

23 February 2009

Raffles Medical Group

Reuters: **RAFG.SI** Bloomberg: **RFMD SP** Exchange: **SES** Ticker: **RAFG**

Slowdown in private healthcare; maintain Hold

James TanResearch Analyst
(+65) 6423 5139
james-s.tan@db.com**Pressure on private healthcare and move towards public healthcare**

FY08 results highlight the slowdown in growth in the private healthcare sector, with flat QoQ revenue growth in 4Q08. The growth in private hospital admissions has slowed to 1.6% YoY in 2008 from 4.4% YoY in 2007. We believe an economic slowdown may drive discretionary medical spending into the public sector and put pressure on private healthcare. Maintain Hold.

Downturn seen in private medical spend in last two recessions

We believe the poor performance of the private medical sector during the last two recessions will likely recur in the current recession. During the Asian Financial Crisis and the dotcom bubble, private hospital admissions declined 23% YoY and 9.8% YoY, respectively. Amid the current global financial crisis, we forecast private patient admission to drop 15% YoY while public admission could increase 5% YoY in 2009. Our DB economics team forecasts GDP to contract by 4.0% in 2009.

Negative headwinds for Singapore healthcare sector

We believe Raffles Medical Group in the short term could face a slowdown in medical tourism and private medical expenditure in Singapore. We have factored in our assumptions of lower hospital utilisation rates and a 5.5% decline in patient admissions in 2009.

Our TP of S\$0.62 implies PE multiple of 11.4x for FY09E; Hold

We raise our TP from S\$0.60 to S\$0.62 based on our revised earnings forecasts and an increase in our cost of equity from 8.6% to 9.0%, with a TGR of 1.0% to factor in DB's new cost of capital. Upside risks are greater operating leverage, an accretive acquisition, and a rebound of regional economies. Downside risks are higher operating costs and a drop in the number of foreign patients. (See p. 6).

Forecasts and ratios

Year End Dec 31	2007A	2008A	2009E	2010E	2011E
Sales (SGDm)	168.7	200.7	206.5	230.9	252.5
EBITDA (SGDm)	30.6	45.3	41.9	48.0	54.3
Reported NPAT (SGDm)	35.9	31.5	28.5	32.8	37.7
Reported EPS FD(SGD)	0.07	0.06	0.05	0.06	0.07
DB EPS FD(SGD)	0.04	0.06	0.05	0.06	0.07
OLD DB EPS FD(SGD)	0.04	0.06	0.05	0.06	0.07
% Change	0.0%	4.4%	5.0%	4.4%	0.2%
DB EPS growth (%)	-	38.8	-9.5	15.4	14.7
PER (x)	31.1	18.5	13.0	11.2	9.8
EV/EBITDA (x)	20.1	10.6	6.7	5.4	4.5
DPS (net) (SGD)	0.03	0.02	0.02	0.03	0.03
Yield (net) (%)	2.6	2.2	3.2	3.6	4.2

Source: Deutsche Bank estimates, company data

Deutsche Bank AG/Hong Kong

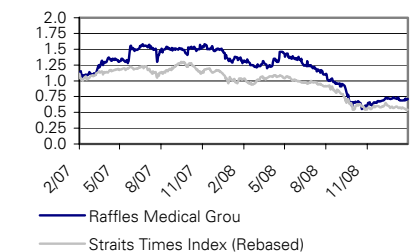
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Forecast change**Hold**

Price at 23 Feb 2009 (SGD)	0.70
Price target - 12mth (SGD)	0.62
52-week range (SGD)	1.46 - 0.55
Straits Times Index	1,595

Key changes

Price target	0.60 to 0.62	↑	3.3%
Sales (FYE)	214 to 207	↓	-3.4%
Op prof margin (FYE)	15.3 to 16.9	↑	10.0%
Net profit (FYE)	27.1 to 28.5	↑	5.0%

Price/price relative

Performance (%)	1m	3m	12m
Absolute	-3.4	15.6	-44.9
Straits Times Index	-5.4	-4.0	-47.7

Stock data

Market cap (SGDm)	369
Market cap (USDm)	240
Shares outstanding (m)	524.1
Major shareholders	Dr Loo Choon Yong (40%)
Free float (%)	50
Avg daily value traded (USDm)	0.1

Key indicators (FY1)

ROE (%)	12.4
Net debt/equity (%)	-2.7
Book value/share (SGD)	0.45
Price/book (x)	1.6
Net interest cover (x)	79.0
Operating profit margin (%)	16.9

Model updated: 23 February 2009

Running the numbers**Asia****ASEAN Singapore****Health Care****Raffles Medical Group**

Reuters: RAFG.SI

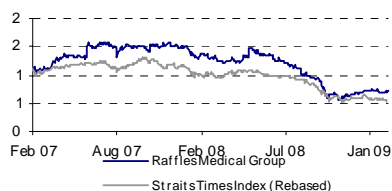
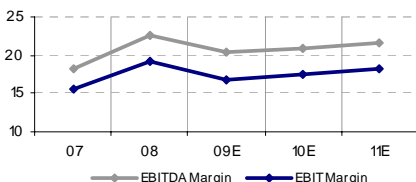
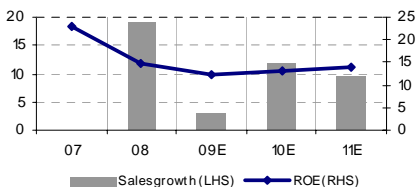
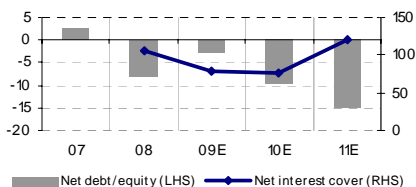
Bloomberg: RFMD SP

Hold

Price (23 Feb 09)	SGD 0.71
Target price	SGD 0.62
52-week Range	SGD 0.55 - 1.46
Market Cap (m)	SGDm 369 USDm 240

Company Profile

Raffles Medical Group is an integrated healthcare organization in Singapore. It has a 380-bed tertiary hospital in Singapore, providing its patients with a full complement of specialist and emergency services combined with advanced medical technology.

Price Performance**Margin Trends****Growth & Profitability****Solvency**

James Tan

+65 6423 5139

james-s.tan@db.com

Fiscal year end 31-Dec

Financial Summary

	2007	2008	2009E	2010E	2011E
DB EPS (SGD)	0.04	0.06	0.05	0.06	0.07
Reported EPS (SGD)	0.07	0.06	0.05	0.06	0.07
DPS (SGD)	0.03	0.02	0.02	0.03	0.03
BVPS (SGD)	0.4	0.4	0.5	0.5	0.5
Weighted average shares (m)	515	524	524	524	524
Average market cap (SGDm)	693	583	369	369	369
Enterprise value (SGDm)	614	481	279	260	243

Valuation Metrics

P/E (DB) (x)	31.1	18.5	13.0	11.2	9.8
P/E (Reported) (x)	19.3	18.5	13.0	11.2	9.8
P/BV (x)	3.87	1.63	1.56	1.43	1.31
FCF Yield (%)	5.2	5.8	0.4	8.3	8.3
Dividend Yield (%)	2.6	2.2	3.2	3.6	4.2
EV/Sales (x)	3.6	2.4	1.3	1.1	1.0
EV/EBITDA (x)	20.1	10.6	6.7	5.4	4.5
EV/EBIT (x)	23.3	12.4	8.0	6.5	5.3

Income Statement (SGDm)

Sales revenue	169	201	207	231	253
Gross profit	51	67	63	72	84
EBITDA	31	45	42	48	54
Depreciation	4	7	7	8	8
Amortisation	0	0	0	0	0
EBIT	26	39	35	40	46
Net interest income/(expense)	1	0	0	-1	0
Associates/affiliates	0	0	0	0	0
Exceptionals/extraordinaries	14	0	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0
Profit before tax	41	38	34	40	46
Income tax expense	5	7	6	7	8
Minorities	0	0	0	0	0
Other post-tax income/(expense)	0	0	0	0	0
Net profit	36	31	28	33	38
DB adjustments (including dilution)	-14	0	0	0	0
DB Net profit	22	31	28	33	38

Cash Flow (SGDm)

Cash flow from operations	40	40	8	37	37
Net Capex	-4	-6	-7	-7	-7
Free cash flow	36	34	1	31	31
Equity raised/(bought back)	69	1	0	0	0
Dividends paid	-18	-13	-13	-12	-13
Net inc/(dec) in borrowings	-60	1	0	0	0
Other investing/financing cash flows	-49	1	0	0	0
Net cash flow	-22	24	-11	19	17
Change in working capital	-23	-22	2	7	17

Balance Sheet (SGDm)

Cash and other liquid assets	20	45	33	52	69
Tangible fixed assets	151	150	150	149	147
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	85	85	85	85	85
Other assets	26	31	41	49	63
Total assets	281	310	309	334	363
Interest bearing debt	25	27	27	27	27
Other liabilities	55	62	44	48	53
Total liabilities	80	88	71	75	80
Shareholders' equity	201	222	237	259	283
Minorities	0	0	0	1	1
Total shareholders' equity	201	222	238	259	284
Net debt	6	-18	-6	-25	-43

Key Company Metrics

Sales growth (%)	nm	19.0	2.9	11.8	9.4
DB EPS growth (%)	na	38.8	-9.5	15.4	14.7
EBITDA Margin (%)	18.2	22.5	20.3	20.8	21.5
EBIT Margin (%)	15.7	19.3	16.9	17.4	18.2
Payout ratio (%)	49.5	41.1	41.0	41.0	41.0
ROE (%)	22.9	14.9	12.4	13.2	13.9
Capex/sales (%)	2.5	3.1	3.1	2.8	2.6
Capex/depreciation (x)	1.0	0.9	0.9	0.8	0.8
Net debt/equity (%)	2.7	-8.0	-2.7	-9.8	-15.1
Net interest cover (x)	nm	105.8	79.0	75.5	120.4

Source: Company data, Deutsche Bank estimates

Highlights of FY08 results

FY08 results show a slowdown in 4Q08 revenue

Figure 1: FY08 results breakdown

FYE DEC SGDm	4Q07	3Q08	4Q08	QoQ	YoY	FY07	FY08E	YoY
Sales	45.7	51.3	51.3	0.1%	12.2%	168.7	200.7	19.0%
Cost of Services	(30.4)	(35.1)	(35.1)	0.0%	15.7%	(121.4)	(140.5)	15.7%
Gross Profit	15.4	16.2	16.2	0.2%	5.4%	47.3	60.2	27.4%
Other Operating Income	(1.5)	0.1	(0.3)	nm	-83.3%	0.3	0.2	-21.3%
Lease expenses	(2.0)	(1.1)	(0.8)	-27.1%	-58.9%	(9.8)	(4.5)	-54.5%
Other Operating Expenses	(5.9)	(4.3)	(4.3)	0.0%	-26.0%	(11.4)	(17.4)	52.7%
Total operating expenses	(7.9)	(5.5)	(5.2)	-5.7%	-34.5%	(21.2)	(21.8)	3.1%
EBIT	10.6	10.2	10.8	5.3%	1.8%	26.4	38.7	46.7%
Interest Income	(1.4)	0.0	0.1	nm	nm	1.8	0.3	-85.8%
Interest Expense	(0.3)	(0.2)	(0.2)	0.0%	-48.0%	(0.4)	(0.6)	65.7%
Share of Associates	(0.7)	0.0	0.0	na	na	0.0	0.0	na
Exceptional Gains/(Losses)	0.7	0.0	0.0	na	na	13.6	0.0	na
Pretax Profit	8.8	10.1	10.8	6.7%	22.1%	41.4	38.4	-7.4%
Tax	0.7	(1.9)	(1.2)	-37.2%	nm	(5.5)	(6.7)	21.7%
Minority Interests	(0.1)	0.0	(0.1)	nm	127.9%	(0.1)	(0.1)	85.2%
Net Profit	9.4	8.2	9.4	14.6%	0.4%	35.9	31.5	-12.0%
Core net profit	8.7	8.2	9.4	14.6%	8.7%	23.4	31.5	35.0%

Source: Deutsche Bank, Company Data

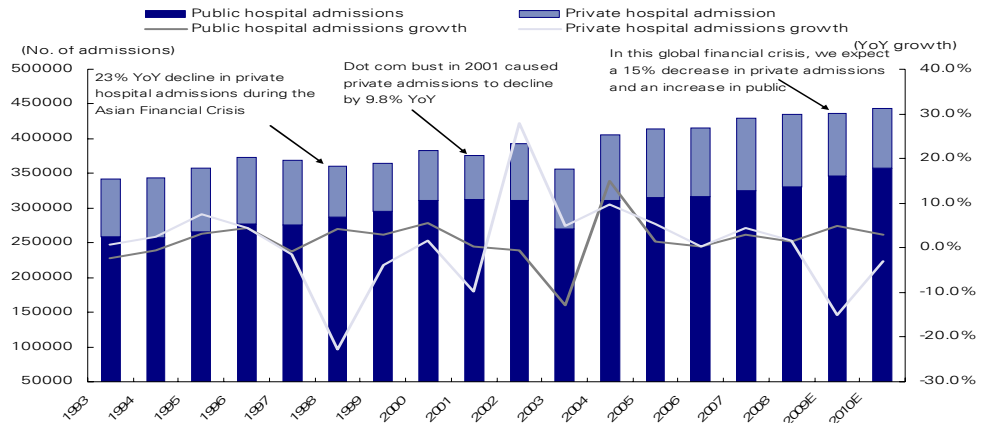
For FY08, Raffles Medical Group posted revenue growth of 19.0% YoY to S\$220.8m and core net profit growth of 35.0% YoY to S\$31.5m. The results were 5% above our expectations and consensus. Revenue for the company's Singapore hospitals division rose 21.2% YoY to S\$119.9m, while EBIT for its hospital division rose 42.3% YoY to S\$28.1m due to benefit from the full-year effect of the acquisition of the remaining 50% ownership in Raffles Hospital. This allowed the company to optimise the use of hospital and clinic space and reduce its operating expenses. Revenue from its healthcare services segment rose 15.9% YoY to S\$80.7m with EBIT increasing 17.5% YoY to S\$7.5m.

Management expects the deepening global economic slowdown to pose challenges for the company and the region, but believes that the healthcare sector may prove to be more resistant. Raffles medical and International Medical Insurers will continue to focus on cost-effective solutions and grow corporate clients. The company has cut its dividend payout ratio to 41% from 50% but maintained its 2.5 S cents dividend in FY08. Management indicated that the drop in dividend payout was to conserve cash for future acquisitions and targets. As of FY08, the company has a net cash position of S\$18.0m.

Outlook for 2009

2009 could mark the worst recession in 32 years

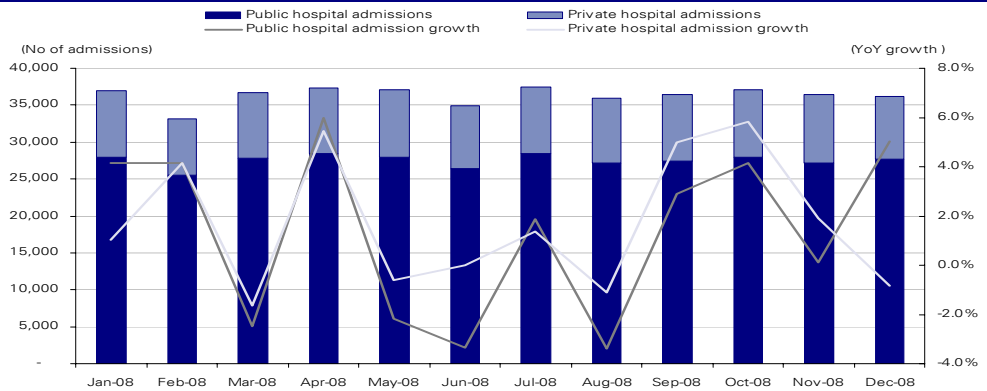
Figure 2: Singapore yearly patient admission data: 1993-2010E



Source: Deutsche Bank, Singstats, MOH

We believe the past poor performances of the private medical sector during recessions will likely resurface in the current recession. During the Asian Financial Crisis in 1997-98, private hospital admissions declined 23% YoY. The recession in 2001 also had a negative impact, with private admissions declining 9.8% YoY. We believe private patient admission may drop 15% while public admission could increase 5% YoY in 2009E, amid the global financial crisis.

Figure 3: Singapore monthly patient admission data



Source: Deutsche Bank, Singstats, MOH

We believe an economic slowdown may drive discretionary medical spending into the public sector and put pressure on private healthcare's market share. On year-over-year basis, private admissions growth slowed from 4.4% in 2007 to 1.6% in 2008. Private hospital admissions in December 2008 also fell 0.8% YoY, while public admissions increased 5.0% YoY.

Visitor arrival to Singapore declined 6.9% YoY in December 2008 which was preceded by declines of 7.4% and 9.1% in October 2008 and November 2008, respectively. For the first time since SARS in 2003, the Asian Financial Crisis in 1998 and the dotcom bubble of 2001, annual visitor arrivals declined by 2% YoY in 2008.

Valuation

We have used a discounted cash flow valuation methodology to value Raffles Medical Group as the cash flow from the company's operations is relatively stable. Using DB's new cost of capital assumptions, we have lowered the risk-free rate from 3.1% to 2.6%, raised the equity risk premium from 4.0% to 4.8% and maintained beta of 1.3 to derive our cost of equity of 9.0% (previously 8.6%). We use a cost of equity of 9.0% as the discounting factor because the company is in a net cash position. We are using a terminal growth rate of 1.0% (discounted from Singapore's long-term inflation rate of 3%). We have raised our earnings for Raffles Medical Group by 5.0% and 4.4% for FY09-10E to S\$28.5m and S\$32.8m, respectively. We have raised our target price from S\$0.60 to S\$0.62 based on our revised earnings forecasts and the increase in our discount rate. Our target price implies PE multiples of 11.4x for FY09 and 9.8x for FY10E.

Risks

We believe the key upside risks to our thesis on Raffles Medical Group (RMG) are:

Achieving greater operating leverage

Raffles Medical Group recently acquired the remaining 50% stake in Raffles Hospital, and this could allow the company to expand its services and redevelop the hospital, which would lead to better operating efficiency and upside risks to our earnings estimates.

The ability to attract and grow its foreign patient base during an economic slowdown

If RMG is able to increase its foreign patient base amid the economic slowdown, it could allow the company to achieve a higher revenue growth for its hospital division and could provide upside risks to our earnings estimates.

Making an accretive overseas acquisition to expand its operations

The company is looking to make an overseas acquisition of a hospital or medical centre. This could boost the company's profile as a regional healthcare player and provide upside risks to our earnings estimates if the acquisition turns out to be accretive.

We believe the key downside risks to our thesis on Raffles Medical Group are:

Higher operating costs could affect the company's profitability

Due to inflationary pressures and the lack of medical professionals, operating costs could rise for RMG.

Drop in foreign patient admissions

The current economic slowdown could lead to a decline in medical tourism and RMG could see a drop in foreign patient admissions, which makes up approximately 30% of in-patients at its hospital. This could be a downside risk to our earnings estimates.

Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Raffles Medical Group	RAFG.SI	0.70 (SGD) 23 Feb 09	6

*Prices are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank and subject companies.

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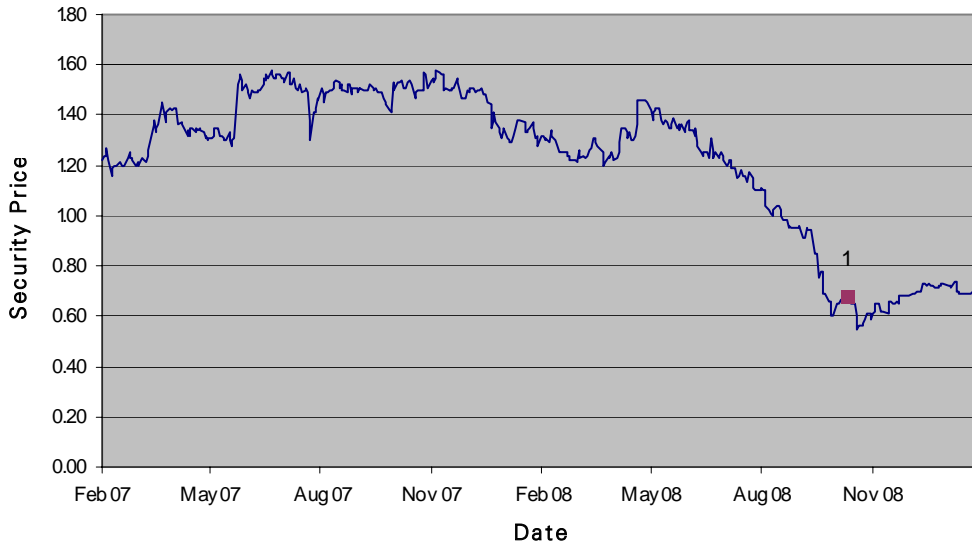
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Historical recommendations and target price: Raffles Medical Group (RAFG.SI)

(as of 2/23/2009)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

*New Recommendation Structure as of September 9, 2002

1. 5/11/2008: Hold, Target Price Change SGD0.60

Equity rating key **Equity rating dispersion and banking relationships**

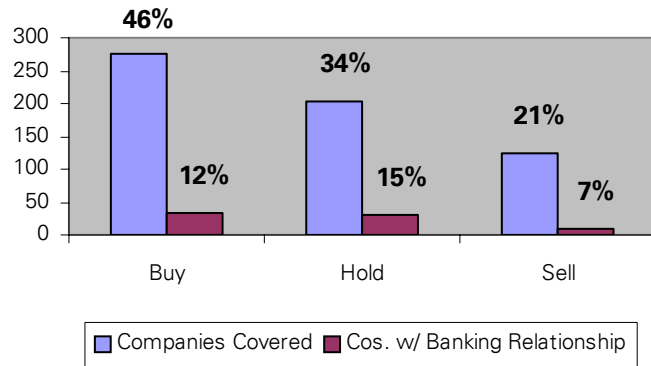
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Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

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Asia-Pacific Universe

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Asia-Pacific locations

Deutsche Bank AG

Deutsche Bank Place
Level 16
Corner of Hunter & Phillip Streets
Sydney, NSW 2000
Australia
Tel: (61) 2 8258 1234

Deutsche Bank AG

Level 55
Cheung Kong Center
2 Queen's Road Central
Hong Kong
tel: (852) 2203 8888

Deutsche Equities India Pte Ltd

DB House, Ground Floor
Hazarimal Somani Marg
Fort, Mumbai 400 001
India
Tel: (91) 22 5658 4600

Deutsche Securities Inc.

2-11-1 Nagatacho
Sanno Park Tower
Chiyoda-ku, Tokyo 100-6171
Japan
Tel: (81) 3 5156 6701

Deutsche Bank (Malaysia) Berhad

Level 18-20
Menara IMC
8 Jalan Sultan Ismail
Kuala Lumpur 50250
Malaysia
Tel: (60) 3 2053 6760

In association with Deutsche Regis Partners, Inc.

Level 23, Tower One
Ayala Triangle, Ayala Avenue
Makati City, Philippines
Tel: (63) 2 894 6600

Deutsche Securities Korea Co.

17th Floor, YoungPoong Bldg.,
33 SeoRin-Dong,
Chongro-Ku, Seoul (110-752)
Republic of Korea
Tel: (82) 2 316 8888

Deutsche Bank AG Singapore

One Raffles Quay
South Tower
Singapore 048583
Tel: (65) 6423 8001

Deutsche Securities Asia Ltd

Taiwan Branch
Level 6
296 Jen-Ai Road, Sec 4
Taipei 106
Taiwan
Tel: (886) 2 2192 2888

In association with TISCO Securities Co., Ltd

TISCO Tower
48/8 North Sathorn Road
Bangkok 10500
Thailand
Tel: (66) 2 633 6470

In association with PT Deutsche Verdhana Indonesia

Deutsche Bank Building,
6th Floor, Jl. Imam Bonjol No.80,
Central Jakarta,
Indonesia
Tel: (62 21) 318 9541

International locations

Deutsche Bank Securities Inc.

60 Wall Street
New York, NY 10005
United States of America
Tel: (1) 212 250 2500

Deutsche Bank AG London

1 Great Winchester Street
London EC2N 2EQ
United Kingdom
Tel: (44) 20 7545 8000

Deutsche Bank AG

Große Gallusstraße 10-14
60272 Frankfurt am Main
Germany
Tel: (49) 69 910 00

Deutsche Bank AG

Deutsche Bank Place
Level 16
Corner of Hunter & Phillip Streets
Sydney, NSW 2000
Australia
Tel: (61) 2 8258 1234

Deutsche Bank AG

Level 55
Cheung Kong Center
2 Queen's Road Central
Hong Kong
Tel: (852) 2203 8888

Deutsche Securities Inc.

2-11-1 Nagatacho
Sanno Park Tower
Chiyoda-ku, Tokyo 100-6171
Japan
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