MOODY'S
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Credit Opinion: ISS A/S

Global Credit Research - 17 Jul 2012

Denmark

Ratings

Category	**Moody's Rating**
Outlook	Positive
Corporate Family Rating	B2
Senior Subordinate	Caa1/LGD6

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Key Indicators

[1]**ISS A/S**

	3/31/2012(LTM)	**12/31/2011**	**12/31/2010**
Pretax Income (USD Million)	**$111**	**$108**	**$158**
Revenue (USD Million)	**$14,428**	**$14,507**	**$13,200**
RCF / Net Debt	**6.1%**	**6.2%**	**6.9%**
FCF / Debt	**1.1%**	**0.8%**	**1.6%**
(EBITDA-CapEx) / Interest Exp	**1.3x**	**1.3x**	**1.5x**
Debt / EBITDA	**6.7x**	**6.7x**	**6.7x**

[1] All ratios are calculated using Moody's Standard Adjustments. Source: Moody's Financial MetricsTM

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- IPO postponed till 2015

- Acquisitive activity scaled back; focus on organic growth

- Despite deleveraging, debt levels remain high

- Diversification and large scale reduce volatility risk

Corporate Profile

Headquartered in Copenhagen, ISS A/S (`ISS', or `the company') is one of the world's leading facility services providers. As of end December 2011, the company reported DKK77.6 billion (EUR 10.4 billion) in revenues and DKK 4.4 billion (EUR 0.6 billion) in operating profit before other items.

ISS is an integrated service provider. In addition to cleaning services, which represent approximately half of ISS's revenues, the company also provides services such as property, catering, support, security and facility management.

Funds advised by EQT Partners and Goldman Sachs Capital Partners own 98% of ISS's shares, with management holding the remaining 2%.

Rating Rationale

The B2 corporate family rating (CFR) primarily reflects the company's weakly positioned credit metrics with, in particular, its high leverage being a constraint on the rating. More positively, the company has a strong business profile underpinned by its (1) scale and diversification; and (2) wide geographic footprint with increased presence in emerging growth markets.

DETAILED RATING CONSIDERATIONS

IPO POSTPONED TILL 2015

2011 was a somewhat turbulent year for ISS and was heavily influenced by (1) the company's postponement of its initial public offering (IPO), originally scheduled for March 2011, due to market uncertainty; and (2) the aborted takeover attempt by G4S. At the presentation of its full-year results for 2011, ISS said it would now target an IPO in 2015 and until then focus on a combination of organic growth, selected divestments and deleveraging.

ACQUISITIVE ACTIVITY SCALED BACK; FOCUS ON ORGANIC GROWTH

Up until 2009, ISS was to a large degree acquisition-driven, with the annual amount spent by the company on acquisitions exceeding its free cash flow. This resulted in leverage, measured as debt/EBITDA, remaining high for the B2 rating category and increasing to 7.4x in 2009.

Against the backdrop of a challenging economic environment and acknowledging that its business had reached a satisfactory global scale, over the past three years ISS has significantly cut its acquisition-related spending allowing for credit metrics to improve with leverage reaching to 6.7x for the 12-month period ended 31 March 2012. While we cannot exclude the potential for further acquisitions, particularly in emerging markets or certain regional markets where the existing service platform may not be of a satisfactory scale, we would expect any transaction to be bolt-on in nature. We would also expect ISS to continue reviewing its existing portfolio of activities and potentially divest itself of activities that are sub-scale or deemed to be non-core, as exemplified by the 12 divestments the company made during 2011. This process has continued into the first quarter of 2012 when ISS made two additional divestments.

DESPITE DELEVERAGING, DEBT-LEVELS REMAIN HIGH

Under ISS's strategy of focusing on deleveraging going forward, the company will target lower absolute levels of leverage and net debt prior to an eventual IPO in 2015.

While we expect ISS's net debt reduction efforts to be boosted by a scaling back of its business investments, we also note positively that over the two last years ISS has managed to increase its level of profitability, although margins for 2011 were slightly below those of 2010. On the back of a difficult operating environment in parts of Europe, we expect 2012 to be a challenging year for ISS. However, a continued strong performance by ISS in emerging markets - where margins overall tend to be higher - and continued growth in the company's integrated facility services (IFS) business should mitigate the pressure on ISS's margins that we expect to see from underperformance in some European countries. As of Q1-2012, ISS's operating margins were down to 4.5% against 4.6% in the same quarter 2011. The company expects full-year operating margins to be around the level realised in 2011.

Despite the deleveraging that has occurred since 2009, the company's high debt levels continue to constrain the rating. In particular, ISS's interest burden remains high and is exerting pressure on its free cash flow and financial flexibility. An eventual IPO in 2015 would have a positive impact on the company's credit metrics, assuming it applies proceeds to the reimbursement of debt. However, such an event is beyond our rating horizon and we expect the overall weak positioning of ISS's credit metrics to remain a constraint on the rating until further debt reduction takes place.

DIVERSIFICATION AND LARGE SIZE REDUCE VOLATILITY RISK

With around DKK78 billion (EUR 10.4 billion) of revenues in FY2011, ISS is a leading facilities services provider in an industry that remains fragmented. While it continues to have a high exposure to cleaning services, which represented 51% of total revenues in 2011, the growing importance and scale of some of ISS's remaining services have allowed for a more complete service offering that differentiates the company from many of its competitors. In particular, we view as a positive the growing importance of multi-services (18% of revenues) and IFS (21% of revenues) in ISS's business mix and believe this makes the company a more attractive partner to global companies and provides some barriers to entry in an otherwise competitive industry. We also positively note ISS's recent signing of its largest-ever contract - a five-year deal with Barclays covering 5,700 different locations. This achievement reflects ISS's ability to be an attractive partner to leading global companies.

With a presence in more than 50 countries, ISS has a wide global footprint, which helps protect it against more regional downturns or issues in operating performance. While ISS's operations remain focused on Western Europe and the Nordics, its home market - which represent 51% and 23% of group revenues, respectively - we note that the company is deriving a growing proportion of its revenues from high-growth regions including Asia, Latin America and the Pacific. In first quarter 2012, for example, ISS reported high double-digit organic growth in Asia and Latin America with India growing at 28%. While we expect ISS's strong growth in these markets to continue, we note that the company currently generates around 20%-25% of its revenues through one-off contracts. We believe this type of contracts to be more vulnerable to the economic cycle and could exert pressure on ISS's operating performance should economic conditions deteriorate.

Liquidity Profile

We consider ISS's liquidity profile to be adequate and it benefits from (1) cash balances of DKK3.490 billion as of end March 2012; and (2) access to around DKK1.4 billion available under the committed revolving credit facility maturing in December 2014. Following the amend-and-extend agreements ISS had with its lenders in June 2011, the company's maturity profile has been extended and only around DKK538 million is falling due in 2013, assuming the company's securitisation programme will continue to be rolled over.

In 2011, selected financial covenants were reset with up to 25% headroom. However, we estimate that there is currently limited room for deviation under some of ISS's financial covenants.

Besides of having a high cash-conversion, the company's liquidity is underpinned by historically low capital expenditures (capex)requirements representing around 1.2%-1.4% of revenues. While revenues are usually stable over the year, ISS's profitability shows a degree of seasonality in the summer months due the nature of the business. ISS's working capital tends to fluctuate, with negative swings in the first two quarters as expenses - such as pension contributions, insurance premium payments, holiday allowance and bonuses as well as a number of financial interests - are paid. Similarly, positive variations occur in the second half of the fiscal year when most revenues are collected.

Structural Considerations

ISS's probability of default rating is B2, which is aligned with the company's CFR. This reflects our assumption of a 50% recovery rate, which is standard for capital structure including bonds and bank debt.

The DKK4.268 billion of senior notes due to May 2016 are structurally and contractually subordinated to all other tranches of debt. As per Moody's Loss Given Default model, the rating of the senior subordinated notes is Caa1.

Other Considerations

The company maps to a Ba3 under the grid for the Moody's Global Business & Consumer Service Industry Rating Methodology published October 2010 and based on LTM adjusted metrics to March 2012. The difference between the grid and the actual rating assigned is mainly ascribed to the company's leverage which - in spite of ISS's solid business model - is considered high for the rating-category.

Rating Outlook

The positive outlook acknowledges ISS's deleveraging since 2009 and our expectation that the company will continue to achieve growth in global contracts and emerging markets. Whereas the uncertain economic environment will make improvements in profitability difficult to achieve during 2012, the combination of continued positive free cash flows and limited amounts spent on acquisitions should lead to further deleveraging.

What Could Change the Rating - Up

The rating could be positively affected by adjusted leverage falling sustainably below 6.5x. An upgrade would additionally require interest coverage (EBITDA-capex/interest expenses) approaching 2.0x.

What Could Change the Rating - Down

Negative rating pressure could develop as a result of a decline in ISS's profitability, and adjusted leverage debt/EBITDA trending towards 7.5x and interest coverage approaching 1.0x.

Rating Factors

ISS A/S

Business and Consumer Service [1][2]	**Aaa**	**Aa**	**A**	**Baa**	**Ba**	**B**	**Caa**	**Ca**
Factor 1: Size and Profitability (30%)								
a) Pretax Income (USD Million)					$111			
b) Revenue (USD Million)			$14,428					
Factor 2: Financial Strength (55%)								
a) RCF / Net Debt						6.1%		
b) FCF / Debt						1.1%		
c) (EBITDA - CapEx) / Interest Exp						1.3x		
d) Debt / EBITDA							6.7x	
Factor 3: Financial Policy (15%)								
d) Financial Policy					X			
Rating:								
a) Indicated Rating from Grid					Ba3			
b) Actual Rating Assigned						B2		

[1] All ratios are calculated using Moody's Standard Adjustments. [2] As of 3/31/2012(LTM); Source: Moody's Financial Metrics

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