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PRESENTATION

Operator

Ladies and gentlemen, welcome to the ISS Trading Update for Q3 2021. (Operator Instructions) This call is being recorded.

Today, I'm pleased to present Jacob Aarup-Andersen and Kasper Fangel. Speakers, please begin.

Michael Bjergby ***ISS A/S - Head of Group IR***

Good morning all, and welcome to ISS conference call for the Q3 2021 trading update. Please pay notice to the forward-looking statements in the appendix, and I'll hand -- give the hand over to Jacob. And slide number 3.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Michael. Let's get started. Good morning, everyone. Let me start out with the executive summary. In the third quarter, we continued to build on our new operating model. We are deep into the implementation phase. And that means that the blueprints and group concepts are slowly but surely coming to life in every single country. This builds stringency, quality and alignment across the group, and it is starting to show the first early benefits.

On the activity side, we're seeing customers gradually returning to the office. We expect a continued measured pace of return in the coming period. COVID-19 infection levels remain high across most geographies and that creates a sense of caution in many countries. That being said, the direction is clear. People are gradually coming back and customers are reemphasizing the importance of the office as the cultural epicenter of the company. We're therefore increasingly confident of the continued relevance of the office and hence the return to the office as soon as short-term uncertainty clears. This has, by the way, been evidenced by recent experience from the countries that have opened up first.

I'm pleased that our turnaround work and strict focus on the underperforming areas are paying off. The financial performance in each of the hotspots are improving. This is creating a fundamentally healthier and stronger group. COVID-19 restructuring is also delivering solid results even at the current reduced volumes. It makes our current margin recovery, to a large extent, independent of the market activities and of the timing of a broader return to office.

As a result, we can now upgrade our financial outlook on both margin and cash flow. For the latter, this is the second quarter in a row. These parameters are the most important at this point in the turnaround, creating the foundation to build a solid and healthy core that we can grow from in the long-term sustainable way. Kasper will be providing the details and the outlook later. So let's turn to Slide 5 for an update on strategy.

Our OneISS strategy can be split into our work on the operating model, our short-term financial recovery and our divestment program. The strengthened operating model is our platform for long-term performance. At this stage, a lot of hard, dedicated work goes into the heavy implementation phase. We're executing on the organization of blueprints, the upgraded group competencies and the new IT setup. It's an important time where our strategy really comes to life but where the main benefits are still to come. As highlighted in December 2020, we expect the build-out of the operating model to last all of '21 and '22. But of course, with initial benefits starting to come through during the period. In Q3, we have finalized the new IT organization and our new chief digital and technology officer has outlined the high-level guardrails for our new IT strategy. In the third quarter, we also rolled out our new daily office cleaning productivity tools, which I will come back to.

So let's turn to the next slide for details on our divestment program. We are streamlining and simplifying our business through our divestment program. We continue to have strong execution momentum with important divestments signed since the first half results.

In the third quarter, we completed the sale of 2 countries and signed 2 single service business units. For the largest business unit, completion is subject to certain conditions and therefore by nature still uncertain. With this, the aggregated net proceeds from the program now amount to around DKK 1.4 billion. As such, we are at 70% of the total target of DKK 2 billion for '21 and '22.

Please go to the next slide. On my final slide on the strategy review, I want to highlight our new productivity tool, which is now rolled out and tested in 6 countries and on selected contracts. We've known for a while that there is a significant difference in cleaning efficiencies around the world. This implies significant potential in getting all countries to best-in-class levels. That's what OneISS is all about. 80% of cleaning costs are labor related. We're now becoming much more databased when estimating cost. And based on the key variables such as number of staircases, windows, building materials, et cetera, we can provide a firmer estimate of the cost of cleaning.

I see 3 significant opportunities in the tool. Firstly, profitability can be increased by improving custom contracts. If we can move the profitability up by just 1% in daily office cleaning contracts, then it will have a measurable effect on our group results. The second part is long-term growth. If we become the most efficient cleaning company across all of the world, we will naturally gain market share and improve retention. And thirdly, it's about risk mitigation. When we are more solid and comprehensive data behind all cost estimates, we will reduce risk in our forecast and commercial bidding.

With those comments on strategy, let me go to the business review from Slide 9. We continue to be satisfied with our commercial development. Since the first half results, we did not win new deals above the DKK 100 million mark, but we won several deals just below. These wins include a large social media company in the U.S., a leading manufacturer of household products in North America as well as a contract with the Uppsala region in Sweden. Our win rate and retention rate in 2021 is fully in line with the historic trends where we over years have gained consistent market share. I also want to mention that we won the right deals during 2021. As announced at our Q2 reporting, we won Equinor and Philip Morris. These are strategically our preferred type of revenue in the right segment, the right type of customer and with a true partnership mindset. Both wins will have a full effect from 2022. And hence, we are still to see the benefits of this.

On retention, we see good progress with DKK 1 billion revenue signed since we last met. We've renewed a large international technology company in the U.S., a global industry and manufacturing company, and we extended and expanded an airport in Australia. We currently have more than usual focus on extensions and many of our 2022 maturities are in the process with good development. We are, at the same time, seeing a solid pipeline of new business building.

Please turn to the next slide for a few comments on our transaction in Turkey. During Q3, we announced a reshaping of our Turkish business. We have acquired a highly attractive asset and divested part of ISS Turkey. This is setting us up for strong financial performance without increasing exposure to Turkey nor impacting our leverage, which you know we've been very firm on. We have now manifested our leadership position in health care in Turkey, and we're already seeing how it's yielding opportunities in this prioritized segment. As a consequence, we have a very encouraging pipeline for more hospital deals, and I feel confident that we'll be announcing more positive developments based on this strengthened position.

On the next slide, we are continuously getting insights into current return to office trends. Since the summer, there is a clear trend that customers are opening their offices and allowing a larger share of employees to the office. There is, however, a difference between number of employees allowed in the office and the number of employees actually coming to the office. Employees are more gradually returning. In the dialogue with our customers, they are focused on the workplace as a critical source of innovation, productivity and sense of cultural belonging. The long-term trend is clear of return to office for more and more employees.

This concludes my business review. I'll now hand over to Kasper for the financials.

Kasper Fangel ***ISS A/S - Group CFO***

Thank you, Jacob, and good morning, everyone. I hope you are well. I would like to start out with some comments on revenue on Slide 13. The nature of the early effects of the reopening are in line with expectations. Portfolio revenue is up more than offsetting a decline in above-base revenue quarter-over-quarter. The organic growth in the third quarter was 2.6% and revenue amounted to DKK 17.5 billion. Growth improved through the quarter as some markets opened up, such as U.K. in September, but you still have a large customer that have delayed a broader return to office until 2022. It is worth noticing that the project and above-base revenue is only around DKK 200 million higher than pre-COVID levels in Q3 2019. As markets reopen, the level of above-base revenue may come down, but it will clearly be offset by higher portfolio revenue, which we also saw in this quarter.

Please move to the next slide for comments on the regions. The first highlight of this slide is that we have delivered positive organic growth in all regions. The second important highlight is that the absolute revenue increased in all 4 regions in Q3 compared to Q2. But the development in growth rates is impacted by a volatile comparison base. Finally, I also want to highlight the accelerating growth in Americas. We have strong momentum in our key account portfolio and the transition of our large manufacturing customer is supporting growth.

Generally, the 2020 comparison makes it difficult to draw any hard conclusions. It's therefore helpful to look at the current revenue compared to 2019 on the next slide. In this early reopening phase, the recovery potential of the business is key. It's not a surprise that we see diverse impacts on the business on both service lines and industries. In total, organic growth is negative 6.4% compared to Q3 2019. This corresponds to the index in the lower right corner of 94.

From a service line perspective, the largest upside is within food and the big-ticket items for food are U.S. and U.K., mainly within the office-based segment. From an industry perspective, we have capitalized well on COVID-19 opportunities within the specialized segments. We've generated underlying growth. This segment is also where we see solid demand for deep cleaning and disinfection both in schools and in hospitals. There is significant recovery potential in the other industries.

I'll now move away from revenue and provide some directional comments on the margin development. As this is a trading update, we will not disclose the Q3 margin, but it should be clear from the development of this slide that our profitability continues to improve, and the run rate margin has improved each quarter of 2021.

In the U.K., the results of our efforts continue to progress well, and our largest market is now again operating at positive operating margin. The low-hanging fruits from internal streamlining has been taken, and we are now entering into a new phase focused on contract optimization and commercial success. In France, our restructuring is progressing according to plan, and cost savings are coming through. This is supporting our run rate margin. Reduced volumes continue to be a challenge and the turnaround is a gradual movement. We have outlined a strong plan for future growth covering both customers impacted by COVID-19 and new sales.

Deutsche Telekom is on track, and we have a comprehensive plan in place to get it to breakeven. The COVID-19 restructuring under the fourth bucket on the slide is clearly having a positive impact on the results and also the reason why this Harvey ball has moved significantly. One example is the U.S. food business performance, which I really have to say is impressive considering the suppressed volumes. As you can see in the lower right corner, we have now completed more than 50% of the turnaround journey. However, the speed of the progress could naturally become slower as we get closer to our above 4% turnaround target by the end of 2022.

Please go to Slide 18 for comments on the financial outlook. As Jacob has already mentioned, we are upgrading our financial outlook. Organic growth guidance is confirmed and still expected to be positive. The overall drivers of the growth have not changed. We expect continued portfolio revenue increase, while above-base by nature is more uncertain. Q4 is normally the largest quarter of above-base revenue. But in this special COVID-19 year, the seasonality may be different. The operating margin is upgraded from above 2% to around 2.5%. The upgrade is a result of the performance of the underperforming entities as reviewed on the previous slide.

Please move to the next slide for comments on upgraded free cash flow. The free cash flow outlook is upgraded from above DKK 1 billion to around DKK 1.5 billion. The upgrade mainly reflects the improved operating margin. The 50 bps on the margin is yielding up to DKK 250 million in free cash flow after the tax is paid. The rest is driven by working capital. We assess the working capital inflow to be partly driven by structural initiatives and partly driven by timing effects as we now expect lower outflow in H2.

Our factoring expectations are completely unchanged, and the level of the end of this year is going to be very close to what we had last year. That is all for me, and I will now hand back to Jacob for some final remarks.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Kasper, and let's have the last slide. In a volatile environment, it is critical to focus on what we can control. That's why we have a clear plan outlined, and that's why we're executing forcefully on it. Our focus on the hotspots is working. I'm satisfied about the progress and how that's setting us up for long-term sustainable performance. With that said, we also acknowledge that the current margin level is far below our potential. And we still have a lot of hard work in front of us to deliver that for you. I want to give a heartfelt thanks to all employees for their daily efforts and contribution to ISS. I also want to thank them for the continued support to our customers. The pride and passion of our people makes us stand out.

With that, I would like to open up the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from the line of Bilal Aziz from UBS.

Bilal Aziz ***UBS Investment Bank, Research Division - Associate Director and Equity Research Analyst***

Three for me, please. Firstly, just on, I guess, the pipeline and the growth outlook going further than this year. I mean, you clearly spoke about trying to target the right level of growth and the right level of contract balance between risk management. How does that impact your midterm aspirations now as we look further out? That's the first question.

Second question, Kasper, you touched on the fourth quarter organic growth. How should we think about that with the exit rate within the third quarter yet within the fourth quarter [table,] please?

And then lastly, just on the margin, there's clearly aspects, which you are now delivering ahead of expectations. Which ones in particular are delivering ahead of plan? And how does that change your thinking for your guidance of 2022 with an exit rate of 4%?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Bilal. Why don't I start with the pipeline and growth outlook and then let Kasper talk about the 2 other questions? So if you look at commercial, we won several new deals since the first half results as I mentioned just before. And they're all closed but not above our disclosure threshold. So you can say we actually feel quite good around the ongoing commercial momentum. And in addition, as you know, we renewed contracts worth around DKK 1 billion since the first half results.

As per the OneISS strategy, we are quite stringent in terms of prioritizing customers that we want to work with. We've extended highly attractive contracts during the year: Barclays, our second largest customer; a significant social media company in the U.S.; and a large Danish manufacturing company. And you know we also won some significant new deals over the last couple of quarters. And at the same time, we invest significantly in the commercial structure and capabilities.

And when I look out at the pipeline that we're building right now and the interactions we're having globally, I have to say that it's firming up for a very nice pipeline when we look 12 to 18 months out. And that's, I guess, the focus of your question, that's the more midterm outlook for growth. So if I look at the commercial side of things, I think we are cautiously optimistic that we have turned the corner over the last couple of quarters in terms of our commercial momentum. There's a lot of focus in the short term around renewals, of course, but it's very nice to see that the pipeline is building globally, and it's a pipeline of the right business in the right segments, which is very important for me.

In terms of talking about what that means for growth in 2022, I think you would appreciate, Bilal, that true to form, we're not guiding on 2022 organic growth as such. But these building blocks of a good commercial momentum and the timing around postponed back-to-office effects in a number of geographies, especially around food and the U.S. means that we, of course, expect to see a growth -- a good growth in 2022, but I'm not going to be specific around how we see that. But no doubt that what we're looking into right now in terms of commercial activity underlines that optimism for the midterm.

Kasper Fangel ***ISS A/S - Group CFO***

Thank you, Jacob, and good morning, Bilal. So let me try to give some additional cover -- color on Q4 growth. I mean, first of all, and overall, we are still in a COVID-19 recovery phase. And we have seen increased base revenue in Q3 versus the first 2 quarters this year. And we expect that to continue in Q4. I think one important data point, obviously, is the actual organic growth in Q3, the 2.6% because on the face of it, it looks like we are supported by a 2% easier comparison base in Q4. But please remember, and this is super important that, that assumes the normal seasonality in a non-COVID-19 year, where above-base revenue typically spikes in Q4 against previous quarters. And that we do not expect to see this year.

So in summary, we expect higher nominal revenue in Q4 compared to Q3, but the organic growth percentage is not expected to be massively higher in Q4 compared to Q3. And of course, it is important, as I know you're all aware of that we are still operating in the middle of a pandemic. And of course, the uncertainties are very high.

In terms of your question on margin and what is going better, then we are following the plan on our margin recovery and things are coming through nicely. It's fair to say that the speed of execution is faster in the U.K. compared to what we initially expected. And I think there are 3 things that are worth highlighting here. The first thing is that the transparency has improved and is still improving in the U.K., which is obviously leading to some strong efficiencies coming through. The other thing is that the restructuring initiatives that we have taken in the U.K. is also coming through faster than expected, and we are adjusting the cost platform. And the third thing I will mention that makes us confident about the U.K. is that the changes that has been done locally to the country management team seems to work out very well, and the enthusiasm is building in the U.K.

Bridging that to your question around 2022, then it's clear. In the first half, we reported an EBIT margin of 1.5% and in order for us to get to 2.5%, then we'll have to deliver 3.5% in the second half of the year. We expect the exit run rate out of this year to be slightly above 3% adjusted for seasonality. And then, of course, it is about getting from 3% to the above 4% in 2022, but we are well on track.

Bilal Aziz ***UBS Investment Bank, Research Division - Associate Director and Equity Research Analyst***

Brilliant. That was very clear. And just a quick follow-up. Jacob (inaudible) with retention. So how is the confidence on some of your large contracts for (inaudible)

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thanks, Bilal. The line was bad maybe just on our side, but I think you asked around retention in 2022 and those deals. So when you look at the chart around 2022, we have around 8% of renewals in that. And that's a little bit higher than usual. There's one big -- there's a top 3 customer in there. If you take that out, then it's the usual around 5% retention we're looking at. All of the big names in that portfolio, we are at this stage in very advanced talks with, as you would expect. These facility management contracts at these levels -- these sizes and complexity do not get agreed with 2 weeks' notice at the end of the year. So we are in very good and constructive conversations with our clients around this. And I can only say that we have a good confidence level around how we conclude these conversations. So I'm not seeing any specific red flags that I feel I need to raise. Good and constructive dialogues that are progressing according to the plans that we laid out in the beginning of the year. So confident, but of course, with the caveat that until the ink is dry, nothing is certain.

Operator

And the next question comes from the line of Michael Rasmussen from Danske Bank.

Michael K. Vitfell-Rasmussen ***Danske Bank A/S, Research Division - Research Analyst***

Congrats from my side as well, guys. So on catering, what was the organic growth in the third quarter, please? And if you could add just more comments on any kind of regional variances here, including also on your large U.S. catering client. Do they still expect to start off offices on the first of January? So that's my first question.

Secondly, on the DKK 550 million extension you won with the U.S. tech client, when will that start up and within which -- sorry, service areas did you win? And what do you think drove that win? And my final question is if you could just discuss any issues on labor shortage and/or wage inflation, please.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Michael. Let me start on the regional variances around food in U.S., especially around U.S. Kasper can comment around growth rates in a second. But regional variances, there's absolutely no doubt when we look at the U.S. that you know U.S. is our biggest food business, followed by U.K. and then a couple of the very large European businesses. Or U.S. is the big swing factor that's also right for you to zoom in on that. What we're seeing is that a number of the larger clients on the West Coast have delayed return to office until January, as you also point out. We are seeing a -- you see a gradual return to office when we look broadly across the base. That's also why you're seeing the 8% growth across North America in Q3.

But there is a number of the large tech clients on the West Coast that have decided to fully open up in the beginning of January. And that is still the message we're getting. When you look at the U.S., there's no doubt that if you haven't opened up moving into Thanksgiving, it's starting to be impractical to mobilize the entire organization with a few weeks before Christmas. So that's why they're doing it. And we have good indications around that sticking. So that also means that's the reason why when we talk about growth and food in the U.S. that we are saying that we do see a further recovery in Q4, but the big -- some of the big contracts, it's only Q1.

You asked specifically around extension in the U.S. on the technology side, when that starts up. So that name is already up and running. So it's simply an extension of the existing contract. It is a client that is not fully back in the office. So we are not getting the full benefits of the size of the contract right now. And therefore, it is one of the contracts that we expect to pick up, especially from January in terms of volumes.

You asked about what type of business it is. It is mainly food, this contract entails. Then let me just -- why don't I finish also on the labor shortage and then Kasper can come in on the growth in catering. So on the labor side, there's no doubt that what we're seeing globally is that there is more pressure around the labor situation and the tightness is especially prevalent in the U.S. Also because you can say that in most other markets, we do see quite a high level of unionization of labor, which also means the wage agreements are relatively locked in. But the U.S., we're seeing both tightening in terms of availability of labor but also wage inflation.

As you know, most of our contracts will pass through the cost itself. And therefore, the main concern we have is around availability of people. And here, the team is working incredibly hard, especially in the U.S. where it's tightest and where we're working on a number of avenues that goes beyond what we would usually do around dealing with recruitment difficulties. One of the biggest and most important initiatives for us and drivers for us is the fact that we've started utilizing AI as a primary tool in our recruitment efforts in the U.S., which is bringing a different type of efficiency and opening of different types of labor pools with a different type of speed.

Beyond that, we have a number of other initiatives, especially in the U.S. around that. And we do also have to resort to, in some specific geographies, sign-on bonuses and retention bonuses, which is part of the game. Overall, I have to say that the message is the same as it was on -- in the first half, which is that we do not see the labor market tightness and the increased wage inflation across the board. We're not seeing that impact our expectations on our profitability levels. We are managing to pass it on, and to find further efficiencies in the few areas where we do not have a good pass-on mechanism.

With those comments, I'll hand over to Kasper on the food side.

Kasper Fangel ***ISS A/S - Group CFO***

Yes. Thank you very much, and good morning, Michael. So you are indeed right, the significant asset in terms of the recovery on food is, of course, the U.S. and the growth that we've seen in Q3 is above 5% on that one. But still, and that's important, the index is only 69 against the 2019 levels. And just to give a little bit of color on the impact and the magnitude of that improving that index to 80 will give us additional approximately DKK 2.5 billion on recovery on top line. So obviously, it is -- the big swing factor here is the Food-as-a-Service line that is what is super important in the recovery, as Jacob mentioned.

Michael K. Vitfell-Rasmussen ***Danske Bank A/S, Research Division - Research Analyst***

So the 5%, was that 5% for U.S. catering or overall catering growth?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

That was 5% for U.S. catering.

Michael K. Vitfell-Rasmussen ***Danske Bank A/S, Research Division - Research Analyst***

Okay. And do you have the global number by any chance?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Yes. We do -- I do not -- it's not far from that because the main portion is Americas, but I do not want to be exact and specific on that one, Michael. I'm sure you will understand that.

Operator

The next question comes from the line of Magnus Jensen from SEB.

Magnus Thorstholm Jensen ***SEB, Research Division - Senior Equities Analyst***

Congratulations the good results. First, a follow-up on Michael's question on difficulty in hiring. You say there's no impact on your margins. But can you give sort of a ballpark indication how much it has impacted your top line for the quarter? And then secondly, on deep cleaning and disinfection, which has clearly been a driver over the last many quarters. How did that perform this quarter? And in relation to that as well, how do you look at the above-base work for 2022? Should we see that as a big headwind? Or do you expect to continue to -- yes, to keep some of this also going into next year? That's my question.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Magnus. Let me talk about hiring and then Kasper can talk deep cleaning, disinfection and above base '22. So on the hiring in terms of how that impacted our growth profile in Q3, that is an immaterial number. So it does not have an impact that stands out as such. So yes, it has a very, very slight positive impact, but it's nothing of materiality. When we look at going into '22 also because that could be your follow-up question, again, we expect it to have a slightly positive effect, but it's not material in the sense that it's going to be a big driver of our growth next year.

Do remember that a number of our contracts are on -- with fixed wage inflations that is driven by unionized contracts. And we have savings slide, paths, on those contracts that are also fixed, et cetera. So it is not a one-for-one effect -- impact on our entire top line. So it will have a slight positive impact next year in terms of the top line growth, but it's not going to be a key driver for our revenue. And maybe you, Kasper, on the deep cleaning and disinfection.

Kasper Fangel ***ISS A/S - Group CFO***

Yes. Thank you, Magnus. It is in Q3 still continue to -- still continue at a high level, the disinfection and above-base. And I think that's underpinned what we are showing in the slide where we're comparing the index against 2019 level, you will see we have 114% on specialized and the underlying driver on that is indeed disinfection and hygiene, so still a very high level. But it is uncertain how it is going to pan out exactly going forward. Obviously, that is the discussions that we are having with the customers as we speak. What we see is that it is a continuing trend that janitorial and cleaning service is high on the agenda. It's not just a procurement exercise. It's something that has moved into the exec management team and something that they have an opinion about. And we don't expect that, that will disappear and go away. So we expect that the importance of that as a service is going to stick. But exactly whether it's going to move into base or continue as above base, that is too early to conclude on that.

Operator

The next question comes from the line of Laurits Kjaergaard from ABG.

Laurits Louis Kjaergaard ***ABG Sundal Collier Holding ASA, Research Division - Lead Analyst***

Jacob and Kasper, congratulations on your results. First of all, 2 questions to Jacob on the statements that you have made. One of them was your closing remarks where you said current margin level is far below the potential. So the first question is what is the potential? And then you've also mentioned previously that reducing churn rates will be a clear tool to mitigate higher wage inflation. Could you comment on churn rate, please, going into Q3 and going into next year?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Laurits, and thanks for also listening to my speech. I'm really impressed by that. So on the -- I thought I had lost you towards the end, it's a long speech. No, just kidding. Listen, it's very fair for you to point out my statement because I firmly believe and that view is shared very firmly by the entire management team that, of course, we are pleased to sit here today and upgrade our margin guidance to 2.5%, but we also have to say that's not where we want to be. And we made a very clear statement that we will -- we want to exit 2022 at a run rate margin above 4%.

And we've also made it clear that that's a turnaround target and that we will be coming back as we get closer to having delivered that turnaround, we'll come back and talk about what we believe the long-term potential of the business is because we have also made it clear that we do not think that, that number is 4%, but we believe it is higher than 4%. But I will not, on this call, give you the new long-term targets. That will be a conversation we'll be having as we progress through the turnaround. But I can guarantee you that you're sitting here with an ambitious management team that is pleased but will be working incredibly hard to continue the progress.

On the second part in terms of reducing churn rate, we have not specifically reduced churn rate in Q3. That would be too big of a statement. There's a lot of work going in right now in terms of our cultural journey and in terms of the people and culture initiatives that we are rolling out across the globe. Part of that is in terms of our leadership development. But the other part is, you say, more hardcore around the systems that we deploy. And one of the key aspects of that is our people at ISS infrastructure that we are rolling out right now in our key countries. That people at ISS infrastructure is a digital infrastructure that will help us link up our workforce management in a much more seamless and real-time way and will give us ability to have many more measurement points and ability to be able to react much faster when we see signs that drive churn.

I do believe that the plan we've laid out for the coming years in terms of our people and culture agenda both from a technology perspective and from a leadership perspective will drive churn down. And -- but sitting here in a very volatile labor market in Q3 and stating that we are seeing permanent effects of that, I think that would be arrogant on me. So I do see initial signs that we are on the right path in terms of the initiatives we're doing. But I think you need to give us a couple of quarters before we start seeing that playing out in our churn rates as such.

Laurits Louis Kjaergaard ***ABG Sundal Collier Holding ASA, Research Division - Lead Analyst***

That's very clear. And maybe one macro question in terms of, let's say, underlying orders because I appreciate the comments on the 3 large orders that you won below DKK 100 million during Q3 and also the 3 extensions, I guess, no larger wins in Q3 so far. But could you comment a little bit on the underlying development of orders across regions? Because it seems to me that penetration of outsourcing is finally increasing, which has been sort of quite slow for the past 10 years, actually. Can you comment if outsourcing is increasing now? Is that what you're seeing in the markets? Or what are you seeing?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Yes. No, I think that's a great observation, Laurits. When I look at the global markets, there's no doubt that we are seeing a trend of increased outsourcing. It's in the countries that are finding their feet earliest in terms of the pandemic. We are seeing a trend that a number of companies are reflecting on their experience during the pandemic and are accelerating the move towards outsourcing. We see that U.S. is a good example where we're seeing an increasing pipeline in terms of the first-time outsourcing opportunities. But we're also seeing it in Continental Europe, but more skewed towards countries where we've opened up faster.

So I do think that the pipeline opportunities are fundamentally increasing, which is your question. But as you know, there's a big lumpiness around especially larger contracts. If you look at our last quarter, where we had 2 larger contract announcements in Equinor and PMI, and the timing is -- for these big negotiations, they run in 9, 12, 18 months, and therefore, there is an element of lumpiness around it. That's also why it was important for us to flag a number of deals just below the threshold because we do continue to win small and midsized deals across the globe on a monthly basis. The big elephants are obviously great signs also for you from an external perspective in terms of momentum, but a large part of our momentum is, of course, driven by the small and midsized business as well.

Laurits Louis Kjaergaard ***ABG Sundal Collier Holding ASA, Research Division - Lead Analyst***

And you mentioned a large social media contract in the U.S., Uppsala contract, and what was the third one that you mentioned below the threshold in Q3?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Let me just have a look. It was a manufacturing company in the U.S. It was a private household products company.

Operator

(Operator Instructions) The next question comes from the line of Klaus Kehl from Nykredit.

Klaus Kehl ***Nykredit Realkredit A/S, Research Division - Chief Analyst***

Yes. Klaus Kehl from Nykredit. A question again related to the food business. You mentioned that you were quite pleased with the performance here in the quarter despite revenue still being quite negatively impacted. How come that you are pleased with the performance? Is that due to the fact that your new cost plus contracts are starting to work? That's my first question.

And secondly, could you remind me the margin in the food business. Isn't that above group level? And my third question would be around your discontinued businesses. Could you give us any input on what kind of profit you are seeing for them here in '21 or potentially in the second half? Or -- yes, any input on that line.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you, Klaus. Why don't I do the food business and then Kasper if you do the discontinued business question, that would be great. Just on the food business, the reason why we are pleased with the U.S. food business, of course, completely in your camp that revenues are not where we want them to be. But the reason why we still express being pleased is the fact that, one, we are seeing growth return. Second, we are winning food business in the U.S. I mentioned some of the contracts that Laurits was just asking around. That's food contracts in the U.S. We're winning new business in food.

And on the margin side, we're not talking margins in this trading statement, as you know, but as we stated in August, we are seeing a very strong margin recovery in food in the U.S. as we move to -- as you also said, Klaus -- you said well, Klaus, is the cost-plus models that are working out very well, that change to the cost-plus model. So we're seeing good margins in the U.S. food business, and we're seeing new wins in the U.S. food business. What we would like to see, of course, in the coming quarters, and as I said, that's more skewed to Q1 than it is to Q4, that is some of the big office-based food contracts really starting to come back in terms of office opening.

On the margin side, we've never been very specific around margins on different service lines for the simple reason that most of our offerings is integrated facility services, which means that the true margin for us lies in the mix. It is correct that if you look at pure food players that they can have a slightly higher margin than pure cleaning players in the market. For us, given the synergies between the different offerings, it's a little bit less clear. But food is not dragging margins down if I can put it like that. Then on discontinued business, Kasper?

Kasper Fangel ***ISS A/S - Group CFO***

Yes. Klaus, I can be quick on that one. The discontinued business. The margins are neutral, broadly the same as we see in the continued business. But of course, it's a mixed bag, so we have some assets that are margin accretive and some that are margin dilutive, but consolidated, it's broadly the same level as in the continued business.

Operator

The next question comes from the line of Rahul Chopra from HSBC.

Rahul Chopra ***HSBC, Research Division - Research Analyst***

I have 3 questions. First, in terms of -- could you just elaborate your comments in terms of your benchmarking? Basically, you said that you're doing some benchmarking and data analytics tool, which is helping increase pricing. Maybe share some more comments on some delta or what you're seeing on the ground there. That would be helpful.

My second question is around margin guidance. So I mean, from memory, I mean, your -- portfolio comes at higher margins, is expected to go down in Q4, and you're still increasing your margin guidance. So just wanted to understand how the margin is looking across the core portfolio basically in terms of sequential improvements?

And finally, in terms of the working capital and free cash flow guidance. I think I suspect the large part of the free cash flow is due to changes in working capital timing and underlying working capital. So some comments around kind of working capital are you seeing in the business?

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Yes. Thank you, Rahul. Why don't I start on the benchmarking tool and then Kasper talk margins and cash flow. So thanks for the question. I think the daily office cleaning benchmarking tool that you've seen in the presentation, that's part of the new developments around our operations performance structure, which is one of the key structures that we developed as part of an OneISS. It is bringing the accountability of owning business outcomes and P&L, together with the former classic operational excellence functions that you see in many other countries -- sorry, many other companies. But we wanted to take excellence to another level in terms of driving true P&L and ownership and accountability out of that unit.

So of course, we've had tools in ISS. We are the world's largest cleaning company, and we have plenty of existing tools. But what we've done here is that we take it to another level in terms of making it significantly more data-driven and that is also, of course, a sign of the times in terms of the IT and technology infrastructure we have around our FMS systems and other core systems, which means we, today, compared to the past, can drive much more data-driven insights into the different sites, and we can bring that into global databases. And then our global team of cleaning experts can then drive best practice development and data-driven solutions around specific sites.

I'll give you an example. When we did the initial testing around 6 countries, we saw significant variations in terms of cleaning efficiency. And obviously, we're not oblivious to the fact that there are significant differences between different countries. But there are some countries where the same type of site would require 2 FTEs in one country and 20 FTEs in another country.

And I'm giving you the extreme there, of course. It's not like we will be able to improve our -- sorry, our productivity by a factor of 10 across all of our sites. But the point is that there is a decent amount of low-hanging fruit across a number of geographies. Once we apply best practice for the specific type of site, the specific type of circumstances down to the specific layout of the specific rooms, we can drive a significant amount of efficiency improvements. That has always been our bread and butter. But you can say what we're doing right now is we're taking it from strong operators who know how to drive it. We're combining that knowledge of the strong operator with a data-driven approach, which gives us different insights and gives us different vantage points and ways to attack it. So we don't expect this to overnight increase our margins massively, but we expect it to be part of the journey we're on right now in terms of driving a structural margin improvement in the coming years as we deploy OneISS. This is a classic example of how we utilize the global footprint and the data-driven approach.

Over to you, Kasper, on the margin guidance.

Kasper Fangel ***ISS A/S - Group CFO***

Yes. Thanks for that. Good morning, Rahul. I mean, ever since we started the journey, we have seen gradual improvement on the underlying margin, and we expect to continue to see that. And the fact that we are increasing the guidance today for the full year is obviously a sign of confidence that we have good visibility, and we are comfortable that the things are coming through. The big ticket items that we still need to improve on, but we have seen a notable and significant improvement already is obviously the hotspots. So that's one key area, but it's also the COVID-19 restructuring where we have very good traction, but there's still a bit more to come on that across countries with cost bases being adjusted and obviously, profit increasing consequently.

In terms of your free cash flow, I want to be very clear on that and take the first half announcement as a starting point where we had an outlook of above DKK 1 billion. The change of approximately DKK 0.5 billion, the DKK 500 million that we are communicating today is basically 2 things. It's one that the increased margin to 2.5% is going to yield another approximately DKK 250 million additional cash after tax. And the other part is improved working capital at the end of the year, which we expect to be around DKK 250 million, DKK 300 million. So combined, that gives you the approximately DKK 500 million. And I want to be very clear on the working capital improvements. That is sustainable working capital improvements that we are comfortable will stick. And it's absolutely not fueled by any deviations in factoring or anything. We've not changed our guidance on factoring, and we still expect factoring like I mentioned and we have mentioned several times, factoring to be broadly at the same level at the end of this year compared to last year. And so there's no news in that regards.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Maybe just one comment from my side, how will -- if I -- the line was not great, but if I heard you right, I think you said margin is expected to go down in Q4. Just to be clear that, that will not happen. I think the previous comment from Kasper around starting run rate of 3% plus was a run rate comment obviously, adjusting for the seasonality in Q4. So we do not see margins falling from here.

Kasper Fangel ***ISS A/S - Group CFO***

Absolutely right.

Operator

And as there are no further questions, I'll hand the word back to the speakers.

Jacob Aarup-Andersen ***ISS A/S - Group CEO***

Thank you very much. Thanks for great questions, as always. Our enthusiastic and highly competent IR team are eagerly awaiting further conversations. So please reach out to them. Looking forward to seeing many of you in the coming days and then wish you a great day. Thank you very much.