

Singapore Company Focus

Raffles Medical

Bloomberg: RFMD SP | Reuters: RAFG.SI

DBS Group Research . Equity

31 Oct 2008

BUY S\$0.665 STI : 1,801.91

(Upgrade from Hold)

Price Target : 12-month S\$ 0.76 (Prev S\$ 1.01)

Reason for Report : 3Q08 Results

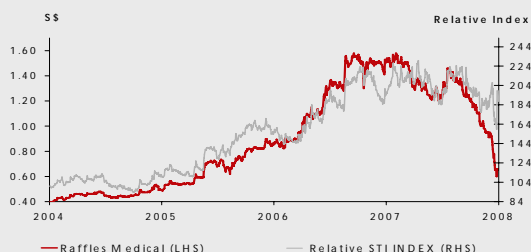
Potential Catalyst: Special dividends, acquisitions

Analyst

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Price Relative



Forecasts and Valuation

FY Dec (\$ m)	2007A	2008F	2009F	2010F
Turnover	169	202	224	249
EBITDA	34	42	48	53
Pre-tax Profit	41	35	40	45
Net Profit	36	29	33	37
Net Pft (Pre Ex.)	23	29	33	37
EPS (S cts)	7.0	5.5	6.4	7.2
EPS Pre Ex. (S cts)	4.5	5.5	6.4	7.2
EPS Gth Pre Ex (%)	29	22	15	13
Diluted EPS (S cts)	6.9	5.5	6.3	7.1
Net DPS (S cts)	2.5	2.5	3.0	3.5
BV Per Share (S cts)	39.0	42.0	45.9	50.2
PE (X)	9.6	12.0	10.4	9.2
PE Pre Ex. (X)	14.7	12.0	10.4	9.2
P/Cash Flow (X)	8.8	9.7	8.5	7.6
EV/EBITDA (X)	10.4	7.8	6.3	5.1
Net Div Yield (%)	3.8	3.8	4.5	5.3
P/Book Value (X)	1.7	1.6	1.4	1.3
Net Debt/Equity (X)	0.0	CASH	CASH	CASH
ROAE (%)	22.9	13.7	14.6	15.0

Earnings Rev (%) :	(0.5)	(6.6)	N/A
Consensus EPS (S cts) :	5.6	6.8	8.0

ICB Industry : Health Care

ICB Sector: Health Care Equipment & Servic

Principal Business: Raffles Medical Group Ltd. is a Singapore-based company that is principally engaged in the provision of integrated healthcare services.

At historical low valuation

Story: Raffles Med 3Q results were marginally above expectations. Revenue grew 17% to S\$51.3m. Net profit was up by 26% to S\$8.2m. 9M08 net profit now forms about 77% of our FY08 estimates.

Point: The higher growth in net profit vis-à-vis topline was a result of better operating efficiencies. Inventories and consumables, and staff costs grew by 12.9% and 16.8% respectively. Also, as a result of its full ownership of the hospital, operating lease expenses declined 61%, but partially offset by a higher depreciation. 3Q08 EBIT margins improved y-o-y and q-o-q from 17.3% (3Q07) and 19.3% (2Q08) to 19.8% (3Q08). The Group continued to generate strong cash flows from operating activities of S\$29.4m for the 9M. As of Sep'08, the Group is in a net cash position of more than S\$9m. Based on our estimates, this should increase to c.S\$16m by the end of 2008.

Relevance: We adjusted our FY09F revenue and net profit forecasts down by 6.6% on assumption of slower growth in its hospital and healthcare revenues, in view of the current economic situation. However, we still expect the Group to return a recurring net profit CAGR of c.17% over FY07-'10F. Stock has corrected over 30% over the past 8 weeks; and, fallen to its historical low PER of around 12x. In our view, we see limited downside from current levels. We upgrade to Buy, from Hold, on (i) current historically low PE; (ii) relatively defensive nature of the healthcare sector, (iii) strong operating cashflow; and, (iv) its net cash position. Our TP is adjusted to S\$0.76 based on 12x (from 15x) on FY09F EPS. We expect a final dividend of 1.5 cents (bringing total dividends to 2.5 cents), similar to FY07.

At A Glance

Issued Capital (m shrs)	518
Mkt. Cap (S\$m/US\$m)	344 / 235
Major Shareholders	
Raffles Medical (%)	39.9
Loo Choon Yong (%)	10.0
Free Float (%)	50.1
Avg. Daily Vol.(^{'000})	256

Results Summary and Comments

FY Dec (\$m)	3Q07	3Q08	3Q Chg y-o-y	9M07	9M08	Chg y-o-y	Comments
Sales	43.8	51.3	17%	122.9	149.3	22%	Growth from Hospital (+17.1%) and Healthcare (+16.9%) divisions
Other Operating Income	0.1	0.0	nm	0.9	0.4	nm	
<i>Inventories and consumables used</i>	(4.8)	(5.4)	13%	(14.4)	(16.9)	18%	
<i>Staff costs</i>	(21.5)	(25.1)	17%	(61.5)	(73.7)	20%	
<i>Depreciation of PPE</i>	(0.9)	(1.7)	80%	(2.7)	(4.9)	81%	Depreciation increase largely due to full ownership of hospital, offset by lower operating lease expenses
<i>Operating lease expenses</i>	(2.9)	(1.1)	-61%	(8.6)	(3.6)	-58%	
<i>Other operating expenses</i>	(7.0)	(7.8)	12%	(18.5)	(22.7)	23%	
Total operating expenses	(37.1)	(41.1)	11%	(105.7)	(121.8)	15%	Lower than topline due to operating efficiencies
Operating profit	6.8	10.2	49%	17.3	27.9	61%	
Interest Income	0.7	0.1	-93%	1.7	0.2	-90%	
Interest Expense	(0.0)	(0.2)	558%	(0.1)	(0.5)	549%	Higher bank loans
Share of Associates' or JV Income	0.6	0.0	nm	1.1	0.0	nm	No contribution from JV in FY08 after full ownership of hospital
Exceptional Gains/(Losses)	0.0	0.0	nm	12.5	0.0	nm	Fair value gains from the Hospital asset in 2Q07
Pretax Profit	8.1	10.1	24%	32.6	27.6	-15%	
Tax	(1.6)	(1.9)	19%	(6.2)	(5.5)	-10%	
Minority Interests	0.0	0.0	420%	0.0	(0.0)	nm	
Net Profit	6.6	8.2	26%	26.5	22.1	-17%	Marginally above expectations; net profit forms 77% of our full year estimates
Recurring net profit	6.6	8.2		16.17	22.1	36%	
Margins (%)	3Q07	3Q08	Chg ppt	9M07	9M08	Chg ppt	Comments
EBITDA Margin	17.7	23.1	5.4	16.3	22.0	5.6	
EBIT Margin	15.6	19.8	4.2	14.1	18.7	4.6	
Pre-tax Margin	18.5	19.6	1.1	26.5	18.5	-8.1	FY07 inflated with fair value gains of hospital asset
Net Margin	14.9	16.1	1.1	21.5	14.8	-6.8	
Depr % of sales	2.1	3.3	1.2	2.2	3.3	1.1	
Effective Tax Rate %	19	18	-0.9	19	20	1.1	
Recurring Net Margin	14.9	16.1	1.1	13.2	14.8	1.6	

Source: Company, DBS Vickers

Results commentary

3Q08 results at S\$8.2m, marginally above our expectations of c.S\$7.6m. According to management, the revenue growth was driven by c.12% in volumes and c.5% in prices. Performance were helped by a slower rate of increase in its consumables and inventories, and staff costs which grew 12.9% and 16.8% y-o-y, lowering than the topline growth of 17%. Operating lease expenses dropped 60% as a result of its full ownership of the hospital, offset partially by a higher depreciation. Recall that the Group acquired the 50% stake it did not own in Jul 07 funded by proceeds from new shares placement to Temasek and Qatar Investment Authority.

4.2ppt improvement in 3Q08 EBIT margin. As a result of its operating efficiencies, 3Q08's EBIT margins increase by 4.2% y-o-y from 15.6% to 19.8%. Recurring net profit grew by 26% vis-à-vis topline growth of 17% in 3Q. 9M08 net profit now forms 77% of our FY08F estimates.

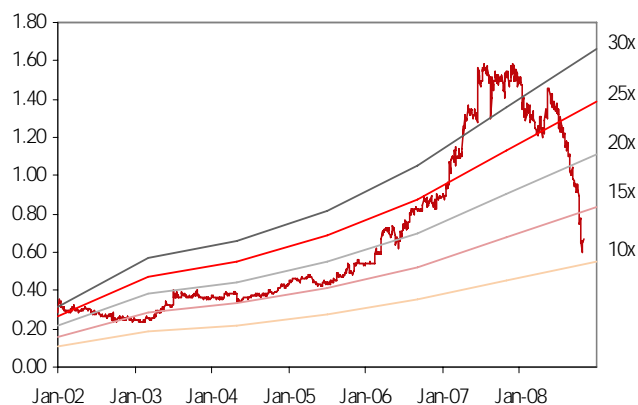
Net cash position of \$9m. The Group generated about S\$29.4m in operating cashflow for 9M08. Net cash stood at S\$9m, up from a net debt position of c.S\$6m as of Dec 07. We estimate that the Group's net cash position should increase to at least S\$16m by Dec 08. We continue to expect the Group to pay out a final dividend of 1.5cents bringing total dividend for the year to 2.5cents, in line with FY07.

Adjust FY09F topline and bottomline down by 6.7% on more conservative assumptions. In view of a more cautious outlook, we trimmed our FY09F topline and bottomline by 6.7% on slower growth in its hospital and healthcare divisions. Notwithstanding this, we still expect the Group to return net profit CAGR growth of c.17% from FY07 till '10F.

Counter trading at historical low 12x PER. The counter has dropped by 36% over the past 8 weeks, along with the market. It is now trading at a PE of c. 12x and 10x on our FY08F and FY09F EPS, which is a historical low. FY08F EV/EBITDA stands at 6.8x and P/B at 1.6x. This is the same level during the SARS period, which affected healthcare players as consumers shunned hospital and clinics. Furthermore, Raffles Med is in a better position now compared to 2003, as its hospital operation is more established, in our view.

Upgrade to Buy, TP: S\$0.76, on valuation grounds and strong company fundamentals. We upgrade our recommendation to Buy, from Hold on (i) current attractive historical low PE; (ii) relatively defensive healthcare sector; (iii) strong operating cashflow; and, (iv) net cash position. Our TP is however lowered to S\$0.76, based on 12x FY09F EPS its historical low PE and in line with peers' average.

Raffles Med trading at historical low PE



Source: Bloomberg, DBSVickers

Risks. Downside risks to our recommendation includes (i) larger than expected fall in hospital admission growth; (ii) prolonged economic slump resulting in massive job losses; (iii) incurrence of epidemics such SARS or Avian Flu; (iv) further de-rating of the equities market, which would indirectly affect the counter's relative valuation.

Peers' valuation table

Company	Curr	Last Px	Mkt cap (US\$)	Hist. PE (x)	PE Curr Yr (x)	PE Nxt Yr (x)	Sales (US\$)	Opg Income (US\$)
Raffles Medical Group Ltd	SGD	0.660	233	14.6*	11.9	10.3	78.4	17.9
Parkway Holdings Ltd	SGD	1.570	1,210	13.4*	18.8	17.4	591.4	86.7
Thomson Medical Centre Ltd	SGD	0.450	90	10.9	9.3	7.0	41.1	9.5
Pacific Healthcare Holdings Ltd	SGD	0.085	16	4.4	na	na	51.3	5.2
Health Management International Ltd	SGD	0.080	26	22.7	na	na	30.4	3.6
Healthway Medical Corp Ltd	SGD	0.085	79	6.1	na	na	57.7	15.1
Primary Health Care Ltd	AUD	4.480	1,150	42.5	16.3	10.7	444.7	73.3
Ramsay Health Care Ltd	AUD	10.100	1,208	20.3	14.7	12.8	1,787.2	159.2
Healthscope Ltd	AUD	4.390	752	16.2	12.8	11.7	1,006.9	104.3
Bangkok Dusit Medical Service Pcl	THB	18.600	649	13.4	12.7	10.6	532.2	61.6
Bumrungrad Hospital PCL	THB	22.800	477	10.1	14.6	14.0	239.7	41.9
Bangkok Chain Hospital PCL	THB	5.950	162	9.8	9.7	8.8	103.6	20.9
					13.3	11.3		

*Note: Excluding exceptionals

Source: Bloomberg, DBS Vickers' estimates

Raffles Medical

Income Statement (\$\$ m)

FY Dec	2007A	2008F	2009F	2010F
Turnover	169	202	224	249
Other Opng (Exp)/Inc	(140)	(167)	(183)	(204)
Operating Profit	28	35	40	45
Other Non Opg (Exp)/Inc	0	0	0	0
Associates & JV Inc	1	0	0	0
Net Interest (Exp)/Inc	0	0	0	0
Exceptional Gain/(Loss)	13	0	0	0
Pre-tax Profit	41	35	40	45
Tax	(5)	(6)	(7)	(8)
Minority Interest	0	0	0	0
Preference Dividend	0	0	0	0
Net Profit	36	29	33	37
Net Profit before Except.	23	29	33	37
EBITDA	34	42	48	53
Sales Gth (%)	25.6	19.8	10.6	11.5
EBITDA Gth (%)	42.4	25.2	13.9	11.5
Opg Profit Gth (%)	46.9	25.2	14.7	12.0
Net Profit Gth (%)	128.2	(20.3)	15.4	12.9
Effective Tax Rate (%)	13.3	18.0	18.0	18.0

Balance Sheet (\$\$ m)

FY Dec	2007A	2008F	2009F	2010F
Net Fixed Assets	151	149	147	144
Invts in Associates & JVs	0	0	0	0
Other LT Assets	86	86	86	86
Cash & ST Invts	20	41	66	93
Inventory	4	5	5	6
Debtors	20	24	27	30
Other Current Assets	1	1	1	1
Total Assets	281	306	331	359
ST Debt	25	3	3	3
Other Current Liab	54	63	71	79
LT Debt	0	22	20	18
Other LT Liabilities	1	1	1	1
Shareholder's Equity	201	216	237	258
Minority Interests	0	0	0	0
Total Cap. & Liab.	281	306	331	359
Non-Cash Wkg. Capital	(30)	(34)	(38)	(42)
Net Cash/(Debt)	(6)	16	43	72

Cash Flow Statement (\$\$ m)

FY Dec	2007A	2008F	2009F	2010F
Pre-Tax Profit	41	35	40	45
Dep. & Amort.	4	7	7	8
Tax Paid	(4)	(7)	(6)	(7)
Assoc. & JV Inc/(loss)	(1)	0	0	0
Chg in Wkg.Cap.	13	5	3	4
Other Operating CF	(14)	0	0	0
Net Operating CF	40	40	44	50
Capital Exp.(net)	(68)	(5)	(5)	(5)
Other Invts.(net)	0	0	0	0
Invts in Assoc. & JV	0	0	0	0
Div from Assoc & JV	0	0	0	0
Other Investing CF	15	0	0	0
Net Investing CF	(53)	(5)	(5)	(5)
Div Paid	(18)	(13)	(13)	(15)
Chg in Gross Debt	0	0	(2)	(2)
Capital Issues	64	0	0	0
Other Financing CF	(55)	0	0	0
Net Financing CF	(9)	(13)	(15)	(17)
Net Cashflow	(22)	22	25	27

Rates & Ratio

FY Dec	2007A	2008F	2009F	2010F
Gross Margins (%)	100.0	100.0	100.0	100.0
Opg Profit Margin (%)	16.7	17.5	18.1	18.2
Net Profit Margin (%)	21.3	14.1	14.8	14.9
ROAE (%)	22.9	13.7	14.6	15.0
ROA (%)	16.6	9.7	10.3	10.8
ROCE (%)	14.3	12.3	13.2	13.7
Div Payout Ratio (%)	36.0	45.1	46.8	48.4
Net Interest Cover (x)	75.0	88.0	212.6	NM
Asset Turnover (x)	0.8	0.7	0.7	0.7
Debtors Turn (avg days)	40.0	40.2	41.7	41.5
Creditors Turn (avg days)	nm	nm	nm	nm
Inventory Turn (avg days)	nm	nm	nm	nm
Current Ratio (x)	0.6	1.1	1.3	1.6
Quick Ratio (x)	0.5	1.0	1.3	1.5
Net Debt/Equity (X)	0.0	CASH	CASH	CASH
Capex to Debt (%)	270.3	19.8	21.5	23.5
N. Cash/(Debt)PS (S cts)	(1.1)	3.1	8.3	14.0
Opg CFPS (S cts)	5.2	6.8	8.0	9.0
Free CFPS (S cts)	(5.5)	6.7	7.7	8.7

Quarterly / Interim Income Statement (\$\$ m)

FY Dec	4Q2007	1Q2008	2Q2008	3Q2008
Turnover	46	47	51	51
Other Oper. (Exp)/Inc	(37)	(39)	(41)	(41)
Operating Profit	9	8	10	10
Other Non Opg (Exp)/Inc	0	0	0	0
Associates & JV Inc	0	0	0	0
Net Interest (Exp)/Inc	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0
Pre-tax Profit	9	8	10	10
Tax	1	(2)	(2)	(2)
Minority Interest	0	0	0	0
Net Profit	9	6	8	8
Net profit bef Except.	9	6	8	8
EBITDA	11	10	11	12
Sales Gth (%)	4.3	3.6	6.8	1.3
EBITDA Gth (%)	26.7	(9.9)	20.2	3.9
Opg Profit Gth (%)	32.7	(12.6)	23.4	4.0
Net Profit Gth (%)	42.8	(34.7)	26.4	6.8
Gross Margins (%)	100.0	100.0	100.0	100.0
Opg Profit Margins (%)	19.8	16.7	19.3	19.8
Net Profit Margins (%)	20.4	12.9	15.2	16.1

Segmental Breakdown

FY Dec	2007A	2008F	2009F	2010F
Revenues (\$\$ m)				
Healthcare services	70	80	86	94
Hospital services	106	131	147	166
Investment holdings	3	3	3	3
Less: Eliminations	(10)	(11)	(12)	(14)
Total	169	202	224	249
Operating profit (\$\$ m)				
Healthcare services	6	7	8	9
Hospital services	20	26	31	35
Investment holdings	2	2	2	2
Total	28	35	40	45
Operating profit Margins				
Healthcare services	9.1	9.1	9.1	9.1
Hospital services	18.6	19.9	20.8	20.9
Investment holdings	72.8	72.8	72.8	72.8
Total	16.7	17.5	18.1	18.2

Source: Company, DBS Vickers

DBSV recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (0-15% total return over the next 12 months for small caps, 0-10% for large caps)

FULLY VALUED (negative total return i.e. > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

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