

Raffles Medical Group

Operating efficiencies add to defensive qualities

OUTPERFORM	Upgraded
S\$0.71	Target: S\$0.88
Mkt.Cap: S\$365m/US\$239m	
Hospitals	

RFMD SP / RAFG.SI

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- **Above Street and our estimates.** 4Q08 revenue grew 12.4% yoy to S\$51m, fuelled by Hospital Services (+20% yoy). Stripping out one-off fair-value gains from the disposal of Raffles Hospital in FY07, FY08 core profit was up 35% yoy to S\$31.5m, or 16.7% above our estimate and 8% above consensus. The main differences were higher operating margins and lower interest payment.
- **Margins and balance sheet improved.** 4Q08 EBITDA margins expanded 1.1% pts yoy (1.3% pts qoq) to 24.5% despite higher staff costs, suggesting still-strong operating efficiencies. What contributed to the reduced interest payment was prudent debt management, which brought down borrowing and turned the balance sheet into a net cash position of S\$17.9m in FY08 (net debt of S\$5.5m in FY07). Operating cash flow remained robust and unchanged from a year ago, at S\$40m.
- **Broke even in insurance management business.** The group has also been seeing healthy patient load increases in Jan-Feb 09, while average occupancy rates are hovering at 50-60% (45-50% in FY07). RFMD will, moreover, enjoy a deductible tax incentive of S\$2.5m-3m from the government's Jobs Credit scheme in FY09.
- **Operational efficiency will forge defensive qualities.** RFMD has not elaborated on its expansion strategy or provided sufficient figures for a full appreciation of its good set of results. As such, we believe its ability to bolster margins has not been well appreciated. Higher non-bed-related fee income could come from: 1) recently initiated customer segmentation to derive higher revenue from primary healthcare services; and 2) a channelling of insurance customers to Raffles Hospital, strengthening margins in Hospital Services. We have revised our hospital growth assumptions to 10-15% for FY09-10 (from 8-12%) to capture higher non-bed medical income.
- **Estimates raised; upgrade to Outperform from Underperform; target price raised to S\$0.88 (from S\$0.64).** Our FY09-10 estimates have been raised by 18.3-15.5%. Our target price rises from S\$0.64 to S\$0.88, in line with our higher CY09 P/E target multiple of 13x [(1 - growth/ROE)/(cost of equity - growth)] from 11.9x. We also introduce FY11 forecasts. On the back of our renewed confidence in the group, we upgrade the stock from Underperform to Outperform.

Results comparison

FYE Dec (S\$ m)	4QFY08	4QFY07	yoy % chg	qoq % chg	4QFY08 Cum	4QFY07 Cum	yoy % chg	Prev. FY08F	Comments
Revenue	51.4	45.7	12.4	0.2	200.8	168.7	19.0	197.3	In line, increased Hospital Services
Operating costs	(38.8)	(35.1)	10.8	(1.5)	(155.4)	(136.9)	13.5	(157.3)	In line, costs well contained
EBITDA	12.6	10.7	17.7	5.9	45.4	31.7	42.9	40.0	Above; higher portion of depreciation
EBITDA margin (%)	24.5	23.4	4.7	5.7	22.6	18.8	20.1	20.3	Operating efficiency drove margin improvements
Depn & amort.	(1.8)	(1.6)	12.7	3.2	(6.7)	(4.3)	56.2	(6.3)	Depreciation on PPE climbed 57% yoy
EBIT	10.8	9.1	18.5	6.4	38.7	40.0	(3.2)	33.7	Above
Interest expense	(0.2)	(0.3)	(48.7)	(1.3)	(0.6)	(0.4)	65.7	(0.9)	Below; loan repayment
Interest & invt inc	0.1	(0.0)	(415.4)	49.1	0.3	1.8	(85.8)	0.3	Lowered yoy with conservative investment
Associates' contrib	-	(0.0)	(100.0)	-	-	13.6	(100.0)	-	No more contribution from CRPPL
Exceptionals	-	-	-	-	-	-	-	-	
Pretax profit	10.8	8.8	22.1	6.7	38.4	41.4	(7.4)	33.1	Above; FY07 skewed by one-off gain
Tax	(1.2)	0.7	(277.7)	(37.2)	(6.7)	(5.5)	21.7	(5.9)	In line with higher pretax
Tax rate (%)	10.9	(7.5)	-	-	17.4	13.3	-	18.0	Tax rate in line
Minority interests	(0.0)	(0.0)	136.8	73.1	(0.1)	(0.1)	85.2	(0.1)	
Net profit	9.5	9.4	1.0	16.5	31.5	35.9	(12.0)	27.0	FY07 profit included S\$12.5m of divestment
EPS (cts)	1.8	1.8	0.7	16.6	6.1	7.0	(12.3)	5.2	
Core net profit	9.5	9.4	1.0	16.5	31.5	23.4	35.0	27.0	Core profit 16.7% above our FY08 estimate
Core EPS (cts)	1.8	1.8	0.7	16.6	6.1	4.5	34.7	5.2	

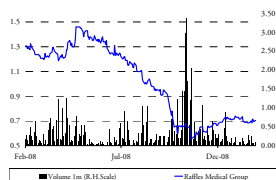
Source: Company, CIMB-GK Research

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Financial summary

FYE Dec	2007	2008	2009F	2010F	2011F
Revenue (S\$ m)	168.7	200.8	222.8	255.4	292.7
EBITDA (S\$ m)	31.7	45.4	46.6	53.5	60.7
EBITDA margins (%)	18.8%	22.6%	20.9%	21.0%	20.7%
Pretax profit Ex EI (S\$ m)	28.9	38.4	39.8	47.0	54.4
Core profit (S\$ m)	23.4	31.5	35.0	38.4	44.5
EPS (S cts)	4.5	6.1	6.8	7.4	8.6
EPS growth (%)	46.5%	36.7%	10.9%	9.8%	15.9%
P/E (x)	15.8	11.6	10.4	9.5	8.2
Core EPS (S cts)	6.4	6.1	6.8	7.4	8.6
Core EPS growth (%)	110.0%	(4.7%)	10.9%	9.8%	15.9%
Core P/E (x)	11.0	11.6	10.4	9.5	8.2
Gross DPS (S cts)	2.5	2.5	2.5	2.5	2.5
Dividend yield (%)	3.5%	3.5%	3.5%	3.5%	3.5%
P/BV (x)	1.8	1.6	1.5	1.4	1.2
ROE (%)	14.9%	14.9%	15.0%	15.0%	15.6%
Net gearing (%)	2.7%	N/A	N/A	N/A	N/A
Net cash per share (S\$)	N/A	0.03	0.06	0.13	0.20
P/FCFE (x)	(1.6)	10.1	18.7	8.1	7.8
EV/EBITDA (x)	11.8	7.6	7.1	5.5	4.3
% change in EPS estimates			18.3%	15.5%	N/A
CIMB/Consensus (x)			1.09	1.05	N/A

Price chart



Source: Bloomberg

Source: Company, CIMB-GK Research, Bloomberg

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OUTPERFORM: The stock's total return is expected to exceed a relevant benchmark's total return by 5% or more over the next 12 months.

NEUTRAL: The stock's total return is expected to be within +/-5% of a relevant benchmark's total return.

UNDERPERFORM: The stock's total return is expected to be below a relevant benchmark's total return by 5% or more over the next 12 months.

TRADING BUY: The stock's total return is expected to exceed a relevant benchmark's total return by 5% or more over the next 3 months.

TRADING SELL: The stock's total return is expected to be below a relevant benchmark's total return by 5% or more over the next 3 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT: The industry, as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 12 months.

NEUTRAL: The industry, as defined by the analyst's coverage universe, is expected to perform in line with the relevant primary market index over the next 12 months.

UNDERWEIGHT: The industry, as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 12 months.

TRADING BUY: The industry, as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 3 months.

TRADING SELL: The industry, as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 3 months.

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STOCK RECOMMENDATIONS

OUTPERFORM: Expected positive total returns of 15% or more over the next 12 months.

NEUTRAL: Expected total returns of between -15% and +15% over the next 12 months.

UNDERPERFORM: Expected negative total returns of 15% or more over the next 12 months.

TRADING BUY: Expected positive total returns of 15% or more over the next 3 months.

TRADING SELL: Expected negative total returns of 15% or more over the next 3 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT: The industry, as defined by the analyst's coverage universe, has a high number of stocks that are expected to have total returns of +15% or better over the next 12 months.

NEUTRAL: The industry, as defined by the analyst's coverage universe, has either (i) an equal number of stocks that are expected to have total returns of +15% (or better) or -15% (or worse), or (ii) stocks that are predominantly expected to have total returns that will range from +15% to -15%; both over the next 12 months.

UNDERWEIGHT: The industry, as defined by the analyst's coverage universe, has a high number of stocks that are expected to have total returns of -15% or worse over the next 12 months.

TRADING BUY: The industry, as defined by the analyst's coverage universe, has a high number of stocks that are expected to have total returns of +15% or better over the next 3 months.

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