

Raffles Medical Group

STOCK RECOMMENDATION

OUTPERFORM

SECTOR

Healthcare Services

12 MONTH RANGE

S\$1.61 – 1.20

NEXT RESULTS DUE

30 July 2008 (H1)

LAST RESULTS

29 April 2008 (Q1)

ANALYST

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We maintain our OUTPERFORM recommendation on Raffles Medical Group (Raffles). Our SOTP fair value estimate of S\$1.89 per share implies upside of 46%. Raffles is our top pick in the sector.

Emerging player in the medical travel segment. With occupancy rates at its flagship hospital running at only c. 50% currently, Raffles is more comfortably positioned than its peers to absorb the rising influx of medical travellers into the region. International patients now account for 35% of total patient loads at its flagship hospital.

Key beneficiary of means testing. The implementation of means testing in January 2009 should lead to a migration of higher income patients from the public healthcare system to private hospitals like Raffles. Apart from offering one of the most competitive rates in the private sector, Raffles hospital is one of the few in Singapore to offer an entry-level six-bed ward option for potential up-graders. Against a backdrop of tight (and inelastic) bed supply within the private sector, we also expect Raffles to benefit from overspill demand from capacity-constrained players like Parkway and Thomson Medical.

High revenue intensity levels underpinned by sub-specialization capabilities. In our view, the recent purchase of Capitaland's 50% stake in Raffles Hospital was transacted at a bargain (S\$108m or S\$432 psf ppr). The purchase has reduced rental expenses and enabled Raffles to reconfigure and redevelop specialist centres within the building to expand its capabilities in several subspecialties. Full ownership of the hospital has also provided management with the flexibility of replicating Parkway's hospital REIT strategy over the longer term.

Resilience and growth. At current levels, the shares are well supported by a decent dividend yield and a low net gearing position. Downside risks to revenues are limited as a portion is derived from long-term corporate contracts.

PRICE

S\$1.29

REUTERS CODE

RAFG.SI

BLOOMBERG CODE

RFMD SP

MARKET CAPITALISATION

S\$775m (US\$539m)

PRINCIPAL LISTING

SGX

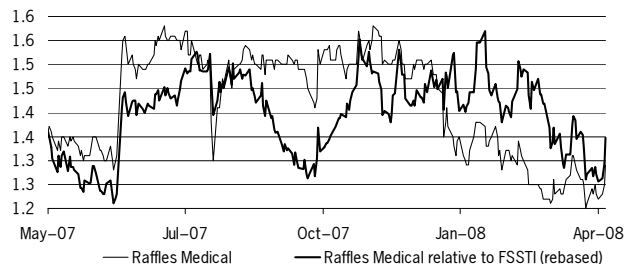
CHANGE IN STOCK RECOMMENDATION

No

CHANGE IN EPS ESTIMATES

No

Share price performance



Source: Bloomberg

Share price (%)	-1 mth	-3 mth	-12 mth	
Ordinary shares	+4	0	-5	
Relative to sector	-	-	-	
Relative to FSSTI	-1	-5	-1	
Average daily volume shares				423,107
FSSTI				3,147
Year end: December	2007	2008E	2009E	2010E
Turnover (S\$m)	168.7	203.9	245.2	292.5
Earnings – reported (S\$m)	35.9	27.9	36.4	46.8
Earnings – excl exceptionals (S\$m)	23.4	27.9	36.4	46.8
EBITDA (S\$m)	32.5	46.6	57.7	71.2
Tax (%)	13.3	21.3	21.3	21.3
EPS – excl exceptionals (S cents)	4.8	5.4	7.0	8.8
Growth (%)	+38.8	+12.1	+28.6	+26.8
DPS-net (S cents)	2.3	4.4	5.6	7.1
Growth (%)	-36.3	+91.7	+27.7	+25.9
Div payout-net (%)	35.8	90.0	90.0	90.0
EV/EBITDA (x)	20.5	14.3	11.6	9.4
PER – excl exceptionals (x)	26.7	23.8	18.5	14.6
Yield – Net (%)	1.8	3.4	4.4	5.5
PBR (x)	3.1	3.3	3.3	3.2
EBIT margin (%)	16.7	18.7	19.9	21.2
EV/sales (x)	4.0	3.3	2.7	2.3
Market cap:sales (x)	3.9	3.2	2.7	2.3
NAV per share (S\$)	0.42	0.40	0.40	0.40
ROE (%)	14.9	13.8	17.7	22.3
ROCE (%)	16.5	16.7	21.2	26.4
Interest cover (x)	75.0	14.8	19.0	24.2
Net debt/equity (%)	2.4	2.9	Cash	Cash

Source: Company, Cazenove

Key points

Background

- Established in 1976 by two doctors as an independent two-clinic practice, Raffles Medical Group (RMG) is one of the largest and most prominent healthcare service providers in Singapore. Listed on the SGX since April 1997, it is now the second largest healthcare service provider listed on the local bourse.
- **Shareholders.** Co-founder and executive chairman Dr Loo Choon Yong, also holds several government positions. He is a nominated Member of Parliament, Singapore's Ambassador to Italy and chairs the Healthcare Services Working Group, a group tasked by the government to review and recommend strategies to enhance Singapore's competitiveness as a medical hub. Dr Loo owns a 50.1% stake in the company. Other notable shareholders include Temasek Holdings and Qatar Investment Authority, who each hold a 4.9% stake.
- **Clinic network.** RMG operates the largest primary healthcare network in Singapore, with a total of 65 ambulatory medical centres and general practitioner (GP) clinics under its umbrella. RMG also operates four medical centres in Hong Kong and is the appointed exclusive clinic operator for the existing airports in Singapore and Hong Kong. The company is also one of only two multi-disciplinary tertiary private hospital operators in Singapore. The target is to add five new clinics every year.
- **Flagship hospital.** In March 2001, RMG transformed itself from a pure outpatient facilities operator into an integrated healthcare group with the opening of its flagship hospital, *Raffles Hospital*. Located within the city centre, the hospital is a 13-storey hospital with a total floor area of more than 46,000 sq m. It is one of only four multi-disciplinary private tertiary hospitals in Singapore. The hospital is licensed for 380 beds, but operational bed capacity stands at only 200, suggesting that there is ample scope for further capacity expansion.
- Current operational bed utilisation rate stands at 50%, one of the lowest amongst its domestic peers. With most private healthcare providers struggling to cope with space / bed capacity constraints, we expect RMG to be in a strong position to absorb surging patient volumes at whilst raising prices.
- **Group practice model.** *Raffles Hospital* is operated under a group practice model, whereby most doctors and medical specialists are salaried employees. On the other hand, most of RMG's private hospital-based competitors, including Parkway rely on referrals from a network of individual doctors / specialists who run their own independent clinics i.e. sole proprietors. On this basis, RMG is a more integrated healthcare provider relative to most of its peers.
 - RMG's group practice model is a relatively new model to be employed in Singapore / Malaysia, but it is similar to that used by top US medical institutions in the world. Examples include Mayo Clinic, Cleveland Clinic, Memorial Sloan Kettering and Kaiser Permanente.
 - Operationally, the model allows RMG to leverage on the expertise of its team of doctors and provide a more integrated / coordinated experience to its patients.
 - Financially, the model allows RMG to recognise consultation fees as part of its revenue stream. Hence, for every patient visit, RMG is able to capture a larger portion of the total case bill. On the flip side, the model exposes the company to staff cost inflation and recruitment issues.
- **Doctor network.** RMG's network of doctors consists of 170 full-time resident doctors who are employed by the group. The company complements this exclusive network through affiliations with 300 visiting consultants and 20 other doctors who operate at the hospital during certain periods of the year.
- **Customer base.** RMG's patient base comprises of more than 1m individuals, including both self-paying patients and employees from 5,500 different corporate clients. Its corporate clients include both government bodies as well as major MNCs with operations in Singapore. In

December 2006, RMG's healthcare contract with the Ministry of Home Affairs was renewed for an 8-year period, to include GP and dental services, specialist outpatient consultations and psychiatric rehabilitation services.

Q1 2008 results

Raffles Medical (Raffles) reported a strong set of Q1 2008 results on 29 April 2008, posting record revenues of S\$47.4m for the period.

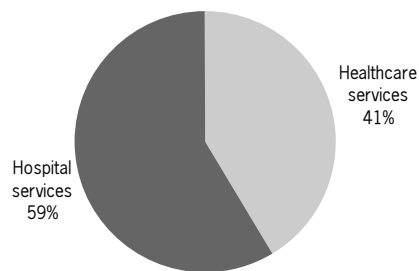
Corresponding net profit of S\$6.1m (+48% YoY) puts the company firmly in place to meet or exceed our full year net profit forecast of S\$28m. Note that Q1 is a seasonally weaker quarter.

Growth was broad-based with both clinic and hospital operations contributing. Hospital operations were robust (revenue +31% YoY), underpinned by increased patient loads and new medical specialities offered during the quarter. Clinic operations (revenue +17% YoY) also grew strongly and this was attributed to a larger corporate and self-pay patient base.

As at April 2008, Raffles Hospital had 200 operational beds with occupancy ranging from 40–60%. Raffles Hospital is licensed for a maximum 380 beds.

Operational review

Fig 1 Revenue split by segment FY2007



Source: Company, Cazenove

Fig 2 EBIT split by segment FY2007

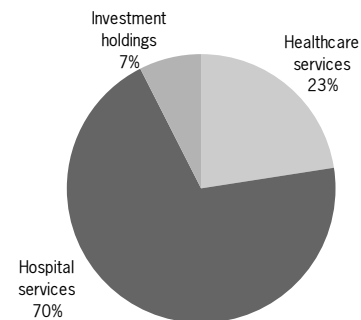
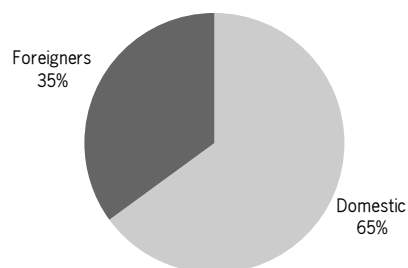


Fig 3 Revenue split by geography FY2007



Source: Company, Cazenove

Fig 4 EBIT margins by segment FY2007

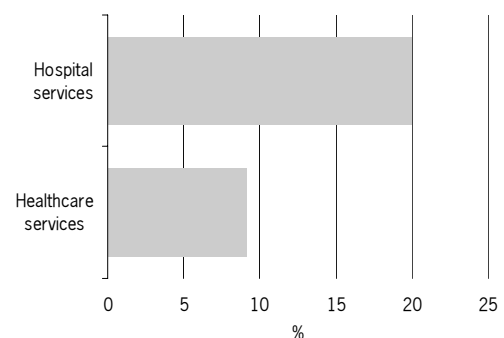
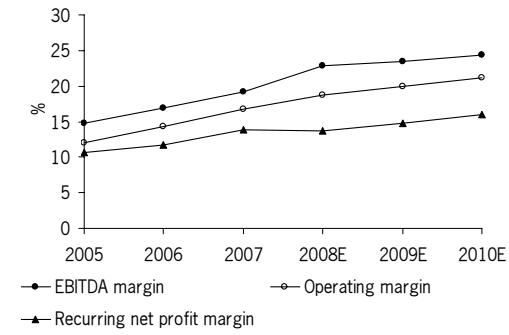
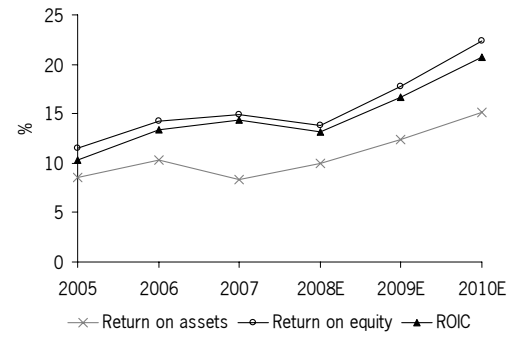


Fig 5 Normalised margin trend



Source: Company, Cazenove

Fig 6 Normalised returns



Raffles Medical Group

Profit and loss accounts

Year end: December	2006	2007	2008E	2009E	2010E
Sales (S\$m)	134.2	168.7	203.9	245.2	292.5
EBIT (S\$m)	19.2	28.2	38.1	48.9	62.1
EBITDA (S\$m)	22.6	32.5	46.6	57.7	71.2
Finance costs (S\$m)	-0.1	-0.4	-2.6	-2.6	-2.6
Share of JV profits (S\$m)	0.9	13.6	0.0	0.0	0.0
Exceptionals – revaluation gain on hospital (S\$m)	0.0	12.5	0.0	0.0	0.0
PBT (S\$m)	20.0	41.4	35.5	46.3	59.5
Effective tax rate (%)	21.3	13.3	21.3	21.3	21.3
Minority interest (S\$m)	-0.1	-0.1	-0.1	-0.1	-0.1
Earnings – reported (S\$m)	15.7	35.9	27.9	36.4	46.8
EPS (S\$)	0.035	0.074	0.054	0.070	0.088
EPS – excl exceptionals (S\$)	0.035	0.048	0.054	0.070	0.088
DPS –net (S\$)	0.04	0.02	0.04	0.06	0.07
Interest cover (x)	176.2	75.0	14.8	19.0	24.2
Dividend cover (x)	1.0	3.2	1.2	1.2	1.2
Sales growth (%)	+18.9	+25.6	+20.9	+20.3	+19.3
EBIT growth (%)	+42.3	+46.9	+35.1	+28.3	+27.0
EPS excl exceptionals growth (%)	+28.4	+38.8	+12.1	+28.6	+26.8
DPS–net growth (%)	+43.1	-36.3	+91.7	+27.7	+25.9

Source: Company, Cazenove

Cash flow statements

Year end: December	2006	2007	2008E	2009E	2010E
	S\$m	S\$m	S\$m	S\$m	S\$m
EBITDA	22.6	32.5	46.6	57.7	71.2
Working capital	0.7	13.3	-10.0	2.8	3.2
Other	-3.7	-5.7	-10.2	-12.5	-15.3
Operating cash flow	19.7	40.1	26.4	48.0	59.1
Capex	-2.3	-68.3	-2.4	-2.9	-3.5
Disposals / (acquisitions)	0.0	0.0	0.0	0.0	0.0
Investments/Other Investing	0.4	15.5	0.0	0.0	0.0
Investing cash flow	-1.9	-52.8	-2.4	-2.9	-3.5
Dividends paid	-15.5	-17.8	-25.1	-32.8	-42.1
Net borrowings	0.0	-60.3	0.0	0.0	0.0
Equity funding	4.8	69.0	0.0	0.0	0.0
Other financing	0.0	-0.1	0.0	0.0	0.0
Financing cash flow	-10.7	-9.2	-25.1	-32.8	-42.1
Net change in cash/ST investment	7.1	-22.0	-1.2	12.3	13.5

Source: Company, Cazenove

Management

Executive Chairman	Dr Loo Choon Yong
Medical Director, Raffles Clinics	Dr Wilson Wong
Medical Director, Raffles Hospital	Prof Walter Tan
Group Financial Controller	Mrs Kimmy Goh

Shareholder information

Dr Loo Choon Yong	49.9
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Market information

Estimated free float %	49.5
Main listing(s)	Singapore
Average daily volume (3 months)	314,238

Financial calendar

Financial year end	December
Quarterly accounts	Yes
Reports & accounts	March
AGM	April

Source: Company, Bloomberg

Balance sheets

Year end: December	2006	2007	2008E	2009E	2010E
	S\$m	S\$m	S\$m	S\$m	S\$m
FAs – tangible	20.2	235.2	229.2	223.5	217.9
Jointly–controlled entity	54.0	0.0	0.0	0.0	0.0
Other LT Assets	1.3	1.8	1.8	1.8	1.8
Total LT Assets	75.5	237.0	231.0	225.2	219.7
Inventories	3.4	3.8	5.0	6.1	7.2
Receivables	16.8	20.2	25.5	30.6	36.5
Cash & equivalents	56.2	20.4	19.3	31.5	45.0
Other current assets	0.0	0.0	0.0	0.0	0.0
Total current assets	76.4	44.5	49.8	68.2	88.8
Total assets	151.8	281.5	280.8	293.4	308.4
Payables	30.0	47.7	44.2	53.1	63.4
Borrowings	2.0	25.3	25.3	25.3	25.3
Other liabilities	6.7	7.5	7.5	7.5	7.5
Minority interest	0.3	0.2	0.3	0.3	0.4
Shareholders' funds	112.9	200.8	203.6	207.2	211.9
Capital employed	115.1	226.3	229.1	232.8	237.6

Source: Company, Cazenove

Key ratios

Year end: December	2006	2007	2008E	2009E	2010E
EBITDA margin (%)	16.9	19.3	22.8	23.5	24.4
EBIT margin (%)	14.3	16.7	18.7	19.9	21.2
Net margin (%)	11.7	21.3	13.7	14.8	16.0
Op cash/EBIT (x)	1.0	1.4	0.7	1.0	1.0
Deprn/capex (x)	1.5	0.1	3.4	3.0	2.6
Quick ratio (x)	1.9	0.5	0.6	0.7	0.9
ROE (%)	14.3	14.9	13.8	17.7	22.3
ROCE (%)	17.1	16.5	16.7	21.2	26.4
Net debt/equity (%)	Cash	2.4	2.9	Cash	Cash
Working cap/sales (%)	15.0	14.3	15.0	15.0	15.0
Receivables days	45	45	45	45	45
Inventories turnover (x)	39.2	44.3	40.4	40.4	40.4
Asset turnover (x)	0.9	0.6	0.7	0.8	0.9
EV/sales (x)	5.0	4.0	3.3	2.7	2.3
PER – reported earnings (x)	37.0	17.4	23.8	18.5	14.6
PER – earnings excl exceptionals (x)	37.0	26.7	23.8	18.5	14.6
EV/EBIT (x)	34.7	23.7	17.5	13.6	10.7

Source: Company, Cazenove

APPENDIX

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Desmond Lee.

RESEARCH RECOMMENDATIONS

STOCK RECOMMENDATION DEFINITIONS

OUTPERFORM – the total return on the security is expected to outperform the relevant market index by 5% or more over the next six months.

IN-LINE – the total return on the security is not expected to outperform or underperform the relevant market index by 5% or more over the next six months.

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RECOMMENDATION HISTORY

12 months recommendation changes for Parkway Holdings Ltd;
28-Nov-2007 OUTPERFORM

12 months recommendation changes for Raffles Medical Group Ltd;
28-Nov-2007 OUTPERFORM

12 months recommendation changes for Bumrungrad Hospital PCL;
No changes in recommendation over the last 12 months.

12 months recommendation changes for Bangkok Dusit Medical Services PCL;

No changes in recommendation over the last 12 months.

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