MOODY'S
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Credit Opinion: ISS A/S

Global Credit Research - 25 Jul 2011

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**

	2010	**2009**	**2008**	**2007**	**2006**	**2005**
Pre-tax Income (DKK millions)	**929**	**159**	**-440**	**-27**	**-710**	**1,398**
RCF / Net Debt	**7.5%**	**6.9%**	**7.8%**	**7.0%**	**5.3%**	**-15.2%**
FCF / Debt	**1.6%**	**1.1%**	**3.0%**	**1.5%**	**0.1%**	**-19.9%**
Debt / EBITDA	**6.6x**	**7.4x**	**7.2x**	**7.1x**	**7.8x**	**6.8x**
(EBITDA - Capex) / Interest Expense	**1.5x**	**1.3x**	**1.3x**	**1.5x**	**1.2x**	**2.3x**

[1] All ratios adjusted according to "Moody's Approach to Global Standard Adjustments in the Analysis of Financial Statements for Non-Financial Corporations - Part II" Rating Methodology located at www.moodys.com

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

Opinion

Company Profile

ISS World Services A/S is the wholly owned subsidiary of ISS A/S and one of the world's leading facility services providers. In 2010, the company reported around DKK74.1 billion (close to EUR 9.9 billion) in revenues and DKK4.3 billion (about EUR 577 million) in operating profit before other items and impairment.

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

Funds advised by EQT Partners and Goldman Sachs Capital Partners own 98% of the group. Management holds the remaining 2% of the shares. The company is contemplating an IPO but the timing is subject to market conditions and therefore remains unknown.

Rating Rationale

Although ISS has not executed its IPO plans due to continuing challenging equity market conditions (originally planned for launch in March 2011), the B2 corporate family rating with a positive outlook reflects (i) steadily improving operating performance driven by the rapid growth in emerging markets and integration of past acquisitions resulting in improved financial metrics, (ii) extended maturity profile of around DKK18 billion of its bank debt removing medium-term refinancing risk and (iii) continued focus on organic growth and more disciplined approach towards acquisitions.

The rating of the senior subordinated notes due 2016 is Caa1. This reflects the subordination of the notes to the other tranches of debt.

Key Rating Drivers

Diversification and large size reduce volatility risks

ISS's business profile appears strong for the rating category, mainly due to the breadth of its operations, both in terms of segments and geographies.

As a global player, with employees in more than 50 countries, ISS appears less vulnerable to regional variations and changes in regulations than its smaller local competitors. In addition, the broad range of services it can offer multiply cross-selling opportunities. The company benefits from some economies of scale, with the potential for cost savings especially in the purchasing and marketing corporate functions.

ISS's business profile is also enhanced by its large customer base. The company has indicated that it serves over 200,000 customers with the top ten accounting for less than 5% of 2010 revenues. ISS has also indicated that churn rates are relatively low, with clients usually remaining with ISS for eight to ten years or more. About 75%-80% of ISS's revenues are stemming from portfolio-based contracts, the remaining being generated by one-off projects.

The creation of the global Corporate Client organisation set up in 2007 to win integrated facility services (IFS) contracts with large global clients epitomises the drive toward an integrated facility services business. So far, ISS has signed international IFS contracts with HP, EDS, Shell, Sony Ericsson, the UK Foreign Commonwealth Office and Citi.

Large footprint with presence in mature and emerging markets

Northern Europe and Continental Europe still represent ISS's main markets. However, the company is increasing its presence in high-growth regions including Asia, Latin America and Pacific, where it expects higher growth rates than in mature markets. Expansion in the US is also high in the agenda. Revenues from the US comprised 4% of total turnover in 2010 (1.7% in 2007).

In Q1 2011, ISS reported continued strong development in emerging markets, delivering organic growth of 15% with high double digit growth in Asia and Latin America.

ISS has established relatively good brand recognition in its traditional markets which provides the business with a certain degree of stability. In emerging countries however, ISS's scale is currently limited and we expect the company to continue to grow both organically and through acquisitions. In Q1 2011, emerging countries contributed 19% of the company's total sales.

Improving credit metrics but ISS's large debt remains costly

Since 2009, ISS reduced its spending on acquisitions in order to protect its key credit metrics. In the context of the economic downturn which affected the company's top line and profitability, ISS also focused on cost saving measures. This combined with the disciplined acquisition spending the last years have had a positive impact on the company's 2010 key credit metrics. In particular, the debt to EBITDA ratio decreased to 6.6x and the retained cash flow to net debt increased to 7.5%.

We expect ISS's profitability to further improve in the medium term as the company continues to win global contracts and expand in emerging markets. However, the company's cash flow generation will remain weak until ISS reduces its interest burden through debt repayment. The contemplated IPO, if completed, will strengthen the company's financial profile given that the proceeds are expected to be used to repay a portion of the debt.

Liquidity

ISS's liquidity profile is adequate despite the postponement of the proposed IPO. As a result of the completion of the amend and extend process with its lenders in June 2011, ISS's debt maturity profile has been lengthened and the capacity to increase the revolving credit facility by DKK1.5 billion to DKK4 billion has been ensured. The extension of the revolving credit facility and the letter of credit facility to 2014 and of around DKK15 billion of the remaining bank debt to 2015 from 2013 has removed short term refinancing risks.

In addition, selected financial covenants have been reset with up to 25% headroom. The new definitions of covenants include the securitisation programme in the debt calculation.

The company's liquidity is underpinned by historically low requirement in terms of capital expenditures representing around 1.2%-1.4% of revenues. While revenues are usually stable over the year and profitability shows some degree of seasonality in the summer months due the nature of the business and given various dynamics on the salaries, working capital tends to fluctuate. It tends to undergo negative swings in the first two quarters, when expenses - such as pension contributions, insurance premium payments, holiday allowance and bonuses as well as a number of financial interests - are paid, and positive variations in the second half of the fiscal year, when most revenues are collected.

Structural Considerations

ISS's probability of default rating is B2 - 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 EUR581.5 million senior notes due 15 May 2016 are structurally and contractually subordinated to all other tranches of debt. As per our Loss Given Default model, the rating of the senior subordinated notes is Caa1.

Rating Outlook

The outlook is positive reflecting our expectations that ISS will continue to benefit from positive market momentum due to a combination of continued outsourcing, growth in global contracts and in emerging markets. We also expect further improvement in ISS's operating margins thanks to its flexible cost base.

What Could Change the Rating - Up

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

What Could Change the Rating - Down

There could also be negative pressure on the rating or outlook in case of decline in operating profitability, adjusted debt/EBITDA trending towards 7.5x and interest cover closer to 1.0x.

Rating Factors

ISS A/S

Global Business & Consumer Service Industry	Aaa	Aa	A	Baa	Ba	B	Caa-C
Factor 1: Size and Profitability (30%)							
a) Pretax Income (USD Million)					165.6		
b) Revenue (USD Million)			13,199.7				
Factor 2: Financial Strength (55%)							
a) RCF / Net Debt						7.5%	
b) FCF / Debt						1.6%	
c) (EBITDA-CapEx) / Interest Expense						1.5x	
d) Debt / EBITDA							6.6x
Factor 3: Financial Policy (15%)							
a) Financial Policy					X		
Rating:							
a) Indicated Rating from Grid*					Ba3		
b) Actual Rating Assigned						B2	

*Based on FY2010 results

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