Company Name: ISS A/S
Company Ticker: ISS DC
Date: 2017-02-23
Event Description: Q4 2016 Earnings Call

Market Cap: 48,663.64
Current PX: 262.1
YTD Change($): +23.7
YTD Change(%): +9.941

Bloomberg Estimates - EPS
Current Quarter: 3.340
Current Year: 15.772
Bloomberg Estimates - Sales
Current Quarter: 19566.667
Current Year: 80993.286

Q4 2016 Earnings Call

Company Participants

- Nicholas Richard Ward
- Jeff Olsen Gravenhorst
- Pierre-François Riolacci
- Unverified Participant

Other Participants

- Bilal Aziz
- Michael Rasmussen
- Jonas Guldborg Hansen
- Kristian Godiksen
- Srini Sarikonda
- Paul D. Checketts
- Anvesh Agrawal
- Jesper Herholt Jensen
- Michael Vitfell-Rasmussen

MANAGEMENT DISCUSSION SECTION

Nicholas Richard Ward

Ladies and gentlemen, good morning. This is Nick Ward, Head of Investor Relations at ISS, and I'd like to welcome you to our Full Year 2016 Results Teleconference. Please be aware, as always, that the announcements, the annual reports as well as the slides used for this call can also be found on our website and later today, a replay will be available, and we will post a transcript of the call as soon as it is ready.

Again, as always I'd like to draw your attention to slide number 2 regarding forward-looking statements. Presenting today will be Group's CEO, Jeff Gravenhorst and for the first time, our New CFO, Pierre-François Riolacci. We will open for Q&A at the end of the presentation, and with that, I would like hand over to Jeff.

Jeff Olsen Gravenhorst

Thank you, Nick. Please turn to slide number 5. 2016 has been another year where were ISS has delivered against the stated objectives, with regards to our key financial metrics, organic growth was 3.4% for 2016 consistent with our guidance throughout the year. Q4 organic growth of 2.9% proved resilient, thanks to the largest end to high levels of project works.

The operating margin was 5.77% for 2016, 7 basis points higher than for 2015. Cash conversion, strong once again at 98%. During the year, we maintained our leverage at or below 2.5 times consistent with our clearly stated ambition. We've said repeatedly since our IPO that we wish to maintain a strong and efficient balance sheet in the absences of major acquisitions in 2016,we have as promised returned surplus capital to our shareholders, while via an extraordinary dividend of DKK 0.4 paid in November. We are today promising an ordinary dividend for the year of DKK 7.7 per share, in line with our stated policy of approximately 50% payout of our adjusted net income.

Ladies and gentlemen, I am pleased as we approach the third anniversary since our IPO that we've delivered against everyone of our stated objectives, at the outset I would like to thank each of our my 494,232 colleagues from around the world for their commitment and for helping to make these ambitions a reality.

Please turn to slide number 6. I'm especially pleased that our financial performances is underpinned by our strategic initiatives and the specific choices we've made. Integrated Facility Services, IFS remains our growth engine, and today accounts for about 37% of our group revenue, supported by the contract launches and expansions during the year.

Revenue from Global Corporate Clients increased by 19% in local currency, and today accounts for 11% of the group revenue. The expansion of our relationship with Novartis, Nestlé and Rolls-Royce has been a notable part of this success in 2016.

Our growth has been impacted by weakness in both Australia and Brazil, and to a less extent Eastern Europe. Fourth quarter and 2016 was the first quarter, impact by the loss of all three big Australian contracts, i.e. Royal North Shore, Rio Tinto and Citic Pacific.

Meanwhile, our decision to significant cut back of our business in Brazil and Eastern Europe, mostly notably within the Greek public sector also became stronger headwind to our growth as the year progressed. GREAT, is the primary vehicle for accelerating our strategic implementation. A set of initiatives aimed at maximizing the value from our volume from our concepts and from our talents, and ensuring that the benefits are realized at each and every customer sight.

During the year, we again improved both our employee engagement and our customer satisfaction These measures are important to us. We believe they should prove leading indicators driving better retention off and expansion with our customers. We have successfully rolled out new organizational structures across countries representing 70% of our group revenue and the response from our lower management teams have been extremely positive. As I mentioned, IFS is driving our growth and we will continue to invest to enhance our IFS capabilities across key geographies.

Finally, we have established operational excellence in this to ensure we deliver best practice across our organization. We're making better use of technology, and benchmarking to drive efficiency through in form decision making. And of course we continue to reduce our unit cost through ongoing assess with procurement and the outsourcing of business processes.

All of these factors has helped us to support our margin improvement and we believe that we can continue to do so. Finally, we remained heavily focused on maximizing our cash generation. Our 98% cash conversion reflects our efforts to insure timely payment for our services. Our free cash flow for the year was DKK 2.9 billion some 3% up on 2015.

Please turn to slide number 7. We launched The ISS Way strategy back in 2008 and central to that strategy were our choices. Choices on which services we wanted to provide, which customers we wanted to serve, and which geographies we wanted to operate in. This has led to a major refinement of our portfolio all recent years. We've exited businesses that are not core call to IFS and our key account approach, we've concentrated our operations primarily on site based delivery as oppose to route based.

Over the 2010 to 2016 period, we realized cash proceeds of DKK 5.7 billion from these divestments. Some DKK 13 billion of revenue of annual revenue has been sold over the period, accounting – amounting to 18% of our 2010 group revenue base.

We have also exited countries that are not part, that is not important for our key account customers. In recent quarters, we started to acquire businesses again, but with the clear focus on enhancing our IFS credentials. Strengthening our capabilities with key account customers in area such as technical services, catering, and likely workplace management.

We're committed to this process. This has been a major transformation, but these headline figures do not reveal the full extent of what have actually been achieved.

So, please turn to slide 8. Let me illustrate our transformation by taking a deeper dive within one pillar called property services. Property services in 2016, generated 19% accrued revenue. Little change from the 2009 contribution.

However, property services today is largely comprised – lastly comprised of technical and building service solutions, a very different offering versus 2009 offering. Since 2009, we've divested 28 businesses with an annual revenue of some DKK 7 billion within the sector.

We have illustrate the largest divestment here on the slide, but they include activities such as landscaping, damage control, pests control, and waste management. None of these active services is core to our value proposition. They're not important to the chosen key account segments and that they're generally group based The DKK 0.8 billion of acquired revenue highlighted also on this slide, relates to the 2015 acquisition of GS Hall. The subsequent increase in revenue comes almost entirely from organic development of our technical and building service offering. Services that are at the heart of our IFS solutions.

Our engineers ensure properties run in a smooth and efficient manner both from a cost and an energy perspective, and maximize uptime minimize risk, while seeking to reduce a negative impact buildings have on the environment.

Please turn to slide 9, why is this relevant, well quite simply because technical service is the most important component of our delivery to key account IFS customers. We illustrate this year with reference to our global corporate clients. Our growth with MGCC has been extraordinary. In 2009, we have one global corporate client customer HP, generating 1% of group revenue. In 2016, we had 10 global corporate clients generating 11% of group revenue.

However, what is clear from our analysis of these customers is the importance of property services and especially technical services. Almost 50% of our GCC revenue comes from these services and that is why we will continue to invest in developing our capabilities just as we did with the GS Hall and more recently [indiscernible] acquisition.

Our future priorities are unchanged from what we said in the past. We will continue to exit businesses that is not consistent with our strategic choices and reallocate that capital more efficiently.

We will pursue acquisitions to drive our IFS credentials, most obviously within technical services, catering and workplace management. We will remain focused on our chosen customers in industry segments and primarily in existing geographies, although we will monitor opportunities in new markets, if this allow us to logically spend with our key account customers.

Please now turn to slide 11, where we'll discuss the regional performance for Q4 in more detail. Q4 organic growth in Continental Europe was 2% versus 4% in Q3. The main positive contributors here were Turkey, Switzerland, Belgium and Luxembourg and Austria. We saw soft organic growth in Germany, but this is largely due to the timing of non-portfolio work, which is particularly strong in Q3.

We are proactively reducing our exposure to public sector across Eastern Europe, most notably in Greece. This reflects our strict focus on both profitability and payment terms. The pipeline for Continental Europe is encouraging. The Q4 regional operating margin of 8.1% was underpinned by strength, underpinned by strength in Switzerland, Turkey, Germany and Spain. Year-on-year improvement was most notable in Spain, partly due to timing, and Germany, where our great restructuring commenced in late 2014 has been a clear success. The full-year margin improved by 0.3%, driven by Germany, the Netherlands and France.

In Northern Europe, Q4 organic growth of 5% versus 3% in Q3. Growth in Denmark slowed, due to the annualization of contract launches. The UK and Ireland experienced its strongest organic growth of the year. Thanks to healthy level of non-portfolio revenue and new contract wins. At this point what's the outlook for the UK is clearly uncertain. We have still not seen any meaningful impact from Brexit either on our trading or on our pipeline. Margins were generally solid in all countries except Sweden whilst the regional operating margin was 40 basis points lower the year-on-year in Q4. The full year margin was flat at 7.5%, a solid performance for the year.

Please turn to slide 12. Organic growth in Asia Pacific retained to minus 3 in Q4. This was consistent with our expectations and our prior communication driven largely by Australia. As I mentioned earlier, Q4 in the first quarter – Q4 was the first quarter to be impacted by each of the three sizeable Australian contract losses. The third loss Citi Pacific ceased in October, Australian organic growth remain under pressure during 2017, especially in the first half.

While as we face some disappointments in the remote side resource segment in Australia. We remain competitive in this sector. We've launched new contract with Wesfarmers Resources in Q4, more recently we secured a contract with Aspen Villages in Western Australia. And I'm also pleased to announce that just this week we won another more sizeable contract at a camp in the Bowen basin in the Northern Queensland. This will provide another important reference side for ISS within the Australian mining community.

Despite the challenges in 2016, we remained very happy with our Australian business. Australia remains a good market with good growth opportunities. Moreover, ISS is well-positioned with excellent delivery capabilities and a strong local management team.

Excluding Australia, Q4 organic growth in Asia was 3%. Growth was negative in both Singapore and China. In Singapore, this was nothing other than a timing issue with project activity in 2016 skewed towards Q1 to Q3, whereas work in 2015 was heavily skewed to Q4. Singapore has had a very strong 2016, and the outlook remains promising. We have recently secured IFS work for two more hospitals with [indiscernible] and Health.

In China, we started to make some structural adjustments to our operating model. We're reducing exposure to price driven customers, especially within retail, and strengthening our efforts with multinational customers, where broader value propositions is more suited.

In the near-term, we're seeing some pressure from contract losses, however, we have made some important management changes and confident that these changes will help us to deliver better quality growth, long-term growth opportunity in China remains significant.

Elsewhere, Asia continues to deliver a very good growth. India, Indonesia and the Philippines were notably strong. Organic growth in Asia for the full year of 2016 was 8%.

The increase in the Q4 operating margin to 8.8% was mainly driven by one-off provision release related to Indonesian pensions, however, we did see underlying margin improvements. As you know, we frequently phased one-offs, both positive and negative. To be absolutely clear, at group level, the net effect of such one-off effects in Q4 items were immaterial. For the full year, the operating margin Australia was slightly improved in line with our expectations.

Q4 organic growth in the Americas was 11%, up from 7% in Q3. The strength driven by North America, thanks to the positive impact from contract launches, but also significant level of project activity towards the end of the year, which we will see as a non-recurring in nature.

The outlook for our North American business is certainly encouraging. Elsewhere, the performance in Mexico and Chile was good. As you know Brazil, our greatest challenge in the region. We made good progress during 2016 and significantly reducing exposure, but this progress – this process will continue into 2017. As such, Brazil will negatively impact our overall organic growth throughout the year. The operating margin for the region was stable for both Q4 and the year as a whole.

With that, I would like to welcome Pierre-François Riolacci on the call. Pierre-François joined ISS CFO in November last year, having previously been CFO at Air France-KLM and Veolia. We're delighted that he is joined us. Welcome, Pierre.

Pierre-François Riolacci

Thank you, Jeff and you have done very well pronouncing my name, so congrats for that. Good morning, everyone. I'm actually very excited to be with you this morning for the first call as ISS CFO. I must say I'm also very pleased to have an easy start with obvious set of result for this Q4. Thank you, Jeff and thank you to the team.

If we look at page 14, and revenues maybe you can – I should flag first that you see no significant impact in Q4 from the net divestments and acquisitions. You may remember that for the full year, the impact – the net impact of divestment and acquisition is about DKK 425 million and we expect actually some further impact in 2017, which could be a negative of up to 1%, based on the transaction which have been completed so far.

The impact of currency was quite significant minus 3% in the quarter, more than 90% of this impact is actually related to the sterling pound. I remind you that in Q1 the currency impact was a minus 3%, Q2, minus 5%, Q3, minus 3%. So we have the same sort of trend. For the full year of 2016, the currency impact is about minus 3.5% half of which it under back of the sterling pound, but also some of that currencies coming from Turkey, Argentina or Norway or even Switzerland.

If we move to the organic growth, which is of course is a very important path, you can see that Q4 was plus 2.9% which is indeed lower than the recent quarter, but as you can see on the graph on the right hand side, very much in line within our earlier range. It's good to know, that Q4 was supported by a very high level of our phase and projects with a few large customers especially in America, especially in the U.S. and it's good to flag this extra revenues, because excluding this extra revenues probably a organic growth trend in Q4 would have been below 2%.

That's was the revenues and if we move to page 15 for the operating profit before other items, I would like first to flag this is the continuous margin improvement since H2 of 2013, as you can see as at Q4 – so Q4 in 2016 margin is up 12 basis points year-on-year, so from 656 basis points to 668 basis points. So that's an improvement. It is a further improvement of 4 bps on the last 12 months trialing that you see on the graph. For the full year 2016, we have a 5.77 margin, which is up 7 bps These 7 bps have been achieved despite two significant headwinds, the first one coming from divestment from the ForEx because we had two countries which are high-margin contributors, the UK and Turkey which relative weight has been decreasing on the back of the currency that accounts for 4 bps and another headwind of 3 bps coming from disposals as we have competed in October 15, the sale of some good assets in Turkey which were yielding high margin.

So the self-help actually is about 14 basis points which is definitely a significant improvement which is coming from a selective growth, a very strong cash control, procurement initiatives which are flowing in the P&L and also all the great measures and also reorganization which have been associated to the implementation of GREAT.

I would like also to point out that like Jeff mentioned earlier that the net impact of the one-offs in Q4 were definitely negligible in terms of margin and that this margin is a fair representation of our earnings power. The operating profit is up by DKK 33 million, year-on-year. Again, you have these headwinds which is about DKK 50 million for divestment and acquisition and about DKK 180 million for the ForEx which means that we have improved operating profit by DKK 260 million based on that self-help and I would like also to mention that this was supported by some very interesting, exciting turnaround stories which are at different points in the cycle in Europe like Germany which is at the end of this turnaround and which has been delivering very good results but also some other countries which are more at the beginning and it's good to see that restructuring efforts in Europe but you'll see in America are paying off and now contributing to the improvement of margins.

If we move to page 16 to give you some financial color on the income statement, I will not come back on revenues and operating profit, because I think it was discussed with regional review by Jeff, I would just like to point out that in Q4, we had a lower percentage of staff cost, and which is linked to the higher above base revenues, which as you know are largely subcontracted.

If we look at the operating income and expenses, which is a negative for the full year of DKK 139 million. It is made of capital gains of divestments, and mainly security business in Finland. It is also for a total amount of plus DKK 140 million, it is also linked to some fair value adjustment available for sale for about minus DKK 100 million, and restructuring cost for DKK 140 million more than half of it coming from Brazil, the rest being the implementation of great projects in different countries.

If we look at the financial income and expenses. For Q4, as you can see they are down by DKK 46 million, there was no refinancing cost in Q4 2016. So net debt average rate flat, the net debt average rate is flat in Q4 2016 compared to Q4 2015 at 2.1% with full year average net debt rate is 2.1% in 2016, it is down by about 20 bps compared to last year [indiscernible] beginning of the year.

So tax chart, as you can see is pretty stable, as apparent rate is 27.1%, but it is structured by capital gain, which is not taxable, and if you adjust from that amount, we're bang in line with 28% guidance. It's fair to say that we believe this run rate in terms of tax should get lower or closer to 27% and 28% in 2017 because we are taking gently advantage of our more efficient capital structure and that's being up again throughout the year.

The net profit adjusted is DKK 2,873 million it is up DKK 88 million compared to last year. We had some goodwill impairment for about DKK 200 million which were we have figured by our divestments of adjustments of fair value and available for sale assets and the net profit therefore is stable due to this goodwill impairment.

Moving to page 17 to cash flows. As you can see Q4 was good quarter which was supported by strong working cap evaluation and contribution, DKK 104 million period of 2015 Q4. If you look maybe at the full year basis, you see that the adjusted EBITDA is flat at DKK 5.3 billion, and this is including of course headwinds that I've signaled for the operating profit both from forex and divestments. The cash generated by operation is DKK 5.2 billion which is down 2%, this is due to a pension one-off that we had in 2015 for about DKK 80 million, as always advised to be flattish.

We have a negative contribution of the working capital requirements which is due to the very strong position, cash conversion that we had in 2015, we've been good in 2016 at 98 but a bit less good that we were in 2015.

The other expenses asset paid at that minus DKK 211 million, [indiscernible] about DKK 100 million compared to last year with the lower cash out and restructuring expenses.

The cash net interest minus DKK 276 million is decreasing. It reflects of course the underlying evolution in our net interest growth maybe you should also keep in mind that we had a first interest payment on our 2021 bond that was paid in January 17. The cash tax is very stable DKK 871 million and therefore the cash flow from operating activities is at DKK 3.7 billion.

Our investment cash flow is negative DKK 748 million with capital expenditure of little higher than DKK 800 million, which is about 1% other revenues compared to 1.1% last year. The free cash flow is at DKK 2.9 billion at 3% year-on-year and maybe I should flag that the cash flow from financing activities is reflecting the much higher dividend payments that we had in 2016 both ordinary and of course extraordinary.

Page 18, on the free cash flow, I would like just to add two comments which are linked to the, you can see on the graph on the right. The first one is that the CapEx, that we has – the level of capital expenditures and level of depreciation and other equivalent which means that we are supporting asset base through investment in the air and the second point which I think is major point is that for the second year we have a free cash flow conversion of operation profit excluding divestment and acquisition over 60% which I think is very strong number.

I will then move to page 19, and the capital allocation. What do we do with this DKK 2.9 billion of free cash. As you can see, there is a very small impact of M&A activity in 2016. We have bought back treasury shares for DKK 150 million to hedge LTIP. But the most important part, of course, is a DKK 2.1 billion, that we have allocated to our shareholders through ordinary dividends and extraordinary dividends. We were left with DKK 700 million allocated to debt reduction that you don't find in the net debt reduction for two reasons, one is that we have a high amount of finance lease of DKK 260 million, that reflects contractual arrangements that we have with IBM, which is related to very important point of this project, which we expect a lot of benefit of.

And clearly you should see that as investing on a self-investing self investing on an base, and we see that as very positive point. And of course, we had also ForEx impact on the net debt for DKK 250 million, which is linked mainly to cash and some foreign currency denominated.

In terms of – with the net debt prediction of DKK 158 million to DKK 11 million for the net debt. You can see on the graph on the right that we have a – we have delivered a long data on August deleveraging mainly based on the net debt cuts, which has been completed over the quarters. We had a coverage ratio below DKK 2.5 million throughout the year, and we expect to similar seasonality profile for our leveraging 2017. I would just add final word about our liquidity, which is very strong with DKK 6 million available on a committed lines as we have on top, of course, of our cash position.

Thank you. And from that, I will hand it back to Jeff.

Jeff Olsen Gravenhorst

Thank you, Peter. Please turn to slide 21, we will of course continue to be – to have a very straight focus on our costs as we move into period of potentially higher inflation, we remain confident that the protection afforded to us on our contract terms, coupled with our costing models and our ability to drive ongoing efficiencies. We'll support additional margin accretion over the medium-term. Our core business is not to offer our customers protection to guess macroeconomic variables over which we have no control. Our purpose is to deliver high quality services and experiences for our customer across our real estate portfolio, ensuring transparency, compliance and well being of their employees and their guests.

As such, we absolutely seek to protect ourselves from inflation and other variables. For our larger contracts, which are of longer duration, we typically seek to protection in three key areas. First, we look to include price indexation clauses; second, we seek specific labor related loses to cover a collective Bakken agreements, including minimum wage increases benefits or the like. And thirdly, we seek protection against any statutory change. Now we cannot completely offset all risk, however through this approach we are confident in our ability to offset inflationary pressures as we've done it for many, many years.

For shorter duration contracts, we will simply look to reflect any changes to our costs at the point of retender. So in general, we see inflation as a positive process, inflationary pressure are felt by our competitors and our customers alike. These pressures drive a need for a change, with ISS embracive technology and fostering innovation we are able to deliver both solutions and associated efficiencies that customers' demands. All our results in the recent years provide a clear illustration of this.

Within consumables, the largest spend item is food, representing approximately half of the total. The way we structure our catering contract does vary from country-to-country, but typically we employ a P&L model whereby we take revenue and cost risk.

The key here is market insight on pricing, and maintaining a strong positive dialogue with our customers. If we can clearly evidenced the fact is by improved food price inflation, customers are far more supportive around our initiatives to reengineer menus and push-through selective price increases.

We see current food inflationary development as business as usual. We have previously quantified, expected gross savings from waves one to three, of our procurement program as being between DKK 450 million and DKK 550 million, that target remains in place. However, we are today quantifying additional gross savings of DKK 200 million to DKK 300 million that we expect to realize from way four plus our extension of procurement initiatives to the Americas and Asia.

These additional savings will be delivered over the 2016 to 2020 period. As always many of these benefits will, of course, go back to our customers. That said, we'll continue to see our procurement initiatives as ongoing drivers of business development, and group margin improvement opportunities.

Please turn to slide 22. Now I'm delighted to announce that we have secured a new global corporate client, the global biotech company, Shire. Shire will become our 11th global corporate client, and we will service their facilities in more than 40 countries across the globe.

These facilities will include manufacturing sites, bio lab sites and corporate facilities. The U.S. will be the single most important country for this contract. We're planning a phased rollout, starting from June 1, 2017. Under the terms of our agreement, we're unable to disclose the specific size of the contract. But when fully up and running, we expect it to approximately contribute to an additional 1% improved revenue.

Through this development, we are taking a local customer relationship to a truly global partnership. We are moving from multi-service into an integrated facility services delivery. And we're increasing our revenue with this particular customer by a factor of 12. This development further strengthened our credentials, not just in the U.S. but also in the global pharmaceutical sector given our success also with Novartis.

Please turn to slide 24. So with regards to our outlook for 2017, we are targeting an organic growth in the range of 1.5% to 3.5% and operating margin that is above that realized of 2016 of 5.77%, the cash conversion above 90%.

As Pierre highlighted, if we exclude the unusually strong project work in Q4, organic growth was below 2%. As we articulated in Q3 release in November, revenue weakness from Australia and Brazil will weigh in our performance, most notably in the first half of 2017. Brexit does create some additional uncertainty, which we have to be mindful of. However, our sales pipeline is healthy and [indiscernible] start to contribute together with other contracts that we won, also during the last half year.

We will remain – we've remain confident in our growth potential from IFS and our ability to increase share of wallet with existing customers, most notably our key accounts. The anticipated drivers of our margin remains unchanged. This includes selectivity over growth.

We will remain very focused on our cash generation, as we have in prior years. 2016 has been another good year for ISS. Good organic growth, solid margin expansion, strong cash generation, our balance sheet is where we wanted to be. And we've demonstrated our ambition to return surplus funds to shareholders, if major acquisitions opportunities do not materialize. We anticipate further good progress in 2017.

With that, I'd like to open up for Q&A.

Q&A

Operator

Thank you. We will now begin the question-and-answer session. [Operator Instructions] The first question comes from Bilal Aziz from UBS. Please go ahead. Your line is now open.

<Q - Bilal Aziz>: Good morning, everyone. I'm Bilal Aziz from UBS. And just three quick questions from me, please. In the UK you see, as you know, real find of weakness as of yet. And can you perhaps give us an indication of how the non-portfolio business and the GS Hall business have performed so far in the year, and your expectations for the remainder of the year for those segments?

Number two in Brazil, and we're exactly are you in that exit process, what more need to be done and how perhaps should we think about the phasing of that as we think about the magnitude of impact in 2017? And very finally, the contract with Shire, can you in fact give us some sort of indication of the mix between subcontracting and self delivery initially this year that contract ramps up and how we should tie that to the margin? Thank you.

<A - Jeff Olsen Gravenhorst>: All right. Thank you very much. To start with the UK, clearly it is very difficult to have any sort of prediction on the UK. What we can say is that, our business is pretty strong. We've done very well in 2016. Our pipeline is also very strong for 2017. Of course, we have to be a little bit mindful that uncertainties never grateful for decision making.

So far on the non-portfolio or the extra works in 2016, at the end of the year, we actually saw a strong delivery. All we're saying is that there is a long way to the end of this year and the impact of Brexit nobody really know, so we are a little bit cautious, when we look at the second half here, also from a UK perspective.

Having said that it's very important that I don't see the weakness yet. Now, at the same time, look at the customers that we have. We have a big sector within the public sector, part of our business, hospitals, MOD is a big part of our business in the UK. They will of course remain and they'll remain probably also strong and as we can see it. We also have customers that are really focusing on servicing other customers, so that could be advisory, accounting companies, consultancy companies, which are big for us, they of course also will see other opportunities.

So it's more on the banking sector, and with banking sector in the UK, of course, the uncertainties are little bit higher because are they going to move out or they're not going to move out.

The things is we're used to this in the banks because there are so many movements in that just from an inherent part of the business model. So we have helped our clients to reduced the scope in the UK and increased the scope in off-shoring activities. But also these are global contracts. So should they move offices from, let's say, from London to Frankfurt, well, we'll pick it up in Frankfurt. If they move to New York, we'll pick it up in New York. So, I'm not too nervous about that. But, of course, we have to be mindful that it can have some impact on project works at the end of the year and that's all we're saying. So that's the part of that. So we do see a still a strong performance, UK a very strong part of our business.

In Brazil, we've gone through a major sort of overhaul of the business during 2016. But we're likely to see that the first half of 2017 it will pan out. So we should see more of a lower impact from Brazil in the second half of 2017 on the efforts that's been done and I think we're getting to a good run rate that's stable at a breakeven right now for Brazil from an owner's perspective. So, I think we'll go forward from first to second half. Of course, it does mean less to the group now, because it's a significantly smaller scale.

On Shire, yes, it will start off from around 1st of June. We will start the mobilizing and, of course, in the beginning we're going to take all – some of the subcontracting that they already have and then we'll ramp up our own self delivery and we expect it to get to the usual self-delivery degree of around 65% within a relatively short period of time and then of course, we will work on improving that over the course of the contract.

<Q>: Thank you very much indeed.

Operator

Thank you. The next question comes from Michael Rasmussen from ABG Sundal Collier. Please go ahead. Your line is open.

<Q - Michael Rasmussen>: Thank you very much. First of all, on Watson, are using this as a selling argument, and what has the feedback then been from a customer so far, and are you going to amortize some of that costs as we move along? Secondly, if you could just – did you actually say that the tax rate in 2017 was going to go all the way down to 27%? And my final question is on the fourth quarter, how would the margins have been, if you didn't have the extraordinary work, i.e., if organic growth had been below 2% like you mentioned, what would that have done to margins? Thank you.

<A>: Thank you, Michael. And I'll start with IBM deal. I think it's important that the IBM deal has three things, it's not Watson, all of it. Most important in that, and the number you see on the finance leases actually licenses that will replace all other licenses that we already have today. So that is the – called FMS@ISS system which is just gets a different engine, which gives us better opportunities within the technical environment. So, yes, of course as and when that gets replaced and then of course that also has a license cost, so you can argue that's the amortization. The second part of it is the integration at ISS, integration at ISS is where we can use the system to help us take to integrate service streams within a customer, and that we expect to give us a very good benefit from profitability stroke pricing perspective towards our customers because we see, we could take out significant savings on our cost out of our production.

So as and when that gets implementing, yes then there the cost [indiscernible] amortize the cost but that's all included in the business model. And then of course, the last part, which is the probably the more exciting part and that's also why you mentioned it, Watson. Right now, we're testing Watson on some of our locations, and the selling point of that of course is great because it will support our front-line staff in doing better services, we don't believe in, we do believe in people and power of the human tough here, but we can support the knowledge and decision-making from using Watson.

So, ordering meeting rules for that matter, it could be setting off different sort of catering solutions, but particularly, within help desk is where Watson will be a big ticket for us. And yes, there is a big interest and a very keen interest in this from our customers, but it is the last part of it which is – will be rolled out. So right now, that is in the test mode. So I hope that covers the question for the part one.

If I just jump to your last question on the margin side, and then, I'll leave the tax to Pierre-François. On the margin side, it will be the same. What we have to look at here, when we'll have larger projects of course, it is not done with the existing resources. We do buy in the scale, it is what buying in also other sub-contractors which will have a normal margin. So the margin in Q4 would have been the same without the extraordinary project work.

So, on the tax rate, Pierre?

<A - Pierre-François Riolacci>: Yes. Indeed, we expect the tax rate to decrease in 2017. It could decrease up to 27%. We are getting more and more efficiency in different countries, in the back of a stronger balance sheet and that's why we believe we can indeed go further. And you know that the weighted average tax rate of the group is lower than 28%. If it increase, it'll make sense, but being more efficient, we get closer to a lower level.

<Q>: Thank you very much. And very well done on the 12 basis points of higher margins than in Q4.

Operator

Thank you. The next question comes from Jonas Guldborg from Carnegie. Please go ahead. Your line is open.

<Q - Jonas Guldborg Hansen>: Yeah. Good morning, and thank you for taking my questions here. First of all, you had a very strong margin development in Continental Europe in Q4 and year-on-year and as I've read it, it is primarily down to Spain and what you called quarterly timing differences, could you just try and explain what is a quarterly timing differences. Then did you say and if you did, could you please say it again when the Shire contract would be fully implemented? Thank you.

<A>: All right. Thank you. On the – we just start from Shire. We have doubled the ramp-up from June, we expect it to be up and running by the end of the year, beginning of next year. And on the margin on Spain, can you just repeat that question one more time. I'm just got to make sure, I get that right.

<Q - Jonas Guldborg Hansen>: Yeah, but by the way, it was just around what that explains this 1 percentage points margin uplift a year-on-year or more specifically you explained it by quarterly timing differences in Spain, what is quarterly timing differences?

<A>: Okay. On the – you're talking about the Continental Europe difference. It is simply a matter of that sometimes you will have more working days or less working days in one quarter over another quarter. So there is definitely underlying margin improvement, but there are also some timing differences between the quarters. That's why we say, quarters can jump up and down a little bit. We got to look at the year, and as Peter was saying, the 5.77 over the year before is a good expression of our margin expansion.

<Q>: Okay. Thank you very much.

Operator

Thank you. The next question comes from Kristian Godiksen from SEB. Please go ahead. Your line is open.

<Q - Kristian Godiksen>: Yes, hello. A couple of questions from my side. What is the potential – firstly, what is the potential impact from Brexit and unrest in Turkey you've implemented in your guidance? And secondly, how should we think about the low-end of your guidance range of the organic growth of 1.5%, when we think about Q1. Should we think that Q1 should be lower than this, as we know that organic growth will pick-up during the year?

And then third, could you please explain to me, I have a number of questions on the capitalization of the softened and then other intangible assets, which more than doubles in 2016 year-over-year. And this has a net effect on your margin of 42 bps. And three questions on that. So how should we think about that going forward? Secondly, I guess is solely due to IBM Watson or is this a general trend of higher IT investments. And then thirdly, how long should we think this as being a multi-sized over? Thank you.

<A>: Okay. And thank you, Kristian. On Brexit, if I just start with that, I think the key thing here when we guide is, of course, it's still early in the year. And nobody knows whether what kind of an impact Brexit will have, nobody knows what kind of an impact there will be on EU depending on elections and so forth. The only thing we know is that uncertainty is never great for decisions on projects. Sometimes it can be if they start move projects from one country to another or restructuring businesses so forth. So when we guide with a range of 2%, between 1.5% and 3.5% what we put in that is that uncertainty that there is a long ways of the end of the year, and it can have an impact on project works, this is uncertainty in EU at the second half.

As I said earlier, we don't see anything right now. I just need to have a little bit of a leeway for predicting the revenue that far out. On the low end of it, what we're saying is that, we're seeing a run rate of below 2% as we say for the Q4 and getting into Q1. We have the impact of course, which is already in Q4 of Brazil and of the mining sector in Australia to say so, that's the best guys that gives that we have with goals expect to ramp off from there. So, we will see a steady growth during the year, but that's the best guideline we give you right now on that. On the last question, Pierre, if you will try to answer that?

<A - Pierre-François Riolacci>: Yeah, it's pretty clear. At times it's good to see that people are looking to the balance sheet and it's pretty clear indeed that we have an increase in our software mainly in the software ITs, indeed IT related. We have about DKK 100 million, which is related to the IBM and to [indiscernible], so that indeed reflects much higher level of investment in IT and that's part of the story.

<A>: Just to make sure, of course, this is a very important part of our future on our key accounts is to get deficiencies out and also become even better at delivering our promises.

<Q>: Yeah. Just a follow-up on that. So the net effect of capitalization was the 42 bps and how do you see that going forward and I guess that the higher effect is that due to, is that an elevated CapEx level, how long should we see this and the spillover and impact in the coming years?

<A>: Well, you need to look at the full year basis, and if you look at that as a full year basis, you don't see such a dramatic increase in CapEx. You see of course a [indiscernible] falling back, but if you look at the full year, we are in line with our CapEx spending and looking forward, we do expect our CapEx expense or our capital expenditures has to maintain at the high level we keep on trying to invest in our business. Of course, following that we find the right opportunities, and we do the right thing. But we would keep on maintaining a high level of CapEx and especially in the IT field.

<A>: What that means Kristian, of course is that we're within the guidance we've given before the longer term, so it's between the historic figures of 1 to 1.3.

<Q>: Yeah. And that's perfectly clear. Thanks for that. But I was more referring to the effects from the capitalizations, which was 42 bps in 2016, which has been historically you won't be in that single-digit impact from beyond – net effect from capitalization and amortization, so that elevated impact in 2016 will that continue going forward or should we, which kind of impact should we expect. If you just, the CapEx in or the capitalization of software and intangibles that more than double since 2016?

<A>: Yeah. You will not expect to see that repeated. That's for sure. Part of that will be the IBM launch that we do right now. But I think you have to look at that as the complete picture, Kristian.

<Q>: Okay. Thank you.

Operator

Thank you. The next question comes from Srini Sarikonda from HSBC. Please go ahead. Your line is open.

<Q - Srini Sarikonda>: Hi, this is Srini from HSBC. Can you help me understand the increasing central cost, and 124% drop to EBITDA of marginal sales in the Continental Europe? Are there any changing cost allocations we should understand?

<A>: Can you repeat that question again, please?

<Q - Srini Sarikonda>: Yeah. I mean, I'm trying to understand the reasons for increase in central cost, and there is a 124% drop through to EBITDA from marginal sales increase in Continental Europe. Are there any changing cost allocations we should understand there?

<A>: There will be – I think it's actually quite minor, central cost were 0.84 I think in 2016, it was 0.8 in 2015. Of course, that has an impact in absolute numbers. But there is no doubt that there will be some investments into excellence centers from the group perspective. So it can move a little bit from year-to-year. I think the more we centralize their best practices, the higher or the more we centralize, of course, we will have more – we will have more cost central compared to what we have in our decent sliced model today. I think from 2017 we are about the same level as what you've seen for 2016.

<Q - Srini Sarikonda>: Okay. But was there a moment between 2016 and 2017 within divisions to central cost.

<A>: Yeah. But it is the investment into excellence centers, for example. It is also driving to a global corporate client. So, costs to drive procurement benefits, costs to drive the implementation of the technology for example is the reason why it goes up just a little bit, and which is then set in the countries.

<Q>: Yeah, understood. And your EBITDA performance is very good but EBITA is less so, and how long can this be sustained?

<A>: On the EBITDA versus the EBITA, it's quite important to remember that we do actually lease a number of our assets. And with that of course we have the leasing cost in our EBITA, so that's very important and that's why we do believe that we can continue to improve both our EBITA and our EBITDA. I don't see a major difference in that as you can also see on the cash flow statement.

<Q>: Okay. One last one please. Can you give us an update on M&A, which regions and what businesses you are mainly looking at? And how is the pipeline looking at in that business and regions?

<A>: Yeah, you would have noticed that we have made some minor acquisitions over the last few months notably a Danish company called SIGNAL, which is strategically very important within workplace management gives us better advisory and better execution on new ways of working which is a very important part of our strategy with our key accounts.

So we will continue to look for the expanding workplace management resources, but these are minor acquisitions. Most important is the Americas, and the North America in particular where we are looking for both catering and technical acquisitions. And there we are constantly working with the targets, it has to be the right price, it has to be the right company, that will fit into our strategy of course, so that's why we are picky as I say every time. The pipeline is there and it's active and we are confident that we will get to what we need to get to in the North American part. I can't give you any specific timing obviously.

In Europe and the rest of the world, technical services is key to us, so like GS Hall acquisition we made a couple of years back, we're still looking for areas like that. And then of course we always keep an eye on whether there are new markets we need to get into, but in all honestly that from a priority perspective is technical services across in line with what I had explained today, and it is North America with catering and technical services, and then is the smaller more strategic niche add-on of workplace management.

<Q>: Okay. Then North America catering business, is there any particular end market here looking at like industrial healthcare, are you still open for that?

<A>: We are of course as a business overall very focused on business services and IT, pharma, manufacturing and industry, and particularly in the U.S. that's our strong hold, so that is of course where we are focused the most. But from a company perspective, we also have a strong hold in healthcare, so it could be either all, but of course it's business services, IT, manufacturing and particularly also in pharma.

<Q>: Okay, perfect. Thank you.

Operator

Thank you. The next question comes from Paul Checketts from Barclays Capital. Please go ahead. Your line is open.

<Q - Paul D. Checketts>: Good morning, guys. And I have got three questions. The first is regarding sales pipeline. You described it as healthy, Jeff. Is it possible to give anymore color on the size and timing of potential new deals through this year? And related to that, of the 10 GCC clients excluding Shire, are any of those due to end this year? That's the sort of first question.

Second is related to the margins, and if you think about the various cost-saving initiatives that you have collectively, can you give us a sense of how much is still to benefit the business this year and beyond? And the last one is a follow-on the question of capitalization. Can you remind us if your policy on capitalization of contract mobilization costs, please?

<A>: Yeah. All right, Paul. On the sales pipeline, obviously, we don't give a – we don't give numbers out on what the size and the number of contracts and so forth. But compared to last year and the year before we are very strong in our pipeline, and of course, they will start, they will be negotiated and started during the year. So, there is no difference to what we've seen from a patent in that. But it is a strong pipeline also compared to two earlier years.

On the 10 global corporate clients, yes, of course, everything has retention at the end of it. So, we are constantly also in dialogue we have two contracts that will come up at the end of year for a retention. And of course, we are in dialogue with those as we speak. On the intangibles...

<A>: Well. We have a rule that, of course, we – when you tell the transition cost that can be capitalized under balance sheet and we have a rule that they need to be in excess of DKK 5 million so they're related to large operations and I think you'll will [indiscernible].

<Q>: Thanks.

Operator

Thank you. The next question comes from Anvesh Agrawal from Morgan Stanley. Please go ahead your line open.

<Q - Anvesh Agrawal>: Hi. Can I ask one on the IFS and GCC? Can you talk about the contract pipeline and the large IFS contracts, and given that these contracts are higher margin, why we're not seeing more material impact or more material acceleration in your margins, please?

<A>: Yeah. The first question on the pipeline. I think, I've answered that, but the pipeline on, the growth engine behind ISS is of course the Integrated Facility Services capabilities. So we are continuing to see a good strong pipeline on that. It is a demand from our customers more and more. They want to have simpler interfaces with customers with the supplier side easier to do business with i.e. bundling all of the services it takes to run a facility. That also creates efficiency improvements. So of course they expect to get savings from bundling services and giving it to one provider.

Those savings will come from management cost reductions, but of course also from integrated services on the shelf floor and that was more notably be from the integration at ISS technology that we're also installed. So we do see a good margin potential in that. Now, overall the margin expansion that we see year-on-year is a combination of few things. Obviously, we do see a better earnings coming from a higher proportion of IFS, but of course we also have pressure on some of the single service businesses, but they are of course having a smaller part of our business as we speak. So this is part of the journey and this is part of the reason why we can every year expand our margin.

<Q>: Okay. Thank you, very clear.

Operator

Thank you. The next question comes from Matija Gergolet from Goldman Sachs. Please go ahead. Your line is open.

<Q>: Yes. Hello. Good morning. I've a two sets of questions. One on the organic growth and secondly on the margins. So firstly on the organic growth. So you commented [indiscernible] 2.9% is the growth for the quarter but excluding the sizable non-portfolio revenues is a bit under two. Just to be clear, this non-portfolio revenue contracts they were both in the Americas and in the UK or were they only in the Americas? I'm thinking about this very strong 11% organic growth in America. So, how much of that perhaps is from non-portfolio revenues? That's the first one.

<A>: Yeah. Do you want me to answer that one first, I'll go – clearly we had good above base work, part of work, both in the Americas and in the UK. And in the U.S. it was related to some particular incidents. So that's why we called that a little bit or more than normal. But in general, we've had very good underlying organic growth in the U.S. with the start-up of Bombardier and Rolls-Royce also in America. So, there has been some very good start-up in America that underpins the ongoing organic growth. So still we are confident that we have a strong opening also for 2017 particularly also with the Shire coming on-board.

On the UK, I think I've answered that part. That was – also was a good non-portfolio work also in the UK, which could be repeated again next year as it could be in the U.S. we're just saying that. They don't come into the Q1. So, typically you'll see more projects at the end of the year than you see at the beginning of the year and that's why we're highlighting it.

<Q>: Yeah. Okay. Thank you. A secondly, so you mentioned Argentina's one of the currencies that help the value. Clearly inflation is very high there. Can you just remind us – also the council supports a high organic growth. Can you just remind us, how big is Argentina within the Americas mix? Please.

<A>: It is tiny. I can tell you. So we're talking about 0.5% of the business.

<Q>: Over the our group business, okay. Thank you. And then second set of question is on the margin. So, fairly strong margins in three of the four regions, the one that stands over a bit of negative in the Northern Europe, so this see decline in margins in Northern Europe, you mentioned Sweden, could there be something structural there just maybe margin being so high that they cannot go much higher or do you think it's more of a one off? And then conversely, for the other regions, now there this is convergence, which actually had happened [indiscernible] in Continental Europe towards 8% Northern European margins, basically – you're clearly saying that there is still more to go, just the 4Q was a fairly a sharp increase in three of the four regions, I mean should we expect that momentum to continue in the first half of the year or over this significant margin improvement in three of the four regions?

<A>: Yeah, I think first of all, what we have to remember is that the quarter-over-quarter thing that can be very, that there could be swings between the quarters, year-over- year, as I said earlier. One is the number of working days, the other one is the timing of events that happened and so forth. But so I think it's very important to look at this over a little bit longer period, the northern region is actually flat, so it's not going backwards, it's flat for the year, and that's also what we see.

I do believe that we're at high level here. So, of course, I don't see a major expansion here. There are some possibilities, but in general, I think this is a good margin also compared to competitors, so it's all about growth. Now in Sweden, it's something – so it happens once in a while that the margins are a little bit down, and then in Sweden is particularly within healthcare that we've had a turnaround on a couple of contracts, but over time I don't see that as an issue. That is certainly is not a structural part.

I think we have a good market share in the Northern region, and we can defend that because of our critical mass. So we can also defend the margin.

<Q>: And in the rest of India, the three regions, should we expect like in the way of a bit more margin contribution to – particularly the first half of the year?

<A>: Well, the point is that we will continue to work on expanding our margin as we say. Obviously, it depends a little bit on the individual competitive situation country-by-country here. And the individual status of our country operations. I think what we have to look at, what we have a large part of IFS contracts like Switzerland, UK, Nordic region, and the margins are generally higher. So of course, as we move into more IFS in the countries you're talking about, we will also see a margin expansion.

Remembering that we still have a dilution from a breakeven business in Brazil, for example, which is the one that the rest have to compensate for. That would, of course, also improve over time.

<Q>: Okay. Thank you very much. I think the focus on the margin is because this quarter, that seems to stand out in terms of say, a big improvement. Thank you very much for the clarity.

Operator

Thank you. The next question comes from the Jesper Jensen from Nordea. Please go ahead. Your line is open.

<Q - Jesper Herholt Jensen>: Thank you. Good morning. I'm just coming back to the Shire contract that you announced yesterday. I'm just trying to understand whether that, I guess, primarily will be U.S.-related revenue, I guess, if you assume it is like two-thirds U.S., and one-third other countries. Does that accelerate your need to make some acquisitions in the U.S., and also perhaps the simulation to that? What is the market profile of this account? Would that be similar to what we've – similar PCC accounts, in general accreted to the group once it's fully implemented and up and running?

<A>: If you just look at the overall Shire contract, we actually – we don't give that on the announcement from yesterday, but it is not predominant in the U.S. – the largest part of the U.S., but is less than 50% of the contract sits in the U.S. But it still makes a relevant question on the second part, which is that the self-delivery capabilities, of course. We have been working very hard on the major accounts that we have in the U.S. to improve our self-delivery degree, both with technical services, with catering services and of course, all of the janitorial and building services and front-of-house services. So we do have a decent self-delivery capability now in the U.S., and we expect to have the same on this account as we sit said around the 50% to 65% over this date.

Now, it will of course improve our capabilities within catering in particular, if we have the catering business onboard. So it clearly does not change our ambition to go for more acquisitions and thereby strengthen our critical mass and our scale, and scale benefits in that market. But from just delivering it day in day out, we are actually not bad as we speak, but it can be improved by those acquisitions. So you are right. It will just confirm, if nothing else to strengthen of what we already embark to do.

<Q>: Okay. And on the margin profile, would that be similar to what we've seen with the other TCC accounts, is the phasing in progression?

<A>: It will start low and then it will improve over time.

<Q>: Okay. And another one, that's obviously being in a split, I guess of your major accounts. HP is split into three. Now, is there any color you can give on how that is progressing from your side? <A>: Yeah. There is of course a very clear dialogue with all three. So we have HPE and HPI and the HPCC combination. And we are the incumbent in all of this, as you know, and we're working very heavily with all three parties as we speak.

<Q>: Is that one of the launch you mentioned before the two contracts that we already signed in addition to the two that's coming up.

<A>: That was in addition to the two that's coming up.

<Q>: Okay. And just the last question. I just noticed in your accounts that the provisions for onerous contracts is going up a bit, and it is not a huge amount. But it's still maybe that's a few basis points to the margin going into 2017. Could you just help us understand if this particular account in the single countries like the ones you mentioned where you have difficulties, Brazil, Australia and so on or this is related to anything elsewhere?

<A>: Did you get it?

<A>: Yeah. Indeed, we provided for onerous contract for very small amount of our DKK 20 million in activities related to operation into Nordics.

<Q>: Okay, thanks.

<A>: Answer is on the rest, we don't actually to see any other onerous contracts or difficult contracts.

<Q>: Thank you.

Operator

Thank you. The next question is from the follow-up question from Kristian Godiksen from SEB. Please go ahead. Your line is open.

<Q - Kristian Godiksen>: A follow-up from my side, please. So organic growth was driven by project work in Q4 and it decreased to more than 16% for the full year. What have you assumed in your guidance for 2017? And do you still see the high end of the range being 20% and it seems like you're not – included any impact in your margin guidance? And then just secondly, if you could comment a bit on if whether the price pressure in Australia is easing within the remote site services sector as you begin to win some contracts? And then thirdly, I know let's keep you on those two to start with? Thank you.

<A>: Yeah. So, if we start with above base work, as we're saying is there is a more above base than we expected to have in Q4 on certain selective projects. Going forward in the outlook, we expect that to be as we've seen it earlier, so we have a range of 1.5% to 3.5% that includes, that will continue to buildup a little bit more above base work as we get more key accounts. So on the margin, you're saying, it doesn't have impact on the margin, well, what we're was saying on the margin is that we believe that we can expand the margin again in 2017, so that's all lumped into together with everything else.

So whether that's inflation cost that goes up, it benefits to our clients and then of course that we need to make sure that we also expand our margin, so that's already in there, but no major difference to expectations from earlier.

In Australia, you have to remember that that was a very specific situation where you had North West Australia, the [ph] Pilgary area that's where that whole the three contract, the Australian mining sector actually had an impact on. I think, on the other contracts we won, it's a different value proposition altogether, it's a different type of mining where we go into different types of resource business, so you can't really compare it between the two. We've won contracts in Queensland also last year with farmers and so forth. So I've not seen that to be the same sort of price pressure or consolidation pressure.

<Q>: Okay. Thanks a lot. And just maybe so the price pressure continues in the Northwest to a region within those specific off site remote service contracts?

<A>: Yeah. It really depends a little bit on where the world is going here because it – of course, it was initiated by iron ore prices going down. I think there is a little bit better outlook for that at the moment, but again, there are certain uncertainties that could get that the iron price, iron ore prices to go up and down, and it is just a very, very specific case when that happen, when they consolidated some sites.

<Q>: Okay. Thanks a lot.

Operator

Thank you. The next question is also a follow-up question from Michael Rasmussen from ABG Sundal Collier. Please go ahead. Your line is open.

<Q - Michael Vitfell-Rasmussen>: Thank you very much. Firstly, on the contracts that are up for renegotiation this year, can you confirm whether that city and Telenor that expire in 2017? Second question goes on the cost savings. Now, how do they actually distribute over the next three years to four years? Is it kind of an even distribution or is it very back-end loaded, in terms of the potential cost savings? And finally, how your pension funds funded at the moment? And I'm here mainly thinking on the UK, are you running into having to fill that up at some time? Thank you.

<A>: Okay. Michael, on the – of course, I cannot tell you exactly what customers it is. I can tell you that Telenor is not one of our TCC accounts, so that sits in our Nordic region account, and we are of course, negotiating as early as we can on these. And the reason why I won't give names is that certain customers are very particular on not going out with this, so I can't actually break that confidentiality.

On the cost savings going forward I assume that you mean on the savings profile for the procurement program?

<Q>: Yes, exactly.

<A>: Yeah. That will be gradually moving up over the next – up to 2020.

<Q>: So fully implemented DKK 350 million to DKK 450 million, plus the DKK 200 million to DKK 300 million by 2020.

<A>: Yes. Actually we do not have country-by-country, a major unfunded obligation. Especially when we look at the UK, we are in a pretty good shape with assets which are very close to DDO. And I think that we have a few in balance, but to give you as a full picture, we have a funded obligation of about DKK 7 billion and assets which are about DKK 6.2 billion. So we have a very – very narrow unfunded situation.

<Q>: Great. Thank you very much.

Operator

Thank you. The next question is also a follow-up question from Paul Checketts from Barclays Capital. Please go ahead. Your line is open.

<Q - Paul D. Checketts>: I just had a one short one which is relating to the interest charge. It was around DKK 120 million in the quarter. Is that a sensible level for a quarterly run rate through 2017? Thanks.

<A>: I thought you're maybe referring to the net financial charge and if you look only at the net indirect expense, it's much lower than that. So if you look at the net indirect expense, which is in line with our net debt, you're talking about a number which is north of DKK 250 million for the year. So I think I'm a bit surprised by the number.

<Q - Paul D. Checketts>: And so what do you think what will be the interest – what should we be factoring in for 2017?

<A>: I mentioned that the average interest rate on the net debt and the average net debt is about 2.1%. I think that's a fair proxy, and the things that we expect in 2017 at our net interest charge would not be very different from 2016.

<Q>: Great. That's clear. Thanks.

<A>: ...number.

Operator

Thank you. There appear to be no further questions, I'll return the conference back to you.

Unverified Participant

Great. Well, thank you everybody for your questions and your time, of course if there are follow-ups please don't hesitate to contact Martin or myself, and with that I just like to thank Jeff and Pierre-François and we look forward to seeing you in due course. Take care.