

# RatingsDirect®

---

## Summary:

### ISS A/S

#### Primary Credit Analyst:

Paul O'Reilly, London + 44 20 7176 7087; paul.oreilly@spglobal.com

#### Secondary Contact:

Anna Stegert, Frankfurt (49) 69-33-999-128; anna.stegert@spglobal.com

## Table Of Contents

---

Rationale

Outlook

Our Base-Case Scenario

Company Description

Business Risk

Financial Risk

Liquidity

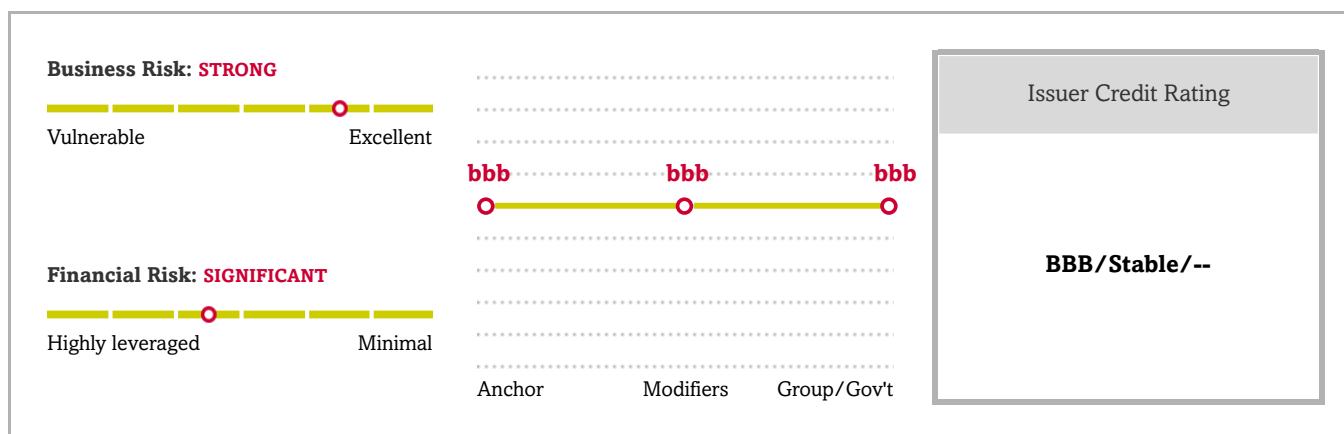
Issue Ratings--Subordination Risk Analysis

Reconciliation

Related Criteria

## Summary:

# ISS A/S



## Rationale

Business Risk: Strong	Financial Risk: Significant
<ul style="list-style-type: none"> <li>• Leading player in the naturally resilient facilities services industry.</li> <li>• Wide geographic and customer diversity.</li> <li>• Resilient nature of the basic services business.</li> <li>• Highly competitive and fragmented facilities management sector, with relatively low margins.</li> <li>• Limited flexibility in pricing.</li> </ul>	<ul style="list-style-type: none"> <li>• Strong cash generation from business operations, with low fixed asset intensity and capital expenditure (capex) needs.</li> <li>• Forecast funds from operations (FFO) to debt of 24%-27%.</li> <li>• Bolt-on acquisition strategy targeted at enhancing core service offering. Financial policy targeted at maintaining stable credit metrics.</li> <li>• Exceptional liquidity position.</li> </ul>

**Outlook: Stable**

The stable outlook on ISS A/S reflects S&P Global Ratings' expectation that the company will continue to see modest growth in revenues and generate sustainable cash flows. We also expect that ISS will continue to distribute excess cash to shareholders, such that credit metrics will stay relatively stable over time. We consider ISS' S&P Global Ratings-adjusted FFO to debt of 20%-30% as commensurate with the current rating, and expect the ratio to remain at the higher end of that range.

**Downside scenario**

ISS' credit metrics provide comfortable headroom at the current rating. However, we could lower the rating if shareholder distributions rose significantly, debt levels increased, or ISS' operating performance deteriorated such that FFO to debt fell below 20% on a sustained basis.

**Upside scenario**

We could raise the rating if ISS' operating performance continues to be stable while it maintains strong free operating cash flows. An upgrade would depend on the company implementing a financial policy to continually reduce leverage and refraining from distributing excess cash to shareholders. We could consider raising the rating if ISS sustained FFO to debt above 30%.

**Our Base-Case Scenario**

Assumptions	Key Metrics
<ul style="list-style-type: none"> <li>GDP growth in the eurozone of 2.1% in 2018 and 1.7% in 2019, and of about 3.0% in 2018 and 2.5% in 2019 in the U.S. In ISS' other key operating region, Asia Pacific, we forecast GDP growth of 5.6% in 2018 and 5.6% in 2019.</li> <li>About 2.0%-4.0% organic growth in 2018 and 2019.</li> <li>A slight deterioration in the adjusted EBITDA margin to 7.0%-7.5% in 2018, followed by a rebound to 7.5%-8.0% in 2019.</li> </ul>	<p>2017A 2018E 2019E</p> <p>EBITDA margin (%) 7.5 7.0-7.3 7.5-8.0</p> <p>Debt/EBITDA (x) 2.8 2.9-3.2 2.6-2.9</p> <p>FFO/debt (%) 26.5 22.0-24.0 25.0-28.0</p> <p>A--Actual. E--Estimate.</p>

## Company Description

ISS is a large, long-established facilities services group with operations in over 50 countries in Europe, Asia-Pacific, Latin America, and North America. ISS provides single services, multi-services, or integrated facilities services for private and public entities locally, regionally, and globally. Services include cleaning, office support, catering, security, and property and facilities management. The company is publicly held following its IPO in 2014.

During the first half (H1) of 2018, ISS reported revenue of Danish krone (DKK) 39.1 billion (down from DKK39.5 billion in H1 2017) as currency fluctuations offset stronger organic growth of 3.2% (H1 2017: 1.8%). This organic growth was driven by recently won contracts. The group continues to record strong revenue growth from integrated facilities management contracts, which now represent 39% of total group revenues, up by 9% year-on-year (yoy). The group's reported EBITDA in H1 2018 declined by about 15% yoy to DKK 1.8 billion. However, we attribute most of that decline to contract ramp-up expenses and exit costs. The decline also relates to exceptional restructuring costs that we already expected ISS to incur given the number of contracts up for tender during the first half of 2018, and the group's recent acquisitions.

Over the past few years, ISS has made significant disposals to allow it to focus on its core competencies. The company has reinvested a proportion of the proceeds in acquisitions allowing it to shift toward technical services, which are key to facilitate the expansion of its integrated facilities services. We expect the group to continue looking for acquisitions to expand its technical service capabilities as well as selectively closing gaps in its service or geographical portfolio. An example of this is its acquisition of U.S.-based catering company Guckenheimer in 2017.

## Business Risk: Strong

ISS holds leading market positions in the facility services industry across its key geographies, mainly throughout the Nordic region and Western Europe, as well as in emerging markets. ISS has good geographic diversity, and a highly diverse customer base comprising thousands of private and public customers. Historically, ISS has had a strong track record of integrating its many acquisitions, which has produced a solid global service delivery platform with critical mass to support future organic growth opportunities. The company has also managed to maintain less volatile operating profitability (measured by EBITDA margin) than that of most its peers, contributing to what we see as its strong competitive position.

ISS' integrated facilities management business offers some barriers to entry due to the necessary scale required for global service offerings, while single services generally have low barriers. ISS exhibits good contract retention, which has remained stable in recent years at about 90%.

Our business risk assessment is constrained by the competitive nature of the facilities services sector, which leaves limited pricing flexibility for service providers, keeping operating margins relatively low at about 4%-7% across the sector. Ongoing efforts to control overheads, staff costs, and food price inflation are therefore necessary.

## Peer comparison

### Financial Risk: Significant

ISS' financial metrics have improved following the company's focus on profitable organic growth and the divestment of noncore activities. We believe that ISS will continue to generate organic growth in the near-to-medium term by securing integrated facilities management contracts with new clients such as the 10-year contract with Deutsche Telekom announced in October 2017. We expect growth to be further bolstered by ISS' bolt-on acquisition strategy targeted at enhancing its core service offering.

We forecast that ISS' adjusted debt to EBITDA will marginally weaken to about 2.9x-3.2x in 2018 as restructuring costs are likely to burden operating results. We expect that leverage metrics will then strengthen to 2.6x-2.9x in 2019 as the company continues to generate organic revenue growth in the low-single digits, while benefiting from the newly won Deutsche Telekom contract and continued strong organic growth from the emerging markets. We expect the company's FFO-to-debt ratio to be around 22%-24% in 2018 and around 25%-28% in 2019, consistent with a significant financial risk profile.

Furthermore, we expect ISS to maintain its acquisition spending and shareholder returns policies in line with recent years such that credit metrics will not deviate materially from current levels. We believe that ISS will continue to generate healthy free operating cash flow given its high cash conversion rates and the flexibility it enjoys in terms of capex requirements.

## Financial summary

### Liquidity: Exceptional

We assess ISS' liquidity as exceptional because we forecast that the company's sources of liquidity will exceed its uses by more than 2.0x over the next 24 months, and that sources less uses would continue to be positive should EBITDA fall by 50%. We consider that ISS has well-established and solid relationships with its banks and exhibits prudent risk management.

Principal Liquidity Sources	Principal Liquidity Uses
<ul style="list-style-type: none"> <li>Cash and cash equivalents of about DKK4.4 billion as of June 30, 2018;</li> <li>Approximately DKK6.1 billion available under its current revolving credit facility; and</li> <li>Cash FFO of about DKK3.4 billion over the next 12 months.</li> </ul>	<ul style="list-style-type: none"> <li>Capex and working capital requirements of DKK1.2 billion;</li> <li>About DKK1.6 billion of assumed dividends and share repurchases;</li> <li>Seasonal working capital requirement of about DKK1.4 billion; and</li> <li>Post-retirement employee benefit top-ups of around DKK250 million.</li> </ul>

## Issue Ratings--Subordination Risk Analysis

### Capital structure

As of June 30, 2018, ISS's capital structure consisted of DKK17.3 billion of total borrowings, all of which were unsecured.

### Analytical conclusions

We rate ISS' unsecured notes 'BBB', in line with the issuer credit rating, as we do not consider there to be subordination risk in the capital structure.

## Reconciliation

### Related Criteria

- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, Sept. 21, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Corporates - Industrials: Key Credit Factors For The Business And Consumer Services Industry, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+ / a	a-	bbb	bbb-/bb+
<b>Strong</b>	aa/aa-	a+ / a	a-/bbb+	<b>bbb</b>	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

### Additional Contact:

Industrial Ratings Europe; Corporate\_Admin\_London@spglobal.com

Copyright © 2018 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, [www.standardandpoors.com](http://www.standardandpoors.com) (free of charge), and [www.ratingsdirect.com](http://www.ratingsdirect.com) and [www.globalcreditportal.com](http://www.globalcreditportal.com) (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at [www.standardandpoors.com/usratingsfees](http://www.standardandpoors.com/usratingsfees).

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.