Event:	ISS A/S Q3 Report 2013
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Speakers:	Martin Hansen Jeff Gravenhorst Heine Dalsgaard Barbara Plucnar Jensen
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Tuesday, 12 November 2013

OPERATOR: Welcome to the ISS Q3 report call. At this time participants are in 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 Martin Hansen from investor relations.

Please go ahead.

(Introduction played)

MARTIN HANSEN: Ladies and gentlemen, welcome to the investor call and presentation of the Q3 results. Please be aware that our announcement, the report as well as the slides used for this call can be found on the website where the webcast will also be available after this call.

I would like to draw your attention to slide number 2 regarding the forward looking statements.

If you turn to slide number 3 you will find the agenda for this call. We will go through a few key events, as well as give you an update on financials and capital structure. We will conclude with the outlook for 2013 followed by a Q&A session.

With me today I have Group CEO, Jeff Gravenhorst; Group CFO, Heine Dalsgaard; Group Treasurer, Barbara Plucnar Jensen who will take you through the presentation.

I will start the presentation by passing you over to Group CEO Jeff Gravenhorst on the key events.

JEFF GRAVENHORST: Thank you, Martin. Good afternoon everybody and welcome also from my part to the Q3 results of ISS 2013. If I could just ask you to pay attention to slide number 5 in the presentation that has been forward.

I am going to take you through a couple of key events in ISS over the last quarter but basically for the year of 2013. The first thing is the operational performance. I will talk a little bit about the divestment of non-co activities, the financing and of course, the strengthening of the management team.

If I can draw your attention to slide number 6. So, starting with the operational performance overall we have had some solid results for the first nine months of 2013 with robust organic growth, stable operating margin and a very strong cash conversion and cash flow. This is pretty much in line with the expectations. We are particularly happy with organic growth which, of course, is influenced by some very large wins at the end of last year which are basically the Barclays accounts, the Novartis account and of course, also the Citi account in Asia Pacific and we are now up and running almost 100% on those three major accounts.

Other major wins for this year has been Heinz in Europe, HJ Heinz in Europe, the Nordea bank we now have throughout the Nordic region, Vattenfall which includes the nuclear plants in Sweden is also some of the recently won contracts.

Just as late as yesterday we announced the win of the terminal 2 in Heathrow Airport as well and these are all relatively large IFS contracts where we deliver a suite of services to support our clients.

This is obviously one of the reasons why we have had good growth also in the developed markets and this is one of the best part of the development of ISS is yes we have had good organic growth in the emerging market but also in part of the European zone.

So, despite up against relatively weak macro-economic conditions in the European zone, we have been able to via these large IFS contracts and international contracts to get through the first nine months with around 4% organic growth.

Margin wise, on a like for like basis or adjusting for the divestment of pest control, we also are slightly up on last year's margin and as I said, the cash flow is pretty strong with a cash conversion of 108 which we will come back to in just a second.

It is important when we look at the top line that it is impacted by three things: one, the organic growth of 4% but also from the fact that we are selling off non-core activities.

So, if I can draw your attention to slide number 7 and lastly, of course, the top line is also impacted by currency which Heine will come back to in a second. But if you look at the divestment of non-core activities for the year,

we will continue and are continuing to review the portfolio within ISS of services and in that we have, as we said before, identified a number of businesses which there are better owners to than ISS, services that we have acquired, either via other acquisitions or which are no longer in part of the core of ISS.

The core in our services are predominantly site based services where we can deliver to the large enterprises, large hospitals, etc, the full suite of cleaning, security, reception services, catering, hardware or hard services to all of these clients basically as a one-stop shopping solution.

Services that falls outside of this we are reviewing whether in some parts of the world it is better value in selling it off or to keeping it as part of our core.

In that we have during the year sold off a significant part of our businesses and predominantly in the Nordic region we have sold off the damage control business in the last quarter. We also earlier this year sold off the pest control business. Both of them, of course, have an impact on the top line but also as a result have helped us to reduce the overall leverage of the company.

We still have another five businesses which is held for sale. The asset value is about 1.3 billion. These non-core activities include areas over the region's Nordic and Western Europe which is the predominant part of it.

On the financing side, if we can turn to slide number 8, we have continued to optimise on our financing structure. Both Heine and Barbara will take us through more details on that in a second but very importantly is that we in May redeemed about €232 million of the 8.875% senior subordinated note for 2016 and that in itself is giving us an interest savings of around €20 million a year. This combined with the leveraging that we have done over the last few years, of course, puts us in a position where we have good cash surplus on an annual basis which, of course, again gives us even better opportunities to keep the deleveraging of the company.

We have also extended our securitisation programme. We did that in August, also with a reduced interest margin of around 25 basis points.

We have, in connection with the refinancing earlier this year, also built in a number of or a good -- refinance flexibility which, of course, should we embark on the listing that could take us through also in the event of a listing of the ISS company in the future.

So, from that perspective, we are in a very good financing position. We have a good operational result and the focus on the business due to the divestment of non-core activities, of course, make ISS an even stronger company also for the future.

With that, we have, as the last part, strengthened the management team during the year and if I can draw your attention to slide number 9, that we in the beginning of this quarter, had the privilege of introducing Heine Dalsgaard as the Group CFO of the company and also John Peri joined the organisation as the Group COO (Chief Operating Officer) for America's operations and the Asia Pacific operation.

That, together with, of course, Henrik Andersen, our former CFO, taking over the responsibility for the operation in EMEA has strengthened the capabilities of the organisation to continue to focus and execute on the ISS Way strategy that makes the company even stronger towards the selected sectors that we are working with, i.e. continue to serve the multi-service contracts to large international, both local and regional and global contracts.

This is also the reason, as I said before, why we can finish this third quarter with some very solid results. This is because of the growth in the IFS business. It is the growth in the emerging market business and it is the focus on being able to achieve the margin and the cash flow as expected.

So, with that in mind, it has been a good first nine months but let's go a little bit more into the detail of the financial results. I would like to hand over to our new Group CFO, Heine Dalsgaard.

HEINE DALSGAARD: Thank you, Jeff and good afternoon. Let's go to slide number 11.

I will now take you through the three key operational activities and priorities of ISS which are organic growth, operating margin and cash conversion.

So, if we start with the organic growth the revenue for the first nine months of the year is 58.8 billion Danish kroner corresponding to an organic growth of 4% year to date. The 4% organic growth was partly offset by a successful divestment of non-core activities and a negative effect from exchange rates.

The organic growth was driven by both developed and emerging markets with Asia contributing again with a double digit growth. I will take you through this in further details in just a while.

On a global basis, the organic growth was mainly driven by a start-up of the Barclays and the Novartis contracts as well as continued strong growth in emerging markets.

On operating margin we closed the first nine months with 3.1 billion year to date in operating profits, which corresponds to an operating margin of 5.3% year to date compared to 5.4% year to date in 2012. The operating margin was in line with our expectations and the operating margin was negatively impacted by the strategic divestment of non-core activities as well as the start-up of multinational IFS contracts.

The divestment of the pest control activities reduced the operating part of it for the third quarter by 58 million and the margin by 21 basis points compared with the same period in 2012.

On cash, we closed Q3 with a LTM cash conversion of 109% compared with 98% last year which is the result of a strong cash flow performance in all regions. Cash continues to be very important to us in ISS so this is a result that we are particularly proud of.

Now let’s go through the three key priorities per region and let’s turn to slide number 12. That’s under revenue. In total we have a revenue decrease of 0.3% year to date which consists of negative currency impact of 2.5% and negative impact from divestment of non-co activities of 1.8% which then again takes us to an organic growth year to date of 4%.

With the exception of the Pacifics we have positive organic growth in all regions. So:

Western Europe an organic growth of 5% and in particular strong performance in UK, Turkey and Switzerland;

Nordic 0%+ growth, strong performance in Norway which was offset by a negative growth in Denmark, Finland and Sweden;

Asia 15% organic growth, again strong double digit growth, strong performance across several countries in the region with Indonesia being the largest contributor;

Pacific, which then consists of Australia and New Zealand, an organic growth of minus 2% and the organic growth was negatively impacted by the loss of some large contracts;

Latam, again that comprises of the Latin-America region, a growth of 6% organic growth year to date, all countries reported positive organic growth in the region driven by a continued high level of new sales;

North America which is then US and Canada, an organic growth of 3%;

Eastern Europe an organic growth of 4% and particular strong performance in Slovenia, Russia and Hungary.

This then overall takes us to an overall group performance year to date with an organic growth of 4%.

Then let's move on to the second key priority and that is the operating margin and then I ask you to go to slide number 13. So: operating margin before other items in total an operating margin of 5.3% year to date which is in line with our expectations in comparison with last year. Please remember the **divestment** of the margin accretive pest control activities which on an annualised basis has a negative effect on our margin of 0.2%.

So:

Western Europe an operating margin of 5.4%, negatively impacted by the divestment of non-core activities by the start-up of Barclays and Novartis and by operational challenges in certain countries;

Nordic, a very strong operating margin of 7.1%, up 0.2% with particular strong performance in Finland;

Asia, 7.5% which continues to be the highest margin region we have, strong performance in particular in Thailand and Indonesia;

Pacific, 4.6%, a decline of 0.4% which primarily relates to divestment of the pest control activities;

Latam, 4% operating margin, a decline of 0.5%, primarily coming from Uruguay, Mexico and Argentina;

North America, 2.8% operating margin, down 0.8% and the decrease in North America is mainly a result of the loss of a couple of very large contracts combined with initial investments relating to the start-up of new contracts;

Eastern Europe, a very strong performance, up to 6.1%

And that in total gives us an operating margin year to date of 5.3% which, as mentioned, is in line with our expectations.

Then, move on to the last of our key priorities on slide number 14 which is cash and cash conversion. Again, cash remains a key priority for ISS and we closed the quarter with an LTM cash conversion of 109% compared to 98% last year and here we have a very strong focus and thereby also very strong performance across all our regions: Western Europe 108%, Nordic 102%, Asia 111%, Pacific 130%, Latam 146%, North America 99% and Eastern Europe with 96%.

This then ends the update on the financial result and I will now hand it over to Barbara to take us through the capital structure. Barbara

BARBARA PLUCNAR JENSEN: Thank you very much, Heine.

If I can turn your attention to slide number 16 this is a true demonstration of our commitment to delever the company.

During 2013 several incidents have caused the fact that we can continue the path we are on. First of all, as both Jeff and Heine has mentioned, we have divested a number of companies which we can use the proceeds to repay debt with.

Furthermore, this has an accelerated impact on the interest cost if you take, the bonds that we have taken out this year which is €232 million of the 2016 notes, together with the interest savings from the bond 2014 of 11% that we took out last year. This together gives us a saving of annual interest almost close to 600 million Danish kroner.

So, that of course has a positive impact on the deleveraging profile of the company.

Furthermore, as Heine just went through, the very strong focus on the cash performance also continues to support the performance of the company. So, despite the typical seasonality that we usually have in the first half of the year, this has just been a continued positive trend throughout 2013.

If you look at the absolute level of debt this alone year on year has decreased to the tune of 3.3 billion Danish kroner, amounting to a deleverage of half a turn.

If you turn to slide number 17 you will see the details of our capital structure. The significant change in the last quarter has been the redemption and excess proceeds relating to the 2016 notes where we, as mentioned, took out €232 million in July.

This means that, as mentioned, alone on this redemption we will have annual savings of around €20 million going forward. It strengthens the profile of the capital structure and together with the refinancing of the majority of our debt back in April, we believe that we have a good and solid capital structure to bring us into the future.

If you look at the maturity profile of the company, you can see this on slide number 18, you can see that we have now managed to address all the upcoming maturities of the company.

As mentioned in April we executed the refinancing where we addressed the majority of our senior facilities as well as refinancing the second lien we had previously expiring in 2015.

So, this means that we now have the senior facilities running until 2017 and 2018.

Furthermore, in August we rolled the securitisation programme, as Jeff also mentioned, with one additional year to 2015.

So, all in all, we have a comfortable maturity profile ahead of us as we go into the next quarter.

This concludes our update on the current trading of the company and I would, therefore, like to hand over to Jeff to take you to the outlook for 2013.

JEFF GRAVENHORST: Thank you, Heine and thank you, Barbara.

For the first nine months, as I said, we have delivered some solid results on the growth line, margin wise and of course, also from a cash perspective. I think from our financing perspective we are also in a very good shape when we look also for the future.

The outlook for 2013 is, of course, based on a little bit of a mixed bag of the global macro-economic outlook.

We still see that the developed markets, particularly Europe, is low in growth. We have some difficulty macro-economically. We still see strong growth coming out of the emerging markets, so on that sort of backdrop what we expect for 2013 is for a full year effect to be higher than 3%.

I think it is important to highlight that we had a good strong start of the first nine months organically because of some of the large contracts started up at the end of last year. These large contracts started up in Q4 2012 gradually which, of course, will also mean that we will have a lower growth in the fourth quarter than we had in the third quarter. But overall we still expect it to be above the 3% for the year end.

Operating Margin wise, we expect a negative impact from the divestment of the margin accretive pest business, as already mentioned. That effect will be around 0.2% on an annualised basis. We expect to be slightly lower than last year at the end of this year but that means also for on a like for like basis slightly above when the year is over.

From a cash conversion point of view, we are still performing very well, as you can see also from the debtor days that is dropping in the third quarter.

We expect to continue that strong cash flow in also the fourth quarter and we will be above the 90% on the cash conversion for 2013, so our expectation is to continue the business in a good way and we are pretty happy with the first nine months of 2013.

Now, before we hand over to the Q&A, just one short comment on the potential of an exit for our owners of ISS ownership.

I want to reiterate that an IPO remains the one option for the company to exit and we do have some expansion work that has been undertaken on that option. However, we have taken no decision yet and there will be no further details on this matter that we can give at this point in time.

So, basically, yes we are working with it but there is no decision taken and there is no further details on this matter today.

So, with that in mind, I would like to pass over to the Q&A session.

OPERATOR: Thank you. We will now begin the question and answer session. If you have a question, please press 0 and then 1 on your touch tone phone. If you wish to be removed from the queue, please press 0 and then 2.

If you are using a speakerphone, you may need to pick up the handset first before pressing the numbers.

Once again, if you have a question please press 0 then 1 on your phone … that is 01 to ask a question. 01.

I would like to remind you that it is 01 to ask a question, 01.

Our first question comes from Mr Paul Checketts from Barclays. Please go ahead.

PAUL CHECKETTS: Hi everyone. I was hoping to ask about the pipeline of IFS work please and also you have talked about the outlook for the rest of this year but how are you feeling about underlying trends across the group going into next year?

JEFF GRAVENHORST: Thank you. From an IFS perspective, we do have a strong pipeline of contracts also both global contracts but also by country. We don't publish the numbers for the pipeline right now but the underlying trend is that the market is moving towards the bundling of contracts. There is a lot of activity and there is a lot of demand for integrated facility services offering but also across the countries.

So, from a trend perspective, country by country, I think the underlying growth looks good. It is, of course, still impacted by weak growth in the European market but that is, of course, also then helped by the fact that we can sell bundle services across countries, which is the region why we had very good or decent growth in Europe also in the first nine months of 2013. We will expect that to continue.

PAUL CHECKETTS: Thanks.

OPERATOR: I remind you that you have to press 01 on your telephone to ask a question. That is 01.

It is 01 to ask a question.

Ladies and gentlemen, this concludes today's investor call. Thank you for participating. You may now disconnect.