



RafflesMedicalGroup

BUY

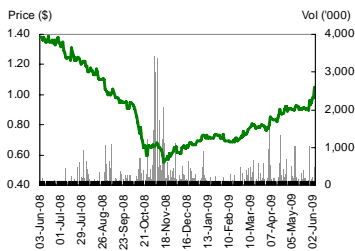
Initiating Coverage

Analyst

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Price \$1.05
Target \$1.38
ST Index 2,383.82

Historical Chart



Performance	1m	3m	6m
Absolute (%)	16.7	41.9	70.7
Relative (%)	-0.7	-8.1	17.7

Stock Information

Ticker code	RAFG.SI RFMD.SP
Market cap (US\$m)	376.5
52-week high (S\$)	1.43
52-week low (S\$)	0.55
Shares issued (m)	518.5
6m avg d.vol (US\$m)	0.1
Free float (%)	55.7
Major shareholders (%)	
Dr Loo Choon Yong	(40.0)

Key Indicators

ROE (%)	14.3
Net gearing (%)	Net cash
NTA (S\$)	0.45
Interest cover (x)	62.6

Raffles Medical Group

Fit and Ready to go

Caring for the unwell since 1976

Founded as a two-clinic practice in 1976, Raffles Medical Group (RMG) now operates the largest local network of 65 General Practice clinics. Its flagship, Raffles Hospital, was established in 2001. Its impressive performance was reflected by the fact that it broke even within two years. In fact, the Group has been a model of consistency since its listing in 1997, registering double-digit profit growth almost every year.

An apple a day won't keep the doctor away

We believe a congruence of factors such as an aging population, coupled with the influx of foreign immigrants, has benefited the private healthcare sector. Moreover, this year, the government introduced means testing in public hospitals, with the aims of increasing its efficiency in allocating subsidies and potentially shifting demand towards the private sector.

Alignment of interest at all levels

The employee remuneration model is a key criterion for healthcare providers. We believe RMG's Group Practice Model, in which all its medical professionals are employees of the Group, is a more scalable model and gives it a higher operating leverage than peers. We expect its staff cost as a percentage of revenue to continue declining.

Licensed to grow

Licensed for 380 beds, Raffles Hospital is capable of ramping up its capacity from its current 200 operational beds. This is in contrast to a potentially tight private sector supply, with new beds only by 2011. With a strong financial position, this is an opportune time for RMG to expand overseas, where it has previously been more conservative than its peers.

Charging ahead with confidence

Even with just organic growth, we expect net profit to increase 14% CAGR over the FY09-FY11 period. Its strong cash position could prompt M&A activities as well as an increased dividend payout. Our Free Cash Flow to Equity (FCFE) target price implies 20x FY09 estimated earnings. Since 2002, RMG has traded at a P/E trough of 13x and a peak of 29x.

Year End Dec	2007*	2008	2009F	2010F	2011F
Sales (S\$ m)	168.7	200.8	214.0	238.4	266.0
Pre-tax (S\$ m)	41.4	38.4	44.7	51.1	59.1
Net profit (S\$ m)	35.9	31.5	37.0	42.3	49.0
EPS (cts)	7.0	6.1	7.2	8.2	9.5
EPS growth (%)	83.7	(12.4)	17.4	14.2	15.8
PER (x)	15.6	17.8	15.1	13.3	11.4
EV/EBITDA (x)	16.9	11.5	9.5	8.0	6.5
Yield (%)	2.4	2.4	2.4	2.4	2.4

* 2007 net profit includes S\$12.5m fair value gain

SEE APPENDIX I FOR IMPORTANT DISCLOSURES AND ANALYST CERTIFICATIONS

Investment Summary

Consistent growth since 1997 IPO

Raffles Medical Group (RMG) is an integrated healthcare Group providing Primary Care, Specialist Care and Tertiary Care across multiple disciplines. It operates primarily its flagship Raffles Hospital, as well as the largest network of 65 local General Practice (GP) clinics. The Group has been a model of consistency with no losses since its listing in 1997. It has also enjoyed double-digit net profit growth (excluding exceptional items) each year except for 1998 and 2001 where there were exceptional circumstances.

An apple a day won't keep the doctor away

We believe a congruence of factors makes local private healthcare a defensive sector that will continue to thrive. In terms of population, the Singapore government is aiming for a population target of 6.5m. The increase in non-residents, as well as an aging population, will benefit private healthcare since non-residents are ineligible for subsidies, while the elderly requires more healthcare resources. Means testing in public hospitals effective this year could shift some demand towards private hospitals. While the private sector market share has hovered around 20%-25%, it could go up to 30%, as the Singapore government continues to allocate resources and promote Singapore as a medical travel hub.

When interests are aligned

The employee remuneration model is an important criterion for healthcare providers, given that medical professionals are highly-paid personnel. RMG has fared well in this area, with staff costs (as a percentage of its revenue) declining steadily as revenue grows. We believe RMG's Group Practice Model is scaleable and gives it a higher operating leverage than peers. In terms of its exposure to foreign patients, RMG clientele is also more diversified, hailing from more than 100 countries. Its GP clinics provide a strong earnings base and serve as an important referral feed to Raffles Hospital.

Licensed to grow

Licensed for 380 beds, Raffles Hospital is capable of ramping up its capacity from its current 200 operational beds, where the occupancy rate is at only 40%-60%. We believe this puts RMG in a good position to benefit from a potentially tight private sector supply with new beds coming onstream only by 2011. Its pricing also puts it in the best position to reap the benefits of any migration of patients from public hospitals. With a strong financial position, RMG could also benefit from expansions overseas, where it has been previously more conservative than peers.

Unstoppable growth

Even with just organic growth, we expect net profit to increase 14% CAGR over the FY09-FY11 period. We expect further incremental improvements in its operating margin, driven by lower staff costs as a percentage of revenue, as well as operating efficiencies. Following the acquisition of its remaining 50%-stake of Raffles Hospital from CapitaLand in 2007, its cash flow generation has improved even further. We believe this could prompt M&A activities as well as an increase of dividends from FY09 onwards.

Free Cash Flow Valuation target price of \$1.38

Our Free Cash Flow valuation derives a target price of \$1.38, which implies 20x its estimated FY09 earnings. While this is at a premium compared to its peer, we believe it is justified by a strong track record, higher Returns on Equity (ROE) and margins. Since 2002, RMG has traded at a P/E trough of 13x and a peak of 29x. We also note that both Temasek and Qatar Investment Authority paid \$1.30 per share for a 4.84% stake in a 2007 share placement exercise.

Consistent growth since 1997 IPO

The early years

Founded in 1976

The Group was founded in 1976 by current Chairman Dr Loo and Senior Clinical Director Dr Alfred Loh as a two-clinic practice. Since its early years, the Group has not deviated from its philosophy to deliver quality and cost-effective healthcare services to both private and corporate clients.

These unwavering efforts over the years have now positioned RMG as the largest private healthcare Group practice in Singapore, armed with a strong network of corporate clientele.

Listed on SESDAQ in April 1997 with a market cap of S\$93.1m

On the back of its success in the Primary healthcare sector, the Group increased its range of services to provide specialist healthcare services in 1992, opening Raffles SurgiCentre -- South-East Asia's first stand-alone day surgery on Clemenceau Avenue in Sep 1993.

Net profit has increased 8-fold

The Group was listed in April 1997 with a share price of S\$0.38, with a valuation of \$93.1m. Its historical turnover at the time was \$32.5m with a net profit of \$3.7m. During this period, the Group operated an island-wide network of 27 GP clinics and four dental clinics in Singapore.

Inception of Raffles Hospital in March 2001

When the idea of Raffles Hospital was originally conceived in 1996, RMG teamed up with CapitaLand to redevelop Blanco Court into a 13-floor hospital at a cost of \$200m. CapitaLand retained a 50%-stake on the property as a co-landlord. The existing Raffles SurgiCentre was shifted into Raffles Hospital when the latter was established in March 2001.

While RMG had to take a revaluation write-down of \$6.6m on this property, the hospital managed to break even within a mere two years of its operating history. This milestone established RMG as a solid player in the private hospital sector.

Double-digit revenue growth each year except 2004

A model of consistency

Since its listing in 1997, the Group has been a model of consistency. During this period, RMG achieved double-digit revenue growth each year except for 2004 when its revenue grew by 2.4%. The CAGR of its revenue was 15% for this period. This is a testament to the Group's commitment to the incremental expansion of its operations.

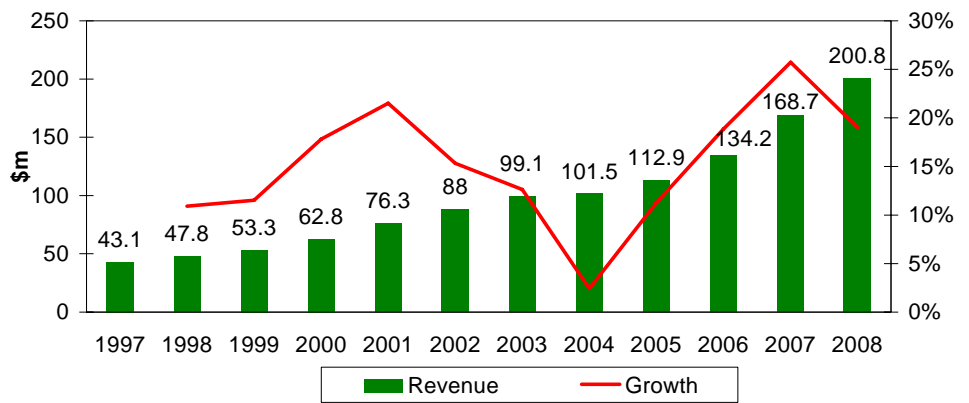
Double-digit profit growth each year except 1998 and 2001

Excluding one-time adjustments for the revaluation of its properties in FY01 (-\$8m) and FY07 (+\$12.5m), its rate of profitability has largely followed the same trend. Except for FY98 and FY01, RMG achieved net profit growth rates within the double-digit range, with a CAGR of 25.5%. We believe FY98 and FY01 were exceptional years operationally; FY98 saw increase in expenses associated with the listing of RMG, while FY01 registered losses related to the opening of Raffles Hospital in 2001.

Operating leverage is key to our investment thesis

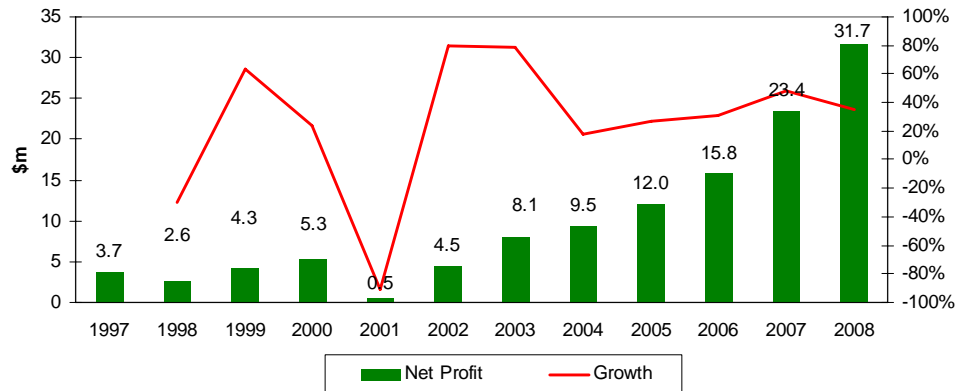
RMG has been able to achieve more profitability as its operational scale increased during this period. Its net profit increased at a CAGR of 25.5% versus 15.0% in revenue growth. This historical evidence backs up our belief that RMG's astute cost control and its "Group Practice" business model gives it a better operating leverage than its peers, which is a key foundation of our investment thesis.

Figure 1: Historical Revenue and Growth



Source: Company, Kim Eng Research

Figure 2: Historical Net Profit and Growth



*Excludes fair value gain of property of \$12.5m in 2007

** Growth rate for 2002 was scaled down for graph comparison purposes

Source: Company, Kim Eng Research

Caring for all

An integrated healthcare provider

RMG is an integrated healthcare organisation, providing a whole spectrum of Primary Care, Specialist Care and Tertiary Care across multiple disciplines. Primary healthcare is primarily provided by its network of GP clinics, while Specialist and Tertiary Healthcare are provided by its flagship Raffles Hospital. The Group is mainly based in Singapore, which accounts for more than 95% of its current revenue.

Investment holdings is inter-segment profit from hospital

In FY08, Primary healthcare (Healthcare Services in Figure 3) accounted for 37% of its revenue, while Hospital Services accounted for 59%. The remaining balances are accounted for by Investment Holdings that mainly relates to its stake in the building occupied by Raffles Hospital.

Figure 3: Revenue Breakdown (FY08)

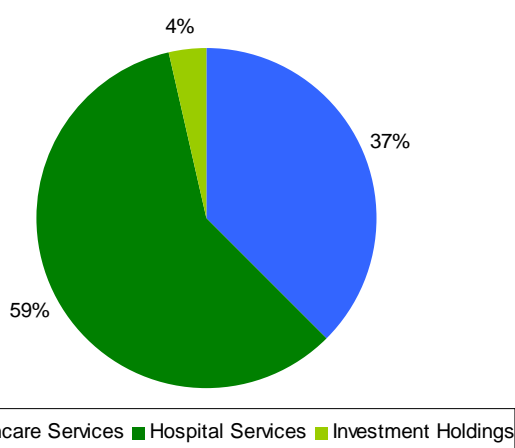
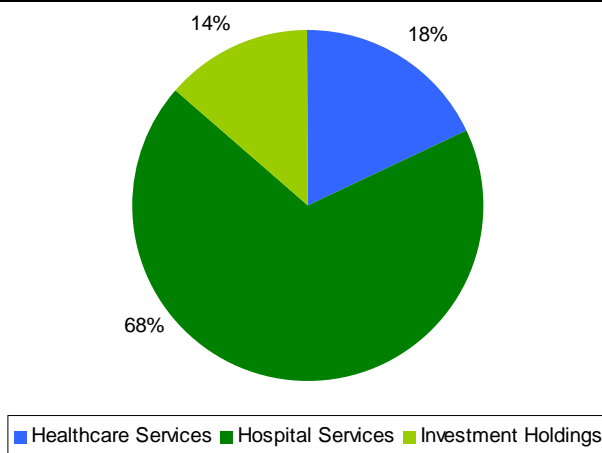


Figure 4: EBIT Breakdown (FY08)



Sources: Company, Kim Eng Research

*Takes into account inter-segment revenue/EBIT

Largest network of General Practice Clinics in Singapore

RMG current has the largest network of GP clinics in Singapore. These 65 multi-disciplinary clinics are located across Singapore from the Central Business District (CBD) to regional estates. The Group also operates the Airport clinics in Singapore's Changi International Airport and Hong Kong's Chek Lap Kok International Airport. Other than providing a stable source of income, these GP clinics also serves as a referral source to its hospital services.

Other than general practice/ family medicine that deals with basic ailments such as coughs and colds, these clinics also offer dental services, health checks, travel health services, vaccination, housecalls, ambulance transport and transfer, x-ray and laboratory services.

Strong-track record of servicing corporations

RMG is the corporate medical provider of more than 5,500 companies in both the public and private sector. These clients include all the major banks in Singapore, Singapore Airlines and Singapore Post. By managing healthcare costs and handling all the related administrative work for its corporate clients, the Group enables clients to effectively outsource their staff healthcare requirements, thus adding value to their cost-control efforts. We believe the reason for RMG's success with corporate clients can be partially attributed to its strong track record of servicing corporation, as well as the accessibility of its clinics to corporate employees.

*Corporate clients
provide revenue
visibility*

Corporate clients currently account for approximately two-thirds of its Primary Healthcare revenue. Since they usually sign a contract for RMG's services over a period of time, these contracts also provide more revenue visibility for RMG.

Raffles Hospital is the newest kid on the block

Tertiary healthcare services are primarily provided in RMG's flagship, Raffles Hospital, at North Bridge Road, in downtown Singapore. The 13-storey hospital is equipped for 380 beds; its full range of medical and surgical facilities include day surgery suites, delivery suites, operating theatres, an intensive care unit, a neonatal intensive care unit, a dental unit, a radiology laboratory, a clinical laboratory, a pharmacy, a dietetics centre and a physiotherapy clinic.

The hospital also offers a full range of specialist, medical and diagnostic services that spans across 35 disciplines. Its 16 specialist centres meet a wide variety of medical needs such as obstetrics and gynaecology, cardiology, oncology and orthopaedics.

Figure 5: Raffles Hospital at North Bridge Road



Source: Company, Kim Eng Research

Overseas Operations and others

Overseas operations at this moment are still limited. RMG currently operates four medical centres in Hong Kong. However, RMG has made strong marketing efforts overseas. To date, approximately a third of its hospital patients are foreigners coming from more than 100 countries including Indonesia, Malaysia, Russia and Australia.

Other than its core medical services, the Group also offers lifestyle services through its Raffles Aesthetics, Raffles Dental and Raffles Chinese Medicine centres to meet the needs of its patients.

RMG also offers insurance and consumer healthcare. RMG has been a specialised healthcare insurer since 1996 and a licenced life insurer since 1996. International Medical Insurers (IMI) provides health insurance policies for both individuals and groups. The consumer healthcare arm, Raffles Health, develops and distributes nutraceutical products in Singapore and the region.

An apple a day won't keep the doctor away

Singapore Government targets 6.5m population

Upon achieving independence, the Singapore government's population policy had originally been that of containment, due to the limited natural resources and small territory of the island-nation. With fewer people entering the workforce due to a decline in birthrates and an aging population, there was a threat to the sustainability of Singapore's economic growth. This resulted in a dramatic change of policy in the late 1990s to encourage higher birth-rates, as well as promote foreign immigration.

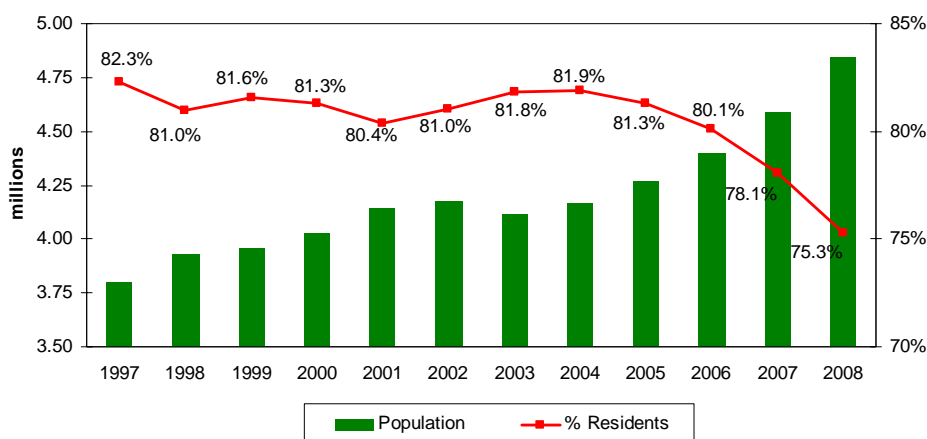
Aggressive foreign immigrant policy

On the back of these policies, the total population in Singapore has increased from 3.8million in 1997 to 4.8million in 2008 at a CAGR of 2.2%, with the eventual target to reach 6.5million. Despite having one of the lowest birthrates in the world, the aggressive foreign immigrant policy will likely continue to drive population growth, with city-planners already factoring in the target population.

More non-residents mean more private healthcare

With the increase of people coming to work or study in Singapore, the percentage of residents amongst the total population has also decreased steadily from 82.3% to 75.3%. Since non-residents are ineligible for public healthcare subsidies, this gradual shift in the population mix implies that the private healthcare sector will benefit from additional healthcare expenditure.

Figure 7: Singapore Population Trend



Source: Singstats, Kim Eng Research

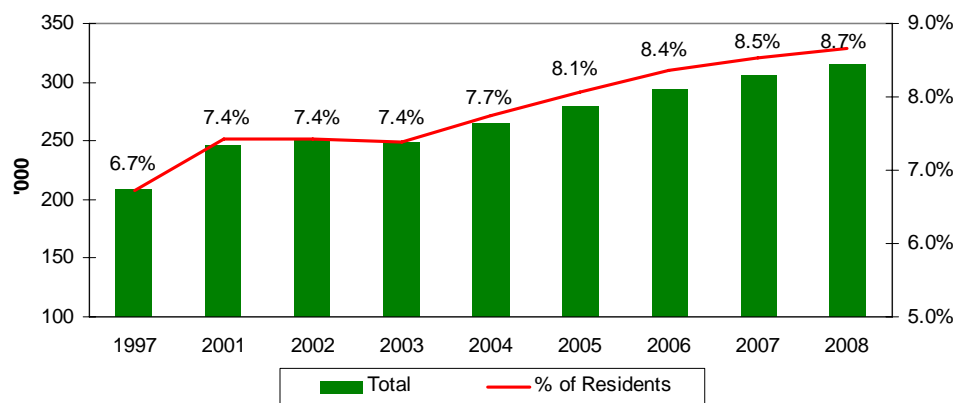
Number of residents 65 years and above will continue to increase

Aging population

With an aging population, the number of residents 65 years and above has increased from 209,700 in 1997 to 315,800 in 2008 as seen in Figure 8 next page. This group now accounts for 8.7% of total residents, up steadily from 6.7% in 1997. The government has also estimated that this group will continue to increase.

People in this age group would need more healthcare resources. Despite forming 8.5% of its resident population in 2007, the aged represented approximately 26.6% of public hospital admissions and 9.5% of private hospital admissions in the same year. This has important implications for the demand of healthcare services.

Figure 8: % Population of Residents 65 Years and Above



Source: Singstats, Kim Eng Research

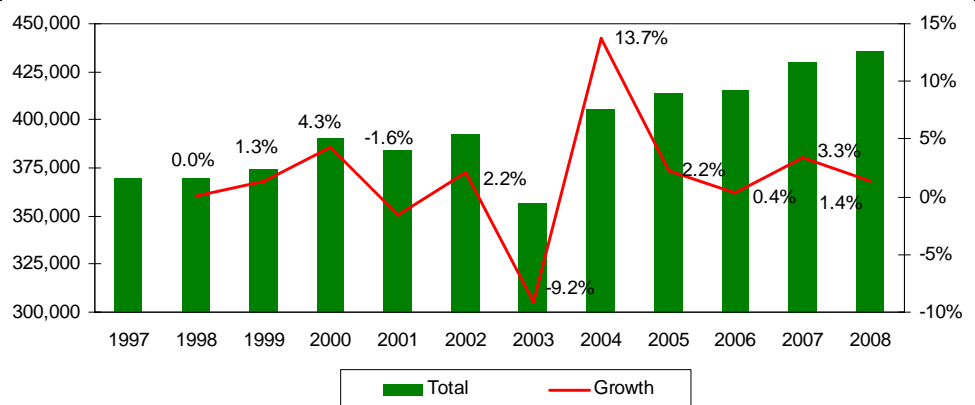
Private Sector market share

Total hospital admissions grew from 369,456 in 1997 to 435,715 in 2008, showing a gradual increase in most years, in line with population growth.

Between 20%-25% historically

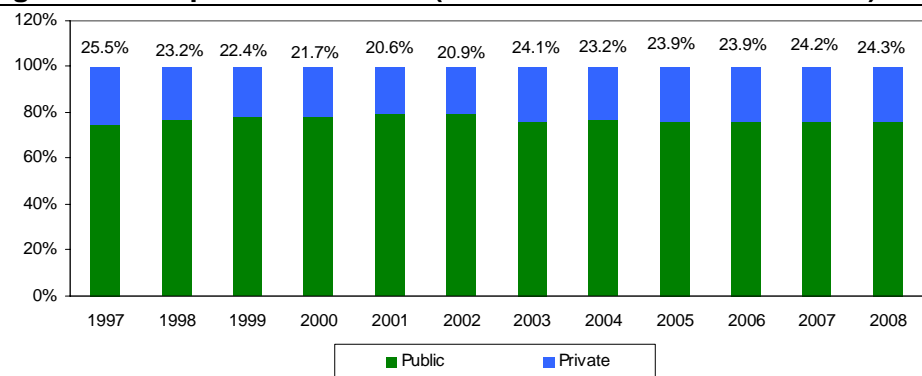
The split between the hospital admissions give us a good gauge of the patient flow between the public and private sectors, even though they do not take into account outpatient attendances. The private sector's share has hovered at around 20.9% to 25.5% for the past 10 years. Due mainly to a decrease in foreign patients, the private sector's market share dropped in the years during the 1998-2002 period.

Figure 9: Total Hospital Admissions



Source: Singstats, Kim Eng Research

Figure 10: Hospital Admissions (Public vs Private market share)



Source: Singstats, Kim Eng Research

Private sector share may increase to 30%

While history may repeat itself again during this economic crisis, the impact will be cushioned by the government’s aim to promote Singapore as a medical hub in the region. Based on a government white paper, the aim is to increase the global market share of foreign patients from less than 1% currently to 3% by 2012. This may involve the increase of the local private sector’s market share from 24.3% to 30%.

More outpatient attendances and day surgeries

With the advent of more efficient medical techniques, medical healthcare is now moving away from a reliance on hospitalisation to more outpatient treatment and day surgeries. Improvements in healing time and post-surgery wounds also result in faster recoveries.

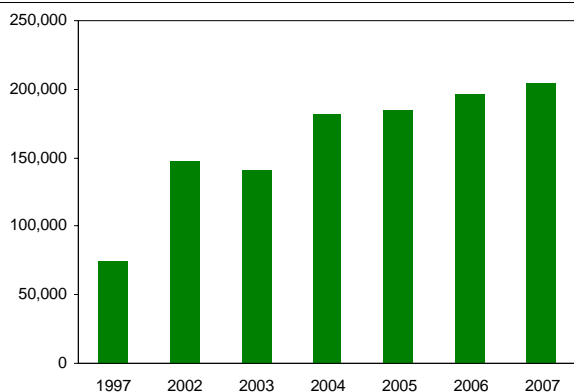
Outpatient attendances belie healthcare demand

Both the day surgery statistics and public sector specialist outpatient attendances over the past 10 years, where numbers have increased much more significantly than hospital admissions, affirm this trend. This implies that the demand for healthcare services have been greater than the hospital admission numbers imply.

More revenue intensity

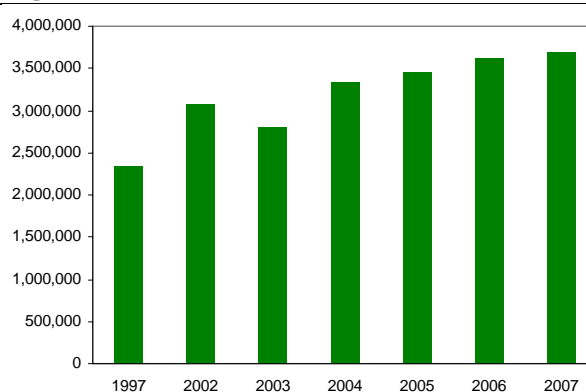
Such a trend that we believe will continue will result in more revenue intensity for healthcare players due to a faster turnaround of patients.

Figure 11: Day Surgeries



Source: Singstats, Kim Eng Research

Figure 12: Public Sector Outpatient Attendances



Source: Singstats, Kim Eng Research

Means testing may shift some demand to private sector

Public healthcare subsidies

The government’s healthcare subsidy plays an important role in the healthcare landscape due to the significant subsidies that residents enjoy. Changes in such policies may have an effect of shifting the demand mix between private and public healthcare. Previously, subsidies are allocated based on the class of inpatient accommodation chosen by patients. Class B2 wards and Class C wards are provided to citizens at subsidy rates of 65% and 80%, respectively. It is, therefore, no surprise that these wards have excess demand, with more than 40% of patients opting for Class C currently.

Effective from 1st Jan 2009

Effective from 1st Jan 2009, patients opting for these wards will be means-tested based on their income (value of homes for non-working). Only patients with a monthly income of less than \$3,200 will continue to enjoy the same subsidy. This income group is smaller than the 40% that has previously opted for Class C. Subsidies for patients with income higher than \$3,200 will decrease accordingly, with the lowest bound of 65% for B2 wards and 50% for C wards for patients earning more than \$5,200. New subsidy policies also apply to Permanent Residents on a lower scale.

These measures appear to be a part of the government's long-term strategy of lowering subsidies for the non-needy and shifting healthcare demand towards the private sector. We believe such moves will continue to benefit the private healthcare players.

Medisave withdrawal limits raised from 1st June 2009

Health Minister Khaw Boon Wan announced revisions to the Medisave limits during the parliamentary session in February 2009. Under the revisions, patients will be able to withdraw more money from their Medisave accounts in their Central Provident Fund (CPF) to pay for their hospital bills than currently. The changes would affect minor to major procedures in 21 categories, depending on their complexity.

Will benefit private hospital patients

The revisions are estimated to benefit mainly those opting for Class A/B1 patients, as well as private hospital patients. For most patients in the B2/C wards, current withdrawal limits are already sufficient to cover most of their bills.

These changes will be funded by a \$700m-increase in the Ministry of Health (MOH)'s \$2b operating budget. We believe this will benefit private hospitals such as Raffles Hospital.

Singapore has poured resources into this area

Target of one million foreign patients by 2012

Having identified the healthcare sector as an area where Singapore can carve a niche in the international market, policy makers have invested significant resources into the healthcare industry to position Singapore as a regional medical hub and a world-class destination for medical tourists.

In 2003, Singapore launched SingaporeMedicine, a multi-agency government-industry partnership, committed to this aim. This is led by the Ministry of Health (MOH) and supported by Economic Development Board (EDB), Singapore Tourism Board (STB) and International Enterprise Singapore (IE Singapore). Singapore hopes to attract one million medical travelers annually. On the back of these strong initiatives, foreign patients have increased at approximately 20% per year, with 410,000 foreign patients treated in 2006.

A blip, but goal is still achievable

Under the current economic conditions, this aim has become more of a challenge. The latest data for 2007 remained mixed, with exit surveys at airports suggesting a 15%-decline in medical travellers for the year. However, the same survey showed that medical tourist spending increased by 30% to \$1.7b for the same period.

With the Singapore healthcare system being consistently ranked to be amongst the best in the world, we still expect the growth trend to continue in the medium-to-longer-term period, even with a possible blip in the current climate.

A Concoction of Quality and Scalability

Major impact on profitability

RMG has fared well historically

Adopted by some top medical institutions

Specialists/doctors are effectively employees

Model is more scaleable

Look out for employee remuneration model

For healthcare providers, employee remuneration typically form the majority of the Group's cost, given that doctors and specialists are highly-paid personnel. We believe the remuneration model is thus an important criterion to study when investing in healthcare providers. In this instance, we believe RMG has fared well historically, with staff costs constituting about 49.0% of revenue in FY08. This percentage has also gone down steadily from 56.4% in 2004.

Group Practice Model

RMG operates a Group Practice Model, which is unique amongst private healthcare organisations in the region. Under this model, doctors work in a multi-disciplinary group, as opposed to individual doctors running their own practices within the Group. With each doctor having their own specialties, they can work in teams to provide integrated and coordinated care for the patients. This Group Practice model is adopted by some of the top medical institutions in the world, such as the Mayo Clinic, Cleveland Clinic and Kaiser Permanente.

Operating Leverage

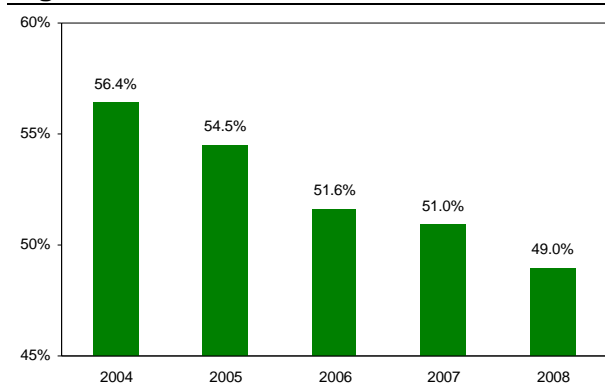
Beyond the medical practice benefit of the Group Practice Model, this business model also provides RMG with more operating leverage than peers due to a higher portion of fixed costs versus variable costs.

In RMG, all its specialists and doctors are effectively employees, with fixed and variable salary components depending on the overall Group and individual performance. This is in contrast to other business models whereby: 1) Each specialist/doctor runs his/her own practice under the Group's umbrella, with the Group taking a cut out of the doctor's individual profit & loss statements; 2) The Group charges the specialists/doctors under its umbrella a fee for providing hospital and other facilities.

We believe RMG's model is more scaleable: as its revenue grows, the Group is better able to extract profitability as the spread between revenue and staff costs widen, hence enriching shareholders' returns. This can be seen in Figure 14 below where RMG has been able to increase its operating margins.

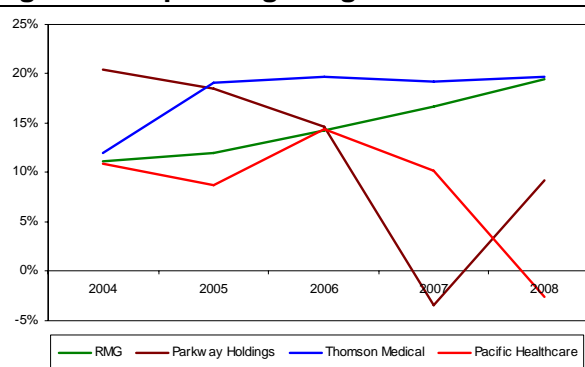
Admittedly, this model may be detrimental in attracting top medical talent, as these individuals would not want their monetary upside to be limited. However, we argue that while the presence of these individuals would lend credibility to the Group, they do not actually enrich shareholders' return significantly as their bargaining position would ensure contracts are skewed highly in their favour.

Figure 13: Staff Cost as % of Revenue



Source: Company, Bloomberg, Kim Eng Research

Figure 14: Operating Margins vs Peers



Source: Company, Bloomberg, Kim Eng Research

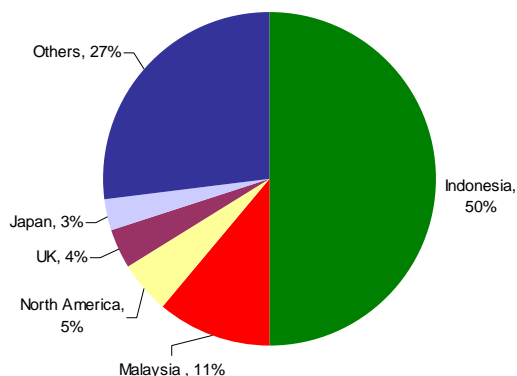
More diversified exposure to foreign patients

In an economic crisis, we believe that the foreign patients segment is typically most at risk due to the amount of destination choices these patients are likely to have. This has proven to be the case in the past Asian crisis when both hospital admissions and day surgeries decreased significantly in 1998. On this front, we believe that Raffles Medical business is relatively more defensive than its peers.

More diversified than peers

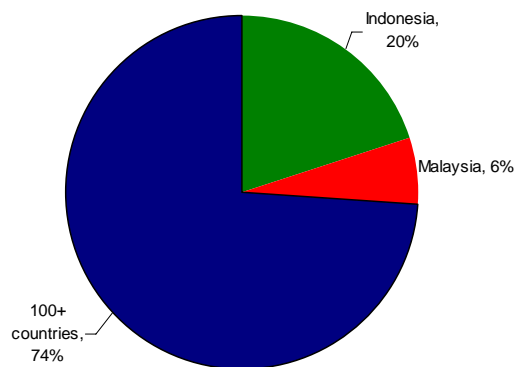
Approximately one-third of its customers in the tertiary and specialist segment are currently foreign patients. Having made efforts to diversify its foreign clientele base, RMG's foreign patients now hail from about 100 countries, with Indonesian clients forming the largest share at 20%. This is more diversified than the whole private sector healthcare industry where it is believed that Indonesian patients form about 50% of foreign patients.

Figure 15: Foreign Patients to Singapore



Source: Ministry of Health, Straits Times, Kim Eng

Figure 16: Foreign Patients to RMG



Source: Ministry of Health, Straits Times, Kim Eng

Primary healthcare is defensive

Primary healthcare provides earnings base

Amongst its peers, RMG also has one of the highest percentage contributions from the Primary healthcare segment. This currently accounts for 37% of its revenue and 18% of its EBIT. While primary healthcare is unlikely to drive overall Group growth due to the lower dollar value of such services, this segment provides a very solid earnings base for RMG.

Corporate clients account for about two-thirds of its primary healthcare patients. These clients typically sign an annual contract with RMG, and are not likely to switch healthcare providers since there are usually no strong incentives to do so. Consequently, we believe that the primary healthcare earnings stream is highly defensive and has good visibility.

GP clinics serve as invaluable referral feed

Other than the direct revenue contributed to the Group, the network of GP clinics also serve as a referral feed for Raffles Hospital. We believe this stream of patients is also more resilient than non-referral hospital patients who are likely to have the sophistication and ability to choose from a wider selection of hospitals.

Licensed to grow

Can ramp up capacity from 200 beds to 380 easily

Ability to ramp up bed capacity

Raffles Hospital currently has 200 operational beds, and is licensed to operate up to 380 beds. According to the management, its occupancy rate currently fluctuates between 40%-60%. We believe this puts RMG in a good position to take advantage of any increase in the volume of private patients.

In anticipation of the growing demand for healthcare services, there are already concrete plans within both the public and private sectors to increase the number of hospital beds and related services. The most significant of these expansions is the Khoo Teck Puat Hospital in Yishun, which is expected to operate 550 beds.

Private sector capacity tight until 2013

However, it is notable that most of the expansion within the private sector would only come onstream in 2013. Furthermore, new hospitals would typically need some time before achieving a more stable state of patient stream. The two years that Raffles Hospital themselves took to break even was considered a notable achievement.

Figure 17: Upcoming Hospital Beds

Public hospitals		
Khoo Teck Puat Hospital	550 beds	2011
Private hospitals		
Farrer Park	200 beds	2011
Novena (Parkway Holdings)	350 beds	2013
West Point Hospital (China Healthcare Group)	200 beds	2013

Source: Kim Eng Research

Current B1 ward users most likely to migrate to private hospital

Price positioning will allow it to take advantage of flight from public

Under its Group Practice model, all prices including consultation and hospital services are set at the sole discretion of RMG. In other private hospitals, specialists retain the right to set their own prices for consultation. Other than giving its patients the benefits of more transparency and standardization in pricing, it also gives RMG the flexibility to remain competitive against its competition.

We think amongst the private hospitals, RMG's pricing makes it most likely to reap the benefits of any migration of patients from public hospitals. We identify these patients to be currently staying in A/ B1 wards where they receive subsidy rates of 0% and 20%, respectively. A class wards are approximately 5-15% pricier than their B1 counterparts.

Figure 18: Average Total Bill (Medical)

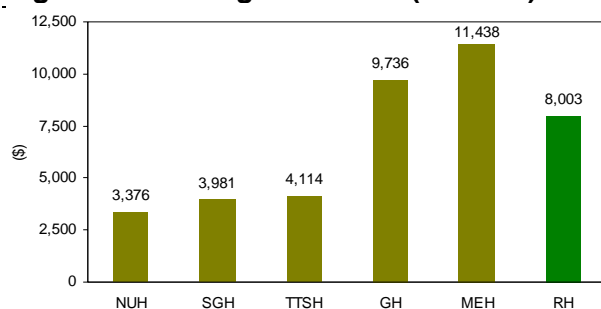
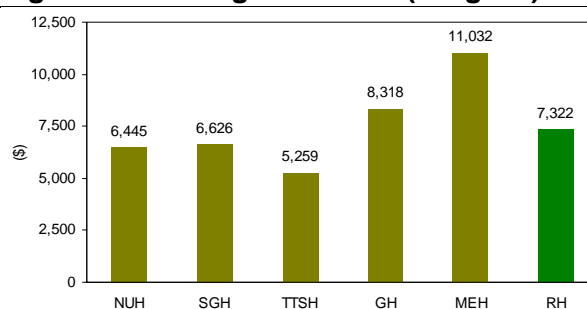


Figure 19: Average Total Bill (Surgical)



Figures based on 2008, figures for NUH, SGH and TTSH are for B1 wards

Source: Ministry of Health, Straits Times, Kim Eng

In a comparison with B1 wards in Figures 18 and 19 above, Raffles Hospital's prices are substantially higher for medical specialties, but only about 20% higher for surgical specialties that can be easily justified by the better bed facilities.

***Less costly than
Gleneagles and
Mount Elizabeth***

In a comparison with the two largest private hospitals, Gleneagles Hospital and Mount Elizabeth Hospital, Raffles Hospital is on average about 24% less costly for both medical and surgical specialties. On this pricing basis, we believe Raffles Hospital represents a more attractive value proposition for upgraders from public hospitals.

***Has been more
conservative than
peers in this respect***

Time to expand overseas

RMG has traditionally avoided aggressive overseas expansion, in comparison to its peers who have expanded abroad aggressively over the past few years. The prudent management has cited reasons such as the higher regulatory risk, as well as being reluctant to split its limited resources to overseas ventures. As a result, other than the clinics in Hong Kong, its concrete overseas expansion has been negligible.

However, with its current robust financial position and asset prices lower than before, RMG is well-placed to make its mark overseas with a lower risk of overpaying for possible acquisitions, in our opinion.

We believe the management is actively looking into this area, with China, India and Southeast Asia as the countries of interest, with a preference for gateway cities. These countries offer potentially large untapped markets, as well as similarities in culture. The possible set-ups include medical centres and clinic chains, Raffles Hospitals, as well as healthcare consultancy and management services.

Financials

FY09 should be brief hiatus in growth

Hospital should continue to be growth driver

We believe that hospital services will continue to be the revenue growth driver during the FY09-FY11 period, given the abundant spare capacity in Raffles Hospital currently, which is in contrast to the overall tight supply of hospital beds in Singapore. With the global economic uncertainty affecting spending, we have forecasted only a growth rate of 5% for this segment in FY09. We believe this should be a brief hiatus, which will be followed by stronger growth of 15% annually for the FY10/FY11 period.

GP clinics unlikely to be affected

As discussed earlier, the healthcare services segment that mainly constitutes the earnings of GP clinics is unlikely to be affected and we continue to forecast a growth rate of 7-10% a year for the FY09-FY11 period, based on the growing population, as well as the increased number of clinics. However, since this segment enjoys much lower margins, it will not contribute as much to overall growth.

Figure 20: Segmental Revenue

Segmental Assumptions	FY07	FY08	FY09F	FY10F	FY11F
Hospital Services Revenue \$m	69.7	81.1	89.2	95.5	102.2
Operating Margin	9.1%	9.2%	9.3%	9.5%	9.5%
Healthcare Services Revenue \$m	106.3	127.8	134.1	154.3	177.4
Operating Margin	18.6%	22.0%	23.5%	24.0%	25.0%

Source: Company, Kim Eng Research

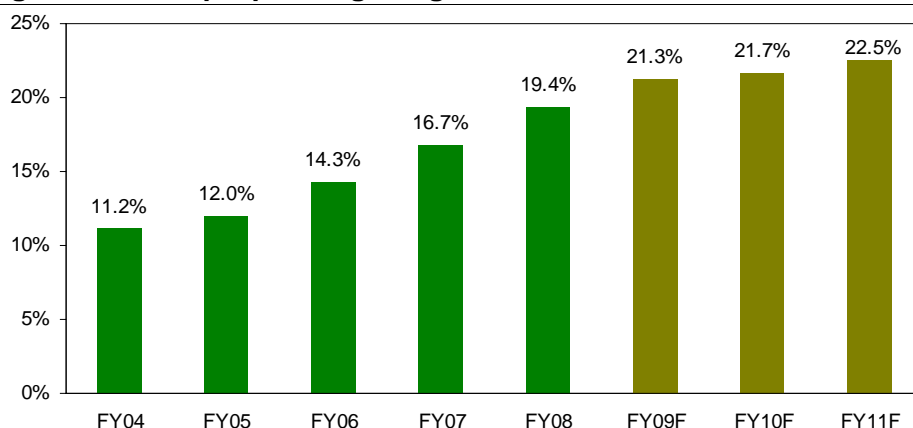
Operating margins will trend higher

Rising operating margins

Operating margins have been improving for the past five years, a trend that we believe is sustainable over the FY09-FY11 period. The management has shown discipline in terms of its operating costs and is committed to continuing this policy. This improvement in its operating margins will be a key factor for profitability growth.

With staff costs constituting about 61% of its total operating costs, marginal improvements would exert an impact on its overall operating margins. We expect staff costs as a percentage of its revenue to decrease from 49% to 47% by FY10, as revenue continues to grow.

Figure 21: Group Operating Margins



Source: Company, Kim Eng Research

Generating more cash than ever before

With a low requirement for inventories (\$4.8m for FY08), and a quick receivables turnaround of less than 45 days historically, RMG generates strong operating cash flow every year.

Aided by acquisition of remaining 50%-stake of Raffles Hospital

In 2007, RMG acquired the remaining 50%-stake of its Raffles Hospital from partner CapitaLand for a sum of \$66.9m. This has effectively reduced its operating lease expenses significantly, though that is offset against higher depreciation and other operating expenses associated with being an owner of the hospital. This has been the main factor in the improvements of its operating cash flow from \$19.7m in FY06 to \$40.1m in both FY07 and FY08.

No major capital expenditure needed to expand local business

Minimal capital expenditure barring major acquisitions

With Raffles Hospital still operating at less than 60% capacity, there is no major capital expenditure needed for the expansion of its business. Barring any major acquisitions or forays abroad, the management has indicated that capital expenditure requirement for the FY09-FY11 period will likely be in the range of just \$3m-\$5m. Even providing for the repayment of its long-term \$22m loan and dividends, RMG will continue to generate very healthy cash flows going forward, even as profitability grows.

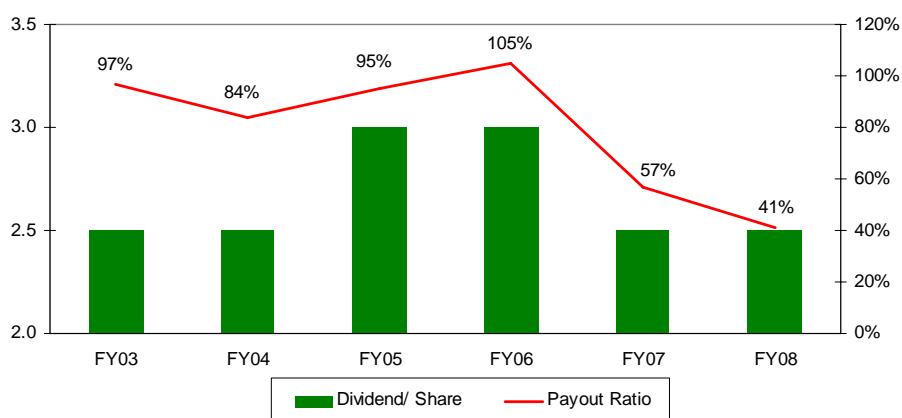
A possible upside to dividend policy

While RMG has no fixed dividend policy, we note that it has had a generous payout ratio in recent history. The Group paid out almost 100% of its earnings from the FY03-FY06 period, prior to its purchase of the 50%-stake of Raffles Hospital from CapitaLand. Since then, we believe the Group has been prudent in paying out a lower amount, after taking on some long-term debt associated with the said purchase.

Could happen in FY09

We believe the management's dividend strategy is to maintain the same dollar amount per share before they are in a more comfortable position to scale up to the next level. Hence, we think that there is a good possibility that this will happen in FY09, given that we estimate a net cash position of \$39.8m, up from \$17.9m the previous year. This would especially be the case, if economic conditions become more certain.

Figure 22: Dividend History and Forecast



Source: Company, Kim Eng Research

Valuation

Free Cash Flow To Equity Valuation

Our FCFE valuation gives us a target price of \$1.38, a 31% upside from the current price of \$1.05. Our target price also implies 20x FY09 estimated earnings. Our conservative model only implies a growth rate of 4.7% in free cash flow over the FY11-FY12 period.

Defensive earnings and strong cash flow generation

We believe an FCFE valuation is the most appropriate valuation matrix for RMG. This method allows us to value the strong cash flow generating nature of its business. The defensive and non-cyclical nature of its business also gives us confidence in the visibility of its future earnings stream.

Figure 23: FCFE assumptions

S\$ m	FY09	FY10	FY11	FY12	FY13
FCFE	20.2	34.3	37.8	39.9	41.5
Terminal Value					779.9
PV	19.0	30.4	31.4	31.2	603.0
Total discounted FCFE	715.0				
Value/ Share	1.38				
Cost of equity	6.8%				
Risk-free rate	2.5%				
Beta	0.66				
Market risk premium	9.0%				
Terminal growth	1.5%				

Source: Bloomberg, Kim Eng Research

Peer Comparison

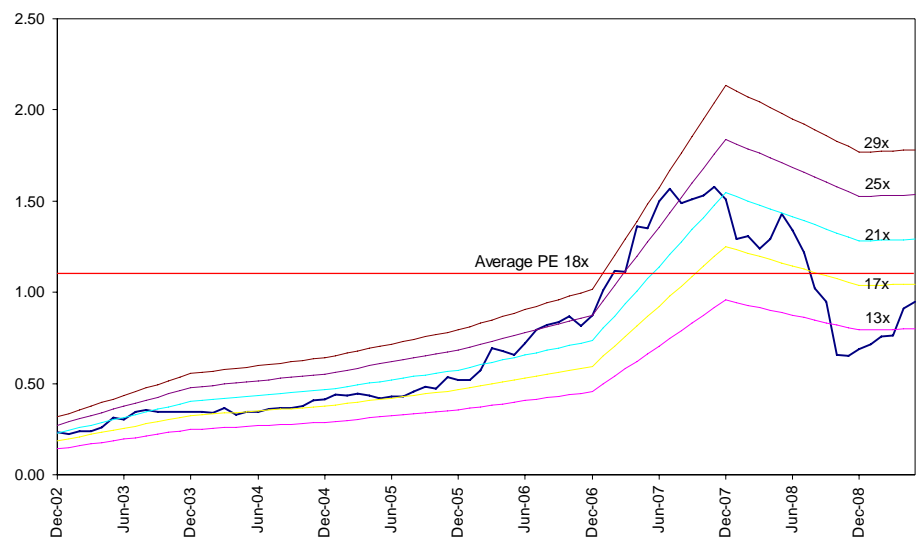
Raffles Medical is currently trading on par with its SGX-listed peers. We believe a premium valuation is justified due to its superior ROE, net margins, lower gearing, as well as its strong track record of profitability.

Figure 24: Peer Valuation

	Share price (lcl curr)	Market Cap (lcl curr)	PE Historic (x)	PE Current (x)	PE Forecast (x)	EPS growth Current (%)	EPS growth Next Yr (%)	Price/ book (x)	ROE (%)	Net Margin (%)	Net Gearing (%)	Div Yield (%)
Raffles Medical	0.98	508.1	16.1	15.8	14.4	1.6	9.7	2.2	14.9	15.7	(8.0)	2.4
Parkway Holdings	1.59	1797.3	46.1	15.6	14.7	195.7	5.9	1.3	3.7	3.7	51.8	2.3
Thomson Medical	0.57	165.0	14.7	12.8	11.3	14.6	13.6	1.5	11.1	18.6	(10.3)	4.4
Pacific Healthcare	0.10	28.1	(2.4)	na	na	na	na	0.6	(23.1)	(14.8)	12.0	na
Healthway Medical	0.13	176.2	13.0	na	na	na	na	1.3	13.5	11.8	44.2	na
China Healthcare	0.16	35.6	51.7	na	na	na	na	1.2	(2.0)	2.0	60.9	na
Average			23.2	14.7	13.5	70.6	9.7	1.4	3.0	6.2	25.1	3.0

Source: Bloomberg, Kim Eng Research

Figure 25: P/E Band



Source: Bloomberg, Kim Eng Research

Average P/E of 18X

RMG has been trading at an average of 18X P/E since 2002, with a peak of 29X and a trough of 13X. With its strong prospects going forward, we believe that RMG should be trading above its average P/E, as implied by our target price that suggests a P/E of 20x.

Key Risks

Change in Government healthcare policies

The healthcare industry is still highly regulated by the government in Singapore, and government policies have a large impact on the sector. The flow of local patients between private and public providers will be highly affected by these policies.

While we are optimistic that private providers such as RMG will continue to thrive under the current conditions, an unexpected change could be negative for the Group. This is more likely if the economic conditions deteriorate, with the government likely to provide more subsidies to citizens, which may tilt the favour towards public hospitals.

Ability to attract talent to its Group Practice Model

Unlike its peers, RMG uses a Group Practice Model that involves its doctors/ specialists coming under the direct employment of the Group and working as part of a team. While this model has proven to be successful in treating its patients, it is not as attractive to professionals who may prefer to set up their own practice as they may enjoy greater profit upside and full control of their practice.

With a limited supply of doctors/ specialists, RMG may face challenges in attracting and keeping its current medical professionals.

Potential overseas ventures could fail

It is notable that the RMG does not have any significant experience overseas other than its four clinics in Hong Kong. Without any track record of success, an overseas venture could involve significant execution risks such as country regulation and the ability to attract medical professionals. Furthermore, unfamiliarity in overseas market could possibly result in RMG overpaying for any possible acquisitions abroad.

Deeper recession than expected

Should the current global recession turn out to be longer and worse than expected, the private healthcare sector could be adversely affected. Private healthcare is still considered discretionary consumer spending in many instances. Prolonged lower income levels and economic pessimism could lead to more patients switching to cheaper public alternatives.

While we are confident in RMG's defensive positioning within the private healthcare sector, growth could still be negatively impacted by such a situation.

Appendix

Board of Directors

Dr Loo Choon Yong: Chairman and Co-Founder

Dr Loo co-founded the Group in 1976 and was appointed as Executive Chairman in 1997. He was appointed by the President of Singapore as the Ambassador to the Italian Republic from March 2006 and the Nominated Member of Parliament from January 2007. Besides his medical training, Dr Loo also read Law at the University of London. He was awarded the Public Service Medal in 2003 and the Distinguished Service Award in September 2005 from the Ministry of Home Affairs for contributions to Singapore's fight against drug abuse.

Dr David McKinnon Lawrence: Independent Director

Dr Lawrence joined the Board in 1997 and currently serves on the Boards of Agilent Technologies, Dynavax Technologies Corporation, McKesson Corporation and the Rand Health Advisory Board, among others. He is the retired Chairman and CEO of Kaiser Foundation Health Plan, Inc and Kaiser Foundation Hospitals, in the United States.

Associate Professor Wee Beng Geok: Independent Director

Dr Wee joined the Board in 2000 and is Associate Professor of Strategy, Management and Organisation at the Nanyang Business School. She has worked both in the corporate sector and academia, and held management positions in various companies.

Mr Tan Soo Nan: Independent Director

Mr Tan joined the Board in 2000 and is the CEO of Singapore Pools (Private) Limited, a wholly-owned subsidiary of the Singapore Totalisator Board. He is also a Member of the Income Tax Board of Review, Goods and Services Tax Board of Review, and the Council Member of Football Association of Singapore. Mr Tan was formerly the CEO of Temasek Capital (Private) Limited and the Senior Managing Director of DBS Bank.

Professor Lim Pin: Independent Director

Professor Lim Pin joined the Board in 2001, and is Professor of Medicine at National University of Singapore and Senior Consultant Endocrinologist at the National University Hospital. He was the former Vice Chancellor of NUS from 1981 to 2000. Prof Lim chairs the National Wages Council and several other committees including the Singapore-MIT Alliance for Research and Technology.

Shareholding structure

Dr Loo, the founder and chairman is currently the substantial shareholder, with a deemed interest of 40%. While there are no other named parties with a more than 5% substantial interest, both Temasek Holdings (through V-Sciences Investments) and Qatar Investment Authority (the investment arm of the Government of Qatar) subscribed for 25 million shares or 4.87% in June 2007. During this exercise, RMG placed out 50 million shares for a net proceed of \$63m to fund the purchase of the other 50%-stake in Raffles Hospital. We believe both parties are still holding at least the same amount of shares currently.

Figure 26: Shareholding Structure

Substantial Shareholders	Shares held
Dr Loo	40.01%
Temasek Holdings	4.84%
Qatar Investment Authority	4.84%

Source: Company, Bloomberg, Kim Eng Research

Profit and Loss

YE Dec (\$ m)	2007	2008	2009F	2010F	2011F
Sales	168.7	200.8	214.0	238.4	266.0
Consumables & services	(31.3)	(35.5)	(36.4)	(40.5)	(45.2)
Staff costs	(85.9)	(98.3)	(102.7)	(112.0)	(125.0)
Depreciation	(4.2)	(6.6)	(7.3)	(7.5)	(7.7)
Operating lease	(9.8)	(4.5)	(4.5)	(4.5)	(4.5)
Other op expenses (net)	(9.3)	(16.9)	(17.6)	(22.0)	(23.8)
Operating profit	28.2	39.0	45.5	51.8	59.8
Financing costs	(0.4)	(0.6)	(0.8)	(0.7)	(0.6)
Share of joint entity	13.6	0.0	0.0	0.0	0.0
Pretax income	41.4	38.4	44.7	51.1	59.1
Income taxes	(5.5)	(6.7)	(7.6)	(8.7)	(10.1)
Minority interest	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Net profit attributable	35.9	31.5	37.0	42.3	49.0
Net profit (normalized)	23.4	31.5	37.0	42.3	49.0
EPS (SG cents)	0.0	0.0	0.0	0.0	0.0
EBITDA	32.5	45.6	52.9	59.3	67.5

Source: Company data, Kim Eng estimates

Cashflow

YE Dec (\$ m)	2007	2008	2009F	2010F	2011F
Operating cash flow	40.1	40.1	39.5	48.7	53.2
Pretax profit	41.4	38.4	44.7	51.1	59.1
Depreciation & amortization	4.3	6.7	7.4	7.5	7.7
Change in working capital	13.3	(1.8)	(4.4)	(0.2)	(3.5)
Others	(18.9)	(3.1)	(8.3)	(9.6)	(10.2)
Investment cash flow	(52.8)	(5.0)	(4.5)	(4.5)	(4.5)
Net capex	(4.3)	(6.1)	(5.0)	(5.0)	(5.0)
Acquisition of sub	(64.0)	0.0	0.0	0.0	0.0
Others	15.5	1.2	0.5	0.5	0.5
Financing cash flow	(9.2)	(10.7)	(19.7)	(15.0)	(15.0)
Dividends	(17.8)	(12.9)	(12.9)	(12.9)	(12.9)
Net change in debt	(60.3)	0.9	(6.6)	(2.0)	(2.0)
Issue of shares	69.0	1.3	0.0	0.0	0.0
Others	(0.1)	0.0	0.0	0.0	0.0
Net cash flow	(22.0)	24.4	15.3	29.2	33.6

Source: Company data, Kim Eng estimates

Balance Sheet

YE Dec (\$ m)	2007	2008	2009F	2010F	2011F
Total assets	281.5	310.4	324.9	355.1	390.1
Current assets	44.5	74.2	91.0	123.8	161.4
Cash	19.7	44.5	59.8	89.0	122.6
Inventories	3.8	4.8	4.8	5.4	6.0
Receivables	20.2	24.9	26.4	29.4	32.8
Others	0.7	0.0	0.0	0.0	0.0
Long term assets	237.0	236.2	233.9	231.4	228.7
Plant and equipment	150.8	150.3	147.9	145.4	142.7
Intangibles	0.3	0.3	0.2	0.2	0.2
Investment properties	84.4	84.4	84.4	84.4	84.4
Others	1.5	1.3	1.3	1.3	1.3
Total liabilities	80.4	88.2	78.6	79.4	78.3
Current liabilities	79.7	65.4	57.8	60.7	61.6
Payables	47.7	51.5	48.7	52.0	52.5
ST borrowings	25.3	4.6	0.0	0.0	0.0
Others	6.7	9.3	9.1	8.7	9.0
Long-term liabilities	0.7	22.7	20.7	18.7	16.7
LT borrowings	0.0	22.0	20.0	18.0	16.0
Others	0.7	0.7	0.7	0.7	0.7
Shareholder's equity	200.8	221.9	246.0	275.4	311.4
Paid-in capital	170.0	171.3	171.3	171.3	171.3
Reserve	30.8	50.6	74.7	104.0	140.1
Minority interests	0.2	0.3	0.3	0.3	0.3

Source: Company data, Kim Eng estimates

Key Ratios

YE Dec (\$ m)	2007	2008	2009F	2010F	2011F
Growth (% YoY)					
Sales	25.6	19.0	6.6	11.4	11.6
Operating Profit	46.9	38.1	16.9	13.8	15.4
EBITDA	43.5	40.5	15.9	12.1	13.8
Net Profit	48.7	35.0	17.4	14.2	15.8
EPS	83.7	(12.4)	17.4	14.2	15.8
Profitability (%)					
Gross margin	Na	Na	Na	Na	Na
Operating margin	16.7	19.4	21.3	21.7	22.5
EBITDA margin	19.3	22.7	24.7	24.9	25.4
Net profit margin	21.3	15.7	17.3	17.7	18.4
ROA	12.8	10.2	11.4	11.9	12.6
ROE	17.9	14.3	15.1	15.4	15.8
Stability					
Gross debt/equity (%)	12.6	12.0	8.1	6.5	5.1
Net debt/equity (%)	2.7	(8.1)	(16.2)	(25.8)	(34.2)
Int. coverage (X)	75.0	62.6	56.9	72.0	93.4
Int. & ST debt coverage (X)	1.1	7.4	56.9	72.0	93.4
Cash flow int. coverage (X)	(58.4)	39.1	19.1	40.5	52.5
Cash flow int. & ST debt (X)	(0.9)	4.7	19.1	40.5	52.5
Current ratio (X)	0.6	1.1	1.6	2.0	2.6
Quick ratio (X)	0.5	1.1	1.5	2.0	2.5
Net debt/(cash) (\$ m)	5.5	(17.9)	(39.8)	(71.0)	(106.6)
Per share data (\$ cent)					
EPS	7.0	6.1	7.2	8.2	9.5
CFPS	(4.1)	4.6	2.9	5.5	6.3
BVPS	38.9	42.9	47.5	53.2	60.1
SPS	31.7	37.6	40.1	44.6	49.8
EBITDA/share	6.1	8.5	9.9	11.1	12.6
DPS	2.5	2.5	2.5	2.5	2.5

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

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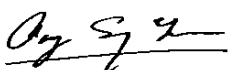
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