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INXN - Q2 2013 Interxion Holdings NV Earnings Conference Call

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PRESENTATION

Operator

Thank you for standing by and welcome to the Interxion second quarter earnings conference call. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session (Operator Instructions). I must advise you that this conference is being recorded today, Wednesday, the 7th of August, 2013.

I would now like to turn the conference over to your speaker today, Mr. Jim Huseby. Please go ahead, sir.

Jim Huseby - *Interxion Holding NV - VP, IR*

Thank you, operator. Hello everybody and welcome to Interxion's second-quarter 2013 conference call. Today you'll be hearing from David Ruberg, Interxion's Vice Chairman and CEO; and Josh Joshi, the Company's CFO.

To accompany our prepared remarks, we are again providing a slide deck. The slides are available on the Investor Relations page of our website at investors.interxion.com. We encourage you to download these slides to use during the call if you've not already done so.

Before we get started, I'd like to remind everyone that some of the statements that we will be making today are forward-looking in nature and involves risks and uncertainties. Actual results may vary significantly from those statements and may be affected by the risks we identified in today's press release and those identified in our filings with the SEC. We assume no obligation and do not intend to update or comment on forward-looking statements made on this call.

In addition, we will provide non-IFRS measures on today's conference call. We provide a reconciliation of those measures to the most directly comparable IFRS measures in today's press release, which is posted on the Investor Relations page at investors.interxion.com.

We would also like to remind you that we post some important information about Interxion on our website at www.interxion.com. We encourage you to check our website for the most current available information.

We also post information on social media sites, such as Facebook at facebook.com/interxion, and Twitter at @Interxion. We encourage you to follow us on these sites.

Following our prepared remarks, we will be taking questions, and now I'm pleased to hand the call over to Interxion's CEO, David Ruberg. David?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Thank you, Jim. And welcome to our second quarter earnings call. As Jim mentioned at the beginning of the call, we've prepared a slide deck to accompany our prepared remarks and we encourage you to download the deck and follow along as Josh and I will refer to these slides during our comments. So please turn to slide 4.

I'd like to begin today by discussing Interxion's performance in the second quarter of 2013. Once again, Interxion produced another quarter of consistent growth based on solid execution. Financial and operating results in the second quarter show strong year-over-year growth. Our all organic revenue growth was again in double digits with operating leverage significantly expanding our adjusted EBITDA margins and driving faster growth in adjusted EBITDA than in revenues.

Bookings were solid in the second quarter. Churn was again consistent with our expectations. Our sales pipeline is stable and pricing remains relatively unchanged over the last few quarters. Just after the quarter end, we successfully refinanced our high yield bonds and revolving credit facility as part of our ongoing strategy to reduce our cost of capital.

Operationally, we completed the two Scandinavian projects sketched for this quarter, one which was in Copenhagen and the other in Stockholm, and we also announced another data center build in Frankfurt, Frankfurt 8. Today we are also announcing additional demand driven expansions in three markets; Stockholm, Vienna and Zurich. We'll talk more about that later.

Demand for our services in each of these markets is healthy. So we are adding capacity in a disciplined manner with additional right size expansions to meet market demand. During the second quarter, we had a 1,200 revenue generating square meters and increased our utilization rate to 74%.

We continue to see demand across all of our target market segments with strong demand from cloud platform providers who are establishing their positions in our data centers in advance of anticipated enterprise customers migrating to hybrid and shared services. In our opinion, the outlook for the European data center market remains healthy and interaction is well positioned for continued growth and future success as we create -- continue to create customer demand and derive shareholder returns from the business.

Please turn to slide 5. Let's look at the second quarter's financial performance in more detail. Revenue for the second quarter exceeded to EUR76 million, which is an increase of approximately 13% from Q2 2012 and a 3% increase when compared to the first quarter of 2013.

Recurring revenue was EUR72 million, which is up 15% year over year and 2% sequentially and accounted for 94% of total revenues. Year-over-year recurring revenue growth continued to be stronger in the Big 4 reporting countries. Customers continued to have extended decision-making timeframes, but demand remains healthy and the pricing environment is consistent with previous quarters as is the sales pipeline.

Adjusted EBITDA was EUR32.7 million in the second quarter growing at an 18% year-over-year rate and exceeding revenue growth due to the operating leverage in our business model. Adjusted EBITDA margin was 42.8% in the second quarter, which is 200 basis points better than the second quarter of 2012.

Please turn to slide 6. During the second quarter of 2013, Interxion added 800 square meters of equipped space and we ended the quarter with 78,900 square meters of equipped space. We had sold 1,200 net square meters of revenue-generating space across our footprint and ended the quarter with 58,200 square meters of revenue-generating space, which is 20% higher than a year ago. This resulted in a utilization of 74%, which is up from Q1 2013 and consistent with our targeted utilizations of about 75%.

Please turn to slide 7. We completed the two projects scheduled for the second quarter. The one in Copenhagen called Copenhagen 1 remote side expansion and the first phase of Stockholm 2. Both of these projects were constructed in response to market demand.

We remain on track with our 1,800 square meter build in Frankfurt 8. The first phase of 900 square meters is scheduled to open in the first half of 2014. We continue to see strong demand in the Frankfurt market. As a result, we are evaluating the possibility of accelerating our expansion plans to meet the near-term need for additional capacity.

As our planning and decision-making process continues, we'll be sure to keep you posted on our developments. As mentioned before, Interxion is announcing today expansions in three data centers in our rest of Europe segment. First, in Vienna. We've already constructed the fourth phase of Vienna 1, we call it Vienna 1.4, and it was due to continued demand from financial services and cloud committees of interest.

Vienna 1.4 became operational earlier in the third-quarter 2013 and provides approximately 400 square meters of equipped space. In Zurich, we are constructing the fourth phase of Zurich 1 in response to continued demand from various segments. Zurich 1.4 will provide approximately 500 square meters of equipped space and is scheduled to become operational in the fourth quarter of 2013.

And in Stockholm, we are constructing the second phase of Stockholm 2 in response to continued demand from various segments. Stockholm 2.2 will provide approximately 500 square meters of equipped space and is scheduled to be operational in the first quarter of 2014. We ended the quarter with 81 megawatts of customer available power with a total of 113 megawatts available within our current and announced data centers.

Please turn to slide 8. This slide provides an update on the revenue development of our target segments. Building resilient communities of interest in these target segments is the key to the strategy for interaction and we've put a lot of focus and investment into our facilities, our sales force and our customer service offerings over the last couple of years to enable us to succeed with this strategy. These communities of interest provide competitive differentiation and become increasingly powerful organic growth engines due to the network effect that develops over time.

In the second quarter, we continued to execute well with a particularly strong performance in the managed services or cloud provider segments as these companies and other cloud platform providers continue to invest in the infrastructure which is required to enable enterprises to make the transition to integrated cloud solutions for their dedicated and shared applications. While end customer adoption of these cloud solutions has been slower to evolve or develop than people anticipated, there are strong incentives for this migration and we expect this migration to be a source of sustained long-term demand across a number of our target segments.

In the quarter, we added more than 80 logos in our target segments further adding to the value that these communities of interest can deliver to our members. Our focus on our current and target customers and the communities in which they participate differentiates our positioning in the market. It is how we help create value for our customers. We know this because our customers tell us this.

I would now like to turn the call over to Josh.

Josh Joshi - *Interxion Holding NV - CFO*

Thank you, David. And welcome to everybody on the phone and online. As usual, I'd like to start by discussing the Group results, follow that with some additional color on our two geographic reporting segments, followed by discussion of our capital expenditures and then a review of the balance sheet.

If you could, please turn to slide 10. Once again, Interxion experienced consistent quarterly growth, three solid execution. We saw sequential growth in total revenue, recurring revenue and adjusted EBITDA which grew faster due to expanding adjusted EBITDA margins as we recover from expansion drag and enjoy the operating leverage of our business model.

As expected, recurring ARPUs grew modestly from the first quarter and our utilization ticked up. Total revenue in the second quarter was EUR76.5 million, up 13% organically compared to the second-quarter 2012 and up 3% sequentially. On a constant currency basis, total revenue would have been EUR0.5 million higher year over year though there was no meaningful impact sequentially.

Recurring revenue in the second quarter was 94% of the total at EUR72.2 million, a 15% year-over-year increase and 2% sequential increase. On a constant currency basis, year-over-year growth was 16%. Nonrecurring revenue was EUR4.3 million in the second quarter, slightly ahead of our typical EUR3 million to EUR4 million range due to an increase in installation revenues though down 16% from last year's second quarter.

I think at this point it's worth taking a moment to make you aware of a development with one of our top 15 customers. This customer has been facing ongoing significant challenges with its business model. We've been working with them for some time to explore alternatives. In the end, they decided to bring all external data center services back in-house into data centers which they own as part of an internal restructuring and resizing program. This migration started in the second quarter and will continue through the rest of the year. We expect this will have some impact on recurring revenue growth rates for the rest of the year, but has no impact on our guidance for 2013.

Moving on to discuss ARPU, our monthly recurring ARPUs were modestly higher and in line with our expectations. Recorded last quarter, most of the sequential ARPU decline was due to adverse foreign currency effects. Off of the first quarter base, foreign currency had very little impact. So sequential ARPU growth was mostly related to the increase in power revenues offset by some geographic dilution.

Power revenues picked up their rate of growth during the quarter, but remain below the average growth rate we've seen in prior quarters. This is consistent with my comments last quarter given the number of complex deployments we've installed over the past year and the extended time lines that these types of deployments incur when ramping their power usage.

As we look ahead to the third and fourth quarter and excluding factors such as currency and geographic mix, I would expect to see continued increases in power capacity and energy utilization contribute to continued modest sequential quarterly increases in recurring ARPUs.

Cost of sales in the second quarter was EUR31.3 million, up 11% over the second quarter last year and 6% higher than the first quarter of 2013 due primarily to an increase in people costs. Gross profit was EUR45.2 million, an increase of 14% year over year and 1% sequentially with gross margins at 59.1%.

So the marketing costs were EUR5.5 million in the quarter or 7.2% of total revenue within the 7% to 8% range that we've spoken about previously. These costs were flat for the third consecutive quarter.

Other G&A costs remained tightly controlled at about 9% of total revenue and declined by 5% on a year-over-year basis. Other G&A cost declined also by EUR0.5 million or 8% from the first quarter to EUR7 million.

Adjusted EBITDA was EUR32.7 million, an increase of 18% year over year and 3% sequentially. Adjusted EBITDA margin in the second quarter was up 200 basis points year over year and 20 basis points sequentially. Depreciation and amortization was EUR14.9 million, a 46% increase year over year and a 6% sequential increase. The increase in these non-cash expenses relates to our new facilities that became operational over the past year and is consistent with the increase in the gross cost of data center assets held on the balance sheet.

Net finance expense was EUR7.3 million in the second quarter, higher both year over year and sequentially. This reflects the significant capitalized borrowing cost during the data center constructions in last year's second quarter in line with IFRS requirements and to a lesser extent the increased interest expense on the Paris 7 capital lease and our mortgages.

During the last week of the quarter, we closed another mortgage, this time for EUR6 million over our Amsterdam 3 data center at very attractive rates. This quarter's finance cost also reflect our final four quarters worth of expenses on the retired 9.5% senior notes. A refinancing transaction closed on the third of July. So the third quarter will have nearly a full quarter of the 6% senior notes and very little of the 9.5% notes. I'll talk more about the refinancing transaction in a moment.

Income tax expense was EUR3.1 million in the second quarter resulting in an effective book tax rate of 32% once again. The cash tax rate in the quarter was 17% and 13% on an LTM basis. Since the beginning of 2012, our LTM cash tax rate has been slowly but steadily creeping up and as we've highlighted on previous calls, we expect this trend to continue over the next two years of so as we utilize our tax shield.

Net profit for the second quarter was EUR6.6 million, a 24% year-over-year and 5% sequential decline due primarily to the completion of our expansion projects and the coincident increase in depreciation and financing costs.

Earnings per share during the quarter was EUR0.10 on 69.4 million diluted shares compared to EUR0.13 in the second quarter last year and EUR0.10 last quarter.

Now, let's take a closer look by geography. Please turn to slide 11. In the second quarter, the growth rate differences between the two segments narrowed. While the Big 4 segments once again showed significantly stronger growth, the rest of Europe year-over-year growth rate increased back into double digit. Within each segment, Germany, the Netherlands and Sweden were notable strong performance.

Looking just at the Big 4, total revenue was EUR48.3 million, up 14% year over year and up 4% sequentially and again represented 63% of total Company revenue. The Big 4 segment grew recurring revenues by 18% year over year, 19% on constant currency. Recurring revenues grew more than total revenues due to an unusually high EUR3.9 million of nonrecurring revenues in last year's second quarter. Big 4 adjusted EBITDA margins were steady compared to the first quarter at 54.0% and 250 basis points higher than the second-quarter 2012.

Revenue in the rest of Europe segment was EUR28.3 million, up 10% year over year and 2% sequentially.

Recurring revenue growth was 11% year over year. Adjusted EBITDA was EUR14.7 million with margins that continue to be consistently around 52%. Levels of activity in the rest of Europe segment vary across markets. We continue to invest selectively in this segment based on visible customer demand as is the case with Interxion expansions in Stockholm, Vienna and Zurich.

Moving to slide 12, let's discuss our capital expenditures. Capital expenditures including intangibles as seen on the left-hand chart totaled EUR28.8 million during the second quarter with EUR27.1 million of that devoted to expansion capital and EUR1.7 million to maintenance and other CapEx.

We continue to invest more heavily in the Big 4 markets with EUR21.0 million or 73% dedicated to that geographic segment in the second quarter compared to EUR7.3 million in our rest of Europe markets. As we've discussed before, we allocate capital to where we see demand that meets our return on requirements -- on the required investments.

We've announced three smaller expansions in the rest of Europe segment today and we continue to work on as yet unannounced expansions in our Big 4 markets.

Please turn to slide 13 where I will discus our balance sheet. But before I speak about the balance sheet itself, I'd like to discuss the refinancing that closed on July 3rd. As we stated on the last few earnings calls, reducing our cost of capital is a key strategic focus for Interxion.

We continually watched the market and felt that it was the right time to refinance the 9.5% senior notes and expand and restructure our revolving credit facility in order to achieve three objectives; one, to bring down our borrowing costs; two, to extend the maturity of our debt instruments; and three, to increase financial flexibility.

Through this NPV positive refinancing exercise, we have been able to successfully restructure our core debt package to meet these three objectives. We were able to reduce the interest rate on our bonds by 350 basis points and push maturities out until 2020. We were able to simplify and lighten our covenant and security packages. We expanded and increased the flexibility of our debt baskets to allow us to further improve our cost of debt in the future. We also expanded our revolver to EUR100 million and added some cash to the balance sheet enhancing overall access to liquidly.

We expect one-time costs of approximately EUR31 million to flow through the third quarter financial expense line and this includes the premium on the old bonds of around EUR27 million together with the write-off of about EUR4 million of unamortized financing costs relating to the old revolver and bond.

Given that the transactions closed on the 3rd of July, we thought it would be helpful to present both actual balance sheet figures at June 30 and June 30 figures adjusted for the refinancing.

Summarizing the movement in actual cash during the second quarter, Interxion generated EUR24.1 million from operations after absorbing about EUR8 million in working capital. We also raised EUR6.8 million from financing activities, paid EUR2.8 million in cash interest and taxes, and invested EUR28.8 million in capital expenditures during the quarter. This left cash and cash equivalence of EUR59.8 million at the quarter end. The bond refinancing would add approximately an incremental EUR30 million to the quarter and cash balance before payment of accrued interest.

Borrowings, when adjusted for the refinancing, would be carried at EUR363 million and this includes the small EUR6 million mortgage on our Amsterdam 3 property that I mentioned earlier. Gross leverage ratios remained low at 3 times adjusted EBITDA and net leverage at 2.3 times adjusted EBITDA, both of which are stated adjusting for the new debt structure.

It's worth noting a change in our leverage covenants, which have gone from a gross debt leverage test previously to now a net debt leverage covenant of 4 times adjusted EBITDA. We remain well capitalized, fully funded with no near-term maturities, plenty of headroom and a decreasing cost of capital. Looking ahead, we will continue to tweak the balance sheet, optimize our tax position and pursue other initiatives to improve returns for shareholders.

And with that, I'd like to turn the call back over to David. David?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Thank you, Josh. Please turn to slide 15. One of the topics that we -- I get asked to address all the time is the supply-demand situation, which really very quickly just to discussion on demand.

We get asked two questions, how much, how big and when. So we thought that I would take this opportunity to delve a bit deeper into one of the fundamental long-term drivers of demand for us and that is the migration of enterprises or companies to cloud-based solutions.

As I mentioned earlier, this migration appears to be taking longer to materialize than was originally expected by the cloud platform and service providers. But it is an important demand driver of the future, so it's worth spending a few minutes to share with you our vision on the migration phases and the potential for Interxion to deliver against this opportunity.

Companies have been undergoing continual structural changes in the architecture of the IT infrastructure over time. Across what we see here are the three most recent eras of IT architecture, starting with the traditional client server in 1980. The first of these three again was the traditional client server architecture and it was characterized by dedicated company-owned servers supporting individual applications, which were delivered to end users.

From the early 2000, companies started to deploy hardware virtualization and used shared applications for discrete tasks such as Salesforce.com or Workday, which were often remotely based and hosted by third party providers. However, the majority of the software remained on a dedicated in-house platform.

More recently, companies have begun the transition towards the use of a hybrid architecture consisting of a mix of shared and dedicated platforms, software and service, legacy applications. Moving to this architecture often requires low latency, high capacity, low cost and reliable connectivity between multiple platforms, applications and the end user in order to provide the uniform end user experience. The benefits of this architecture are reduced costs, potentially better reliability and security, access to more forms of data and portability, the ability to have your data on any device anywhere.

But there is an obstacle and in many cases it's a conversion cost. We have and are working with dedicated managed service providers, systems integrators and carriers to secure their core cloud platforms or access to these core cloud platforms in our data centers to support corporate migration to the cloud.

While we have seen growth to date within the Interxion's data centers from these cloud platform providers, adoption of the platforms by companies has been slower to materialize than originally anticipated. This phenomenon appears to be similar in the United States and in Europe and is driven by both technical factors and business sentiment.

As mentioned before, barriers to these migrations include such issues as upfront conversion cost, software complexity, organizational impact, the need to reenter business processes, data security and service quality assurance. These mostly technical barriers to technology adoption are being overcome or worked around as companies recognize that not all applications need to be treated in the same fashion. From our perspective, the bigger factor in the slower-than-anticipated migration has been weak business sentiment.

But companies evaluate making the migration to hybrid architecture. They do so in a context of the health of the economy, the anticipated growth in their business, the upfront investment required to migrate, the ability to extract cost efficiencies and other factors. What we found is that if IT managers cannot tick the boxes on all of these factors, they will likely just continue to make do with what they have for the time being.

We believe that as economy start to recover we will see companies refocus on innovation versus cost control and as more than technical impediments are migrated, we'll see the phase of adoption of cloud IT-based solutions start to accelerate. As a result, we believe that the opportunity presented by this era of IT architecture continues to be a unique long-term growth opportunity for data providers such as Interxion.

Interxion is ideally positioned to meet the needs of companies seeking these capabilities based on our data center's excellent external fixed and mobile connectivity as well as the ability to cross connect within the data center to a wide portfolio of cloud platform on and off ramps as well as community of interest members.

Please turn to slide 17. As usual, I will close my remarks with a couple of comments on our outlook. We are reaffirming our previously announced full-year guidance, financial guidance. To be specific, for the full-year 2013 we are expecting revenue to be in the range of EUR307 million to EUR322 million. We expect adjusted EBITDA to be in the range of EUR130 million to EUR140 million and we expect to invest between EUR130 million and EUR150 million in capital expenditures this year.

I would like to thank again all of our employees in all of our companies for staying focused on our customers and continue to deliver strong results. I would also like to thank our shareholders and bond holders for their continued support.

Now let me hand the call back to the operator to begin the question and answer segment. Operator, can you please read out the instructions to register questions?

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). David Barden, Bank of America.

David Barden - *Bank of America - Analyst*

I guess the first question, Josh, obviously we just have to dig in a little bit to this question of the top 15 customers. Is it fair to assume that it's going to be something like a 1% type of revenue headwind and should we be then expecting that the lower range of the guidance is the more likely outcome at the margin?

And then second I guess, Dave, you kind of elaborated a lot on kind of some of the challenges that the cloud end user demand has been facing. Is that something that we should be thinking about in terms of the growth rate in the business as a headwind or is it just a delay of a tailwind that's building down the road? Thanks.

Josh Joshi - *Interxion Holding NV - CFO*

Thanks for your questions. Hey Dave, so let me deal with the guidance question first. So, yes, I think your assessment, David, of approximately 1% recurring revenue is reasonable. Look, we've been working with this customer for some time and we figure that they are going to be moving out of our data centers progressively over the course of the year and overall as we have reaffirmed our guidance for the remainder of the year. I think that that covers it.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

David, to your other question, I believe it's more of the -- no, not believe, I am convinced it's more of a delay in the tailwind. Without elaborating too much, and I apologize for the analogy, but I look at this -- there are three basic drivers of demand for our services and one of them is Internet traffic, okay. And I view it as a two-cylinder engine. It's running reasonably smoothly, but is slow, but it's pretty consistent. So it's Internet traffic.

Another one is business growth and it is because its businesses today which are growing their business based on adding new products, new services and new customers. And that's a four-cylinder or six-cylinder engine, and that's -- relatively it's slower than the other growth. The big elephant in the room is this 16- or 32-cylinder engine, if there is one that's that big, which is the way people migrate, the way people change business from in-house specific applications on dedicated platforms to outsourced hybrid which is shared and dedicated.

And again, I've tried to pick the engine side to reflect what I believe and we believe are the relative opportunities in the terms of tacking them. So it's giving me poetic license here, 2 cylinder, 4 cylinder, 16 to 32 cylinder. One of the things we tried to depict on the chart is these things take time to develop because there's inertia, but when it happens, they are huge. So I hope I didn't over-answer your question, David, but it's a slowdown in the tailwind, that's all.

David Barden - *Bank of America - Analyst*

And that's great, Dave. Thanks. And Josh, if I can just follow up with one more just with respect to the refinancing and the maximum leverage being four times, some of it may be slower than previously expected expansion in rest of Europe. Is there any appetite to take some of that financial capacity and bring it back to the stockholders in terms of stock repurchases or even dividend which would kind of close the gap between yourself and some of your peers out there? Thanks.

Josh Joshi - *Interxion Holding NV - CFO*

Thanks, Dave. The focus for us, as I said, is to continually look on where are the best returns on investment for our shareholders' capital. And I think David was very clear. In looking at the opportunity that we see going forward, I believe our belief right now is that we see the best returns on investment on our investment thesis within the business going forward.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

David, I don't want to pile on you, but if in fact there is even a 10% or 20% truth in what we did on page 15 and what we are trying to depict, there will be ample opportunity for us to deploy that capital in the next couple of years to give superior returns to our investors, superior to either a dividend or a share buyback.

David Barden - *Bank of America - Analyst*

All right, great. Thanks, guys.

Operator

Michael Rollins, Citigroup.

Michael Rollins - *Citigroup - Analyst*

I was wondering if you could talk a little bit more about the specific geographical markets. For example, you mentioned you're thinking of expanding in Germany. Are you seeing some incremental competition in Germany or anything different in that market maybe versus some of your other markets, and maybe you can give us a ranking where you're positioned the best and maybe where you are seeing the most competition or the most challenging demand environment. Thank you.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay. Thanks for your question. I'm not going to rank them because rankings change week over week, month over month. It's also difficult to rank because these countries, the different segments are different stages of the development. With our competitors, we have different approaches in terms of market opportunities and size of customer, size of applications. So I don't think our ranking would be beneficial.

We have been asked quite a bit over the last couple of weeks on what's going on in Germany, and all I can tell you is that we believe that the problem that's been alluded to by a number of other people are unique to them, not to the market in Germany.

Michael Rollins - *Citigroup - Analyst*

But is there a reason that you believe it's different for Interxion that you can share with us?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Well, I know we are going to get asked this question. We can neither be humble about this or conceited about it. But how about we do it somewhere in between? We have a market segmentation strategy. We have stayed consistent to that. It's all organic, and it presents some competitive advantages. And I think they have showed up, they have been highlighted by the performance in the last two quarters in Frankfurt or in Germany.

Michael Rollins - *Citigroup - Analyst*

Thanks very much.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

You're welcome.

Operator

Jonathan Schildkraut, Evercore Partners.

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Robert Gavin - *Evercore Partners - Analyst*

It's Robert Gavin for Jonathan. I was wondering if you guys could talk about the monthly recurring revenues and sort of the pace of recovery from the earlier year kind of flows in the perspective about delivery of expansions base and the other factors that affect that?

Josh Joshi - *Interxion Holding NV - CFO*

Yes, thanks, Robert. If you recall, we -- our ARPU development because of the significant amount of space that we brought on in 4Q 2012, our ARPUs dropped -- recurring ARPUs dropped at that point in time. And since then we've seen the development of power and energy across these sort of multiple complex deployments. As we see that develop over time, we've seen sort of the modest growth in the second quarter.

And what we would expect to see for the remaining quarters of this year is a continued sort of steady modest growth that we have already seen. Does that cover your question?

Robert Gavin - *Evercore Partners - Analyst*

Yes, pretty much. Yes, I'd say so. Thanks.

Josh Joshi - *Interxion Holding NV - CFO*

Thank you.

Operator

Colby Syneseal, Cowen and Company.

Colby Syneseal - *Cowen and Company - Analyst*

So I just wanted to follow up on that question on ARPU. So you guys have mentioned that you expect ARPU to be up moderately. You said that last quarter as well and when I do the calculation, at least it looks like it was flat, actually technically down just slightly on a quarter-over-quarter basis. I'm trying to understand what I missed there.

And then specific to that, is the -- what's having the greater impact as we move into the second half of the year? Is it a change in power? I know you mentioned last quarter for example that some customers are now doing a power pass-through, so that's potentially having a negative impact on ARPU. But also this top 15 customer, what's the expected impact on ARPU from that customer? Were they above the average, below the average, and may be some color on that?

And then just one last follow up. G&A, it was down about EUR600,000 on a quarter-over-quarter basis, obviously one of the areas where you saw flat year to your EBITDA. Was any of that one-time? What allowed you to actually see that come down and how sustainable is that? Thanks.

Josh Joshi - *Interxion Holding NV - CFO*

Great. So there're a number of things there. The customer impact is going to be, as we said, approximately 1% on ongoing basis. And I think it's -- the ARPU levels of that customer I would say are around average. Going back to your comment on ARPU development, we actually saw a EUR2 up-tick in our recurring ARPUs in the second quarter over the first quarter. And my commentary has been very careful. The characterization that we use in the first quarter and also now is to say that we would expect it to grow modestly, and that's how we would expect it to continue to grow.

With regard the other G&A, yes, there was some benefit that was broadly from a few incidental items. We had some impact on adjustment on accruals on payroll item and one or two other items. I would think in terms of one-time items there, there's probably a lot of couple of hundred thousand euros going forward. So we will see some of that benefit going forward. I hope that covers it for you, Colby.

Colby Syneseal - *Cowen and Company - Analyst*

Yes, that's great. Thank you.

Operator

Milan Radia, Jefferies.

Milan Radia - *Jefferies - Analyst*

A couple of questions actually. The first was are you seeing any kind of clear differentials between buying patterns in say London versus Amsterdam or Frankfurt in terms of the way deals are configured? Is there an appetite in certain markets to perhaps take more power per square meter upfront and compared to say other markets where there's more deferral of that or is there no real change to those buying patterns?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay. Thanks for your question. I don't believe that country by country if we put application A into the UK and application A into Amsterdam, that you would see any difference, okay. It's application specific, now -- and also the company that's dealing with that application and whether they are successful in bringing customers on to their platform.

But if you are asking me are they different, the follow-on question is are there different applications going into the different countries, the answer is yes.

Milan Radia - *Jefferies - Analyst*

Okay. And then how do you -- so I'm trying to understand, I suppose to some extent as everyone is, is why we're seeing such disparities in organic performance. So is it a London issue versus other markets? Is it a end-market issue, ecosystem issue? I mean, if you had to sort of provide an overlay on what we're seeing right now, what would be your kind of broader observations on those diversions that we're seeing between the various operators?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay. I was going to ask you -- Milan, I can only tell -- I can tell you what we're seeing and I will refrain from making comments. I would do -- I know nothing that you -- you may know nor more than we do, and the end result is I will take their press releases at face value in terms of why their growth was not what ours is, okay.

Milan Radia - *Jefferies - Analyst*

Okay.

Josh Joshi - *Interxion Holding NV - CFO*

One thing that we've said time and time again is that we believe that we differentiate ourselves in our market based on our focus on communities of interest. And I think from a long-term organic growth perspective, Milan, it has historically shown up in our numbers and will continue to show up in our numbers in terms of both superior organic growth. And that is where I think, for want of a better word, the secret source is within the Interxion engine.

Milan Radia - *Jefferies - Analyst*

And one final question. I mean, looking at London, I guess, I'm kind of positive there's a mini cycle at work in London. Is there any change to your appetite to open up space in London? Does that kind of -- are you more kind of minded to just slightly differ things a little bit on the bigger project?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

No. Look, the way we have tried, following on to what Josh said, we look at these markets. We try to position ourselves with access to GDP in a time-sensitive fashion. The London market for financial services may've changed, but the fundamental market in London long term for access to cloud services, digital media and all the rest has not changed at all. It continues to expand. So our appetite to be in that market and to service those needs has not changed at all.

Milan Radia - *Jefferies - Analyst*

Okay, thanks very much.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Thank you.

Operator

Tim Horan, Oppenheimer.

Tim Horan - *Oppenheimer - Analyst*

Two broader questions. One, can you just may be discuss where you are with the timing of adding new capacity in terms of how much really campus capacity do you have, how long does it take to get the permitting and the design phase and may be just the overall construction costs because I think what you're trying to imply here is you're probably going to slowdown some of the incremental additions over the next 12 to 18 months, but if demand picks up, you can kind of accelerate those additions.

So just curious how much spare capacity you had and how much time would it take you to really accelerate if you needed to, or slowdown kind of how much flexibility do you have, and then overall just what the overall construction cost are there? Thanks.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay. I'll let Josh chime -- I'll encourage Josh to chime in here. I don't think that we send -- I hope I did not send any message one way or another or Josh will slap my hands about this. What we do is we look at these things constantly. We encourage our local MDs to know what the next project is and what the project is after that, and so we're constantly looking, and especially since we have gone public and have a much better balance sheet to deal with some of these issues that we've talked about in the past.

So we are constantly looking at getting permits, looking at acquiring leases and things like that so that we can do our just in time and match our capacity to the needs. So I didn't imply any slowdown. Actually, what I hope will happen is we are beginning to see, I think all of you read the same newspapers that I do, that there is a slowdown in negativism both in United States and in Europe. There is actually some, let me call this, sprouts --

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Jim Huseby - *Interxion Holding NV - VP, IR*

Green shoots.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Green shoots, a hope for the future coming up all over the place. So I wouldn't be so negative and I wouldn't draw any conclusion that we intend to slowdown. We intend to match our availability as best we can to the needs of the target segments that we're going after.

Josh Joshi - *Interxion Holding NV - CFO*

I would completely agree with that, David, and our focus or our pursuit of agility has not changed. We, as David said, our local managing directors have the responsibility to have that inventory of future capacity and how to access it available to them. And that will include engaging power companies, taking options over property. As I said, we try to agile. We want to reduce that commitment and maintain as many choices as possible.

Each country is different. Remember, we are trying to focus our investments within city center locations and therefore, on a per square meter basis, on a -- our investments tend to be about EUR10,000 to EUR15,000 per square meter. But we can see some significant divergences from that where there are city center locations in London, for instance, we're surrounded by pebbled streets, it's more expensive. And if you build in multiple storeys, again it's more expensive. In a city center location, that tends to be what you need to do.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

But we do that for a reason because there's more value there.

Josh Joshi - *Interxion Holding NV - CFO*

Right, right, exactly right, David. We are focused on the campuses where we are in the pursuit of value.

Tim Horan - *Oppenheimer - Analyst*

Josh, that's really helpful, but your announced the kind of a capacity for next year is kind of well below the 6,000 or 7,000 that you've kind of done for per year over the last four or five years. Should we expect a ramp up in that or do you think next year you might come in below what the trend has been?

Josh Joshi - *Interxion Holding NV - CFO*

Well, Tim, the first thing is that we are not going to be giving next year's guidance out today with respect, but our approach will not change. And one thing that I did say was that we are working on unannounced projects in relation to our sites. And I can tell you it's in the Big 4 as well as the rest of Europe and I think that this would develop over the course of the next several months and quarters.

Tim Horan - *Oppenheimer - Analyst*

Thanks very much.

Operator

Prasad Borra, Goldman Sachs.

Prasad Borra - *Goldman Sachs - Analyst*

A couple if I may. Firstly, can you indicate if there has been any market share shift, especially in Germany or in London and also is there any cannibalization of the retail space by wholesale vendors? The second question is what's your current position on the interconnect fees in Europe? Competition seems to indicate that they are already rolling out interconnect fees to the customers. Has your position changed at all?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay. On market shift, I don't believe there has been any substantial market shift. One or two quarters doesn't shift the market, okay. In terms of wholesalers and retailer, I know we get asked this question and I'm delighted to answer it every time I get asked, there is a world of difference between wholesalers and retailers and it is -- wholesalers don't care who comes in their data centers. We are really picky about it.

And so our focus on these communities of interests which we're geared throughout the Company to make sure that we have a consistent population that has the potential to interconnect and create value over time is something you just -- I don't care who you are, you just can't wake up the next morning and say I'm a retail co-location provider and I'm going to compete effectively. It's just -- it's not in the DNA.

And the last question was?

Josh Joshi - *Interxion Holding NV - CFO*

The interconnect.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay, on the interconnect. As we indicated the last time, we believe that interconnection is a core foundation of our base product and so what we are doing -- and we have always provided that. So what we are looking at is to see whether we want to unbundle certain elements of this for a specific class of customers and how we would provide that service. And so we indicated the last time, we are looking at both a pricing and a service model, which may unbundle some of this. So, yes, we are looking at it.

Prasad Borra - *Goldman Sachs - Analyst*

Okay, that's very helpful. Thank you.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

You're welcome.

Operator

Jonathan Atkin, RBC Capital Markets.

Jonathan Atkin - *RBC Capital Markets - Analyst*

If you could remind us of your major currency exposures versus the euro. And then in Paris, that's not a market that has been talked about much but it is one of your larger markets and if you could talk about kind of the overall environment there. And then I was curious about just the mix of new business, the incremental revenues, how much of that -- was there any notable shift in the out-coming from new logos versus existing customers?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Okay. No, we didn't talk about France. I'm not going to belabor the point. I think everybody knows that France continues to be a challenge and both from a cultural, economic situation and I'm going to let it go with that.

Josh Joshi - *Interxion Holding NV - CFO*

Foreign exchange, our biggest exposure is to sterling, Jonathan, and then to Swiss francs and then to Danish and Swedish Kroner, but less so because they are more pegged to the euro. As I said before, the UK exposure is something in the region of 10%, 15% of revenues and Swiss francs is about half of that. I hope that answers your question.

Jonathan Atkin - *RBC Capital Markets - Analyst*

Thank you. And then can you talk a little bit about what's driving the interest in Stockholm and kind of (inaudible) from the demand drivers there?

Josh Joshi - *Interxion Holding NV - CFO*

Jonathan you were cutting out, but I think that you were saying could we talk about the interest in Stockholm and the demand drivers. Did I have that right?

Jonathan Atkin - *RBC Capital Markets - Analyst*

That's correct.

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

I'd say, Jonathan, it's across the board. A different orientation in our part and a little change in our -- in implementation of our segmentation strategy, tweaking some of the people, some of the way we approach it. But it's been across the board.

Jonathan Atkin - *RBC Capital Markets - Analyst*

Thank you. And then finally if there's any additional color you could maybe provide on the third quarter versus fourth quarter seasonality in terms of the margin developments and the ARPU growth and overall kind of revenue trends within the second half?

David Ruberg - *Interxion Holding NV - Vice Chairman and CEO*

Well, I think the MRR development, I've been pretty clear on in terms of the modest growth for the remainder of the quarter -- remainder of the year per quarter. We have some seasonality in the business. As you know, in the first quarter that was when the pay rises came through, and also in the third quarter, that's the summer months. In Europe, it's for my children an extraordinarily good summer because it's been very hot, yet for data centers it gets a little bit more expensive with the cost of power and energy.

And as we -- so I would expect that to have an impact on margins, but we would expect to manage through. That's part that is factored in within our guidance. And overall our margins, we've planned, as we have done for the last six, I think seven years, to grow our adjusted EBITDA margins somewhere between 100 and 150 to 200 basis points each year and our guidance hasn't changed.

Jonathan Atkin - *RBC Capital Markets - Analyst*

Great. Thank you very much.

Operator

Thank you. I would now like to hand the conference back to you, Mr. Huseby. Please go ahead.

Jim Huseby - *Interxion Holding NV - VP, IR*

Thank you everybody for joining us on our conference call. We look forward to seeing you out on the road, and our next conference call will be in November. Thank you for joining us today.

Operator

Thank you, ladies and gentlemen. That does conclude our conference call today. Thank you for participating. You may now disconnect.
