Credit Analysis

Moody's Global
Corporate Finance

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This Credit Analysis provides an in-depth discussion of credit rating(s) for ISS Holding A/S and should be read in conjunction with Moody's most recent Credit Opinion and rating information available on Moody's website. Click here to link.

ISS Holding A/S

Copenhagen, Denmark

Corporate profile

ISS A/S is the wholly owned subsidiary of ISS Holding A/S (B2/STA) and one of the leading facility services providers in the world. In 2007, the company reported approximately DKK63.9 billion (circa €8.6 billion) in revenues and DKK3.8 billion (circa €509 million) in operating profit before other items and impairment. While the company continues to derive the majority of its revenues from the provision of cleaning services, the successful implementation of management's plan to broaden its revenue base and transform ISS into a truly integrated services provider has increased ISS's revenue diversity.

Figure 1

Revenues per segment

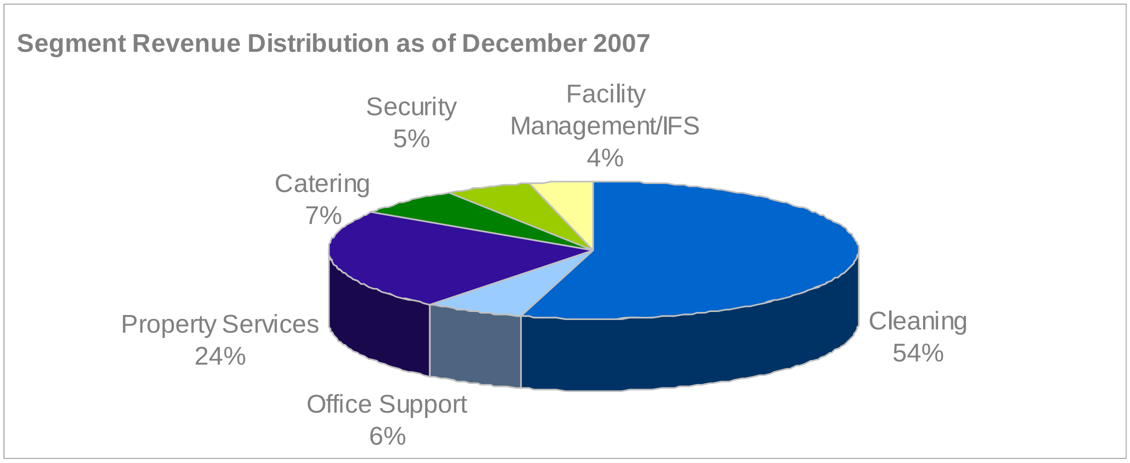
	Revenues		
DKK Million	**2005**	**2006**	**2007**
Cleaning	28,315	32,060	34,773
Office Support	1,602	2,936	3,881
Property Services	10,719	12,632	15,186
Catering	2,487	3,635	4,198
Security	-	2,427	3,406
Facility Management/IFS	2,958	2,082	2,478
Discontinued Operations	359	-	-
TOTAL	**46,440**	**55,772**	**63,922**

Source: Company data

Moody's Investors Service

ISS Holding A/S

Figure 2



ISS distinguishes between services offered and the way in which these services are delivered. The services offered include cleaning, property services, catering, office support, security and facility management. While the company continued to grow in all segments, the relative contribution of cleaning services to total turnover decreased to 54% in 2007 from 57% in 2006 and 65% in 2004, as the company continued to diversify into other areas.

The company's model encompasses three delivery models: single services, multi services and integrated facility services. Under the single service outsourcing, the company delivers a service solution based on a single service to its clients, which are divided into key accounts (22% of total revenues) and other (47% of total revenues). Clients agreeing to a multi-service contract will benefit from service integration whenever possible, while under contracts based on fully integrated facility services ISS will deliver two or more services under one single contract and through a single point of contact at the customer's premises. Integrated facility services offer the highest potential of cross selling to ISS and represented around 15% of total sales in 2007.

FS Funding A/S, the predecessor of ISS Holding A/S, was incorporated in March 2005 for the purpose of acquiring ISS and is 100% owned by funds advised by EQT Partners and Goldman Sachs Capital Partners.

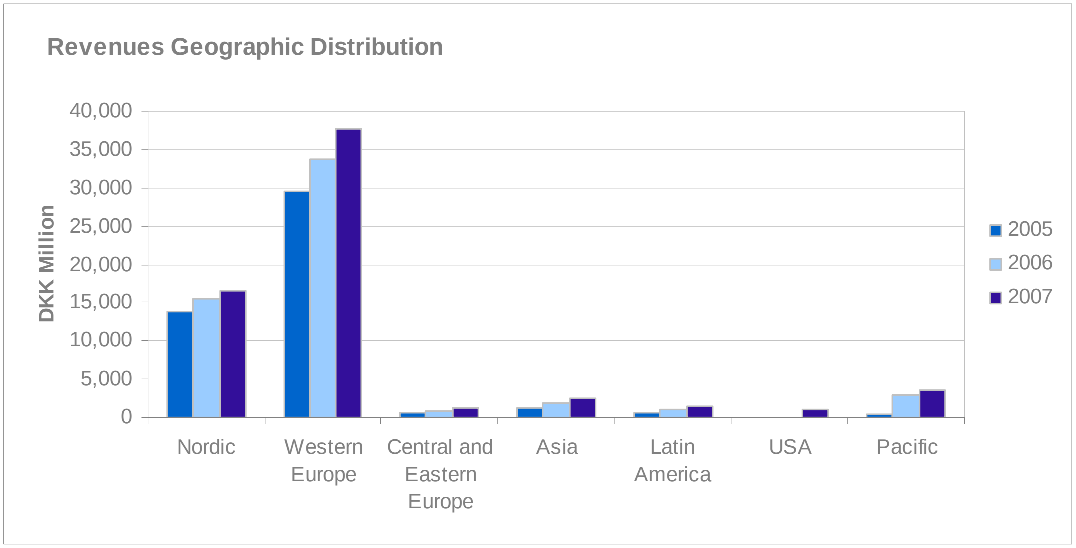
Figure 3

Operational Highlights

DKK Million	Revenues			Growth			Operating Earnings			Operating Margin		
	2005	2006	2007	2005	2006	2007	2005	2006	2007	2005	2006	2007
Nordic	13,782	15,475	16,488	13.8%	12.3%	6.5%	906	987	1,162	6.6%	6.4%	7.0%
Western Europe	29,519	33,666	37,709	16.0%	14.0%	12.0%	1,829	2,139	2,356	6.2%	6.4%	6.2%
Central and Eastern Europe	615	935	1,226	15.4%	52.0%	31.1%	36	59	91	5.9%	6.3%	7.4%
Asia	1,174	1,818	2,409	27.2%	54.9%	32.5%	75	113	158	6.4%	6.2%	6.6%
Latin America	598	1,049	1,484	49.1%	75.4%	41.5%	30	50	86	5.0%	4.8%	5.8%
USA	-	-	1,100	-	-	-	-	-	62	-	-	5.6%
Pacific	393	2,846	3,519	62.4%	624.2%	23.6%	42	176	225	10.7%	6.2%	6.4%
Other	-	-	-	-	-	-	-23	-	-	-	-	-
Discontinued Operations	359	-	-	-	-	-	40	-	-	-	-	-
Other Eliminations	-	-17	-13	-	-	-	-285	-290	-305	-	-	-
				-								
TOTAL	**46,440**	**55,772**	**63,922**	**15.1%**	**20.1%**	**14.6%**	**2,650**	**3,234**	**3,835**	**5.7%**	**5.8%**	**6.0%**

Source: Company data

Figure 4



Northern Europe and Continental Europe still represent the main markets for the company, and in 2007 accounted for 26% and 59% of its turnover, respectively. ISS is aiming to increase its presence mainly in high-growth countries including Eastern Europe, Asia and Latin America, where it expects higher growth rates. Revenues from the US comprised only 1% of total turnover in 2007.

Moody's positively views the introduction of the "Service culture – the ISS way" programme which intends to develop single-service excellence concepts of knowledge and best practice sharing. A strong corporate culture may limit integration risks due to the increasing number of employees from multiple countries.

Moreover, despite ISS's focus on three operational objectives (i) cash flow; (ii) operating margin; and (iii) profitable organic growth, the multiple acquisitions constrain the financial metrics in the short-term.

Management strategy

External growth will continue to be targeted…

We expect ISS to continue to broaden the scope of its operations with acquisitions going forward, albeit at a somewhat slower pace. The company's strategy is aimed at increasing its geographic diversification and its penetration in key markets which tend to strengthen its business profile. In 2007, the company completed 67 acquisitions in 33 countries and entered two new markets, the US and Taiwan. The acquisition of Sanitors (with sales corresponding of around DKK1.8 billion or 2.8% of total turnover) was the largest acquisition in 2007. The largest seven acquisitions accounted for just over DKK2.8 billion (4.5% of total turnover), while on average the other 60 acquired businesses contributed to the company's sales by less than DKK30 million. In the first quarter of 2008, 16 new acquisitions were completed.

… albeit with a balanced approach to acquisitions

Since 2000, ISS has acquired and successfully integrated more than 575 businesses, of which 500 have less than DKK100 million in turnover. Bolt-on acquisitions at multiples below corporate levels allow ISS to pursue its stated objective of a reduction in financial leverage on a multiple basis. Acquisitions are typically limited in size thus facilitating their integration and synergies and respond to the double objective of increasing the company's geographic penetration and the scope of its operations in terms of service offering. The relaxation of the set objective of achieving DKK101 billion (Route 101) also means that pressure to increase the average size and pace of its acquisitions will decrease, a credit positive, particularly in the current credit market environment.

In 2007, ISS further strengthened its service portfolio adding new service areas and expanding existing functions through acquisitions. Security was also added as a fifth pillar within its integrated facility services.

ISS's focus will remain its expansion in high growth economies in Latin America (41% sales growth in 2007), Asia (33% growth in sales in 2007) and "new Europe" (31%). ISS is also expected to continue its penetration in the US market, with bolt-on acquisitions complementing the DKK1.8 billion acquisition of Sanitors, a platform involved in cleaning, building maintenance, landscaping and security services. In March 2008, the company announced the acquisition of BGM Industries, a property, cleaning and security services company with annual turnover of about DKK500 million.

Further cost savings and operational efficiency targeted to sustain cash flow generation

ISS aims to continue to leverage its brand and extensive geographic penetration to sustain organic growth and attract new clients, reduce churn rates and increase cross selling and profitability. The company's margins have showed a small improvement in recent years, thanks to the company-wide application of best practices and economies of scale in key regions, with EBITA margins moderately increasing from 6.4% in 2005 to 6.6% in 2007 and EBITDA margins flat at 9.7%. The slightly dilutive effect resulting from the acquisition of lower margin companies is easily absorbed given their typically limited size and ISS's capability to quickly integrate these entities and bring their profitability in line with the enlarged group through initiatives like re-branding and training. Aiming at maintaining conversion rates around 100% with effective working capital management and low capital expenditures, ISS also targets positive free cash flow generation going forward.

Rating Drivers

ISS'S current B2 corporate family rating reflects its strong business profile, which comfortably positions the company within the Baa range and is sustained by its global presence and leadership in the facility services industry and by the broad range of services the company is able to offer which increases the opportunity of cost synergies, cross selling and bundling. The company's business profile is also characterized by low customer concentration, which combined with the company's global penetration, reduces the impact of market volatility on operating margins and by the company's generally stable margins and high cash conversion ratios, thanks to relatively low capital expenditure requirements and good control over working capital.

However, the company's low pre-tax income and financial strength position it in the low single B range, reflecting the company's highly leveraged capital structure, rising nominal debt and high interest burden, with a Debt/EBITDA ratio still above 7.0x and negative pre-tax income at the end of 2007. The rating assessment also reflects the limited post-acquisitions cash flow generation of the company, with the 1.5% FCF/debt ratio and the 1.5x cash flow interest coverage positioning the company at the low end of the single B rating category.

Current ratings also reflect the low barriers to entry and fragmentation of the facility services market, which increase the competitive pressures on the company, ongoing integration risk linked to the company's strategy, the inherent risk in fixed fee contracts and the potentially negative impact on margins resulting from them, partly mitigated by the company's relatively flexible cost base. The development of the company's performance this far has remained in line with Moody's expectations and has been consistent with the B2 rating category.

Figure 5

Business & Consumer Servi Del Zompo ces Industry Rating Factor Analysis

Business & Consumer Services Industry	Aaa	Aa	A	Baa	Ba	B	Caa-C
Factor 1: Size and Profitability (30%)							
a) ROA (NPATBUI / Avg. Assets)							-0.1%
b) Pretax Income (USD)							-3.95mln
Factor 2: Financial Strength (50%)							
a) (CFO-Dividends) / Net Debt						6.3%	
b) FCF / Debt						1.5%	
c) EBITDA-CapEx / Interest Exp						1.5x	
d) Debt / EBITDA							7.1x
Factor 3: Business Profile (20%)							
a) Business Profile				X			
Rating:							
a) Indicated Rating from Methodology						B2	
b) Actual Rating Assigned						B2	

ISS's business profile appears strong for the rating category, mainly due to the breadth of operations, both in terms of operations and geography, and its diversified customer base. On the other hand, the company's financial flexibility remains constrained by a leveraged financial profile and limited cash flow generation after discretionary acquisitions. According to the Global Business & Consumer Service Industry methodology (August 2007), the main credit drivers are as follows:

Factor 1: Size and Profitability (30%)

Figure 6

Operating Earnings & profitability

DKK mln (as reported)	2005	2006	2007
Revenue	46,440	55,772	63,922
EBIT*	2,063	1,489	1,789
Interest Expense	665	2,203	2,388
Operating Income before Other Items*	2,258	1,869	2,606
Other Items	-354	-215	-196
Net Income/(Net Loss)	935	-809	-442

** After goodwill impairment and write-down and amortisation of brands and customer contracts.*

Source: Company data, Moody's Financial Metrics

The company's turnover increased in 2007 to DKK63.9 billion from DKK55.7 billion, mainly as a result of external growth but also thanks to an improvement in its organic growth rate to 6.0% from 5.5% a year earlier.

With revenues of DKK63.9 billion in 2007, ISS is one of the largest facilities services providers in the world. ISS benefits from stable operating margins, which improved in 2007 to 6.0% from 5.8% the year before, mainly sustained by tight cost control measures, and a high degree of operating flexibility. About two-thirds of its cost base is related to personnel, and with high employee turnover rates the company is able to adjust relatively quickly to market downturns.

ISS Holding A/S

While a broad customer base and geographic diversification should shelter to a certain degree the company's profitability through economic cycles and decrease its dependency on single large contracts, the industry trend of substituting "cost plus"-type contracts with "fixed fee" contracts increasingly places the burden of cost overruns on the supplier. Mitigating factors to this risk include the long-term nature of ISS's contracts, usually between one and five years with a typical termination notice of 12 months, and the cost efficiencies achievable thanks to large established platforms in most countries.

ISS's profitability remains constrained by the sizeable interest burden resulting from the company's highly leveraged capital structure and from the intense price competition in the company's relevant markets, favoured by the highly fragmented nature of the services business and by low barriers to entry. To a certain extent, ISS may be prone to competition from companies exploiting illegal workers to keep their prices low and from in-house service providers, which may ultimately result in a compression in its margins. Moody's notes that competition may also increase as more single-service providers migrate towards an integrated services offering. Reputation risk is also a factor, as the company increases its presence in less developed countries and security services.

Factor 2: Financial Strength (50%)

ISS's financial profile is characterised by stable operating margins and a healthy cash conversion ratio (defined as operating profit before other items post capital expenditure as a percentage of operating profit before other items), historically around 100%.

Despite low capital expenditure (historically 1.4% of revenues) and working capital requirements, the company's cash flow generation remains low due to the highly acquisitive nature of ISS and the sizeable interest burden.

Although showing an improving trend, all cash flow measures would still position the company weakly within the B rating category. The FFO/debt ratio increased from 5.1% in 2006 to 6.7% in 2007 and the CFO-dividends on net debt increased from 5.2% to 6.3%. FCF measures also improved, with a FCF/debt ratio increasing from 0.1% to 1.5%. Given the limited prospects for a reduction in total debt, positive pressure on the ratings could result from an increase in efficiencies leading to higher margins and to an improvement in the operating cash flow generation of the company. A slower acquisition pace, while also slowing operating profit growth, might be positive for the free cash flow levels.

The company's ratings continue to be constrained by its high level of total debt and leverage, with total debt increasing to DKK31.9 billion from DKK28.6 billion in 2007. Moody's notes that current leverage is not consistent with a B-rated company and expects positive pressure on ISS's outlook to result only as the ratio will reach levels of 6.5x or below. Moody's expects the company's level of total debt to continue to increase with only limited de-leveraging over the medium term.

Figure 7

Cash Flow & Coverage

DKK mln	2005	2006	2007
FFO	3,566	2,065	2,926
Dividends	7,229	8	14
Retained Cash Flow	-3,663	2,057	2,912
Cash Flow From Operations	3,120	2,028	2,628
Capex	1,535	1,971	1,938
Free Cash Flow	-5,644	49	676
Beginning Cash	3,121	1,293	2,216
Ending Cash	1,293	2,216	2,581
FCF / Debt	**-19.9%**	**0.1%**	**1.5%**

Source: Company data, Moody's Financial Metrics

ISS Holding A/S

Figure 8

Corporate Debt Structure

DKK mln	2005	2006	2007
Short-Term Debt	940	728	764
Long-Term Debt	16,464	27,912	31,157
Total Financial Debt	17,404	28,640	31,921
Free Cash & Marketable Securities	1,352	2,275	2,664
Net Financial Debt	16,052	26,365	29,257
Other Net debt Adjustments:			
Pensions	799	840	627
Leases	8,874	10,152	11,004
Adjusted Debt	28,384	40,742	43,981
Adjusted Net Debt	27,032	38,467	41,317
RCF / Net Financial Debt	**-22.8%**	**7.8%**	**10.0%**
RCF / Adjusted Net Debt	**-13.6%**	**5.3%**	**7.0%**

Source: Company data, Moody's Financial Metrics

The company's cash flow generation has historically been underpinned by limited capex requirements, usually around 1.4% of turnover, and a relatively low level of debtor days. While revenues are usually stable over the year and profitability shows some degree of seasonality in the summer months (mostly thanks to lower salaries for temporary workers), working capital tends to fluctuate. In fact, it tends to have negative swings in the first quarter, when expenses such as pension contributions, insurance premium payments and bonuses are paid then show positive variations in the second half of the fiscal year, when most revenues are collected.

Moody's considers ISS's liquidity sufficient to service its debt obligations and to support its acquisition strategy. For the year ending December 2007, the company reported cash on balance sheet in excess of DKK2.5 billion, up from DKK2.2 billion in 2006. The company also benefits from a committed revolving credit facility of DKK2.4 billion, recently upsized from the previous DKK1.75 billion, of which around DKK735 million was available at 31 December 2007, an uncommitted facility of DKK100 million and from a letter of credit facility of DKK500 million.

The company also benefits from a DKK1.425 billion committed Acquisition Facility A, of which DKK1.384 billion was drawn at the end of 2007, and a DKK3.5 billion Acquisition Facility B, of which DKK406 million was drawn at the end of 2007.

Factor 3: Business Profile (20%)

The company scores Baa in this category, thanks to its global presence, which reduces its vulnerability to regional variations and changes in regulations, while the broad range of services it can offer multiply cross-selling opportunities. In 2007, ISS continued to strengthen its market position in specific market segments and to increase the penetration in specific geographic areas in line with its strategy, further improving its business profile.

However, although regional coverage recently increased as a result of the Sanitor acquisition in the US and several acquisitions in Asia-Pacific, the company still generates around 85% of total revenues in Northern and Western Europe (95% in 2005). Moody's expects ISS will continue with its cautious acquisition strategy, with targets usually representing no more that 5% of total group turnover to reduce acquisition risk.

The company benefits from some economies of scale, with the potential for cost savings especially in the purchasing and marketing corporate functions. The company's ratings are also sustained by its diversified customer base, their limited bargaining power and a certain degree of revenue predictability. ISS has over

200,000 customers with the top ten accounting for less than 5% of 2006 revenues. Churn rates are also relatively low, with clients usually remaining with ISS for eight to ten years or more.

Rating Positioning & Peer Comparison

Figure 10

Peer Comparison - Key Financials Indicators

USD'000 FY 2007	Rating	Revenues	ROA	(EBITDA Capex) / Interest Expense	Debt / EBITDA	FCF / Debt	FFO	CFO
Aramark Corporation	B1	12,384,316	1.0%	1.5x	6.2x	1.4%	540,402	552,272
Gate Gourmet Borrower LLC	B2	2,075,090	0.0%	1.2x	5.3x	8.7%	116,484	164,265
Global Cash Access, Inc	B1	600,889	4.8%	2.1x	2.8x	30.4%	84,604	92,274
ISS Holding A/S	**B2**	**11,759,466**	**-0.1%**	**1.5x**	**7.1x**	**1.5%**	**538,223**	**483,401**
Unisys Corporation	B2	5,652,500	-2.1%	1.3x	4.0x	-3.0%	469,800	342,900

Source: Company data, Moody's Financial Metrics

Moody's Related Research

Credit Opinion

- ISS A/S

Special Comments:

- Global Business & Consumer Service Industry, August 2007 (104176)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

ISS Holding A/S

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