Company Name: ISS
Company Ticker: ISS DC
Date: 2018-02-22
Event Description: Q4 2017 Earnings Call

Market Cap: 43,706.30
Current PX: 235.4
YTD Change($): -4.9
YTD Change(%): -2.039

Bloomberg Estimates - EPS
Current Quarter: 2.955
Current Year: 15.341
Bloomberg Estimates - Sales
Current Quarter: 19597.667
Current Year: 80364.154

Q4 2017 Earnings Call

Company Participants

- Martin Kjaer Hansen
- Jeff Olsen Gravenhorst
- Pierre-François Riolacci

Other Participants

- Kristian Godiksen
- Paul Checketts
- Joshua S. Masser
- Michael Vitfell-Rasmussen
- Allen Wells
- Matija Gergolet
- Tom Sykes

MANAGEMENT DISCUSSION SECTION

Martin Kjaer Hansen

Ladies and gentlemen, this is Martin Hansen, Head of Investor Relations at ISS, and I would like to welcome you to our Full Year Results Teleconference Call. Please be aware that the announcement, the annual report as well as the slides used for this call can be found on our website. Later today, a replay will also be available and we will post a transcript of the call as soon as it's ready as well.

I'd like to draw your attention to slide number 2 regarding forward-looking statements. Presenting today will be our Group CEO, Jeff Gravenhorst; as well as our Group CFO, Pierre-François Riolacci. We'll open for Q&A after the presentation.

And with that, I would like to hand over to Jeff.

Jeff Olsen Gravenhorst

Thank you, Martin, and good morning, everyone. Let me kick off with a brief commercial update. So please turn to slide 5. As previously mentioned, we did lose some contracts in 2017, and some of them larger than average. But with the retention rate that are usually around the 90%, this is in line with the normal course of our business. And our retention rate in 2017 remained stable at 90%. And this includes the annual impact of DXC. However, there is a difference in the phasing in and out of these contracts. The larger losses have already started to kick in, whereas some of the larger wins, Deutsche Telekom in particular, will not support the organic growth in the short-term.

2017 was also characterized as a year of significant contracts up for renewal. However, 2018 will be much more normal. We actually have less than average up for renewal this year, something that Pierre will cover a bit more details later on. But even if we include the larger losses in 2017, our net wins were very solid in 2017. So, overall, 2017 was a year of strong commercial progress evidenced by a long list of significant key account contract wins and extensions, including three global key accounts as well as the extension of our significant partnership with Barclays.

We also signed significant local and regional contracts such as the largest contract ever signed in the history of ISS, Deutsche Telekom, and the Danish Defense is largest contract ever outsourced in the Danish market, ABB in APAC, Natwest in the UK as well as a number of healthcare contracts across the group.

Similarly, we have already had a solid start to 2018 with the extension of our long-standing partnership with Hewlett Packard Enterprise as well as the announcement of additional new global key accounts. One of these contracts we previously communicated [ph] as a winner (00:02:42) for an international food and beverage company.

Today, we are happy to announce a five-year win of LEGO Group, which is already slowly launching as we speak. Once fully operational, ISS will have approximately 1,500 employees delivering all facility services across the LEGO Group's global operations in 10 countries. Our strong commercial progress in 2017 stood as further evidence of our successful strategy. Our pipeline remained strong, and we look forward to 2018 with confidence.

Please turn to slide 6 for a walk through of the financial highlights. With regard to our financial highlights, the total revenue growth in Q4 was 1.4% despite a material negative impact from FX of minus 3.9%. Organic growth finished better than expected at 3.6% for the quarter from 2.3% in Q3, mainly driven by non-portfolio revenue.

The operating margin was 6.4% in Q4, 0.3 percentage points reduction, of which approximately half was driven by FX, acquisitions and divestments. Our full year margin ended slightly lower at 5.7% compared to 5.8% in 2018, and flat if we adjust for the currencies, acquisitions and divestments, which is in line with the guidance that we gave in connection with the Q3 results. As such, selective operating challenges in North America and Sweden were offset by operational efficiencies elsewhere.

Cash conversion ended up very strong at 104%, up from 99% in Q3 as a result of strong cash flow performance across the group as well as [ph] a bit of (00:04:29) timing around the year-end. Net profit adjusted was DKK 604 million in Q4 and DKK 2.4 billion for the full year, both materially impacted by currency as well as one-off non-cash item such as the re-measurement of a business held for sale in Northern Europe and the impact from the U.S. tax reform.

Our leverage at quarter-end was 2.2 times pro forma adjusted EBITDA, slightly above the 2.1 times a year ago. This is mainly influenced by the acquisition of Guckenheimer. Adding to the overall commercial update on the previous slide, I would also like to briefly cover some of the more recent commercial developments. We continued to see strong growth in our key strategic segments. Integrated Facility Services grew again this year strong, so at 6% in constant currency in both fourth quarter and for the full year 2017 and as such now represents 38% of group revenue, up 1 percentage point from last year.

Within Global Key Accounts, growth in constant currency remained solid at 6% in Q4 and 10% for the full year 2017. Fourth quarter was of course impacted by the loss of DXC. Global Key Accounts made up 12% of group revenue in 2017.

In addition to the recent wins and extensions mentioned on the previous slide, we also recently signed the Global Key Accounts with Department for Business, Energy and Industrial Strategy in the U.K. and the Mass Transit Railway in Hong Kong. Finally, HP Inc. started to ramp down earlier this month as expected, but it's now clear that we will be extending the service delivery in parts of Europe.

With this, I would like to turn to slide 8 for the regional update. Let me start by saying that I'm particularly pleased with our performance in Continental Europe in 2017. Not only has Continental Europe launched or won a number of key accounts, including the Deutsche Telekom one, but has also delivered material benefits from our GREAT implementation across a number of countries.

Organic growth in Continental Europe improved to 6% in the fourth quarter, up from 4% in Q3. Growth in the fourth quarter was driven by contract launches in Turkey, Germany and Austria as well as the generally strong non-portfolio demand, partly offset by ongoing reduction in the public sector exposure in Eastern Europe, Greece in particular.

Last month, we completed the divestment of our operations in Greece, a market not important for our overall international key accounts and our overall strategy. The improvement in organic growth compared to Q3 was driven mainly by non-portfolio revenue. Organic growth for the year as a whole was also strong ending at 4%, up from 3% in

2016.

The Continental Europe operating margin in the fourth quarter remained strong and stable at more than 8%, driven by continued strong margin performance across most countries in the region. The slight margin improvement was supported by higher non-portfolio demand as well as operational efficiencies across the region. For the year as a whole, the operating margin reached 6.5%, up from 6.1% in 2016.

In Northern Europe, organic growth was zero in the fourth quarter, down from 1% in the third quarter. Total revenue growth was minus 6%, heavily impacted by currency moves and divestments, principally the depreciation of the pound and the Norwegian kroner versus Danish kroner, and the divestment of the security services business in Finland.

Organic growth were supported by contract launches, especially in Denmark and Finland, but continues to be offset by contract losses and downscaling, in particular Sweden. As expected, organic growth slowed in the UK, among others, driven by the loss of DXC. This was partly outweighed by the launch of recent wins, including National Westminster Bank, RBS, South Warwickshire NHS Trust and another major client within professional services.

Demand for non-portfolio services was weaker year-over-year in Northern Europe, as expected, given the very strong comp in the fourth quarter of 2016. The slight slowdown in organic growth from Q3 was driven mainly by the UK and Norway. For the year as a whole, Northern Europe delivered 1% organic growth, or 2% excluding Sweden, compared to 3% in 2016. Northern Europe continues to be one of our most profitable regions with a fourth quarter operating margin of 7.8%, supported by most countries in the region. However, margin was down 0.3 percentage point year-over-year, among other things due to the operational challenges in parts in Sweden.

As mentioned, we also face a bit of margin headwind from the timing of contract startup and losses within the quarter. These are the same drivers we've highlighted over the last few quarters. In Q4, we took further steps in Sweden in terms of restructuring our organization [ph] reflect (00:10:12) in connection with Q3. I'll come back to this a little bit later on for more details.

For the year, the operating margin remains solid at 7.1%, albeit down from a particularly strong performance of 7.5% in 2016. Excluding Sweden, the margin for 2017 for the rest of Northern Europe would have been 7.7%, actually slightly up year-over-year.

Please turn to slide 9. Q4 organic growth in Asia Pacific was 4%, up from 1% in Q3. Growth was mainly driven by contract launches in Australia, Singapore and Indonesia, partly offset by expected negative organic growth in China as a result of our strategic structural adjustments to our operating model. The improved organic growth was in particular driven by Australia, and there is no longer an impact from the large losses in 2016, as previously communicated.

Actually ISS Australia has had a commercially strong 2017 with a number of key contract wins as well as a high retention rate in the mid-90%s. It is a local example of how we successfully balance risk and long-term growth. We managed business for the long run, and as such accept losing out in the short-term if we lose for the right reason that is, for example, on price or terms and conditions.

Organic growth was 1% for the year, again mainly as a result of Australia and China, both of which are expected to improve in 2018. The APAC operating margin declined 2.6 percentage points, driven, among others, by normalization of margins in Indonesia on the back of a one-off pension related income in Q4 2016 as well as certain one-off cost in the region in Q4 2017. In addition, the margin continues to be impacted by China as a consequence of the structural revenue reduction and further investments in building up our key account capabilities across the region.

Finally, significant revenues retained in Australia are delivering lower margins at the outset, which is typical within our business. We clearly expect these margins to improve in due course, but having delivered exceptional market strength in the recent quarters, we see margins in APAC over the coming quarters to be down year-over-year but will remain significantly above the group average. For the year as a whole, margins remained high at 7.1%, albeit down from the sector's strong level of 7.5% in 2016.

Organic growth in the Americas accelerated to 8%, up from 3% in Q3. The strong growth was driven by North America as a result of project works, contract launches and Guckenheimer offsetting the loss of DXC in the quarter.

We also continue to see strong growth in Mexico and Chile, whereas growth remained materially negative in Brazil, as expected, following the structural adjustments. Albeit, we are starting to see the first signs of the annualization of the 2016 contract exits.

The acceleration in growth in Q4 from Q3 was driven by strong level of non-portfolio business in North America, which enabled us to grow despite the difficult comps in Q4 2016. Significant flooding related projects for clients in North America ended up larger and lasting longer than initially expected.

In addition, growth from Guckenheimer increased further supported by in-sourcing, upselling and new business. For the year as a whole, growth reached 4%, down from 6% in 2016.

The Americas operating margin improved 0.9 percentage points to 5.4% in Q4. Non-portfolio provided a margin tailwind in North America and performances in especially Chile remained strong. This was partly offset by the timing impact of margins from start-up of new contracts and loss of mature margin contracts as well as continued underperformance within our Specialized Services division in North America.

At the same time, we continue to invest for the long-term as North America is the world's largest outsourced FM market and as such represent [ph] as a (00:14:34) single biggest growth opportunity. The margin reached 3.6% in 2017, down from 4.1% in 2016.

This concludes the regional review for 2017. And I would like to take this opportunity to provide an update on our strategy and how it has transformed our business over the last many years. So please turn to slide 11.

The ISS Way strategy was launched almost a decade ago now, a strategy that has become even more relevant over the recent years. ISS Way strategy has transformed our business. It has choice making at its core. Choice is related to which customers we want to serve, which services we want to provide and which geographies we want to operate in. Rather than being tempted to diversify into unrelated services simply to fuel growth, we have deliberately moved the other way. We've streamlined our business to focus on and invest in the part of the market where we see the highest growth opportunities.

Customers today are increasingly asking for services to support their quest to become better businesses. They're asking for simpler solutions, transparent and consistent service delivery and for cost optimization. To fulfill these needs, we have created an Integrated Facility Services model where we preferably self-deliver all relevant services with our own employees. This strategy has led us to focus on fewer clients with higher demands, and this is why we have developed a Key Account approach with leading concepts and tools.

We streamlined our business to focus and invest where we can be among the strongest players in our industry and where we can make a positive difference for the key account customers. We've built a competitive advantage by reinvesting capital and resource to strengthen our core offering, including workplace management and technical services, capital and resources that have been released from exiting areas that are not core to this approach. So through this, we've grown our Integrated Facility Services and our Key Account businesses with great success over the last many years.

Our transformation under the ISS Way strategy will continue to make a stronger and more focused business. We will continue to strike an optimal balance between managing risk and maximizing financial performance for the long run and to show up higher quality revenue, high organic growth and robust margins.

Please turn to slide 12. This transformation had a material impact on our revenue. Since 2009, we divested approximately a fifth of the business, which was non-core in 2009, and only recently started to acquire capabilities to strengthen our core. Examples include the workplace management business such as SIGNAL, the technical services business such as EVANTEC in Germany or GS Hall in the UK and closing [ph] catering wide spots (00:17:51) with Guckenheimer in the North America and Apunto in Chile. So while our total revenue may not have changed significantly over the years, we've actually added DKK 21 billion organically.

Let me put this organic growth into perspective. ISS has a very long track record of solid and resilient growth through the cycle, and we've not had a single year of negative organic growth since 2003. Organic growth has averaged 3.6%

[ph] this 2010 (00:18:23), solid growth despite approximately 70% of our business being in Europe where the macroeconomic environment hasn't been particularly easy. Organic growth reached 2.4% in 2017. Adjusted for all structural adjustments in part of Brazil and China, organic growth would have been 3.1%.

Looking into 2018, guidance is set for another year of organic growth, somewhat below the historical range, driven by the timing of contract wins and contract losses. However, as recent revenue reduction with fewer larger clients start to analyze new contract launch, organic growth will gradually increase, supported further by the launch of Deutsche Telekom in mid-2019. We should enter into a couple of years with above-average organic growth. In medium-term perspective, we're confident that our strengthened Key Account focus will enable us to capture higher organic growth.

Please turn to slide 13. Despite the significant revenue impact, our margins have remained robust through the cycle. Since the IPO in March 2014, our margins are up by 15 basis points, even including regional operational challenges in a couple of countries. This development comes through despite a 6 basis point negative impact from currencies and 10 basis point negative impact from acquisitions and divestments. These are impacts we hadn't foreseen at IPO. However, we are committed to take the right long-term decisions even if it does have some short-term implications.

Underlying margin continues to be supported, among others, by Key Account focus, rollout of the GREAT structure, procurement savings and other ongoing operational efficiencies, including the use of technology. As such, we are confident that ISS will remain a robust margin business.

Now, please turn to slide 14. By the end of 2017, countries covering 80% of our group revenue were either complete or in progress in terms of GREAT implementation. We have three key countries on the agenda for 2018, North America, Sweden and France. In North America, we will leverage our growth momentum to further develop our Key Account organization and will at the same time address the legacy business of smaller accounts. We will also drive further direct cross-selling initiatives between Guckenheimer and the rest of the business. Also, we'll continue to investigate options to add self-delivery capabilities within technical services.

In Sweden, we'll complete the restructuring as communicated. In addition, we are reorganizing the business to shift the focus towards Key Account customers, implementing new setup around legacy business or smaller clients and would also be leveraging our Cleaning Excellence teams to drive best practice and productivity.

In France, we have over the last number of years successfully optimized the business within the existing organizational structure leading to an improved financial performance. However, a large organization transformation is needed to unleash the full potential. [ph] Changes (00:21:49), which includes the strength and focus on Key Accounts and adjustment of our service offering and a simplification of the organizational structure.

Implementation in France is expected to run from 2018 to 2020, with the first improvement starting to become visible from 2019. While we see very compelling business case in taking significant strategic actions across all three countries, there will be an upfront investment. From 2018 to 2020, we expect to invest DKK 400 million to DKK 450 million in our GREAT implementation, mainly in France, with a healthy payback on our investment. In 2018, the P&L impact is expected to be around DKK 300 million charged to other income expenses, heavily weighted to Q1 2018. The cash impact will be weighted towards the second half of 2018.

So, in summary, our investments will have a real cash impact but will also lead to significant permanent improvement in the country organizational structure and business platform for the benefit of both growth and margins. Following implementation in North America, Sweden and France, our GREAT transformation will be largely complete. By then, we will have become a Key Account focused organization with a significant strengthened and more focused platform to capture future growth.

With this, I would like to hand over to Pierre-François to a more detailed run through of our results. Please turn to slide number 16.

Pierre-François Riolacci

Thank you, Jeff. Now that the operations and strategy deck is done, maybe we can go back to the quarter. And you are familiar, page 16, with this wonderful – on the organic growth to highlight the key drivers. So you know that on the left, we are stripping out the impact of discontinued operation, ForEx, divestments and acquisitions, so that we get a comparable base for Q4 2016 revenues at about DKK 20 billion.

The organic growth for the quarter was finally 3.6%. And again, the key drivers you are familiar with, Sweden was still a challenge with a negative broadly similar to what we have seen over the last few quarters. There was also negative impact from a strategic downsizing in Brazil and China, which remains significant as expected, but which is starting slowly to annualize. There is a negative impact from the loss of DXC, which is minus 0.8% of our global revenues in the quarter, slightly less than expected.

Through 2018 onwards, we will cover in that block the loss of DXC, HPI and also the EMEA region of unnamed Global Key Accounts. The non-portfolio revenues came definitely higher than expected in the quarter and they contributed to plus 1.2% despite, you remember, a difficult comparison from Q4 2016. As Jeff pointed out, we had significant flooding related projects in North America, larger and longer than expected but also a good demand, especially in Continental Europe. The rest of the business is growing by 3.9% with the impact of the new compact launches during the quarter, as Jeff again pointed out.

So, plus 3.6%, that's what we delivered in Q4. Looking forward, we expect the organic growth to step-down in the first quarter. The main reason of course is that we expect more material impact on the revenue reduction with these three clients that I mentioned earlier, DXC, HPI and [ph] NAN global account (00:25:50). We expect the combined incremental negative impact on organic growth from Q4 2017 to Q1 2018 to be in the region of 1%, 1.5%, which means that quarter-to-quarter during the first quarter next year, this year and 2018, we would expect organic growth to be penalized by about 2%.

The other driver which would slow down Q1 is that, we had some contact wins which contributed to organic growth in 2017 and they are annualizing, that's part of it, where on the other hand we have recent contracts which have been secured like LEGO, like the Danish Defence and few other that we cannot name, which will start but are starting slowly actually from the first quarter but on a very small basis and then hunting up throughout the year.

It is worth to mention also that we have limited visibility on the non-portfolio, and of course that's a part of the uncertainty, but definitely the Q4 level was very high. All in all, we expect Q1 to start in the lower end of the guided range for the full year.

Since we are talking about 2018, I would like to spend some time on the contract maturity profile. Please turn to slide 17. So this is a bit of a new piece of information, but we recognize that 2017 was a significant year in terms of expansion but also reduction, and I would like to provide you with some visibility on the maturity profile of this large contract.

The chart that you see on the left part is focusing on the existing large Key Accounts defined as revenues being above DKK 200 million in 2017. [ph] The total of (00:27:42) these large Key Accounts generated DKK 16 billion of revenues in 2017, i.e. 20% of group revenues, and these are contracts that we are running at the end of 2017. Out of this DKK 16 billion, about 15%, that is eight contracts, are up for renewal in 2018. 15% of DKK 16 billion, that's about 3% of our group revenues in 2017, coming for renewal in 2018. Of course, the EMEA impact is much lower as these contracts are coming for renewal as you can imagine throughout the year.

You know that these large accounts are technically five years' contracts, so you would expect to see a rate of about 20% up for renewal as an average every year. So with 15%, it's clear that 2018 is not the most challenging year in terms of renewal. So that gives you some insight of what's coming in 2018 and we will of course update the information on a regular basis throughout the year.

Now we can move to profit, and we move to page 18. And we would go for the same logic that follows, the organic growth and we stripped, again, discontinued ForEx, and divestment and acquisition. Just to highlight a few points, operating margin is impacted by the ForEx and divestment and acquisition by minus 12 basis points, that's 5.66% compared to 5.78%. Then again, you would find when you look at the operation a strong profit improvement in

Continental Europe with, I would like to highlight that three quarters of the operating profit growth is driven by solid organic revenue growth and margin benefit from this GREAT implementation that we had in several countries. It's only a quarter of the improvement which is on the back of one-off adjustments.

You noticed of course lower contribution from APAC, despite a record year I should mention in Singapore, and this is the result of the plan contract exits in China, also the normalization of the operating margins in Indonesia following this one-off income that we had in 2016 in Q4. The corporate costs are broadly stable, 0.8% of the group revenue, in line with our expectation.

Just a point about this one-off. Overall for the year, they were broadly neutral in 2017 compared to 2016. They were positive in Q2, negative in Q1, Q4, but on the full-year, you can say globally neutral. As we mentioned that in November, if we adjust for the ForEx and the divestment and acquisition impact on the margin, the operating margin was flat year-over-year from 5.66% in 2016 to 5.65% in 2017.

Now, even if the quarter is sometimes a bit misleading, I think it's good to look at Q4 margin development on the slide 19. I think on that one, I would like to highlight that the margin impact of ForEx and divestment and acquisition is even higher than the full-year, it's minus 16 basis points down, so the margin is down from 6.70% to 6.54%. I think that Jeff has been covering the regions. So, I would just like to highlight that if you adjust from the ForEx and divestment and acquisition impact of 2016, you can see that the underlying decline in the operating margin Q4 to Q4 is about 20 basis points, in line with what we expected when we released Q3.

Again, when we look into the beginning of 2018, the key margins – drivers that you need to be aware, basically the same underlying driver as in Q4 2017, an incremental impact from losing further material contacts, including the key losses that I mentioned a couple of slides ago. We expect margin in APAC to decrease further from peak levels following exceptional, not instant, over a number of quarters, but again these margins will remain significantly above the average.

When it comes to the impact of ForEx and divestment acquisition based on our current assumption of the forward curve, it is expected to be broadly neutral for the year on margin, but it will remain negative, let's say, mid-single digit in H1, and we expect that to recover in H2 slightly positive. So, when you look at Q1, we expect the year-over-year margin to decline to widen actually further during this first quarter. We expect the margin to be down year-over-year in H1 as we discussed when we released Q3, mainly in the first quarter and then to be up year-over-year in H2, driven mainly by the fourth quarter and we expect to reach the end of the year around 5.6%, plus/minus 10 bps, excluding the impact of ForEx and net acquisitions and divestments.

We go to page 20 for the income statement and the other lines, and of course on revenue and operating profit before other items has been covered. Just don't forget that there is a significant impact on ForEx on revenues and therefore also an operating profit even if the impact is limited on margin. But of course, it does impact EBIT and EBITDA.

When you look at the other income and expenses, we have a net loss on divestments in Q4 for DKK 125 million. It's a chart which is mainly related to the re-measurements of a business classified as held for sale in Northern Europe. For the full year, the net loss of divestments is DKK 200 million.

On the restructuring part, we had an expense of DKK 64 million in Q4, majority in Sweden as flagged in Q3 and a few ongoing GREAT implementations. For the full year, the total restructuring charge is DKK 284 million.

Finally, we realized acquisition and integration cost of DKK 42 million in the quarter relating, among other, to the integration of Guckenheimer. On the financial income and expenses, there is an increase of the charge of DKK 37 million in Q4, half of it DKK 20 million is actually linked to the amortization of financing fees due to the refinancing of the FS liquidity line in November.

For the year, it's DKK 538 million, up DKK 70 million. Excluding the refinancing cost and the ForEx, we have a chart of about DKK 500 million. We expect 2018 to be slightly higher than that, again excluding ForEx impact due to the annualization of the [indiscernible] (00:35:16) refinancing that was completed in August. On the back of it, we have secured 100% fixed rate exposure for net debt at year-end for the next few years with a five years' duration of gross debt and interest rate on our portfolio [indiscernible] (00:35:30), which is below 150%.

On taxation Q4 and full year 2017, the effective tax rate was 31% and 27% respectively, and these have been impacted by the revaluation of the deferred tax assets following the lower income tax – corporate tax in the U.S. Lower corporate tax is of course good news for the company, but not necessarily accounting wise for the net operating losses, which have been recognized in the balance sheet. For the full year 2017, tax credit is 26.8%. It is negatively impacted by the non-cash revaluation of the deferred tax asset, as I just discussed, for about 2.9%. This was partly offset by the divestments, which are beneficial to the tax credit of about 1%, and also as a recognition of deferred tax asset in Germany for another 1% on the back of the higher visibility that we have today in this country and of course taking into account the signing of a big compact, as you know.

I just said from this one-off, you could say that the underlying effective tax rate is approximately 26%, in line with our expectation. I would like to mention on this U.S. tax reform that we have a positive impact below the net profit adjusted, which is linked to deferred tax liability that we had in the U.S., so the net impact, P&L impact, on the reported income for the U.S. tax reform is only DKK 8 million negative. The adjusted net profit is DKK 604 million in Q4, that is DKK 2.4 billion for the full year. Both are actually lower year-over-year and this is due to the significant currency impact I mentioned earlier, but also the non-cash one-off items such as the net loss on divestment and the impact of the U.S. tax reform, again, as is adjusted net profit.

I'm done with the income statement. I'll move to of cash flow. And of course, on cash flow, we look primarily to the full year. The cash generated by operation is slightly down 2% to about DKK 5 billion. It is reflecting of course a decrease in operating profit, and especially the ForEx headwind that we had to face. Also I would like to mention that even if the P&L impact of the one-off is neutral, the net cash impact of this one-off is slightly negative.

When you look at the working capital, Jeff mentioned already the cash conversion rate, 104%, which is very high. It is a result of a strong working cap process and good timing at year end. It is also including DKK 57 million in transition and mobilization costs related to the Deutsche Telekom contract. But it's clear that such a good rate is not sustainable in each and every quarter, and that's the reason why we stick to our guidance of achieving more than 90% in quarter.

On the other expenses, I think that I have mentioned already the restructuring cost in 2017 and the cash out is not very far away from the P&L entry, so DKK 300 million versus DKK 176 million in 2016. And this is cash wise, driven by Sweden, Brazil, as well as some exit cost in Argentina and Uruguay, which are not in the P&L but which are of course reflected in the cash flow statement.

The net interest paid is increasing by DKK 64 million in 2017, and this is mainly due to the timing of interest payment at the very beginning of the year with the bond that was issued in 2015, plus also high average net debt on the back of the Guckenheimer acquisition.

On the income tax cash out, it's actually down year-on-year by DKK 59 million with a good payment schedule in several countries, and also tax asset recovery incurring in Guckenheimer, which has been running good in 2017. The cash tax rate has increased to 24% for the full year, and it is gently converging towards the underlying effective tax rate, I mentioned already, 26% as expected.

On the investment side, I would like to mention that the capital expenditures are running at 1.1% of the revenue, which is in the middle of the long-term range 0.914% of revenues. It is slightly up compared to 2016, and we did a bit better than expected, the capital discipline is always very high on the agenda. We however expect capital expenditures to go up in 2018 towards the higher end of the historical range and mainly driven by this transition and mobilization investments related to Deutsche Telekom as well as an ongoing investment in technology.

The free cash flow ended at DKK 2.7 billion, and I will come back to it in the next slide, but before moving to the next slide, I give you a quick update on Deutsche Telekom. On the cash flow side, we expect to spend from 2017 to at the start of the contract July 30, 2019 about DKK 600 million, which have to be recovered through our pricing model during the contract execution. In terms of phasing, we have spent about 10% of this amount in 2017. We expect to spend about 30% in 2018, and the remaining part 60% in H1 2019. There might be some shift again, and it is an indicative phasing that gives you an order of magnitude. Again, on this total amount, we expect about 70% to be recognized in the working cap and about 30% in the capital expenditure. So, it helps you to build your forecast next year.

On the P&L, we expect about 80% of this cost to be capitalized in the balance sheet and there would be [indiscernible] (00:41:44) but we expect about 20%, and again this bit may change to be recognized as revenues, because they are linked to specific milestones and performance obligation, and it is not an option in ISS, you have to account for them in revenues. However, we do not expect any material net P&L impact on this transition and migration before we start operating.

We move to page 22 on the cash flow, and 2017 remained a good cash flow year of DKK 2.7 billion. It is of course DKK 200 million down compared to last year, but this is driven by high restructuring expenses and also higher CapEx, DKK 128 million on the restructuring, DKK 102 million on CapEx. So definitely this decrease in cash flow is linked to investing in the business.

The conversion of EBITDA to operating cash flow is still very high. I think we have continued with the illustration on the right side. It shows something about the stronger earning quality and even if 2017 it's a bit lower, it is also reflecting this one-off that I mentioned about pension that explain that we are a bit at the low-end but still at a very good level of converting EBITDA into operating cash flow.

Looking forward into 2018, we expect both free cash flow and conversion of EBITDA to operating cash flow to be temporarily impacted by the transition and mobilization cost, highlighted through the upcoming launch of Deutsche Telekom. There would be also an impact on free cash of the ForEx, because we lose 4% of the revenues. And even if it is neutral in margin, there is an impact of costs on the bottom line, including on the cash. We expect also some normalization of our cash conversion and significant level of restructuring cost, as Jeff mentioned, but not necessarily much higher that what we had in cash in 2017. I can tell you that the free cash generation will stay at the top – very top of the agenda of ISS.

We move to page 23 and the capital location, and basically our capital location basically is unchanged and is consistent with our communication since the IPO, it is reminder on the left of the slide. The total amount paid in dividends in 2016, as you can see, was DKK 2.1 billion and the balance of the free cash was going to de-leveraging, 2017 is a bit of a different year. We paid the 2016 ordinary dividend for DKK 1.4 billion and now we effectively spend the other half of our free cash flow on the acquisition of Guckenheimer, DKK 1.4 billion net.

Today, we are proposing the 2017 ordinary dividend of DKK 7.7 per share to be paid in 2018. This dividend is stable compared to last year and it does reflect a strong underlying earning power and cash flow generation. Indeed, if you adjust for the two key one-off non-cash items that we had in 2017, I mean, the revaluation impact of the U.S. tax reform on one hand and the revaluation of an asset help offsetting Northern Europe and also cost adjusting for the discontinued operations, then the payout ratio is 50% in line with our policy also and that's very important. That payout will again represent approximately half of our DKK 2.7 billion free cash flow in 2017.

Moving forward, we do not expect any change in this policy. The leverage by the end of 2017 was DKK 2.2 billion, which is slightly higher than the DKK 2.1 billion we had in 2015 and 2016. And this is of course as a result of the acquisition of Guckenheimer in the second quarter. By the end of 2018, we would again target a leverage closer to two, all others things being equal, in order to leave sufficient room for leverage to be seasonally higher in midyear and still be within our leverage target less than 2.5 in any quarter. We will continue to prioritize investing in our business, and this including acquisitions, subject to of course to strict strategic and financial [indiscernible] (00:46:05). If we cannot reinvest capital, if we cannot justify to reinvest capital, we will periodically look to hit around surplus funds to our shareholders either the extraordinary dividend or share buybacks.

With this, I would like to hand back over to Jeff. Please turn to slide 25.

Jeff Olsen Gravenhorst

Thank you, Pierre-François. We expect organic growth will be between 1.5% to 3.5% in 2018. The business environment is supportive by better macroeconomic conditions in most of our major countries, with exception of the U.K. where Brexit related uncertainty clearly persists. We expect continued growth from Key Accounts supported by the wins and expansion discussed few slides ago. The negative impact from the lost revenue with DXC, HP Inc. and the EMEA operations of one other Global Key Account will impact most of the year and will partially offset progress elsewhere. We also see continued healthy growth coming from our emerging markets. First quarter is expected to come out towards the lower end of the guided range for the year as covered by Pierre.

Our 2018 operating margin expected to be around 5.6%, around meaning plus/minus 10 basis points excluding the impact from FX and net acquisitions and divestments, which is currently set to be broadly neutral on the margin for the year. A number of mature contracts [ph] are re-tendered (00:47:40) during the year, some we have retained, and some we have faced reduction in scope, and some we lost, but replaced with wins elsewhere. Either way, mature business is being replaced by business which initially will be less profitable. These dynamics are consistent with our long-standing operating model, but the impact is somewhat larger than right now and we'll weigh on the business for the next few quarters.

These impacts will partially mitigate our ongoing focus on cost and efficiency initiatives – be mitigated by the cost and efficiency initiatives, including expected gradual improvements in a couple of our underperforming countries. All in all, we expect the margins to be down year-over-year in the first half, mostly in Q1, and up year-over-year in the second half driven mainly in Q4, as also mentioned by Pierre.

Finally, the guidance for cash conversion remains above 90%. So, in summary, while 2017 has provided some challenges, the key developments during the year, both the good and the bad, have only strengthened our conviction in the ISS Way strategy. Progress is never achieved in a straight line, however, our recent commercial success is encouraging, the pipeline remains strong and the market opportunities is considerable. Our transformation under the ISS Way strategy is making us a stronger and more focused business. And with this, we're confident that we're striking the optimal balance between managing risk and optimizing performance for the long run, increasing quality of revenue and ultimately enabling us to capture higher organic growth and robust margins.

With this, I would like to take the opportunity now to mention that Nick Ward, who was our Head of Investor Relations have moved on to a senior commercial role within ISS, and that role has now been taken over by Martin Kjaer Hansen and hence the reason why Martin was opening the meeting today. So of course, thank you very much to Nick, and thank you for Martin to just take over.

And with that, I would like to open up for the Q&A.

Q&A

Operator

Thank you. We will now begin the question-and-answer session [Operator Instructions] Our first question comes from the line of Kristian Godiksen from SEB. Please go ahead. Your line is now open.

<Q - Kristian Godiksen>: Thank you. Couple of questions from me to start out with. So, firstly, could you please confirm that the margin will deteriorate further in H1 2018 compared to the 35 bps and you had a contraction in Q4 2017, and if the margin deteriorates further on an underlying basis in H1 2018 as I guess the impact from FX and M&A will be less, what are the main drivers then for margin to expand in the second half where you'll also be impacted from the loss of the HP contracts, will be my first question. The second one would be, the guidance for the organic growth if we adjust for the loss of the larger contracts, you also show on page 8, I guess that would add around 2 percentage point to your organic growth guidance, so I guess that would have been 3.5% to 5.5% instead of the 1.5% to 3.5%.

And then just lastly, now you mentioned that the project grade is largely complete in 2018/2019, should we hence then still continue to expect that you could expand your operating margin underlyingly around 10 bps basis a year on average? Thank you.

<A - Jeff Olsen Gravenhorst>: Yeah, thanks for the questions. All good – actually all good questions. Yes, we expect margin in Q1 to deteriorate further compared to Q4. That would not be on the back of further FX or divestment acquisition because, as I mentioned, we expect it to be slightly negative indeed in H1 compared to H2, but more in the single digits that's what we see today based on the follow-up. So you need to be also very cautious about that, because it could be more or less, but we still see definitely FX and divestment and acquisition to be slightly against us during the quarter.

However, we expect the underlying margin to deteriorate further in Q1 compared to Q4. And clearly the main driver behind that is that in Q1 we are not only losing DXC, but we have HPI and this European part also in H1 will come as a Global Key Account. So we have more mature contracts, which are actually leaving us, and that has a negative impact. The other part which is coming is that we are hunting up this new contract that will come throughout the year, and you know that at the beginning you are actually more [indiscernible] (00:52:55) margin contribution from this contract, and that's precisely the reason why we see the shift between H1 and H2 with definitely low point in margin in Q1, and this is not on the back of strikes but more on the back of this trend on the contract timing.

On the organic growth for the 2% – the guidance of 1.5% to 3.5% and the impact of the 2% on the DXC, HPI and the other global account, you're right. If you just take it on face value, of course it would be plus 2%. However, I will say that 2017 as I started by saying was within the normal retention of 90%. So, again, you can argue, it is normal that we lose contracts, they're just a little bit larger this time. So, on face value, you're right. It does imply that the growth is higher in 2018, which is of course also underpinned by the number of contract wins that we've had.

And then, on the lastly complete within 2018 and 2019, I think on that part clearly we do see that the margins in the Key Account area are better than it is in some of the specialized services. So of course that the more we go towards the larger accounts the better we can see the margin upside of course. The more we can sell more services to current customers, the better we can see also an improved margin. However, it really is all about selling more.

So that key account point will give us a higher growth potential, and of course it can also give us some better margins in relative terms. We have to remember that at some point in time that probably just tails off a little bit as we talked about earlier. But on the mid-term, yeah, I think this is all about growing the top line, the organic growth opportunities with being bigger more [ph] presence with the field lines (00:54:57).

<Q - Kristian Godiksen>: Okay. Thanks a lot.

Operator

Our next question comes from the line of Paul Checketts from Barclays. Please go ahead. Your line is open.

<Q - Paul Checketts>: Good morning, everyone. I've got two areas of questions, please. The first is just more of a bigger market question. Some market participants are saying that it's moving away from large contracts where all the services are bundled together. If you were to look at your pipeline, what would that tell us? And related to the overall market with regards to the LEGO contract, how competitive was the bidding for that? And what would your margin expectations be for it over the course of the life?

And the second question is about the DKK 400 million to DKK 450 million of investment. I mean, that number looks very high to me. Could you perhaps clarify exactly what it is you're going to be spending that on, and what is that you're saying is the issue with the French business if you don't mind clarifying that? And why are you doing this now and not last year and two years ago, any extra color on that would be appreciated? Thanks.

<A - Jeff Olsen Gravenhorst>: Yeah. Thank you, Paul. If you think from a market perspective, we certainly do not see that neither does the people who actually started the market. So, in our pipeline, the key growth areas all tenders that comes out and particularly in the mature markets, I would say, are all bundling; one way or another, they're bundling products. Of course, it means – there is a logic to it. The logic is that it's a simplification of the way that the services are rendered into your own home, your own organization. So we see more and more bundling of services that can be degrees where what is bundle, but it's more and more bundled. I don't see any contracts where we go the other way. You can have the odd service that's taken away or not, but in general I just see more bundling and more bundling also in the tenders that comes out, not just with customers that we know beforehand but also to tender.

So if you look at the ones that we won over the last six months, all of them are bundling services one way or another and also bundling countries one way or another. So go larger more broadly both from a service and a geographical coverage perspective. And the reason is, they want to have consistent services across, they want to make sure it's compliant across, and they want to make sure that they get the efficiencies across. So that's the first part.

On LEGO, of course, we don't mention what margin is in there, we don't do that for competitive reasons. But I will tell you that we did not win on price. With LEGO, this is really about branding or about people. So it's how people approach of self-delivery of making sure that all the employees or many as at all possible that we take on this outsourcing comes to us and does not go via subcontractors. This has been very key to LEGO, the whole people management part of winning that contract. So that is a clear case of a people focus.

On the French situation, I think actually France, we're doing pretty well. However, there is a further step and over the last few years and if you remember far not back. This has been a long good progress of stabilizing the business of improving the underlying margins and so forth. However, it is a market which is predominantly driven with smaller accounts. And in the smaller accounts, we want to spend the investments on simplifying the business of becoming much stronger at the Key Accounts. Because also in France, we're seeing a tendency to go and bundle services within Key Accounts more than we've ever seen before.

So we need to make this investment to make us a stronger and more simplified organization and certainly to capture more benefits in the way that we work together throughout our 35 branches within the French market. We can optimize that. Even though today we're not doing a bad job, we can do even better. And these investments will give a healthy payback. Maybe Pierre add little bit more on the details around it.

<A - Pierre-François Riolacci>: Yes. I mean, thank you, Jeff. And we cannot be too precise because you know that there are also some regulations that we have to comply and local law. But indeed, a big chunk of this DKK 400 million, DKK 450 million are actually deemed to be spent in France. The majority of it is linked to redundancy and severance package. So that's part of it, and you know that in France it's not cheap. That's definitely one thing. The other thing is that we have to – we plan to restructure our networks, that implies also to move officials so they are cost attached to that, that imply investment [ph] in ideas (01:00:07), that implies also to accept a sort of overall up cost, when you are managing that transformation, so that's the reason why we have this [ph] lower amount (01:00:17).

And I think that the point made by Jeff on the timing is key. I mean, we had some – a few things to fix first, which has been done. We have a strong team, which is also very important when you engage that sort of money. And it's clear also that we have a contract today in France, which is [ph] more supportive (01:00:35) for this sort of transformation than before.

<Q - Paul Checketts>: Thanks very much.

Operator

Our next question comes from the line of Joshua Masser from Morgan Stanley. Please go ahead. Your line is open.

<Q - Joshua S. Masser>: Hi. Morning all. Three questions from me, please. First one is on Sweden. I was wondering how is the restructuring going and when you expect to start seeing the special turnaround? The second one is, I noticed that you've lost the contract with the Ministry of Defense in the UK, obviously you won one with the Department for Business as well. What are you generally seeing in the UK public sector and how this changed at all since [ph] Carillion (01:01:19)? And finally, on non-portfolio work, obviously a lot of that was from flooding in the U.S, but whereabouts did you see the demand in Continental Europe for that work? Thank you.

<A - Jeff Olsen Gravenhorst>: The Swedish restructuring is actually ongoing and we've been doing this for the last few quarters, as you know. And we see the stabilization of the situation right now. There are some underlying reasons for the Swedish market being where it is. And we went through this at the Capital Markets Day also in more detail. We have a big competitor which is subsidized by the state, there's now been a ruling from EU that they have to change those conditions so that will, of course, make our market better during 2018 because there are not this unfair competition situation.

The other one is that we had some restructuring within our healthcare sector. We are almost done with that. So that would be finished by the end of 2018 or at least that will be expected to be. And then on the specialized services part of the business, we are one helped by the ruling the EU. Of course, but the other part of our restructuring in the organization to simplify our set-up, and that will also more or less be done in the first half year. We expect to be improving the business back to [ph] former days (01:02:38) in the latter part of 2018 going into 2019 on a more normalized run rate.

If you take from a UK perspective, there's a lot of things happening the UK as we all know. Brexit is one thing of course. But the more recent on some of our colleagues in the market having some difficulties to actually severe difficulties, as you know, with [ph] Carillion (01:02:58). There are of course a lot of attention to the outsource market.

Having said that, we've actually picked up a number of contracts on the back of the term [ph] turmoil (01:03:09) in the beginning of this year, and we do see good opportunities to continue. Now, I think it's quite important for us to just state we are a different set-up, we don't do construction, we don't do major installations. We have key accounts for whom we do a lot of non-portfolio project works, which will predominantly be refurbishments or restructure or rebuild within the current facility. So we're not building new facilities from that perspective. So we're different kind of breed. Now, from a political point of view, I expect that the public arena albeit at a little bit stress right now will continue to see the benefits in the outsourcing, and that's also what we see across.

The growth in 2014 from a non-portfolio point of view, we do expect to have a decline in our non-portfolio in the guidance that we're putting forward now, because we had a very strong non-portfolio growth in Q4, particularly the flooding side, we can never know when these happens, now that happened for the last two years in a row.

But in general, we also see that with the two mature contracts, HPI and DXC in particular going out that has been contracted with higher non-portfolio project works. So, with that in mind, we have taken now the expectations a little bit, so we're looking at a [ph] negative (01:04:35) expectation to the non-portfolio growth. So, the growth in the 1.5% to 3.5% actually comes from decent growth in Europe on the back of good performance in Continental Europe as you've seen, but also good growth in Americas and it comes from portfolio and from wins of contracts.

<Q - Joshua S. Masser>: Okay. Thank you.

Operator

[Operator Instructions] The next question comes from the line of Michael Rasmussen from ISS (sic) [ABG Sundal Collier] (01:05:08). Please go ahead. Your line is now open.

<Q - Michael Vitfell-Rasmussen>: Thank you very much. I'm Michael not from ISS but from ABG. So, since I'm limited to only one question, if you could talk a little bit about the revenue synergies that you've been getting from Guckenheimer, so is this across all services? And can you give us any insight into kind of the magnitude you've been winning and basically what our customers are saying about this new set-up? Thank you.

<A - Jeff Olsen Gravenhorst>: Certainly. We have – the type of synergies that we have from Guckenheimer into the business of course has been that we have been able to convert the part of the catering that we have outsourced to other providers in the past, because we didn't have the ability to self-deliver, and that has actually largely been done now.

Of course, you can argue we will not do it on some of the ones that were [indiscernible] (01:06:05) for example, but the rest of it has been converted, and including the larger global corporate clients has been converted into Guckenheimer product now. And that's gone very well, very well indeed. So basically we're done with all of the first synergies from that perspective.

We're now moving into the synergies where we are providing some of the traditional services. So, the technical maintenance and the cleaning part to some of Guckenheimer's clients, and then of course we have merged the organization into being one organization, so we will not speak about two organizations in the future, but one. And that means we have some traction now on selling both ways of the synergies.

The reception of both types of clients has been very positive. So back to the original question here, do we see more or less bundling? We certainly see more bundling. Even in the U.S., we see that they are welcoming from the Guckenheimer side that we could do more services for them. And on the legacy ISS part, of course, there is a welcoming of the fact that we can self-deliver and with a really good product for our current line. So, the reception of this has been extremely positive, I would have to say, and we can see that we have actually not only converted it but also increased revenue and uptake in the [ph] restaurants (01:07:21) on the ISS side. So very happy with that.

<Q - Michael Vitfell-Rasmussen>: Thank you, Jeff. That sounds good. Can you add any numbers on that?

<A - Jeff Olsen Gravenhorst>: Yeah. I think originally we gave a number of $40 million of sales synergies and they are pretty much all done except that we do a little bit less because we're not doing DXC.

<Q - Michael Vitfell-Rasmussen>: Great. Thank you so much.

<A - Jeff Olsen Gravenhorst>: Yeah, it's the same number actually. Yeah, because we have more revenue. Sorry.

Operator

Our next question comes from the line of Alan Wells from Exane. Please go ahead. Your line is open.

<Q - Allen Wells>: Hey. Good morning, guys. Just a couple from me. Maybe just following up on the non-portfolio work in the fourth quarter, I think from memory typically you see this coming in as above group margin so there should have been some positive mix impact potentially from that in the fourth quarter. Is it possible that you can quantify that? And then obviously with the reduced element of this factored into next year, would that be a bit of a headwind?

Second question, just on the comments around the DKK 450 million of investment in the GREAT initiative, you talk about a good payback, maybe if you could talk a little bit about how you think about good – do you look at payback period or return, that'll be really, really helpful? Thank you very much.

<A - Jeff Olsen Gravenhorst>: On the non-portfolio part, you're absolutely right that there was extra non-portfolio part work in the fourth quarter and during the regional walkthrough also highlighted that as a [indiscernible] (01:08:50) to the North American market in the fourth quarter. All of that has all been factored into 2018 projection on the margin side as well. So we will see the non-portfolio typically come in with a slightly higher margin. Yeah, we do expect to see, as we said, negative growth on the lower non-performing part next year because of the high what we had this year. But again, this will all be factored into the margin development.

On the investment?

<A - Pierre-François Riolacci>: Yeah. I mean, on the investment, usually on the restructuring, we expect to pay back, which is above one year – slightly above one year, but to be very candid it's clear in France we are closer to two years. And especially when it comes to other than fees, so because there are some cuts attached to that, and that's more or less where we are. So, in general, a bit north of one year and in the case of France, given also the investment we need to make a bit less than three years. So I think that's still pretty distant. And I would like just to take the opportunity to your going back on this restructuring path that we plan to be done in 2019 with GREAT implementation. But you need also to figure out that – I mean the group of that size, there will always be a [ph] soft or hardcore (01:10:11) of restructuring. And we discussed that already in the past, so you can bet that about DKK 100 million, DKK 150 million a year is the minimum amount, because we are divesting businesses sometimes and we need to adjust.

We are sometimes here and there losing businesses. We need to adjust. And that's part of the story of a large company like that, and please factor that in when you go for future cash flows and make sure that [ph] shows up number (01:10:37), but of course nothing compared to what we are mentioning today, which is definitely much higher.

<Q - Allen Wells>: All right. Thank you.

Operator

[Operator Instructions] Our next question comes from the line of Matija Gergolet from Goldman Sachs. Please go ahead. Your line is open.

<Q - Matija Gergolet>: Yes. Hello. Good morning. I'll let you come back on the margin in Asia-Pacific, which seems to be like the biggest drop and perhaps the biggest surprise of the quarter down 260 basis points year-on-year. You mentioned there was a positive one-off in the fourth quarter last year and a negative one-off in this quarter. Can you give us a bit more color or maybe even numbers around these two one-off items just to help us understand a little bit what's the true underlying margin?

In the press release also, I read something about – on your report about Thailand is that the area of concern. Just now – help us a bit understand the big volatility in the margin. Okay, I appreciate your saying – it's going to be above the group average but now the group average is quite a bit lower than what you did historically in Asia. A bit more color would be appreciated. Thank you.

<A - Pierre-François Riolacci>: Maybe a few comments on the key drivers and then maybe Jeff will assist you about what we see in APAC, and we definitely are very strong region in terms of margin and sustainable. It's clear that we had one-off, especially in the Q4. And in Q4, as I mentioned, we had a positive one-off last year in Indonesia and we had negative mainly in Thailand this year. So, the net impact is about – in the quarter about DKK 40 million. And if you extend that to the full-year, it's even a bit more than that. So definitely it's not – it was a tough year in terms of one-off.

There is also a run rate impact, which is linked to first in 2017 we have delivered an outstanding performance in Singapore on the back of very stronger contract performance and it's difficult to imagine that we can maintain that sort of performance run rate. You know that we are also downsizing and reshaping our business in China, and that clusters in our revenues and that's also clusters in terms of margin. We will recover and we plan to recover China later this year, but it's clear that it will hit us significantly during this year, and that's basically the key drivers which are behind the change in 2017 to 2018.

You need to remember also that Australia has been through a big transformation of contract, I mean, they had a very strong commercial success, but that means also that they are in Q4 and starting quite a few operations. And that has also has an impact on margin that we expect to recover gradually throughout the year. So definitely a bit of a challenge in this Q4 and looking forward in the next quarter but a very strong very strong business even if we have to take some strong action.

<A - Jeff Olsen Gravenhorst>: We'll just say it is a strong market and it is a market where you can achieve relatively high margin. So, if you take it for the year that despite we had the two opposite poles of the one-offs, the year came out of 7.1%, which is significantly higher than the group average and then we continue to see that potential.

<Q - Matija Gergolet>: Okay. So, margins on that level are more or less sustainable, you would think?

<A - Jeff Olsen Gravenhorst>: I'm not saying that that happens over the next few quarters, you have to listen to what Pierre just said, but – which saying that it is sustainable to be in the high-end of our potential.

<Q - Matija Gergolet>: Okay. Okay. Thank you very much.

Operator

Our next question comes from the line of Tom Sykes from Deutsche Bank. Please go ahead. Your line is open.

<Q - Tom Sykes>: Yeah. Thank you. Morning everybody. Just wanted to focus on that key contract maturity chart that you put up. So, just looking at the 3% in 2018 and the 5% in 2019, could you just remind us please how concentrated the number of contracts in that 8%? And then in the 5% specifically for 2019, would you say that – could you give a view on how much higher than group margin perhaps that business is? And maybe how early you might start hearing or renewing those contracts which will expire in 2019, please?

<A - Jeff Olsen Gravenhorst>: Thank you very much for this nice question, which I think just spot on. First on 2018, so a bit more than DKK 2 billion of revenues coming with eight contracts which are ranging from about DKK 100 million plus – sorry, DKK 200 million to DKK 500 million. So, [indiscernible] (01:15:59) actually, and no one single exposure which is significant. And so far with some decent visibility of the processes. So, no big one and again – and good visibility.

On 2019, we have a bit more contracts, I would say, about probably 12 to 14 contracts, which again we're talking from DKK 200 million to more than that, and we have a chunky one actually which is – we have a bit more than DKK 4 billion. So we have one which is not half of it that's not that far away, so we have this significant one coming. And of course, I mean, that's something that we are looking very carefully, and we will keep you updated. When it comes to margin, there is no secret that these contracts all over, they are not dilutive in margin and they are stronger, most of them they are ISS contracts and they are exactly that grow our business, so that's a good contract.

<Q - Tom Sykes>: Thank you very much. Thank you.

<A - Pierre-François Riolacci>: [indiscernible] (01:17:06) it is less of an issue than the ones that we've seen now.

<Q - Tom Sykes>: Okay. Thank you. And what would you – how would you classify that sort of renewal rate that you're able to see retention rate on key accounts kind of in the DKK 200 million to DKK 500 million range, your experience on that versus the really big ones because it doesn't seem like there's much incumbency benefit on very large contract renewal. But maybe there's a bit more on the DKK 200 million to DKK 500 million, have we really got any comments on that?

<A - Jeff Olsen Gravenhorst>: There are a lot of benefits for being an incumbent, and that's why we continue to extend contract by HP for 10 years, 15 years. And you've just seen it on HP Enterprise that didn't go out to tender, we just prolonged it. Now there, we've had for 40 years and without jinxing anything, these are high success rates on retentions. But you will have once in a while that for example HP is splitting the company in three creates a completely new situation, that's a different thing. So incompetency is definitely a benefit both to the client and to us.

If you look at HP, we continue now with HP Enterprise so that we've actually kept the success rate of global accounts has been almost 100% now for 10 years. You can argue the DXC and HPI, it is actually splitting out of one contract, but the original one we still have. If you're looking countries overall at the Capital Markets Day, I think we showed you also that Key Account has a higher retention rate. So of around the 93% thereabout and that means the rest of the business is below 94%. So we have a much higher retention rate on these accounts.

<Q - Tom Sykes>: Okay. Well, thank you very much for the answers. Thank you.

Operator

And I'll now hand back to the speakers.

Jeff Olsen Gravenhorst

So thank you all for participating in the call. If there are unanswered questions or further questions come up later in the day, our IR is obviously available. But otherwise, thanks and have a nice day.