MOODY'S
INVESTORS SERVICE

Credit Opinion: ISS A/S

Global Credit Research - 02 Apr 2014

Denmark

Ratings

Category	Moody's Rating
Outlook	Stable
Corporate Family Rating	Baa3
Senior Subordinate	Ba1/LGD6/LGD6/LGD6

Contacts

Analyst	Phone
Knut Slatten/Paris	33.1.53.30.10.20
Marie Fischer-Sabatie/Paris	
Eric de Bodard/Paris	

Key Indicators

[1]**ISS A/S**

	12/31/2013	12/31/2012	12/31/2011	12/31/2010	12/31/2009
Pretax Income (USD Million)	$153.6	$139.5	$108.0	$158.5	$29.8
Revenue (USD Million)	$13,970.9	$13,723.6	$14,507.0	$13,199.7	$12,919.0
RCF / Net Debt	8.5%	6.7%	6.3%	7.0%	7.1%
FCF / Debt	3.1%	1.8%	0.8%	1.6%	1.1%
(EBITDA-CapEx) / Interest Exp	1.5x	1.4x	1.3x	1.5x	1.3x
Debt / EBITDA	6.3x	6.1x	6.7x	6.6x	7.4x

[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

- Financial policies have grown more conservative

- Further de-leveraging is expected

- 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 2013, the company reported DKK78 billion (EUR 10 billion) in revenues and DKK 4.3 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, office support, security and facility management.

ISS announced on 13 March 2014 it had priced its IPO at DKK160 per share, giving it a market capitalisation of around DKK29.6 billion (EUR4 billion). 51.1% of the shares are currently in free float (including the stakes of Ontario Teachers' Pension Plan and KIRKBI Invest A/S). Funds advised by EQT Partners and Goldman Sachs Capital Partners - that used to be the majority shareholder of the company - will continue to hold a stake of 48.2% in ISS for at least 180 days after the official listing of the company.

SUMMARY RATING RATIONALE

ISS's Baa3 rating primarily reflects the company's (1) large scale and diversification; (2) wide geographic footprint, with an increased presence in emerging growth markets; and (3) high cash generation, exemplified by its 102% cash conversion ratio in 2013. At the same time, the ratings take into account (1) ISS's current leverage which is still considered to be on the high side for an investment-grade name (2) the competitive and fragmented nature of the facility services market.

DETAILED RATING CONSIDERATIONS

FINANCIAL POLICIES HAVE GROWN MORE CONSERVATIVE OVER TIME

During the IPO, ISS raised approximately DKK8.0 billion (EUR1.1 billion) of gross proceeds that the company will be applying towards reimbursing certain debt liabilities during the course of 2014. The successful listing has contributed to a significantly decrease in the company's net leverage to around 3.0x Net Debt/ EBITDA (as reported by the company). ISS has over the past 2-3 years taken a number of steps to gradually improve its capital structure. These have, among others, included an equity injection by new investors (Ontario Teachers Pension Plan and Kirkbi in 2012) and disposals of non-core assets where proceeds have been applied towards redemption of debt. As such, we consider the listing to be a continuation of the company's financial policies which gradually have grown more conservative over time. We would expect ISS to maintain a balanced approach to shareholders and creditors post the IPO.

FURTHER DE-LEVERAGING IS EXPECTED

While acknowledging ISS no longer is burdened by the aggressive capital structure it had in the past, we consider the company's leverage to still be on the high side for an investment-grade name. As such, we would expect the company to continue de-leveraging going forward. As the debt-burden now has been materially decreased, we expect the company's cash flows to strengthen considerably as interest costs abate. Moody's also notes ISS has obtained a more attractive pricing on its new unsecured senior facility. Whilst ISS will be aiming towards a 50% dividend payout-ratio on profit before goodwill amortisations and impairment on brands and customer contracts starting 2015 (for financial year 2014), we would nonetheless expect ISS to maintain strong free cash flows allowing for net leverage to continue decreasing. ISS has over the past few years focused on organic growth. We would expect the company to pursue a similar strategy going forward. Whereas smaller bolt-on acquisitions financed by free cash flow can be accommodated within the rating category, we do not expect ISS to embark upon larger debt-financed acquisitions.

Moody's expects that the company's leverage -- defined as Moody's adjusted debt/EBITDA -- will be slightly above 4.0x by the end of 2014. During 2013, ISS's operating margins were negatively affected by the divestment of the higher-yielding pest-control activities as the operating margin reached 5.5% (against 5.6% in 2012). The company's EBITDA was also negatively impacted by substantial restructuring-costs (DKK379 million charged for the year). For 2014, we anticipate ISS to again return to growth in EBITDA supported by ongoing good organic growth (organic growth in 2013 was already strong at 4.3% supported notably by the start-up of larger IFS-contracts). We would also anticipate margins to slightly improve as ISS starts deriving scale economies from the abovementioned IFS contracts. Moody's notes, however, that ISS was negatively impacted by FX-movements in 2013 and caution this may also be the case for 2014.

DIVERSIFICATION AND LARGE SIZE REDUCE VOLATILITY RISK

With around DKK78 billion (EUR 10 billion) of revenues in FY2013, 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 49% of total revenues in FY2013, 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 (17% of revenues) and

IFS (26% 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. Moreover, these contracts were also a main contributor (together with emerging markets) to ISS's solid organic growth in 2013. In some regions, we believe there is an increasing market interest in the IFS product and we would expect the solid growth dynamics seen in recent years to continue.

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 21% of group revenues, respectively - we note that the company is deriving a growing proportion of its revenues from high-growth regions in emerging markets. However, we note that the company currently generates around 20%-25% of its group revenues through above base business. 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. Equally, the company is likely to derive additional benefits from such contracts as the economic environment improves.

Liquidity Profile

We expect ISS's liquidity profile to be good over the next 12 months and notes its new unsecured facilities mature in 2017 and 2019 respectively. Pro-forma for reimbursement of the senior secured debt following the IPO, ISS had cash-balances of around DKK1.7 billion (EUR0.3 billion). Further liquidity cushion is provided by the company's new EUR850 million revolving credit facility. Moody's expects ISS to maintain a solid headroom to maintenance covenants it has to meet.

Besides having a high cash-conversion, the company's liquidity is underpinned by historically low capital expenditures (capex) requirements representing around 1.1%-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 to the nature of the business when it is at a low point. 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 new loan facilities are senior unsecured. The company's senior secured indebtedness was reimbursed on March 18, 2014. ISS anticipates to repay the outstanding subordinated notes on 15th May 2014. Moody's anticipates to withdraw the Ba1-rating on these notes when they are repaid.

Other Considerations

ISS mapped to a Ba3 under the grid for the Moody's Global Business & Consumer Service Industry Rating Methodology published October 2010 and based on estimated adjusted metrics as of end 2013. Following the successful IPO and the impact it will have on the company's credit profile, we anticipate the grid-indicated rating to be Ba1 by the end of 2014. The difference between the grid and the actual rating assigned reflects ISS's solid business profile and track record of resiliency as well as Moody's anticipation that credit metrics will continue to strengthen as ISS continues to emphasize further de-leveraging.

Rating Outlook

The stable outlook reflects Moody's expectation that ISS will continue deleveraging, allowing for leverage to improve further from an anticipated high-point slightly above 4.0x by year-end 2014 on an adjusted basis. Moreover, the stable outlook also incorporates Moody's expectation that ISS will maintain conservative financial policies post the IPO, allowing for cash flow metrics to strengthen.

What Could Change the Rating - Up

Upward pressure on the rating could occur if ISS's adjusted leverage were to fall below 3.5x with an RCF/net debt in the high-teens.

What Could Change the Rating - Down

Negative rating pressure could arise if the group's operating profitability were to decline, with adjusted debt/EBITDA remaining above 4.25x and an RCF/net debt below 15% on a sustainable basis.

Rating Factors

ISS A/S

Business and Consumer Service [1][2]	**Current FY 12/31/2013**		[3]Moody's 12-18 Month Forward View	
Factor 1: Size and Profitability (30%)				
a) Pretax Income (USD Million)	$153.6	Ba	$530-$630	A
b) Revenue (USD Million)	$13,970.9	A	$13,500-$14,150	A
Factor 2: Financial Strength (55%)				
a) RCF / Net Debt	8.50%	B	15%-17%	Ba
b) FCF / Debt	3.10%	B	4%-5%	B
c) (EBITDA - CapEx) / Interest Exp	1.5x	B	2.6x-3.6x	Ba
d) Debt / EBITDA	6.3x	Caa	3.75x-4.25x	B
Factor 3: Financial Policy (15%)				
d) Financial Policy	Ba	Ba	Baa	Baa
Rating:				
a) Weighted Average Factor Result		Ba3		Ba1
b) Actual Rating Assigned		Baa3		Baa3

[1] All ratios are calculated using Moody's Standard Adjustments. [2] As of 12/31/2013; Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures