full range of services in more than 90% of the world's GDP.

This is the reason why we can take on global contracts on full facility services offering. That means that we are actually captured... and we are able to capture high growth opportunities throughout the world, both from the global contract point of view, regional, but also from a multi-service and single service contracts point of view.

The margins improvement, clearly they are good operational efficiency possibilities. This business makes possibilities in the world of ISS going forward, which is why we believe that we can go towards the 6.5% margin top within the foreseeable future.

We also have some recovery, which includes both Holland, the Mediterranean area and the French operation, but also some of the once-only business which can actually also improve over the next few years. But despite these possibilities of improving our margins, we have shown ourselves to be a very resilient business model. Throughout the crisis of 2009, we had organic... a positive organic growth, and over the last two years, both 09 and 2010 we're showing very good organic growth, quarter by quarter, basically building on the fact that we're capable of cross-selling and up-selling to existing clients, but also because of our unique service offering.

Combined with a very robust cash generation, and low capital requirements, we are also of course a good cash generative business. The experienced management team speaks for itself, basically, all of the country management and the top management team have been employees for many years, and even now, when we're in the position where we change our CFO, we can actually recruit that internally. So I'm very confident with the strength of the management team to be able to deliver the future also, for ISS in a very strong manner.

If you look at page seven, some of the key events for this year, overall the headline of course, the very positive thing is that we delivered 7% organic growth for the 3rd quarter, and 6.4% for the first nine months of 2011. That was really assured by actually living and fulfilling the strategy as we've talked about for a long period of time now, basically, major account wins, also retention rates being a little bit better. And it is within our chosen customer segment. We've been able to implement very large ISS contracts across the globe, FCO contracts across Asia, the HP contract now in the US. We have now globally, and other major contracts like Citigroup across Europe, and actually doing it according to our expectations.

I'm extremely proud of the organisation that we are. It's one of the only companies in the world capable of doing so, but likewise, we have the same experience within the big countries around the world. Very good growth in Switzerland, very good growth in Italy, Germany and basically, also in the UK, where we have one of our most mature operations where the ISS contracts in the ( ) have been spectacular this year.

Our emerging market story continues. We still have double digit growth in the emerging markets and it's very good across the board organic growth as well. The turnaround in France is moving ahead according to plan. It will be a little bit slower-paced than over the years before we can see it come completely back to the levels of before, but right now we're following the plan [sound slip].

Operating margins, we're up on the operating profit by 7% and our operating results, before other items, by 4%, and actually we saw the reverse [35] because of the investment we've been doing at the same time. So overall, very pleased and satisfied with the overall performance, both on the top line and on the bottom line of ISS.

Turn to page eight, again, of course the growth has been fuelled, as I said, by very large integrated single service offering, but also very successful single service contracts within most of our countries. Basically, it's very good organic growth throughout the world. Some of our regions are really showing good progress in the customer selection, the customer segmentations that we've done. It's very important that we're very focused on the value-added services and the value propositions that we have within our chosen customer segment. This has given very good growth in the UK, Finland, Brazil, Germany, Turkey, India, basically, and as I said, throughout the world.

We've listed a couple of our contract wins on the bottom of page eight. I'm not going to go through that in detail. You can use that as a reference, but it just goes to testimony that this is the strategy, that it actually is coming through. If you look at our emerging market on page nine, obviously we can see that we do have the same exposure and it actually is coming through. Now they're representing 37% of our organic growth for the world, and that's something we're very satisfied with. But I will actually draw the attention to where we do make a difference, but we had very good organic growth in our developed market.

We are not dependent organic growth only coming from emerging markets, we are actually seeing very good growth in the developed markets, as I said, particularly also in the UK market, which is a very competitive market, but also with a very profitable development at the same time, so basically, very strong growth.

If we look at the margin side on page ten, we are very satisfied with the margin, the operating margin EBITDA is up by 7% compared to last year, and that even includes 100 million or thereabouts that's been used on the IPO cost. But if we look at the operating margin before these other items, it's up by 4%, meaning that the operating margin and percentage of sales is slightly below last year. The reason for this is that our investments into our operation and ISS contracts in North America, something we've chosen to invest more resources into in order to be able to sell quicker ISS in the North American market.

We've already had two ISS wins this year on the back of the HP contract. It's also... yes of course we have a number of live start-up's which starts a little bit lower in margin, as we talked about before. And that will gain speed as we go through the year, and basically, according to plan. Apart from that, we do have some very good successes also on the development of the margin in Switzerland, UK, Turkey and the whole Asia region, but it is offset by some more difficult macro-economic conditions in the Mediterranean countries such as Spain, Portugal and Greece. As we know them, in the PICS countries basically, the reality is, we do have an exposure to the public sector there, where the growth is a little bit lower than originally anticipated. And therefore also us holding a little bit back, which has hurt the margin just slightly, and the spend on catering and incremental spend is a little bit lower, also hurting our margins.

But overall, very satisfied with the development, also in these countries where we're disappointing, is clearly in Holland, in the Netherlands where we have some operational issues in our core business, but it is something that is being fixed right now, offset by very good performance, as I said, in other Western European countries. Overall margin, overall growth and margin, we're basically very satisfied with where we are today after the first nine months of this year we see ourselves as fulfilling the strategy as we laid it before you and before the whole organisation. Successful with our large ISS contracts, successful with our customer segmentation and penetration of these segments, and actually, also coming through on the margin side with the investments that we've chosen to make throughout the year. So we're very pleased with that, and with that I would like to hand for more details on the financials to Jacob Stausholm.

Jacob Stausholm – *ISS, Group CFO*

Yes thank you very much Jeff, and just before I diver further into the financial, let me just say that what we have disclosed today should not be of any surprise to you for two reasons. Firstly, because the set of results, I believe, is fully in line with the expectation that we laid out at our Q2 disclosures back in August, and secondly, as part of the proposed [G4S] transaction, we released on the 17th of October a trading statement with headline figures, and those numbers have not changed.

So if you move to slide number 12, here you have a summary of the financials, and I think the starting point, as Jeff has laid out as well, we're growing; we're growing by the top line and by the profit line. Year-to-date 6.4% organic growth, profit up 4% before other items, 7% after other items. If we dive a little bit deeper into the organic growth, you can see we have had this momentum in the year, from 5.8 in Q1 to 6.2 in Q2, to 7% in Q3. And looking a little bit about the peer group are there to say we consider this as industry-leading organic growth at this point in time.

We... what is good for us to see, and that is, as Jeff laid out as well, it is growth that we see across geographies, both in emerging markets and in developed markets. The operating margin is very much in line with the margin we experienced in Q3, year to date, last year we had 5.5 versus 5.6, and the similar pattern you see in the Q3. We have seen improvements in profitability in Western Europe and the emerging markets, somewhat offset by some new major contract start-ups that are early in their profit cycle, and slightly lower profitability in the Nordics.

If you move to the cash conversion, then we recorded in the third quarter, and LCM cash conversion of 80%. That's lower than what we normally perform at. We are used to having a consistent high cash conversion. I would like to first of all remind you that we got, back in 2008, some help in terms of payment pattern when the crisis hit in 2008, in terms of longer payment terms for VAT and social charters.

That has now gone back, and that means that we get five cash conversion percentage points less so you can say, taking that impact, the cash conversion was 85. That's still not the level we are aiming at, and one of the reasons for the lower cash conversion is that the debtor base is up 0.4. That might not sound a lot, but it is actually, around three percentage points, and we certainly aim for getting that back. Secondly, the high organic growth obviously has an impact on our cash conversion, so if you look at those sorts of things, we're not satisfied with 80%. And we aimed for having a higher than 80% cash conversion for the fourth quarter.

We have full focus on trying to improve the position, but overall, it is not entirely out of the possible range when you have a company that grows a lot, and particularly the day-to-day is hit by the significant growth in Latin America, and the tougher credit situation in Mediterranean Europe.

If you move to chart number 13, you basically just see exactly the numbers that I have gone through on the previous chart, so I suggest we move onto slide number 14. And if you go into the organic growth here, we are very proud of the chart. The upper left hand corner, where we see that we, for eight quarters in a row, have increased the organic growth, reaching 7% in the third quarter; on the right hand side you can both for the quarter and the year to date, the breakdown of the overall growth.

We talked about the organic growth. What is interesting here is that we have for a few years had significant positive impact in growth from foreign exchange. We still have positive impact year to date, but the quarter turned out negative 0.6%.

Another thing that changes the overall revenue picture, the revenue development picture is that we successfully completed, I think we mentioned that at Q2, we signed in Q2 but completed the transaction in Q3, the divestment of our non-core business, our damage control business in Germany. That was an excellent divestment at a, for us, attractive price. That also resulted in debt reductions, but as you can in the revenue growth that means that divestment has increased quite significantly to now minus 3%.

If you move to the next chart, chart number 15, you can see the revenue development and let me just pick up from what Jeff was saying. We have an outstanding emerging market business across the globe in Latin America, in Asia, around the globe of emerging markets. It’s very stable, at a very high level. We had 13.5% organic growth year-to-date, and last year we had 14.3%. So that basically, keeps us at a high organic growth level, but the real improvement in the organic growth is actually coming from the developed world. And what you see here is mainly driven by Western Europe and by the Nordics.

Western Europe had only 0.5% organic growth last year, and recorded 4% year-to-date this year. The Nordics last year, year-to-date, had 2.7% and recorded 4.6% year-to-date this year. So those are really... this is where we have the vast majority of our business, and that’s where you see the significant jump in organic growth. If you move to chart number 16, then you will be able to see the development in the operating margin, and you’ll see, as Jeff talked about the continued positive development in Western Europe. Asia, despite high growth, continues to improve its profitability and maybe a word about Latin America.

You will see Latin America is 0.5% lower than last year, but it also should be seen in the light of very high organic growth. Actually, absolute profit is around 14% higher this year compared to last year, so overall not too bad. Nonetheless, we will still aim for getting the profit margin back to where it was and beyond.

In the US, as you know, we were talking about the last couple of quarters from a customer perspective, a successful start of our HP contract in the US, is still dragging our profitability in the US. It is still subject to further improvement initiatives over the next year or two. Finally, the Nordics are slightly lower than last year. It's partly due to once-only income that there was less of this year compared to last year. Amongst others, snow removal, and then we have had some loss and renewal of ISS contracts at lower profitability level. Or put it differently, they are at earlier stages of the profitability cycle of major contracts.

So overall, we are just slightly below the same level as last year, in line with the outlook expectation we painted at Q2 in August. If you move to slide number 17, you see that pattern here, that profitability seasonally improved in Q3 this year, very much in line with last year, for 6.3% versus 6.4% recorded last year. And then on slide 18, you've basically, just got the numbers that we have gone through, so I'll jump quickly over that and end up here with slide number 19, where you can see the outlook statement for 2011.

It is quite similar to the one we communicated to you back in August. We just tried to be a little bit more precise as we are getting towards the end of the year. So we will still say the same thing, that we expect the organic revenue growth to be around 6%, not that we are projecting any big downturns. But no matter how we ( ) this up, it will be around 6%.

Then the operating margin, we stick to as what we have said before, that it would be slightly below the level realised in 2010, and finally the cash conversion will be slightly lower than last year. But we expect it to be higher than what we realised at the end of this quarter. And with that, I will finalise my part and hand over to our Treasurer Barbara Plutner-Jensen.

Barbara Jensen – *ISS Group Treasurer*

Thank you Jacob, if you turn to slide number 21, you can see the continued de-leverage. This is that we have continued... or communicated previously, and the path we're on is going in the direction that we also had before. You can see the seasonality adjustment that is also at some of the lowest levels we have experienced, as you ( ) ( ) coming back to July, back in 2009.

So overall, continued de-leverage with an additional eight times within the existing quarter. If you turn to slide number 22, you will be able to see the breakdown of the capital structure of, and you can see that year on year, we are down with more than half a billion Danish Kroner. If you adjust that, it's even higher at minus kr820 million. Please note that in the current ( ) not had amortisations in this quarter due to the repayment profile on any facilities.

Looking at the maturity profile of ( ), you can see that ( ) extends that week in June 2011, followed also by the innovation programme, we do not have any ( ) upcoming in this term. You can see that the two amounts that we have in 2011 and that's 2,000 ( ). Those are ( ) amortising ( ) as with the repayment of the equity facility A and the chairman on facility A.

In 2013, we have the securitisation programme maturing, but please remember that ( ) that we can roll over on a year basis, see it now [NHI]. Before we turn to the Q and A session, I'd like Jeff to check in.

Jeff Gravenhorst - *ISS – Group CEO*

Thank you Barbara, you probably all, there was a combination of two businesses announced on ( ), for us was to acquire ISS ( ). That was subject to the approval of the ( ) and I just want to make a couple of comments on it. First of all, the reason why IGS wanted to acquire ISS was because they made a market survey and they heard back, basically confirming the strategy of what ISS is all about. That is for more contracts, and it is the integration of the leading services to large premises throughout the world, basically.

And the decision for us as management team and the board was actually to address this issue by acquiring ISF because we had the [plan] which would make them even better performing on our scale. Obviously this transaction terminated as the investors elected not to ( ) but I just wanted to give a couple of reasons why. And the reason why this did not go through was basically the size of the deal.

The size of the deal, and this made this from an investor perspective a ( ) on the integration etcetera. Basically, ( ) decided not to go ahead with it, but this is a confirmation of the direction of ISS and the strategy that it has. Not only can we provide the organic growth figures, but also by the fact that all of our competitors, basically, on an international scale are ( ) market, even to the extent that there is a wish to actually acquire us to be able to do that better. From that, of course, I'm extremely proud but I am also very proud in the sense that we will now have to continue to do this under the brand of ISS. And I would say that we're in a very good shape to bring this strategy forwards towards the longer term aims and target the group, and basically, there is no reason why we should make any changes to what we already set out at the IPO earlier this year, and we will pursue an IPO within the next two years time.

For now, we will be focusing on the business, delivering the results and satisfying our customers, and enriching our employees lives by more career opportunities throughout the world, basically, and not think about exits for the next ( ) but basically this. But when we do it, it will be focusing on our IPO. Thank you very much for listening and we will now turn over to the Q and A.

Barbara Jensen – *ISS Group Treasurer*

Could we have the operator please?

Questions and Answers

Operator

Thank you, we will now begin the question and answer session. If you have a question, please press star then one on your touch-tone phone. If you wish to be removed from the queue, please press the hash key or the pound sign. If you are using a speaker phone, you may need to pick up the handsets before pressing the numbers.

Once again, if you have a question, please press star, then one on your touch tone phone. Your first question comes from [Amit Renzik] from Hermes. Please ask your question.

Amit Renzik – *Hermes*

Hi, just thanks for taking my questions and I've got a couple. You talked about sort of, how attractive the business is to outsiders and obviously the large transaction fell through, but I wonder, have you been in discussions, have you had discussions with other potential trade buyers?

Operator

You are now on the line. Would you like to return to question and answers?

Barbara Jensen – *ISS Group Treasurer*

Yes please.

Operator

Thank you, once again ladies and gentlemen, that's star and one on your telephone to ask a question. We have a question on the line from Nicolai Raastrup from Borsen. Please ask your question.

Nicolai Raastrup – *Borsen*

Hi, I'm happy to ask my question, but do you want to maybe address the first question first?

Jeff Gravenhorst - *ISS – Group CEO*

We didn't get the first question Nicolai, sorry.

Nicolai Raastrup – *Borsen*

Oh I'm sorry, okay I'll go ahead with mine. My question was, you mentioned IPO costs of 100 million, which is a little bit higher than the last time you reported on this. Just wondering the reasons for this, and maybe if you could... if it's possible for you to break down the expenses a little bit?

Jacob Stausholm – *ISS, Group CFO*

Yes, basically we had experienced almost all expenses from the ( ).

Nicolai Raastrup – *Borsen*

I'm sorry Jacob, I can hardly hear you, could you...

Jacob Stausholm – *ISS, Group CFO*

( ) ( ) of the proposed transaction, and what you just heard Jeff saying that we are not pursuing an IPO in the very short term, so basically, what we have done now is we have dispensed all the IPO costs and I don't think you need much more breakdown. It's fully disclosed in our quarterly release. It's the normal expenses to lawyers etcetera.

Nicolai Raastrup – *Borsen*

All right, can I ask you Jeff, perhaps Jacob has decided to leave the company; did you at this point get any other indications from people in the organisation in Denmark or anywhere else wanting to leave the company?

Jeff Gravenhorst - *ISS – Group CEO*

No, actually we had... obviously I guess you're asking in light of the ( ) combination?

Nicolai Raastrup – *Borsen*

Yes.

Jeff Gravenhorst - *ISS – Group CEO*

We had a big conference yesterday with all the country managers, and I think it's something that you need to take very seriously when you're going through a process like this. I would not... I would say basically, the key thing is that everybody's very happy on continuing with ISS as a brand and with the culture of ISS. And from that perspective I actually think that people even more geared up today, so no.

Nicolai Raastrup – *Borsen*

Okay and just a last question, you mentioned that an IPO might be something you want to pursue within the next two years, if I heard you correctly. Would there be any lessons from, I guess, this year's experience that you will take with you going into that process?

Jeff Gravenhorst - *ISS – Group CEO*

Yes of course, I think we have learned a lot from visiting all the investors when we did the IPO. I also joined the ( ) on this tour, but we'll take all the knowledge that we have from that. I will say again that macro-economic conditions like... macro conditions like a nuclear or a tsunami or whatever are very difficult to predict. So from that perspective, I don't think we should be too concerned about that happening at the same time in four years time from now.

But I think it is always good to learn from all the comments we get, I think the key point is that we are going in the right direction with our service. I think that that's been confirmed by everything right now, and then it's about just delivering over the next couple of years.

Nicolai Raastrup – *Borsen*

All right, thank you.

Operator

Thank you, thank you Mr Rezik, if you could re-ask your question.

Amit Renzik – *Hermes*

Ah, thanks very much. Sorry I didn't hear the answer, but the question was... you had talked about how attractive the business is to outsiders and I'm just wondering if you had been in discussions with any other potential trade buyers, aside from G4S?

Jeff Gravenhorst - *ISS – Group CEO*

We have not been in discussion with any other trade buyers in connection with this. I think we made the IPO; we had aborted the IPO because of the tsunami in Japan and the nuclear threat that was happening in the same week. We didn't want to go ahead because it was too tumultuous a situation to launch our company into the stock market.

We then basically just said we'll wait for a while and then go back with the stock introduction, or a trade... sorry, the IPO, and in that period we were contacted by G4S and then we looked at that. So no, we have not been in contact or discussion with anybody else.

Amit Renzik – *Hermes*

Thanks and then, I realised that Henrik is an internal hire is the right word... internal transition to CFO, will that impact at all the financial policy of the company? And can we expect any changes in the financial policy?

Jeff Gravenhorst - *ISS – Group CEO*

No it will not. I think the key point here is that Henrik is a long-time soldier also within ISS, so I think it's the same philosophy, the same strategy, it's the same direction. So we'll continue to do what we do. We'll just do it, you know, really focused on this apart from... when we don't have focus on that.

Amit Renzik – *Hermes*

Okay right, and then so... can I take that as confirmation from the last call, once again, that you don't plan to revert to any kind of acquisition-led de-leveraging?

Jeff Gravenhorst - *ISS – Group CEO*

Yes well, the key is that we have said we will make some acquisitions, but very few, very selective in emerging markets particularly. So you will not see an increase in acquisition activity that is significant.

Amit Renzik – *Hermes*

Okay great, thanks very much.

Operator

Thank you, Fabian Ansorg from M & G is on the line with a question.

Fabian Ansorg – *M & G*

Hi there, two questions, first about the declining operating margin. Could you drill into the reasons for that? It seems to be particularly in the Nordic region as well as North America and Eastern

Europe that would be helpful. And secondly, on the cash flow from operating activities, could you just explain a little bit more on what exactly has been driving that, in particular why ( ) have been increasing, thank you?

Jeff Gravenhorst - *ISS – Group CEO*

If I take the first part, if we take the North American situation, I mean, North America is diluted by the start up of the large HP contract, and the choice that we made, because we wanted to have the capability to ( ) ( ) in North America.

With that, there is a conversion of... coming from sub-contractors into a sub-delivery model, and as we said, for a while this is going to take some time to get that done. So basically, within our first two years, it will be lower margin than average. And it’s a sizeable contract of course, compared to the sites that we have in North America, that’s why it’s ( ).

The Eastern European market, really, there’s nothing in particular on that though actually I think that we are performing fairly well in the Eastern European market. But going forward also, the Nordic market’s impacted by, as Jacob said in the introduction, by the lower than normal once-off income, particularly on snow removal this year. There’s been a little bit of a different snow season than last year. This is something that will go up and down year on year, because we have such a significant market position as we have.

Also, we’ve had start-up off a number of larger contracts, so we have bid early on that cycle in the Nordic region also, so that is the reason why, from a cash flow perspective, Jacob?

Jacob Stausholm – *ISS, Group CFO*

Yes, you’re absolutely right. When you look at a consolidated statement of cash flow, year to date, the cash from operating activities is lower than the year’s date number for 2010. I was trying to explain it the other way around in terms of the lower LTM cash conversion. It is exactly the same explanation and you will see, if you look at page 15 of our interim statement, that the variation is almost entirely in changes in working capital. And I explained to you that our day-to-day is 0.4 day-to-day is higher this year than last year. That’s not a lot, but it does mean a couple of, I don’t know, kr150 million on that account.

And then secondly, we have had this very high organic growth of 7% and that means that when you start up these major contracts, that you start investing some working capital in those new contracts, those new businesses. And that's the reason why the cash generation has been lower.

Having said that, despite the high organic growth, we expect the cash conversion, so increased from the 80% achieved end of Q3.

Fabian Ansorg – *M & G*

Just to clarify then, it's really, if I strip out the start-up issues around the ISS contracts, the underlying data portfolio has not deteriorated, or did it actually deteriorate by 0.4 days?

Jacob Stausholm – *ISS, Group CFO*

It deteriorated by 0.4 days, but what I'm saying is that's something we of course aim to get back. You have to bear in mind that these working capital statements are of course ( ) second at the end of the quarter.

Fabian Ansorg – *M & G*

Okay, thank you.

Barbara Jensen – *ISS Group Treasurer*

( ) saying we would like to close today's presentation of our third quarter results, thank you very much.

Operator

Thank you ladies and gentlemen, that concludes today's conference, thank you for participating. You may now disconnect.