



# BUY

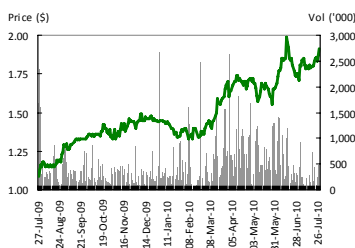
## 2Q10 Results

### Analyst

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**Price**           **\$1.87**  
**Target**         **\$2.24**  
**ST Index**       **2,966.99**

### Historical Chart



Performance	1m	3m	6m
Absolute (%)	18.9	45.6	62.1
Relative (%)	13.4	43.3	49.8

### Stock Information

Ticker code	RAFG.SI RFMD.SP
Market cap (US\$m)	720.6
52-week high (S\$)	1.99
52-week low (S\$)	1.06
Shares issued (m)	524.0
6m avg d.vol (US\$m)	0.7
Free float (%)	55.7
Major shareholder (%)	
Dr Loo Choon Yong - Chairman	(40.0)

### Key Indicators

ROE (%)	15.7
Net gearing (%)	Net Cash
NTA (S\$)	0.51
Interest cover (x)	84.2

# Raffles Medical Group

## Long-term growth secured

### What's New

- Raffles Medical Group (RMG) announced a healthy set of results for 2Q10 with growth all round. Far more interesting was the accompanying announcement that the group will be adding about 30% space to Raffles Hospital within 24 months. This development, coupled with the concluding saga at Parkway Holdings, could spark renewed interest in RMG, in our view.

### Our View

- Second-quarter revenue increased by 8.7% yoy to \$58.6m, pushing net profit up by 20.3% yoy to \$10.6m. Hospital Services and Healthcare Services (clinics) grew by 11.2% yoy and 3.7% yoy, respectively. RMG announced its entry into China via a management agreement for a 13,000-sq-ft medical centre in Shanghai.
- The group is embarking on the expansion of Raffles Hospital to increase its gross floor area by about 30% to 410,283 sq ft over the next 18-24 months. We estimate the total cost to be \$80-100m, which could be easily funded by the group's internal cash. To us, the move is a very clear sign that management is confident of growth.
- The concluding saga at Parkway Holdings highlights the value of healthcare groups with entrenched market positions, which we believe RMG counts as one. The latest offer price for Parkway at \$3.95 per share represents an estimated 31x FY10F core earnings and 3.8x P/BV, significantly higher than RMG's current valuations.

### Action & Recommendation

RMG's 1H10 net profit currently makes up 45% of our full-year estimate. We keep our forecasts largely unchanged for now but make adjustments to account for the capex for hospital expansion. We reiterate our BUY recommendation and adjust our DCF-based target price to \$2.24 on improved long-term growth outlook.

Year End Dec	2008	2009	2010F	2011F	2012F
Sales (S\$ m)	200.8	218.6	237.7	261.0	284.1
Pre-tax (S\$ m)	38.4	45.0	52.4	58.9	67.2
Net profit (S\$ m)	31.5	37.9	43.4	48.8	55.7
EPS (cts)	6.1	7.3	8.4	9.4	10.7
EPS growth (%)	(12.4)	19.9	14.6	12.5	14.1
PER (x)	31.7	26.4	23.0	20.5	18.0
EV/EBITDA (x)	20.8	17.5	15.3	13.7	12.0
Yield (%)	1.3	1.6	1.6	1.6	1.6

**SEE APPENDIX I FOR IMPORTANT DISCLOSURES AND ANALYST CERTIFICATIONS**

### Healthy results for 2Q10

RMG's 2Q10 revenue increased by 8.7% yoy to \$58.6m, pushing net profit up by 20.3% yoy to \$10.6m. Hospital Services and Healthcare Services (clinics) grew by 11.2% yoy and 3.7% yoy, respectively. The revenue growth so far this year has slightly fallen short of RMG's usual double-digit increase, but we are not unduly concerned. Management attributes this to the slower pace of recovery of the regional economies, such as Indonesia, which are important contributors to its foreign patient load.

During the quarter, RMG opened a urology/nephrology centre as well as a new clinic at One Marina Boulevard. The organic growth combined with the solid 2Q results prompted management to maintain interim dividend payout at 1 cent. We expect it will uphold its final-year dividend of 2 cents.

**Figure 1: 1H10 results**

YE Dec (\$m)	1H09	1H10	yoy growth
<b>Sales</b>	<b>104.9</b>	<b>114.8</b>	<b>9.4%</b>
Other operating income	0.1	0.3	283.5%
Inventories & consumables	(11.9)	(13.0)	10.0%
Purchased & services	(8.0)	(8.2)	2.3%
Staff costs	(50.4)	(55.4)	9.9%
Depreciation	(3.4)	(3.4)	-1.7%
Operating lease	(2.6)	(2.7)	1.8%
Other operating expenses	(8.0)	(8.2)	2.4%
<b>Operating profit</b>	<b>20.7</b>	<b>24.2</b>	<b>17.2%</b>
Financing costs	(0.2)	(0.1)	-41.7%
Pretax income	20.4	24.1	17.9%
Income taxes	(3.8)	(4.3)	14.9%
Minority interest	(0.1)	(0.1)	43.8%
<b>Net income</b>	<b>16.6</b>	<b>19.6</b>	<b>18.5%</b>

Segmental Revenue (\$m)	1Q09	1Q10	yoy growth
Healthcare Services			11.2%
Hospital Services			3.7%

Source: Company data, Kim Eng

### A baby step towards China

RMG has taken a small step into the vast market that is China. The group has assumed the management of a medical centre in Shanghai in 2Q10. The centre, Raffles Medical Shanghai, is mainly targeted at the 1m-strong expatriate population in the Greater Shanghai region and will be multi-disciplinary. RMG has invested a modest \$1m for this undertaking. We believe this is in keeping with management's conservative approach to test itself in a new market prior to sinking large funds.

### Raffles Hospital to be enlarged

RMG is embarking on an expansion plan for Raffles Hospital, which will increase its gross floor area by 102,408 sq ft (approx 30%) from 307,875 sq ft to 410,283 sq feet. The expanded hospital will have an area and bed capacity of 380 similar to Parkway's Gleneagles Hospital. The group has

received permission for its plan from the Urban Redevelopment Authority and is currently finalising further submission.

The expansion will be implemented by increasing the plot ratio from 4.2 to 5.6. The hospital was originally built with a view to eventually incorporate more floors and basements, hence minimal disruptions are expected to its operations during construction.

#### **Expansion at bargain price**

The expansion is estimated to cost \$80-100m, including a development premium of \$20-30m. This implies a total cost of under \$1,000 psf, compared with the \$2,345 psf Parkway paid to develop its new Novena Hospital.

The extra space will be used mainly for new specialist services, as management believes that the 300 beds it currently has are sufficient. We also note that there are several white sites around the hospital compound. These could one day conceivably be used for further expansion of the hospital.

The new area is expected to be ready 24 months from now, and management is confident it will be reasonably filled by that time. This also implies that our revenue growth estimates are in line with management's implicit target to increase group revenue by 30% by 2013.

#### **Positive development for shareholders**

We have earlier highlighted in our various reports RMG's strong cash position and its ability to generate cash flow. That the group is now able to comfortably and wholly fund the hospital expansion with its internal resources, maintain its dividend payment and yet remain in a net cash position is testament to this fact. In short, RMG's development thus far has been very positive for the shareholders.

**Figure 2: Comparison of hospital size**

	Strata area (sq ft)	Gross floor area (sq ft)	No. of licensed beds
Raffles Hospital		38,117	380
Mount Elizabeth Hospital	58,139		505
Gleneagles Hospital	49,003		380
Parkway East Hospital		10,993	154

*Source: Company data, Kim Eng*

**Figure 3: DCF assumptions**

<b>(\$ m)</b>	<b>FY10</b>	<b>FY11</b>	<b>FY12</b>	<b>FY13</b>	<b>FY14</b>
FCFE	(5.6)	14.9	19.4	54.0	62.6
Terminal Value					1432.7
PV	(5.3)	13.1	16.1	42.1	1093.5
Total discounted FCFE	1159.5				
Value/ Share	2.24				
Cost of equity	6.5%				
Risk-free rate	2.5%				
Beta	0.66				
Market risk premium	8.5%				
Terminal growth	2.0%				

*Source: Bloomberg, Kim Eng*

**Profit and loss**

YE Dec (\$ m)	2008	2009	2010F	2011F	2012F
<b>Sales</b>	<b>200.8</b>	<b>218.6</b>	<b>237.7</b>	<b>261.0</b>	<b>284.1</b>
Consumables & services	(35.5)	(40.5)	(42.4)	(45.7)	(49.1)
Staff costs	(98.3)	(104.9)	(111.7)	(120.1)	(129.2)
Depreciation	(6.6)	(6.9)	(7.3)	(7.3)	(7.5)
Operating lease	(4.5)	(5.1)	(5.3)	(5.3)	(5.3)
Other op expenses (net)	(16.9)	(15.7)	(18.0)	(23.3)	(25.3)
<b>Operating profit</b>	<b>39.0</b>	<b>45.5</b>	<b>53.0</b>	<b>59.5</b>	<b>67.7</b>
Financing costs	(0.6)	(0.4)	(0.6)	(0.6)	(0.5)
Share of joint entity	0.0	0.0	0.0	0.0	0.0
Pretax income	38.4	45.0	52.4	58.9	67.2
Income taxes	(6.7)	(7.0)	(8.9)	(10.0)	(11.4)
Minority interest	(0.1)	(0.2)	(0.1)	(0.1)	(0.1)
<b>Net profit attributable</b>	<b>31.5</b>	<b>37.9</b>	<b>43.4</b>	<b>48.8</b>	<b>55.7</b>
<b>Net profit (normalized)</b>	<b>31.5</b>	<b>37.9</b>	<b>43.4</b>	<b>48.8</b>	<b>55.7</b>
EPS (SG cents)	6.1	7.3	8.4	9.4	10.7
<b>EBITDA</b>	<b>45.6</b>	<b>52.4</b>	<b>60.3</b>	<b>66.8</b>	<b>75.2</b>

Source: Company data, Kim Eng estimates

**Cashflow**

YE Dec (\$ m)	2008	2009	2010F	2011F	2012F
<b>Operating cash flow</b>	<b>40.1</b>	<b>47.2</b>	<b>43.6</b>	<b>59.4</b>	<b>65.2</b>
Pretax profit	38.4	45.0	52.4	58.9	67.2
Depreciation & amortization	6.7	6.9	7.3	7.3	7.5
Change in working capital	(1.8)	0.6	(6.9)	3.6	1.2
Others	(3.1)	(5.4)	(9.2)	(10.4)	(10.7)
<b>Investment cash flow</b>	<b>(5.0)</b>	<b>(3.5)</b>	<b>(34.5)</b>	<b>(34.5)</b>	<b>(34.5)</b>
Net capex	(6.1)	(3.7)	(35.0)	(35.0)	(35.0)
Acquisition of sub	0.0	0.0	0.0	0.0	0.0
Others	1.2	0.4	0.5	0.5	0.5
<b>Financing cash flow</b>	<b>(10.7)</b>	<b>(13.7)</b>	<b>(22.2)</b>	<b>(17.7)</b>	<b>(17.7)</b>
Dividends	(12.9)	(13.0)	(15.6)	(15.6)	(15.6)
Net change in debt	0.9	(2.0)	(6.5)	(2.0)	(2.0)
Issue of shares	1.3	1.3	0.0	0.0	0.0
Others	0.0	(0.1)	0.0	0.0	0.0
<b>Net cash flow</b>	<b>24.4</b>	<b>30.0</b>	<b>(13.1)</b>	<b>7.3</b>	<b>13.1</b>

Source: Company data, Kim Eng estimates

**Balance Sheet**

YE Dec (\$ m)	2008	2009	2010F	2011F	2012F
<b>Total assets</b>	<b>310.4</b>	<b>336.8</b>	<b>356.6</b>	<b>395.0</b>	<b>438.9</b>
Current assets	74.2	104.5	96.0	106.6	123.0
Cash	44.5	74.4	61.2	68.5	81.6
Inventories	4.8	5.3	5.4	5.9	6.4
Receivables	24.9	24.3	29.3	32.2	35.0
Others	0.0	0.6	0.0	0.0	0.0
Long term assets	236.2	232.3	260.7	288.4	315.9
Plant and equipment	150.3	146.4	174.8	202.5	230.0
Intangibles	0.3	0.4	0.4	0.4	0.4
Investment properties	84.4	85.0	85.0	85.0	85.0
Others	1.3	0.5	0.5	0.5	0.5
<b>Total liabilities</b>	<b>88.2</b>	<b>86.7</b>	<b>78.6</b>	<b>83.7</b>	<b>87.5</b>
Current liabilities	65.4	65.2	59.2	66.3	72.0
Payables	51.5	52.0	50.3	57.3	61.8
ST borrowings	4.6	4.5	0.0	0.0	0.0
Others	9.3	8.7	8.9	9.0	10.3
<b>Long-term liabilities</b>	<b>22.7</b>	<b>21.4</b>	<b>19.4</b>	<b>17.4</b>	<b>15.4</b>
LT borrowings	22.0	20.0	18.0	16.0	14.0
Others	0.7	1.4	1.4	1.4	1.4
<b>Shareholder's equity</b>	<b>221.9</b>	<b>249.8</b>	<b>277.6</b>	<b>310.9</b>	<b>351.0</b>
Paid-in capital	171.3	172.7	172.7	172.7	172.7
Reserve	50.6	77.1	105.0	138.2	178.4
Minority interests	0.3	0.4	0.4	0.4	0.4

Source: Company data, Kim Eng estimates

**Key ratios**

YE Dec (\$ m)	2008	2009	2010F	2011F	2012F
<b>Growth (% YoY)</b>					
Sales	19.0	8.9	8.8	9.8	8.8
Operating Profit	38.1	16.6	16.7	12.2	13.8
EBITDA	40.5	14.8	15.1	10.7	12.6
Net Profit	35.0	20.1	14.6	12.5	14.1
EPS	(12.4)	19.9	14.6	12.5	14.1
<b>Profitability (%)</b>					
Gross margin	Na	Na	Na	Na	Na
Operating margin	19.4	20.8	22.3	22.8	23.8
EBITDA margin	22.7	24.0	25.4	25.6	26.5
Net profit margin	15.7	17.3	18.3	18.7	19.6
ROA	10.2	11.3	12.2	12.4	12.7
ROE	14.3	15.2	15.7	15.7	15.9
<b>Stability</b>					
Gross debt/equity (%)	12.0	9.8	6.5	5.1	4.0
Net debt/equity (%)	2.7	(8.1)	(20.0)	(15.6)	(16.9)
Int. coverage (X)	62.6	110.9	84.2	106.3	138.2
Int. & ST debt coverage (X)	7.4	9.2	84.2	106.3	138.2
Cash flow int. coverage (X)	39.1	73.1	(20.8)	13.0	26.6
Cash flow int. & ST debt (X)	4.7	6.1	(20.8)	13.0	26.6
Current ratio (X)	1.1	1.6	1.6	1.6	1.7
Quick ratio (X)	1.1	1.5	1.5	1.5	1.6
Net debt/(cash) (\$ m)	(17.9)	(49.9)	(43.2)	(52.5)	(67.6)
<b>Per share data (SG cent)</b>					
EPS	6.1	7.3	8.4	9.4	10.7
CFPS	4.6	5.6	(2.4)	1.4	2.4
BVPS	42.9	48.2	53.5	60.0	67.7
SPS	37.6	40.9	44.5	48.8	53.1
EBITDA/share	8.5	9.8	11.3	12.5	14.1
DPS	2.5	3.0	3.0	3.0	3.0

Source: Company data, Kim Eng estimates

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**Recommendation definitions**

**Our recommendation is based on the following expected price performance within 12 months:**

+15% and above: BUY  
 -15% to +15%: HOLD  
 -15% or worse: SELL

**APPENDIX I: TERMS FOR PROVISION OF REPORT, DISCLOSURES  
AND  
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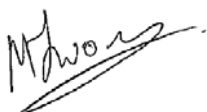
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