Health Management International

Heading for another leg up

SINGAPORE | HEALTHCARE| INITIATION

10 March 2017

Buy (Initiate)

LAST CLOSE PRICE	SGD 0.610
FORECAST DIV	SGD 0.003
TARGET PRICE	SGD 0.83
TOTAL RETURN	36.6%

- Increased capacity, stronger patient demand, and higher revenue intensity to boost revenue growth at 11.5% CAGR over the next five years.
- Quality medical services and improved economies of scale will lead to margin expansion. Robust margin coupled with consolidation of hospitals ownership could translate to 38.0% CAGR in PATMI over the next five years.
- Initiate with "**Buy**" rating and **SGD0.83 TP**, implying a 36.6% upside.

Company Background

Health Management International Ltd ("HMI") is a growing private healthcare provider in Malaysia. The Group's key assets comprise of two tertiary hospitals in Malaysia, the 288-bed capacity Mahkota Medical Centre ("MMC") in Malacca and the 218-bed capacity Regency Specialist Hospital ("RSH") in Johor. These hospitals are supported by a network of 17 patient referral centres across the region. The Group also owns and operates the HMI Institute of Health Sciences ("HMI-IHS") in Singapore.

Investment Merits

1. **Expansion will provide the next leg of growth.** Expansion pipeline set for the next three years: (i) a new ward with c.30 operational beds to be added to each of MMC and RSH by 1H FY2018, and (ii) a Hospital Extension Block at RSH by FY2020. This implied a 14.9% increase in total operational beds in the next one year and more than doubling the existing capacity (in terms of area) at RSH three years from now. We expect revenue to grow at 11.5% CAGR over the next five years, supported by a strong patient load, higher revenue intensity, and expanding capacity. Next prospective expansion in the long term could be a new hospital extension for MMC.

2. **Superior EBITDA and EBIT margins compared to peers, which we view as sustainable and is still growing on improving economies of scale.** Comprehensive multi-specialist hospital focused on middle to upper income patients, with unique business model, provides resiliency in patient volume, as well as helped to attract and retain top specialist doctors. Being a tertiary healthcare provider and delivery of quality medical services warrant a higher average hospital bill size. Scalable model enables it to gain economies of scale as it expands. In near term, we expect EBITDA margin expansion will mainly come from its Hospital segment as RSH has just turned profitable in FY2014. HMI's Hospital FY2016 EBITDA is at 24.8%, with MMC's at 27.5% vs RSH's 19.8%.

3. **Exceptional track record to showcase its core expertise in hospital management and enjoying its first mover advantage.** It managed to turnaround two hospitals within five years since commissioning. Early mover in medical tourism: In adopting independent clinic model and in accrediting HMI under the Singapore Medisave scheme.

4. **Cleaner structure by consolidating the ownership of its two hospitals**, i.e. from 48.9%-owned MMC and 60.8%-owned RSH to 100% each. The Group expects to complete the consolidation transaction by end March 2017. We deem the consolidation as favourable as (i) the transaction is 30.4% accretive to HMI on a FY2016A fully diluted EPS Pro Forma basis, and (ii) HMI's group structure will be clearer with no significant non-controlling interest ("NCI").

Initiate coverage with "Buy" rating with a DCF valuation of S$0.83. We believe that healthcare has a long-term investment potential. Asia's favourable socio-economic landscape and supportive government policies underpins medical tourism in Malaysia. We expect earnings to grow 38.0% CAGR over the next five years, following the consolidation of NCI, expanding capacity, and realisation of operating efficiencies.

COMPANY DATA

O/S SHARES (MN) :	589
MARKET CAP (USD mn / SGD mn) :	253 / 359
52 - WK HI/LO (SGD) :	0.75 / 0.31
3M Average Daily T/O (mn) :	0.75

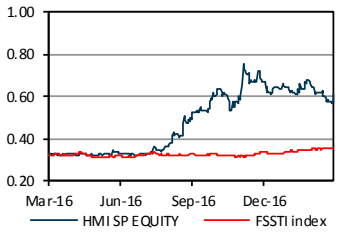
MAJOR SHAREHOLDERS (%)

Nam See Investment Pte Ltd	52.4%
Kabouter Management LLC	8.3%
Cheah Way Mun	2.8%
Gan See Khem	17%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	(11.8)	(13.1)	88.7
STI RETURN	2.63	6.77	17.68

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Jun	FY15	FY16	FY17F	FY18F
Revenue (RM mn)	345	398	449	494
EBITDA (RM mn)	73	85	87	98
NPAT (RM mn)	28	20	31	60
EPS (RM cts)	4.79	3.45	4.45	7.42
EPS (S cts)	1.65	1.15	1.42	2.36
PER, adj. (x)	21.5	29.3	43.0	25.8
P/BV, x	4.1	3.4	5.0	4.7
DPS (S cts)	-	0.25	0.29	0.48
Div Yield (%)		0.7%	0.5%	0.8%
ROE (%)	21.7%	12.6%	14.2%	20.2%

Source: Bloomberg

VALUATION METHOD

DCF (WACC: 7.0%; terminal g: 1.0%)

Soh Lin Sin (+65 6212 1847)
sohls@phillip.com.sg

MCI (P) 118/10/2015
Ref. No.: SG2017_0060

Investment Thesis

– Expansion to bring double digit growth in next five years

1. Organic growth machine, growth pipelines set to see PATMI to grow at 11.5% CAGR in the next five years.

Hospital Services contributed 97.6% to FY2016 Revenue, with the remaining 2.4% are derived from Healthcare Education and Training.

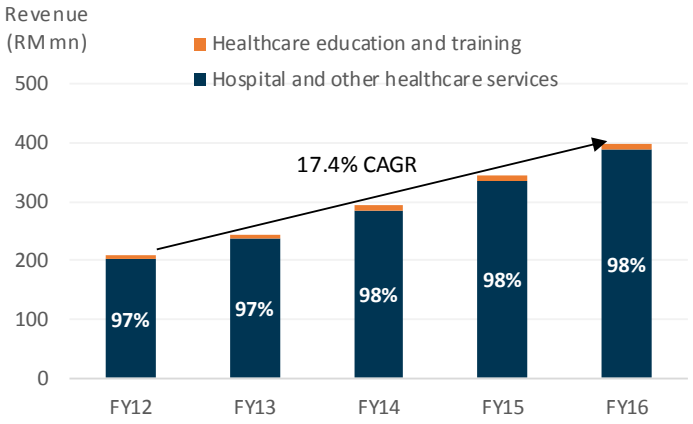
Generally, a private hospital bills has two components, i.e. the doctors' professional fees and the hospital charges. Doctor's professional fees include consultation and procedure fees. While hospital charges include sale of drugs and medical supplies, use of facilities (such as operating theatre, diagnostics, beds, etc.), nursing charges and laboratory tests.

Malaysia's healthcare fees are regulated under the Private Healthcare Facilities and Services Act 1998 and Regulations 2006. The professional fees of doctors are controlled with a maximum ceiling. However, the cost of hospital care, day surgeries, screening and diagnosis services, ambulance services, and clinical laboratories, are not covered under these Acts.

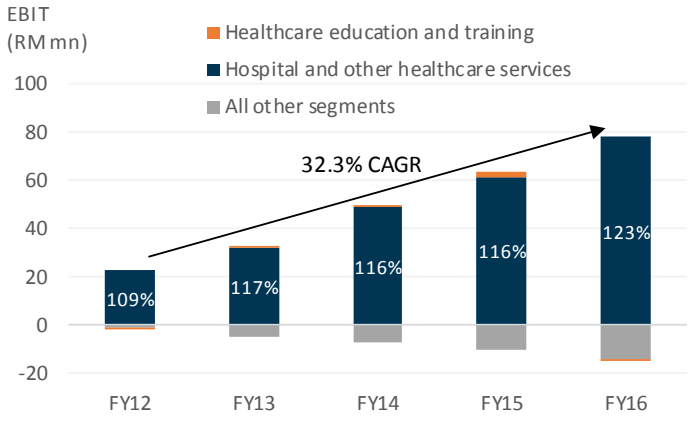
As all partner doctors are independent practitioners, HMI is partially cushioned from the risk of margin compression arising from increasing doctors' fees. On the other hand, to achieve the higher end of average bill size per patient would critically depend on the number of complex cases treated in the hospitals and the utilisation of its services and facilities.

Revenue grew at a 4-year compounded annual growth rate ("CAGR") of 17.4% from FY2012 to FY2016; while EBIT jumped at 32.3% CAGR in the same period. The stellar performance over the past five years was due to (i) increased patient load, (ii) more specialist consultants recruited, and (iii) higher average bill size per patient. The three factors interlink with each other.

Figure 1 & 2: *Hospital and other healthcare services* is the major contributor of HMI's Revenue and EBIT



Source: Company, PSR



Source: Company, PSR

(a) Growing patient base will continue to propel net revenue from HMI's hospitals

Favourable social demographics (such as burgeoning middle income, ageing populations, and increasing health awareness, etc.) and continued growth of the private insurance market will continue to drive the demand for quality healthcare services in Malaysia.

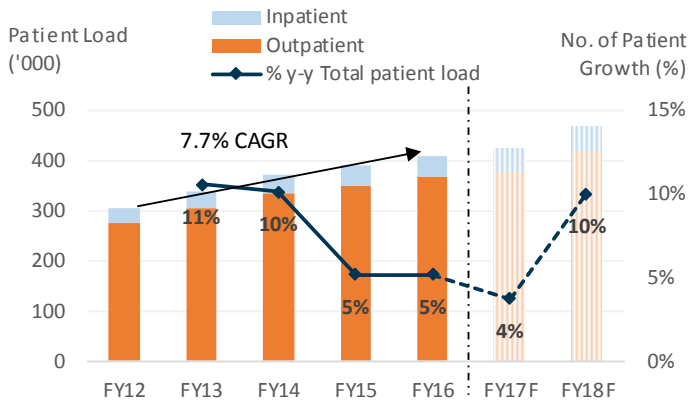
(b) Access to specialists and sub-specialists spur patient volume and average bill size

Net revenue from hospital grew at 17.7% CAGR during FY2012 to FY2016, driven by growth in: patient load in both hospitals (at 7.7% CAGR); and average bill size per patient (at 9.3% CAGR).

In FY2012, an average Inpatient Bill size is c.16x more than an average Outpatient Bill size. As its range of specialty and sub-specialty consultants expanded over the years, revenue intensity and the number of complex cases increased. Growth in average Inpatient Bill size outpaced that of Outpatient's, with CAGRs of 20.8% and 8.0% respectively during FY2012 to FY2016. As in FY2016, an average Inpatient Bill size is c.38x more than an average Outpatient Bill size.

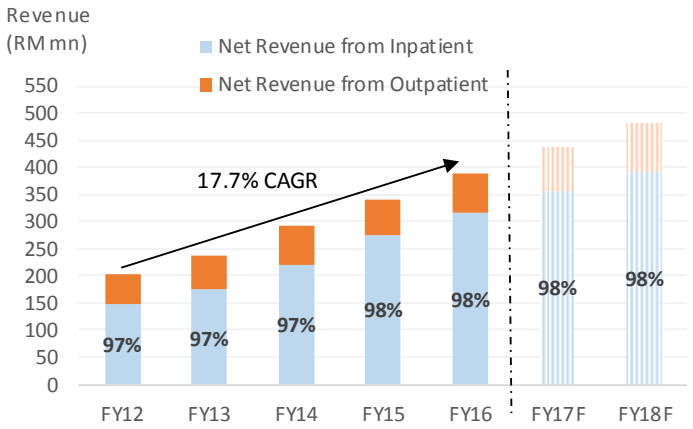
We expect the CAGR for patient load at average bill size to increase at 7.7% and 9.0%, respectively over the next five years, driven by expanding inpatient bed, medical consultants, facilities and services.

Figure 3: Growing patient base from both *Outpatient* and *Inpatient*



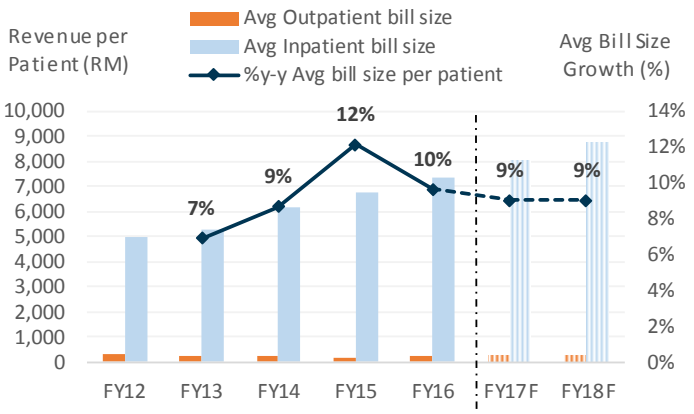
Source: Company, PSR

Figure 4: Inpatient accounts for 11% of total patient load, but contributed 82% of FY15-16 Net Revenue from Hospital



Source: Company, PSR

Figure 5: Favourable mix lifts average bill size per patient



Source: Company, PSR

Inpatient Bill is the main driver for Hospital and other healthcare services revenue growth

(c) Tapping on growing medical tourism to expand patient base and boost average bill size

According to Malaysia Healthcare Travel Council* (MHTC), the number of healthcare travellers in Malaysia registered a 7.3% CAGR over 2011 to 2015. In 2015, it attracted over 850,000 medical tourists in 2015 and HMI had about 10% market share of it.

In addition, medical tourism is lucrative business for HMI as foreign patients tend to seek more intensive and costly treatment compared to local patients. MHTC estimated about RM1 billion revenue from medical tourism in Malaysia in 2016 (0.08% of 2016 Malaysia GDP) and expects to grow 30% in 2017.

Strategic location and favourable macro backdrop has put HMI in a sweet spot to capture demand from foreign patients. By providing same-day surgeries, HMI helps to save time and limit travel costs for foreign patients.

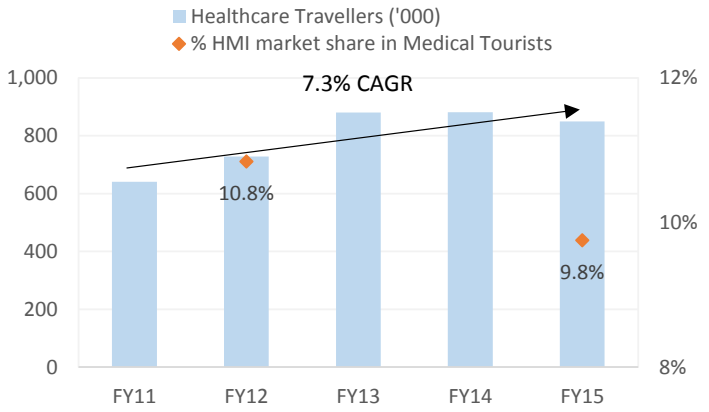
Foreign patient mix in HMI was consistent across past nine quarters at 21% of total patients. HMI is one of the hospital partners with Malaysia Healthcare Travel Council as a Partner Healthcare Provider; while its network of 17 regional patient representative offices would help to promote and cater for foreign patient demand.

Various government marketing efforts as well as improving flight and land connectivity could spur medical tourism in Malaysia. **Prospects for medical tourism have heighten by recent developments in Malacca**, namely (i) the construction of a new off-shore trading port in Malacca (dubbed "the Melaka Gateway"); and (ii) the expansion of Malacca International Airport. The Melaka Gateway is expected to complete by 2025. Upon completion, it is expected to bring in an additional 2.5 million international tourist arrivals per year to Malaysia. *(Source: Melaka Gateway official website)*

**MHTC is "an agency under the Ministry of Health (MOH) Malaysia, tasked to raise Malaysia's profile as the world's top-of-mind destination for world class healthcare services. Established in 2009, MHTC functions to facilitate the overall development of the Malaysian healthcare travel industry."*

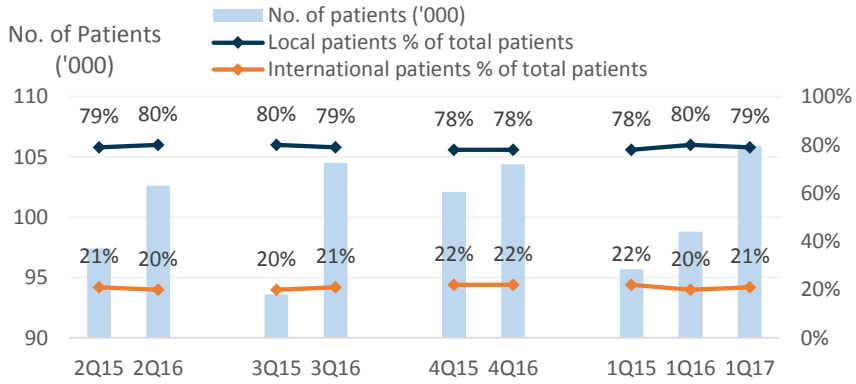
(Source: Malaysia Healthcare Travel Council Official Website)

Figure 6: HMI contributes a significant share of foreign patients to Malaysia's medical tourism market



Source: Malaysia Healthcare Travel Council Website, Company, PSR

Figure 7: Stable patient mix



Source: Company, PSR

(d) Expanding inpatient beds, facilities and services enable HMI to absorb the growing demand

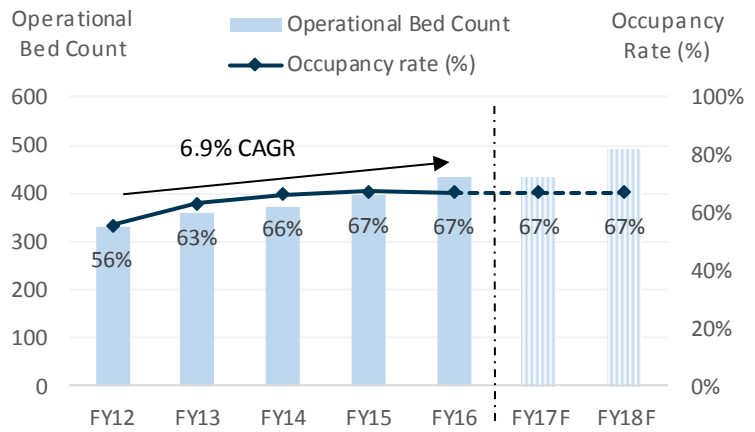
HMI's operational beds grew at 5-year CAGR of 6.9%. Its ability to maintain occupancy rate at above 60% within the same period is a testament to its ability to draw patient demand. Within the same period, its Net Revenue from Hospital grew at 18% CAGR.

Due to strong patient demand, it intends to add a new ward to each of MMC and RSH by 1H FY2018 (end-CY2017), which will add c.30 new beds to each of the hospitals. We expect HMI to be able to maintain its occupancy rate at c.70%. We also took a conservative assumption where its c.14% increase in total inpatient beds in 1H FY2018 would support a c.10% growth in Net Revenue from Hospital.

In medium term, RSH will add a Hospital Extension Block by FY2020 to cope with the overstretched bed capacity. The new Hospital Extension Block was initially planned for Medical Block construction (which consists mainly of clinic suites). It was then re-designed to fit in more inpatient beds, clinical service areas, operating theatre capacity, as well as clinic suites. We expect a full impact kick-in by FY2021.

We expect its combined effort to grow its key disciplines, recruit new consultants, opening more Centres of Excellence ("COEs"), launching new services, and expand its marketing network both locally and overseas, to translate to 11.5% of top line growth per year over the next five years.

Figure 8: Additional bed capacity to meet growing inpatient demand



Source: Company, PSR

Figure 9: HMI's strategic positioning and growth plan

Hospital	Number of Beds and Doctors	Expansion Plan	Competitive Advantage
Mahkota Medical Centre ("MMC")	288 bed capacity (operational bed 266); Over 120 practising consultants (with c.90% are resident consultants)	**New facilities and services** ▪ Further development of COEs ▪ Continue to invest in new services and recruit new sub-specialists – such as nuclear medicine. ▪ Continue to build clinical services and inpatient bed capacity within the existing hospital building, to maximise the current facilities before undertaking the next phase of expansion. Renovation of new ward (with additional c.30 beds) is expected to commission and complete in 1H FY2018. **Potential to build new hospital extension on adjacent plot of land**	▪ **Most comprehensive multidisciplinary private hospital** at south of Kuala Lumpur. ▪ **Strong brand recognition** in Malaysia and Indonesia. ▪ **First** in Malacca, and **probably the only one** in Malacca, to install a Positron Emission Tomography ("PET") scanner. The newly installed PET CT started operations in 2Q FY2017. The Ministry of Health's zoning requirements deter competitors within 30km radius of HMI (almost the entire Malacca) to obtain a PET scanner license. In the past, patients in the vicinity would either be referred to hospitals in Kuala Lumpur or Johor Bahru. Now, MMC dominates diagnostic nuclear imaging service in Malacca while offers hospitals in vicinity a nearer solution.
Regency Specialist Hospital ("RSH")	218 bed capacity (operational bed 166); Over 70 practising consultants (with c.40 resident consultants)	**New facilities and services** ▪ Continue to invest in new services and recruit new sub-specialists – such as developing a cancer centre. ▪ New ward (with additional c.30 beds) to be added in 1H FY2018. **New hospital extension block** ▪ The 10-Storey hospital extension wing will more than double existing capacity at the hospital with more inpatient beds, clinical service areas, operating theatres as well as clinic suites. ▪ Pending approval from relevant authorities to start construction. Nonetheless, construction is expected to commence in 1H FY2018, and take up to 2.5 years to complete. **Potential for medical tourism from regional markets** ▪ Recently started its marketing outreach to international patients, in particular from Indonesia and Singapore. ▪ **One of the two hospitals** in Johor, Malaysia, **approved for Medisave use** (offers a stronger value proposition for Singapore patients).	▪ **Only private hospital in Malaysia** to have 24-hour A&E staffed by emergency specialists. ▪ **Closest tertiary hospital** to Pasir Gudang industrial area and new RM60 billion Petronas oil refinery-petrochemicals complex. Strategic location enables RSH to attract corporate clients within its catchment area.

Source: Company FY2016 Annual Report, PSR

2. Improving and sustainable superior EBITDA margin compared to local peers

(a) Economies of scale and service mix enable HMI to enjoy a robust EBITDA margin

- A resilient, competitive and scalable business model. Its non-cosmetic nature services (its full range of diagnostic, radiology and clinical laboratory services, and non-elective surgery) provide a stable revenue base, as they are more price-inelastic and less susceptible to economic downturn.
- Positioned as a comprehensive one-stop centre for specialist healthcare services. Its specialised centres and extensive complement of medical and diagnostic equipment housed under the same building provide a holistic customer-oriented experience and attract referral of complex cases.
- As HMI focuses on complex and surgical cases, it commands a higher than peers' average Inpatient Bill size. Its advanced medical and diagnostic equipment, such as Magnetic Resonance Imager ("MRI") and 64-slice Computed Tomography ("CT") scanner, also support the delivery of quality medical services. These equipment not only serve internal patients but also capture external demand of referral patients from smaller scale clinics or public and private hospitals in vicinity which lack scale and funding to invest into such expensive capital assets.
- The ready specialist and inpatient capacities enable HMI to respond to critical care cases, acute, severe and emergency cases. Handling of more complex cases could demand a higher price, lifting average hospital bill size per patient and thus EBITDA margin. We expect the average bill size to increase at a CAGR of 9.0% over the next five years, and EBITDA margin for Hospital segment to expand to 25.1% in FY21F from FY16's 24.8%.
- Sale of medical suites to resident consultants provides additional income to HMI, and helps with doctors' retention as all partner doctors are independent practitioners.

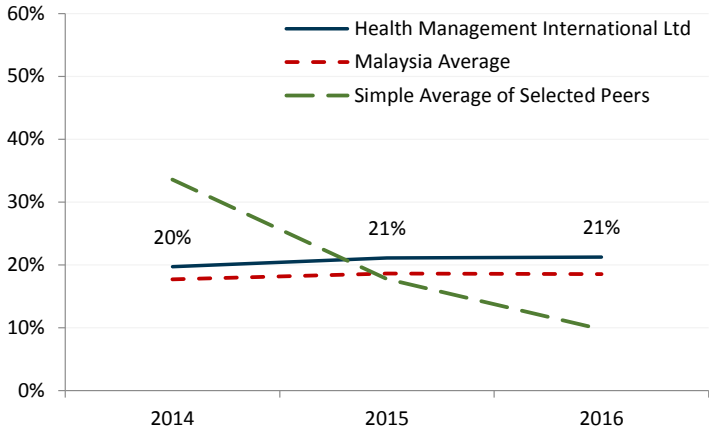
(b) One of the highest margins in Malaysia and room to improve

These effectively elevated HMI's *hospitals services* PBT margin* to 20%, which is comparable to Parkway Pantai's 21% and more than double of KPJ's 8%.

Compared to a selected group of key domestic and regional healthcare service providers, HMI's EBITDA and EBIT margins have improved to surpass its peers.

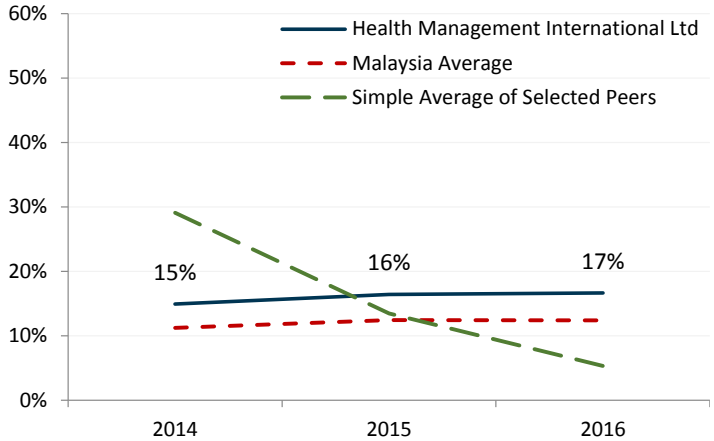
**Both Parkway Pantai and KPJ have strong presence in Malaysia's private healthcare service market. Here, we compare only the PBT margins derived from hospital and support services from respective healthcare groups.*

Figure 10: HMI's EBITDA Margin VS Selected Peers'



Source: Bloomberg

Figure 11: HMI's EBIT Margin VS Selected Peers'



Source: Bloomberg

Figure 12: HMI's 3-year average performances VS Selected Peers'

Company	3-Year Avg Revenue Growth	3-Year Avg EBIT Margin	3-Year Avg Net Margin
Health Management International Ltd	17%	16%	6%
Singapore			
Raffles Medical Group Ltd	12%	19%	17%
Singapore Medical Group Ltd	22%	-4%	2%
International Healthway Corp Ltd	N/A	78%	77%
Healthway Medical Corp Ltd	6%	12%	-9%
AsiaMedic Ltd	12%	2%	-4%
Singapore Average	13%	21%	16%
Australia			
Ramsay Health Care Ltd	28%	10%	6%
Healthscope Ltd	1%	12%	2%
Pulse Health Ltd	15%	3%	0%
Australia Average	15%	9%	3%
Malaysia			
IHH Healthcare Bhd	14%	16%	9%
KPJ Healthcare Bhd	9%	8%	5%
Malaysia Average	12%	12%	7%
Simple Average (Excl. HMI)	13%	16%	10%

Source: Bloomberg

**Parkway Pantai Limited is part of the IHH Healthcare Berhad Group.*

As RSH is a relatively younger hospital with less than ten years history compared to MMC's 20 years, it has much room to grow. It could further scale up its bed capacity within existing plot of land, number of consultants, services and expand its patient base to international patients.

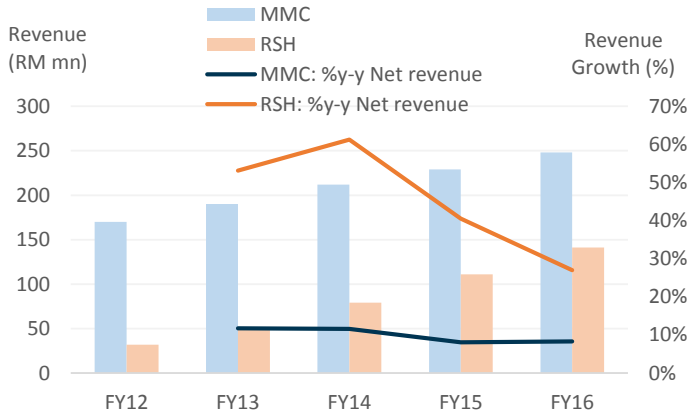
RSH turned profitable in FY2014 and recorded an explosive growth in the past five years. We expect RSH growth to normalise to MMC's level but picks up momentum again when the new extension block is ready by FY2020.

We also think that RSH's margins will continue to improve to par with MMC's, as it starts to gain economies of scale. MMC has a better EBITDA margin at 27.5% in FY2016; while RSH's is at 19.8%.

Large scale with high patient load allows (i) high EBITDA margins, (ii) ability to attract consultants, and (iii) justify investment in latest medical equipment.

Furthermore, the proposed consolidation should boost EBITDA margin in near term. The consolidation in the ownership of MMC and RSH to 100% each would increase scale, enable HMI to further optimise operating leverage, better management of cost pressures, such as rental, purchasing cost and staff cost.

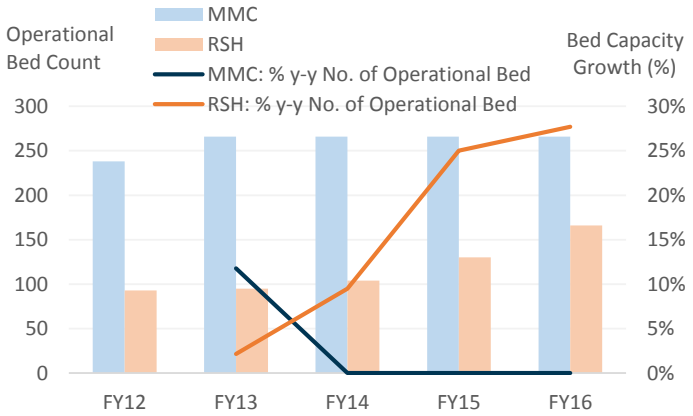
Figure 13: RSH is still at high-growth stage



Source: Company, PSR

RSH experienced an explosive growth in Net Revenue as compared to MMC over the past five years. Its next phase of expansion (the new extension block) will extend such high-growth period.

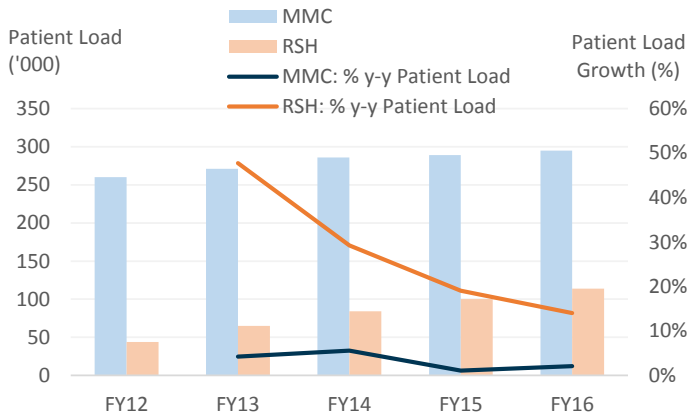
Figure 14: RSH's continues to ramp up its bed counts



Source: Company, PSR

As at FY2016, RSH only has c.62% of MMC's bed count.

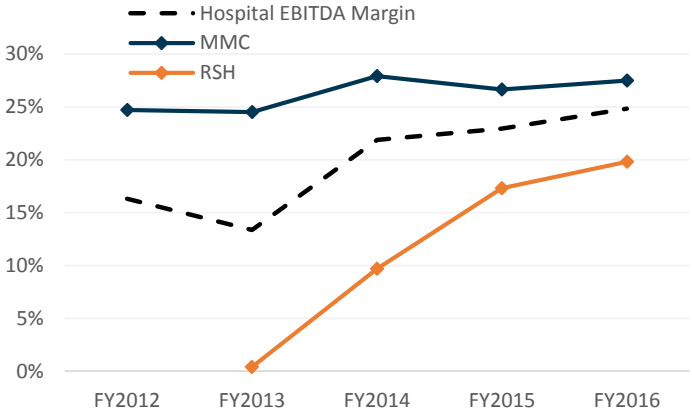
Figure 15: Growing patient volume in RSH, as it gains traction and expand its inpatient beds



Source: Company, PSR

FY2016 inpatient volume to number of inpatient bed ratio:
MMC: 101.5 to 1
RSH: 96.4 to 1

Figure 16: Scalability of RSH will bring its EBITDA margin to MMC's level at c.27%



Source: Company, PSR

3. Core expertise in hospital management, strategy and business turnaround

(a) First mover advantage: securing patient pool and specialists

HMI first began operations in Singapore in 1991 with HMI Balestier Hospital (formerly known as Balestier Medical Centre). It decided to venture into unchartered waters in 1998 when it saw brighter prospect in Malaysia's tertiary healthcare space.

HMI made its first foray into Malaysia in 1998 by acquiring stakes and a five-year management contract in MMC. MMC began operations in 1994 but was a loss-making hospital then. HMI conducted a restructuring exercise after it took over management and successfully achieved a turnaround within two to three years.

With foresight, HMI brought Singapore's private hospital business model into Malaysia. MMC was one of the first hospitals across the Causeway to sell medical suites to doctors, and one of the early movers in attracting patients from Indonesia.

Its opportunistic and dare to be the first mover attitude allow HMI to have an edge over its competitors in terms of patient pool as well as recruitment of consultants.

(i) **Early mover in medical tourism since 1999** – HMI started to develop its strong patient referral network across Southeast Asia, reaching to 17 patient referral centres in the region as of FY2016. Currently, c.20% of its patient load are medical tourists and is still growing on the back of supportive macro backdrop.

(ii) **Not entirely out from Singapore market** – One of the two hospital groups approved by Singapore Ministry of Health for usage of Medisave in Malaysia.

(iii) **Independent clinic model within a hospital setting is unique to HMI in Malaysia and appeals to independent practitioners –** Till day, there are still limited number of Malaysia private hospitals which offer sales of medical suites. Competitors in Malaysia with such model include Landmark Medical Suites and Gleneagles Medini, where both are located in Johor Bahru, Malaysia.

In 2007, HMI subsequently acquired stakes in its second hospital, RSH, in Johor, Malaysia. RSH was only an empty hospital building then. It was officially launched in November 2009 and achieved its first full year of profitability in 2014, i.e. within five years since launched.

(b) Strong brand equity: accolades are testament to HMI's quality service and excellent management

Over the years, HMI has won a total of 18 awards with most of them are medical tourism related awards and quality accreditations. Some notable awards and accreditations are:

- *Health Industry Recognition Award 2009;*
- *Business Award of the Year – Service Provider Category 2010;*
- *Ministry of Health Malaysia Award for Outstanding Achievement 2012 – Highest Number of Healthcare Travelers in Southern Region;*
- *ASEAN Business Awards 2015, AEC Priority Integration Sectors Excellence Award – Healthcare;*
- *2015 & 2016 Frost & Sullivan Malaysia Medical Tourism Hospital of the Year.*

Forecast Assumptions

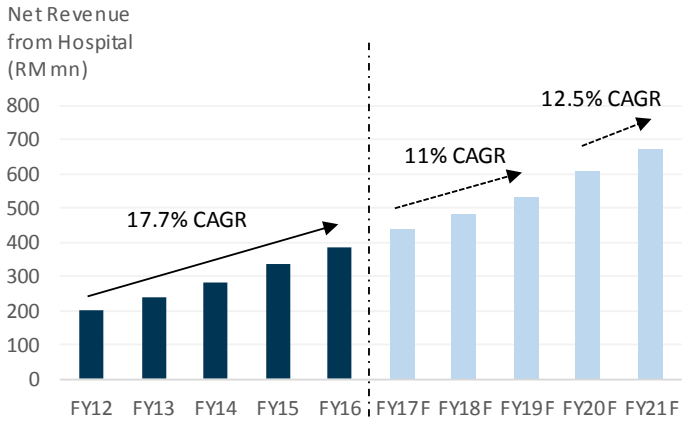
1. Growing patient base coupled with expanding inpatient beds, facilities and services to drive revenue at 11.5% CAGR over next five years

We think Net Revenue from Hospital should remain buoyant with c.11% CAGR growth in FY17-19F, benefiting from (i) favourable macro backdrop, and (ii) the new wards which is slated to complete in 1H FY2018.

We believe that the new Hospital Extension Block, which is targeted to complete by FY2020, will add another leg of growth to HMI. It will provide the necessary capacity for new inpatient beds, services and facilities for RSH, and ramp up Net Revenue from Hospital to c.12.5% CAGR growth in FY20-21F.

Next phase of extension could be the construction of new hospital extension for MMC on its adjacent plot of land, which could be a catalyst for further re-rating.

Figure 17: Double digit growth from Net Revenue from Hospital



Source: Company, PSR

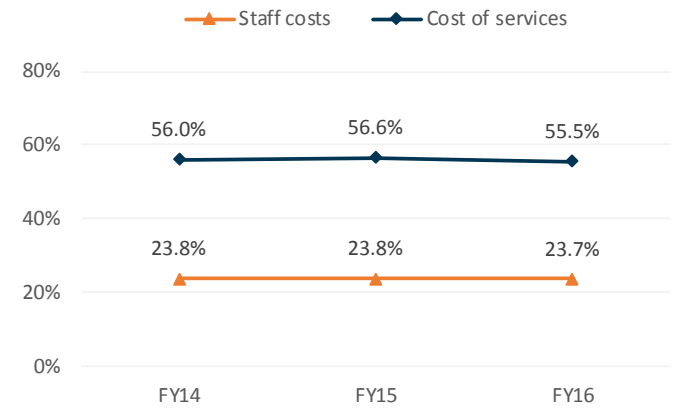
2. Steady costs pressure and enhanced economies of scale to improve margins

Staff costs and costs of services accounts for c.80% of the Group's total expenses. Cost of services mainly comprises materials costs and consultants' fees.

Staff costs as a percentage of revenue had been relatively stable at c.20% in the past three years. Meanwhile, cost of services as a percentage of revenue decreased 1.3 percentage points over the same period to 46.5% in FY2016. The lower materials costs had offset the upward pressure from consultants' fees.

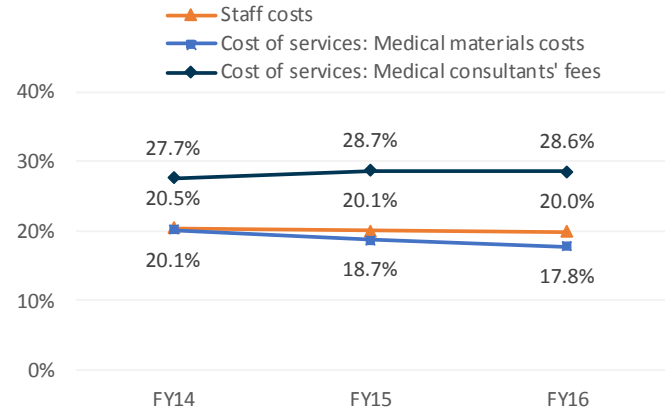
We expect staff costs to remain stable at c.20% of revenue. Meanwhile, (i) effective cost management, (ii) improved economies of scale, and (iii) higher average hospital bill size via expansion, should lift EBITDA and net margins progressively over the next five years.

Figure 18: Key operating expenses form c.80% of total expenses



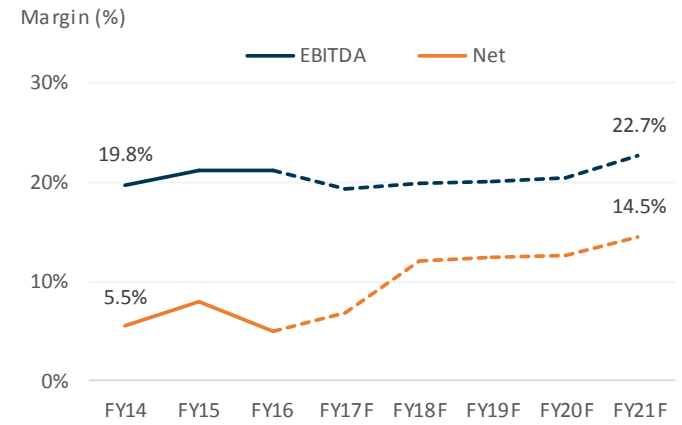
Source: Company, PSR

Figure 19: Key operating expenses as a percentage of revenue



Source: Company, PSR

Figure 20: Improving margins post consolidation in FY17F, coupled with economies of scale and better cost management



Source: Company, PSR

3. Improving cash conversion cycle

HM's cash conversion cycle has been improving over the past five years, with 5-year average of 22 days. We assumed that its cash conversion cycle to remain as FY16's.

Figure 21: Cash Conversion Cycle

	FY12	FY13	FY14	FY15	FY16	5-year Average
Working capital						
Days Inventory Outstanding	13	11	10	14	18	13
Days Sales Outstanding	98	94	88	84	67	86
Days Payables Outstanding	72	77	79	77	79	77
Cash conversion cycle (days)	38	28	18	21	6	22

Source: Company, PSR

Hospitals continue to stock up for medicines and medical supplies to cater for increasing patient load, which is also in line with its expansion strategy

4. Financial position remains strong; consolidation of hospitals ownerships to cut leakage to non-controlling interests

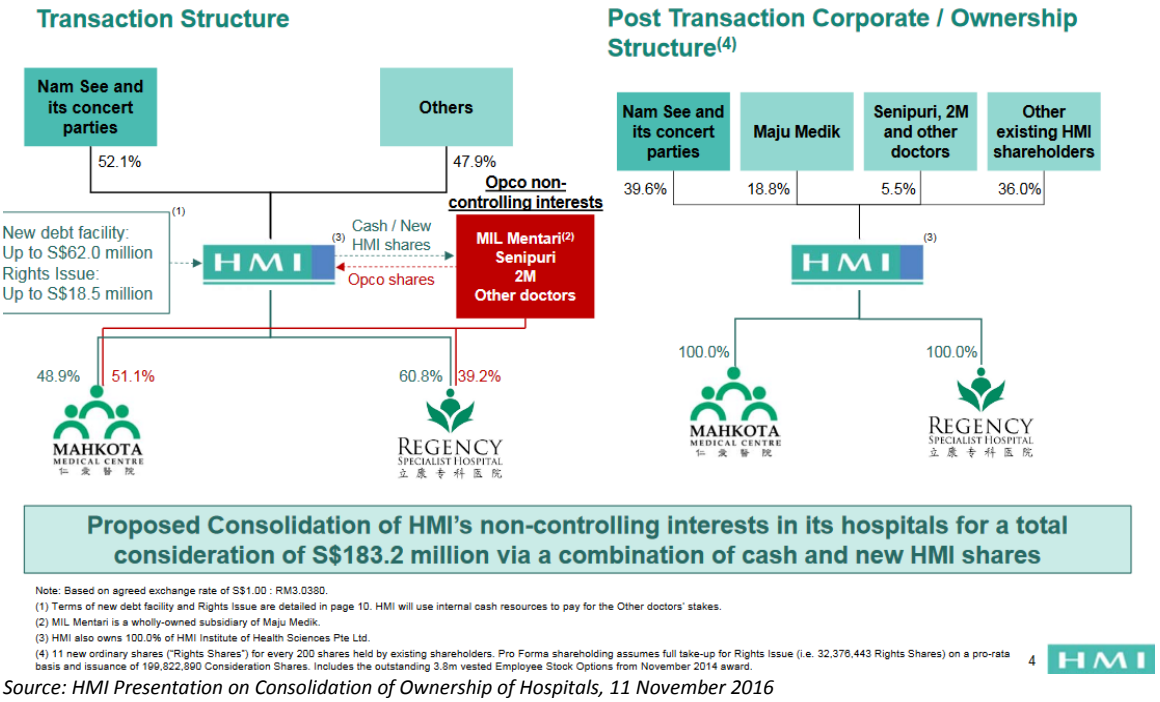
HMI has been deleveraging over the years. Total debt decreased by 40% over the last five years to RM41.9 as at end-FY2016. Its strong and positive cash flow generated from operations brought HMI into a solid net cash position of RM37.1 mn as of end-FY2016, which provides plenty of headroom for expansion.

In November 2016, HMI announced to consolidate its 48.9%-owned MMC and 60.8%-owned RSH to 100% each for a total consideration of RM556.5 mn, via a combination of cash (37.8%) and new HMI shares (62.2%) at S$0.57 per share. The cash consideration of RM210.5 mn (or S$69.3 mn) will be funded mainly via debt facility; while the new HMI shares are subjected for 1 year lock-up period. The transaction is targeted to complete by March 2017.

We expect the transaction to bring HMI from net cash position to net gearing of 0.6x by end-FY17F. However, we deem the consolidation as favourable as (i) the transaction is accretive to HMI, and (ii) HMI's group structure will be clearer with no significant non-controlling interest ("NCI"). Without NCI, FY2016 PATMI would have been RM36.2 mn (+81.7% compared to pre consolidation), and a fully diluted FY2016 EPS would have been RM4.40 cents (+30.4% compared to pre consolidation).

The capital expenditures (CapEx) expected for the new hospital extension block in RSH will be at least RM160 mn. We expect it to spread over two and a half years, and will be funded via a mix of debt and internal cash resources.

Figure 22: Overview of consolidation



Note: Based on agreed exchange rate of S$1.00 : RM3.0380.
(1) Terms of new debt facility and Rights Issue are detailed in page 10. HMI will use internal cash resources to pay for the Other doctors' stakes.
(2) MIL Mentari is a wholly-owned subsidiary of Maju Medik.
(3) HMI also owns 100.0% of HMI Institute of Health Sciences Pte Ltd.
(4) 11 new ordinary shares ("Rights Shares") for every 200 shares held by existing shareholders. Pro Forma shareholding assumes full take-up for Rights Issue (i.e. 32,376,443 Rights Shares) on a pro-rata basis and issuance of 199,822,890 Consideration Shares. Includes the outstanding 3.8m vested Employee Stock Options from November 2014 award.

4 HMI

Source: HMI Presentation on Consolidation of Ownership of Hospitals, 11 November 2016

5. No dividend policy but the increasing cash flow could warrant dividend payout moving forward

HMI made its first dividend payout of RM0.75 cents per share in FY2016 after its last dividend payout in 2008. FY2016 dividend represents 22% dividend payout ratio.

After its consolidation transaction, we think that HMI will continue to payout dividend to its shareholders, as it has been paying annual dividends to its non-controlling interests. We conservatively forecast HMI to maintain its dividend payout ratio at 20% moving forward.

Valuation

We think HMI's scalable business model is well positioned to capture strong patient load.

1. Growing patient demand underpinned by favourable macro environment.
2. Its expansion plan in line with its strategy to lift top line while maintaining robust margins. Higher average hospital bill size with: (i) increasing inpatient beds in RSH and MMC by FY18F, and (ii) construction of a new hospital extension block in RSH by FY20F.
3. Enhance margins via continuous cost management and improved economies of scale.
4. Potential annual dividend payout of 20% payout ratio post consolidation in FY17F.

We initiate coverage on HMI with a "**Buy**" rating with a **target price of S$0.83** based on discounted cash flow (DCF) methodology. This implies an **upside of 36.6%** from its last done price.

Figure 23: Valuation

Free cash flow to firm analysis						
Y/E Dec, MYR mn	**FY17F**	**FY18F**	**FY19F**	**FY20F**	**FY21F**	**Terminal**
Operating profits	64	72	81	96	120	
Less: Tax	(11)	(12)	(14)	(16)	(20)	
Plus: Depreciation & amortisation	22	26	28	32	36	
Less: Capex, net	(13)	(79)	(80)	(51)	(21)	
Adjust for: Change in working capital	(23)	9	1	4	(7)	
Free cash flows	**39**	**16**	**16**	**65**	**107**	**1,807**

WACC (%)	7.0
Terminal growth rate (%)	1.0
Firm value (MYR mn)	1,491
Adjust for: Net cash/(debt), (MYR mn)	37
Equity value (MYR mn)	1,528
Number of shares (mn)	589
Fair value (MYR/share)	2.59
Cross-rate (SGD/MYR)	0.32
Fair value (S$/share)	**0.83**
Cost of debt (%)	
Interest rate (%)	5.3
Tax shield on debt (%)	17.0
After-tax cost of debt (%)	**4.4**
Risk free rate (%)	3.0
Beta (x)	0.70
Market risk premium (%)	7.0
Cost of equity (%)	**7.9**
Long-term debt-to-equity ratio (%)	0.25
WACC	**7.0**

Source: Bloomberg, PSR

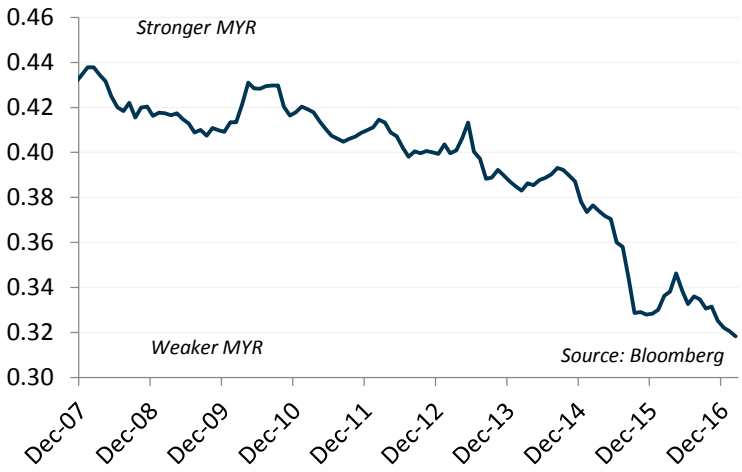
DCF Sensitivity Analysis

	Assumed Perpetual Growth (%)					
WACC (%)	**0.5**	**1.0**	**1.5**	**2.0**	**2.5**	**3.0**
6.00	$0.93	$1.01	$1.12	$1.24	$1.41	$1.63
6.50	$0.84	$0.91	$1.00	$1.09	$1.22	$1.38
7.00	$0.77	**$0.83**	$0.90	$0.98	$1.08	$1.20
7.50	$0.71	$0.76	$0.82	$0.88	$0.96	$1.06
8.00	$0.66	$0.70	$0.75	$0.80	$0.87	$0.94

FX Sensitivity Analysis (MYR against SGD, excluding effects on cash flow)

Fair value (MYR/share):	Appreciation of MYR			Base	Depreciation of MYR		
MYR 2.59	+15%	+10%	+5%	Case	-5%	-10%	-15%
FX (SGD/MYR)	0.37	0.35	0.34	0.32	0.30	0.29	0.27
Fair value (S$/share)	$0.95	$0.91	$0.87	$0.83	$0.79	$0.75	$0.70

Figure 24: MYR weakening against SGD over the past 9 years

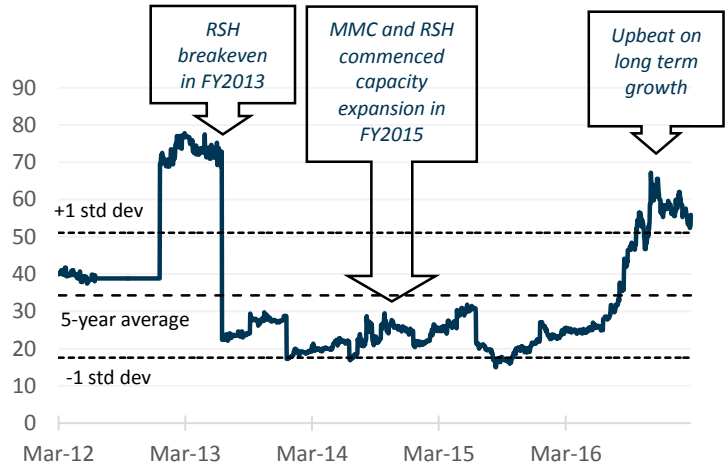


Double edged-sword:
Weakening MYR against SGD would increase its price competitiveness (especially for medical tourists to its hospitals) but would depress the SGD-denominated stock price

Our target price is an implied 58x/35x/31x FY17/18/19F PER.

HMI currently trades at a 55.9x FY16 trailing PER, which is more than one standard deviation higher from its 5-year average. It is comparable to its Malaysian peers' average at 54.4x but at a 27% premium to its regional peers' average at 43.9x.

Figure 25: 5-Yr Historical PER



Source: Bloomberg

Figure 26: Comparable

Company	Mkt Cap (SGD mn)	EV/EBITDA TTM	EV/EBITDA FY1	P/E	P/E FY1	Net D/E (%)	ROA (%)	ROE (%)	P/B
Health Management International Ltd	359.1	7.1	17.9	55.9	43.0	Net Cash	5.3	12.6	6.5
Singapore									
Raffles Medical Group Ltd	2,457.9	25.0	22.6	34.8	32.7	Net Cash	8.2	11.1	3.7
Singapore Medical Group Ltd	225.5	14.5	19.7	69.2	30.3	Net Cash	4.0	6.9	14.4
International Healthway Corp Ltd	175.9	15.0	N/A	N/A	N/A	166.4	-2.0	-5.5	0.8
Healthway Medical Corp Ltd	103.3	34.0	N/A	N/A	N/A	8.2	-0.1	-0.1	0.5
AsiaMedic Ltd	28.9	7.9	N/A	N/A	N/A	Net Cash	-9.7	-15.7	1.7
Singapore Average		19.3	21.1	52.0	31.5	87.3	0.1	-0.7	4.2
Australia									
Ramsay Health Care Ltd	14,443.4	13.4	12.4	28.8	25.4	152.3	6.0	26.2	7.2
Healthscope Ltd	4,141.2	13.6	12.5	22.1	20.7	57.4	4.0	7.4	1.6
Pulse Health Ltd	126.0	N/A	11.2	N/A	25.6	15.2	-3.3	-5.4	1.3
Australia Average		13.5	12.0	25.5	23.9	75.0	2.2	9.4	3.4
Malaysia									
IHH Healthcare Bhd	15,507.5	27.9	20.5	79.6	44.2	21.1	1.7	2.8	2.2
KPJ Healthcare Bhd	1,331.2	15.0	13.8	29.1	27.9	72.2	3.8	9.7	2.6
Malaysia Average		21.4	17.1	54.4	36.0	46.7	2.7	6.3	2.4
Simple Average (Excl. HMI)		18.5	16.1	43.9	29.5	70.4	1.3	3.7	3.6

Source: Bloomberg, PSR estimates

Malaysia Healthcare Industry Overview

Malaysia is operating a two-tiered healthcare system consisting of public (via universal healthcare system, mainly from Ministry of Health) and private (mainly from out-of-pocket spending).

The current healthcare system in Malaysia is imbalance with private hospitals being equipped with better infrastructure and facilities despite recording similar healthcare expenditures with public sector.

With a government-dependent healthcare system coupled with rising healthcare costs, the public hospitals are overcrowded, further stretching the public sector resources in the delivery of quality healthcare services. The capacity constraint in public healthcare facilities is expected to drive affluent patients to private hospitals.

Well-funded private hospitals also have an edge over government hospitals in terms of medical equipment. Private hospitals invest in state-of-art medical equipment which public hospitals could not afford. Referrals from public hospitals within the vicinity could underpin demand for such facility, increase potential patient pool, secure utilisation rate and hence shorten breakeven period of the machine.

Figure 27: Healthcare facilities and staff overview in 2014

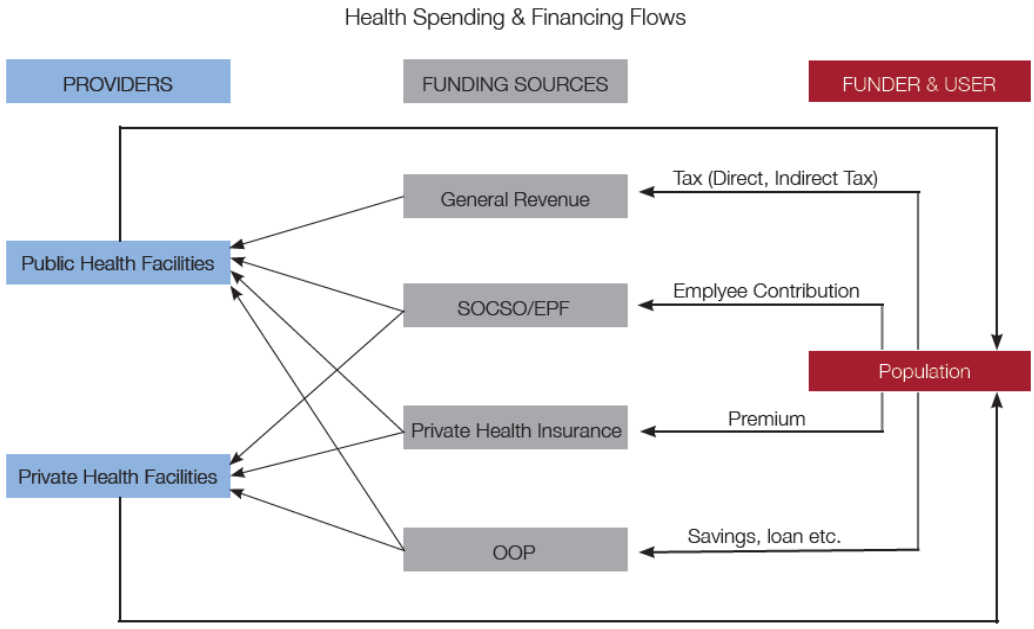
Public Sector	Private Sector
55% of healthcare expenditures	45% of healthcare expenditures
152 public hospitals (including university hospitals and military hospitals)	183 privates hospitals
Received c.72% of total inpatient cases - 78% of total registered beds - ratio of doctors to beds is 0.7:1 - ratio of nurses to beds is 1.5:1 - 30/105 MRI machines - 52/143 CT scan machines	Received c.28% of inpatient cases - 22% of total registered beds in - ratio of doctors to beds is 1.0:1 - ratio of nurses to beds is 2.3:1 - 75/105 MRI machines - 91/143 CT scan machines

Private hospitals are more accessible

*Public hospitals received higher number of admissions, and houses more inpatient beds; **BUT** private sector has a more favourable staffing levels, in terms of doctors and nurses to beds, and are better equipped with more advanced medical equipment*

Source: ISEAS Economics Working Paper dated Dec 2015 by ISEAS – Yusof Ishak Institute, CEIC, PSR

Figure 28: Health Spending and Financing Flows in Malaysia, with out-of-pocket ("OOP") being the main contributor to private health facilities



Source: Malaysia Health Systems Research Volume I, Contextual Analysis of the Malaysian Health System, March 2016

1. Rising private healthcare spurred by domestic demand

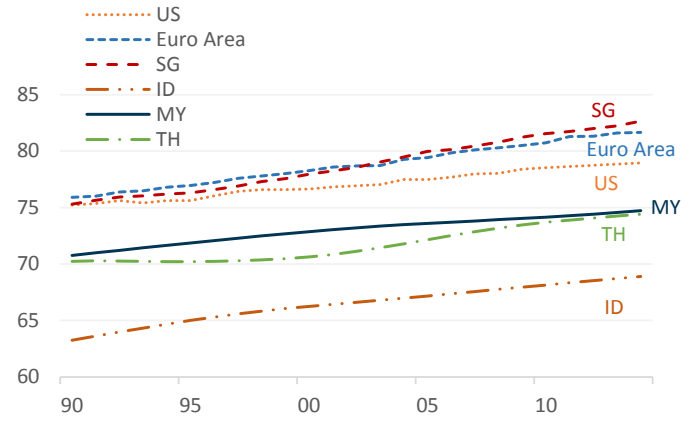
The healthcare landscape in Malaysia is changing due to the economic and social development in Malaysia. Private hospitals grew at c.4.3% CAGR, from 50 private hospitals and institutions in 1980 to 216 in 2015.

(a) **Demographic: Ageing population with growing consumer affluence**

- The life expectancy of Malaysian has increased over the past few decades, and is the trend is expected to continue owing to improved standards of living. On the other hand, **Malaysia is expected to face ageing population issues by 2030**, when the proportion of Malaysia's population aged 65 and above is projected to reach 14.4% according to the United Nations' World Population Ageing Report 2015.
- Disposable income increased at CAGR of 5.5% during 2010 to 2015. The **rising purchasing power in Malaysia will support higher discretionary spending**.
- Healthcare spending in Malaysia lags behind developed countries' and worlds average. With the increase in patient numbers and spending power, we expect healthcare spending to pick up, in particular the proportion contributed by private sector.

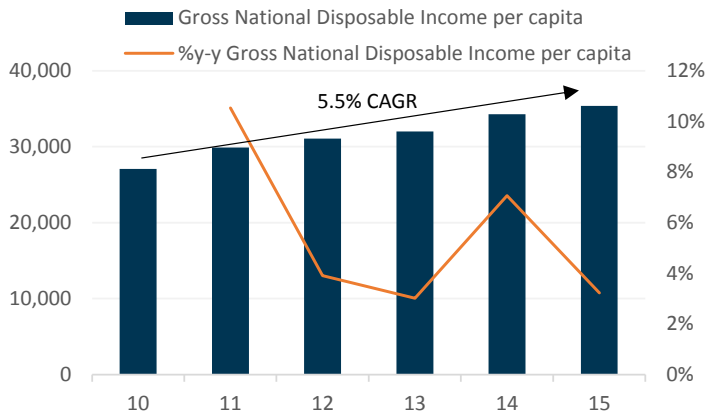
While the changes in socio-economic structure will be a strong driver for healthcare demand, HMI has well-positioned itself as premier tertiary care to capture the growing middle-income segment.

Figure 29: Higher life expectancy at birth, but still lower than developed countries (US, Euro Area and Singapore)



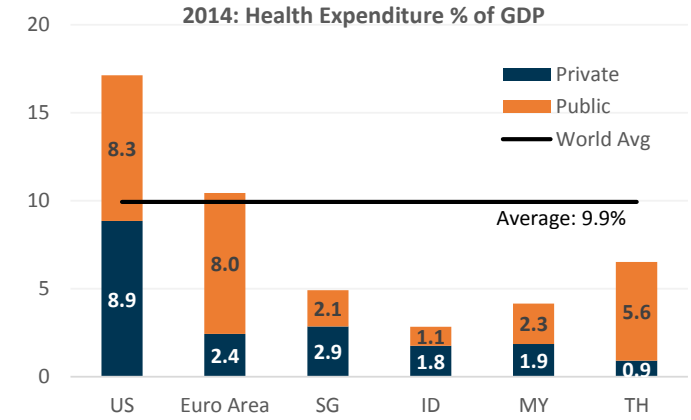
Source: CEIC, PSR

Figure 30: Increasing spending power within Malaysian to spur demand for quality healthcare



Source: CEIC, PSR

Figure 31: Below global average healthcare spending

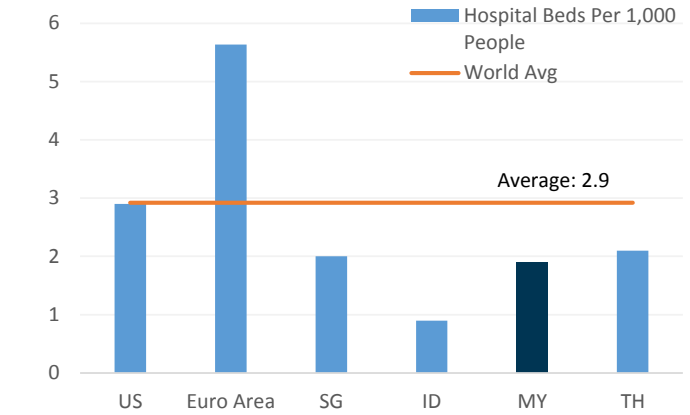


Source: CEIC, World Bank

(b) **Healthcare provision remains undersupplied as compared to developed countries**

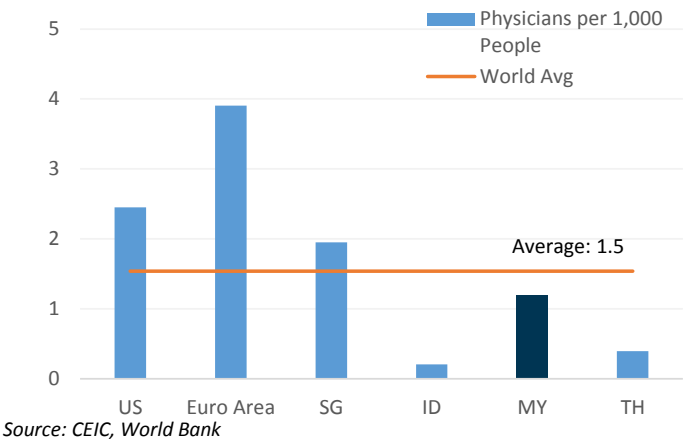
- Compared to world's average, Malaysia's bed capacity and physician density are still below par.

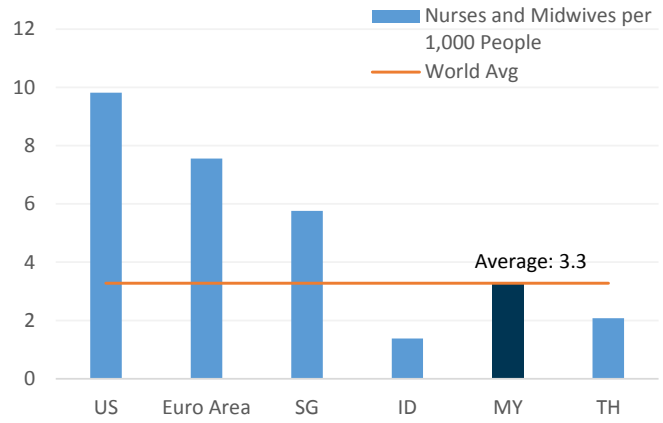
Figure 32: Comparable to regional peers, i.e. SG and TH, but is still below par



Source: CEIC, World Bank

Figure 33 & 34: Strength of healthcare workforce, particularly physicians per population, lags behind developed economies



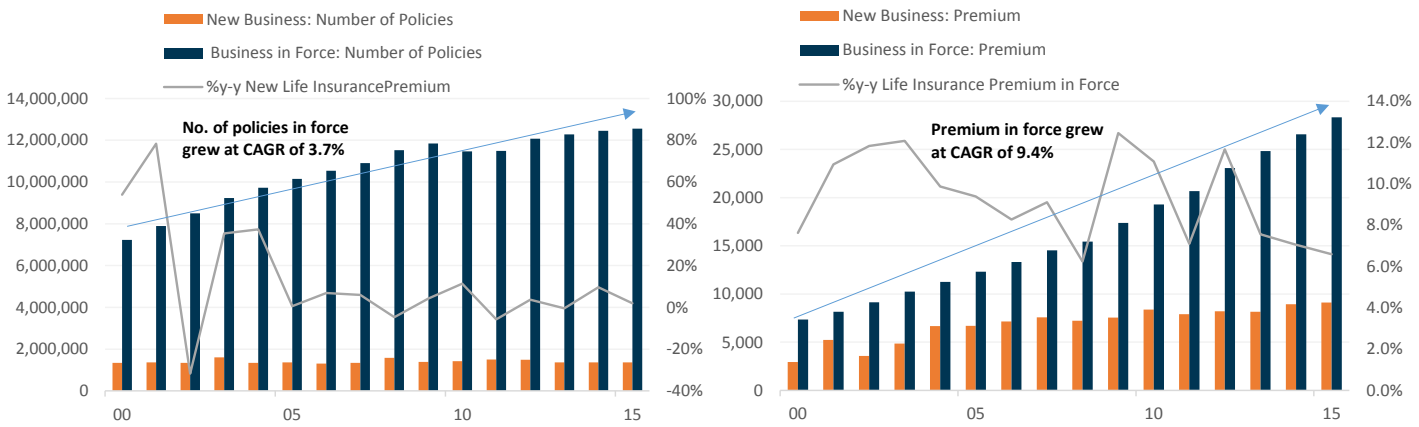


Source: CEIC, World Bank

(c) **Increasing access to healthcare/medical insurance will propel patients transition from public to private healthcare services**

- Malaysia's healthcare insurance market (both public and private) is relatively underpenetrated:
  - (i) Insured rate (number of policies in force as a percentage of total population) is at c.40% in 2015, despite Malaysia government is striving to reach c.70% insured rate by 2020 via universal healthcare program;
  - (ii) Low penetration rate (life insurance premium as a percentage of total gross domestic product) at c.2.4% in 2015, compared to OECD countries' average at c.5%.
- High uninsured rate and low penetration rate suggest plenty of room for growth in healthcare insurance market. Growth for private healthcare insurance will be underpinned by growing middle-income population, as well as increasing availability of medical insurance packages and access to private hospitals.

Figure 35 & 36: Growing number of life insurance policies and premium in the past 15 years reflect raising awareness on the value of healthcare insurance among the affluent consumers



Source: CEIC, PSR

2. Favourable backdrop underpins prospect of medical tourism in Malaysia

Malaysia saw revenues amounting to RM730 million from healthcare travel receipts from more than 880,000 arrivals in 2014 (*Source: Malaysia Healthcare Travel Council*). The number of medical tourists to Malaysia grew at CAGR of 7.3% between 2011 to 2015, and is expected to expand at 18.5% per annum between 2014 and 2020, based on Frost & Sullivan's estimates.

Most medical tourists are from Indonesia, contributing c.60% of total healthcare revenue and numbers. The rest are from the Middle East, India, China, Japan, and United Kingdom. While the most sought-after treatments include cardiology, orthopaedics, in-vitro fertilisation (IVF), neurology, oncology, dentistry, cosmetic surgery and health screenings.

(a) **Malaysia's value proposition: comprehensive and inexpensive healthcare services**

- Equipped with high-quality medical infrastructure, state-of-the art facilities and multi-lingual personnel from diverse cultural backgrounds.
- Capped healthcare fees enable lower medical costs with high quality offerings. In addition, weaker Ringgit against foreign currencies would improves affordability.

HMI being one of the only two Medisave-approved healthcare operators in Malaysia further appeal Singapore residents to seek overseas treatments.

Figure 37: Cost benchmarking of healthcare services (as of August 2014)

(in USD)

Surgeries	Malaysia	Singapore	Thailand
Heart bypass	14,000	23,000	13,000
Angioplasty	8,750	27,750	3,800
Knee replacement	10,900	16,700	11,400
Gastric bypass	8,600	20,000	16,700

Source: HMI FY2016 Investor Presentation Slides

Malaysia is price-competitive versus its neighbouring countries, on most procedures.

When compared to Singapore, its pricing on common surgeries could be c.30-60% lower.

(b) **Attractive destination as medical tourism**

- Improving regional accessibility and transport infrastructure will enhance connectivity and boost medical tourism.
- Malaysia was named "Medical Travel Destination of the Year" in the 2015 International Medical Travel Awards.

HMI's two hospitals are strategically located in popular tourist destinations in Malaysia, i.e. Malacca City and Johor Bahru. Malacca City, the capital city of Malacca

state, was listed as a UNESCO World Heritage Site. Meanwhile, Johor Bahru, the capital city of Johor state, is in close proximity to Singapore and Indonesia.

(c) **Government initiatives to promote medical tourism**

- The government spends RM20 million a year to promote and develop medical tourism. The 11th Malaysia Plan also aims to develop three healthcare hubs in the country, namely, Penang, Malacca, and Johor Bahru.
- Various tax benefits for medical tourism focused hospitals.
- Malaysia Healthcare Travel Council working with healthcare providers to promote medical tourism.
- Opening up Visa requirements. Malaysia has limited Visa restrictions: citizens of Commonwealth countries do not require a visa to enter Malaysia, while the newly implemented e-Visa system eases the application process for Chinese and Indians.

These policies and campaigns are supportive of HMI's initiatives to woo foreign patients.

Competitive Landscape

1. Domestic competition

While public hospital in Malaysia offers a lower price point, HMI differentiates itself by offering a comprehensive range of specialties and sub-specialties, state-of-the art facilities and medical equipment, shorter waiting time and faster turnaround time, quality services in terms of better follow up services and more personalised experience.

The disparities widened when government cut the healthcare budget amidst rising healthcare costs. The allocation for services and supplies under pharmaceuticals and supplies dropped by c.19% despite the increased overall allocation to the health sector under Budget 2017.

Figure 38: Provision of niche healthcare services provides HMI an edge over the public sector

Highlighted in bold green fonts are healthcare services which are offered by HMI, but are offered by three or less specialist units in government hospitals within the southern region (Malacca and Johor)

Out of 68 sub-specialties, HMI are predominant in 46 of them.

Discipline	MMC	RSH	MOH Hospital (Southern Region - Malacca and Johor)
Adult Intensive Care	**Y**	**Y**	**2**
Anatomy Pathology	**Y**	**Y**	**2**
Aesthetics	**Y**	**Y**	
Anaesthesiology	Y	Y	7
Arthroplasty	**Y**	**Y**	**1**
Breast Surgery	**Y**		
Cardiology	**Y**	**Y**	**1**
Cardiothoracic Surgery	**Y**	**Y**	
Chemical Pathology	**Y**		**1**
Child Psychiatry			1
Colorectal Surgery		**Y**	**1**
Dermatology	**Y**		**2**
Emergency Medicine	Y	Y	7
Endocrinology	**Y**		**1**
Ear, Nose, Throat Surgery	**Y**	**Y**	
Forensics Medicine			2
Gastroenterology	**Y**	**Y**	**2**
Gastroenterology & Hepatology	**Y**	**Y**	
General Medicine	Y	Y	7
General Surgery	Y	Y	7
Geriatrics	**Y**		
Glaucoma	**Y**	**Y**	**1**
Hematology	**Y**	**Y**	**2**
Haematology & Haemo-Oncology	**Y**	**Y**	
Hepatobiliary-Pancreato-Biliary Surgery	**Y**	**Y**	
Infectious Disease	**Y**		**2**
Internal Medicine	**Y**	**Y**	
Dentistry - General	**Y**		
Dentistry - Orthodontics	**Y**		
Maternal Fetal Medicine			1
Microbiology			2
Neonatology	**Y**	**Y**	**3**
Nephrology	**Y**	**Y**	**3**
Neurology	**Y**		

Discipline	MMC	RSH	MOH Hospital (Southern Region - Malacca and Johor)
Neurosurgery	**Y**	**Y**	**1**
Obstetrics & Gynaecology	Y	Y	7
Oral Surgery	Y		5
Oral & Maxillofacial Surgery	**Y**		
Oncology - Medical	**Y**	**Y**	
Oncology & Radiotherapy	**Y**		
Oncology - Gynae	**Y**	**Y**	
Ophthalmology	Y	Y	5
Ophthalmology & Vitreo Retinal Services	**Y**		
Orthopaedics	Y	Y	7
Orthopaedic & Trauma Surgery	**Y**	**Y**	
Otorhinolaryngology	Y	Y	5
Plastic & Reconstructive Surgery	**Y**	**Y**	**2**
Palliative Medicine	**Y**		
Pathology	**Y**		**2**
Paediatric	Y	Y	7
Paediatric Cardiology	**Y**	**Y**	
Paediatric Dentistry			3
Paediatric Intensive Care			1
Paediatric Neurology	**Y**		
Paediatric Surgery			1
Psychiatric	Y		7
Radiology	Y	Y	6
Radiology & Interventional Radiology	**Y**	**Y**	
Rehabilitation Medicine			1
Reproductive Medicine	**Y**	**Y**	
Respiratory Medicine	**Y**	**Y**	**1**
Rheumatology	**Y**		**1**
Spine Surgery	**Y**	**Y**	**1**
Sports Medicine	**Y**	**Y**	**1**
Transfusion Medicine			2
Trauma & Burns			1
Urology	**Y**	**Y**	**1**
Vascular & Endovascular Surgery		**Y**	

Source: Company FY2016 Investor Presentation Slides; Malaysia Health Systems Research Volume I (Contextual Analysis of the Malaysian Health System, March 2016)

Excluding public hospitals, HMI's main competitors include IHH Healthcare Bhd, KPJ Healthcare Bhd, Ramsay Sime Darby Health Care and other independent tertiary hospitals.

Figure 39: Brief overview of the three major players in Malaysia's private healthcare sector

	Private Healthcare Group	Description
1.	International Parkway Pantai Hospital Group (part of IHH Healthcare Berhad Group)	Has a network of 14 hospitals (Pantai and Gleneagles chain of hospitals) across the country
2.	KPJ Healthcare Berhad	Has over 20 specialist hospitals nationwide
3.	Ramsay Sime Darby Health Care Group	Three private hospitals, namely Parkcity Medical Centre, Subang Jaya Medical Centre, and Ara Damansara Medical Centre

Note: State governments have a controlling stake in these major private healthcare conglomerates

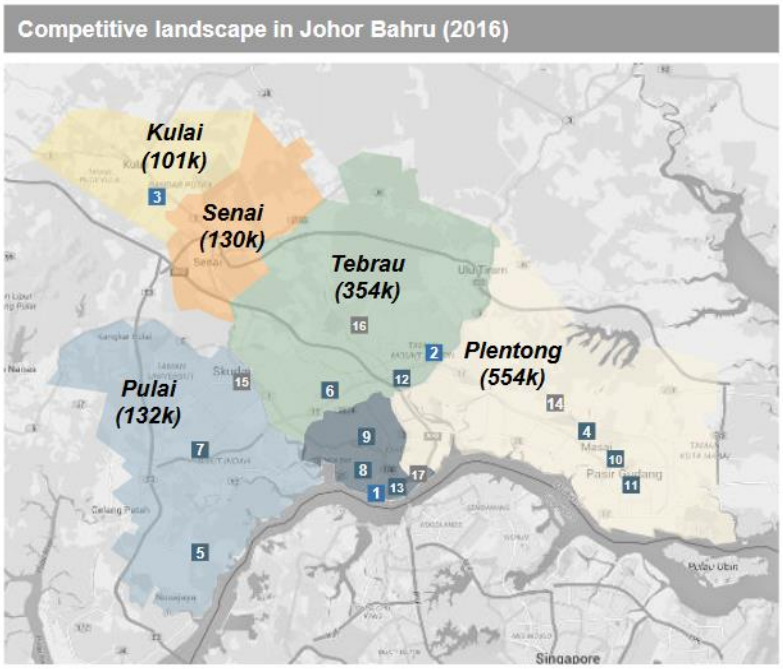
Private hospitals are typically concentrated in urban areas, particularly on the west coast of Peninsular Malaysia, where the more affluent cities such as Penang, Kuala Lumpur, and Johor Bahru are located. Nonetheless, when compared to Malaysia's bed-to-population ratio* at 1.9, Malacca has higher bed density at 2.5, while Johor is still under-supplied at 1.7.

**Number of beds available in both public and private hospitals per 1,000 people (Source: CEIC)*

Figure 40: MMC's strategic location attracts medical tourists

Source: HMI FY2016 Investor Presentation Slides

Figure 41: RSH strategically located in under-served environment; and already have a head start compared to upcoming new hospitals



	Hospital name	Beds
	Public hospitals	
1	Hospital Sultanah Aminah	989
2	Hospital Sultan Ismail	704
3	Kulai Hospital	93
	Private Hospitals	
4	Regency Specialist Hospital	218 (expanding)
5	Gleneagles Medini	40 (300E)
6	Kempas Medical Centre	130
7	Columbia Asia Hospital	81
8	KPJ Johor Specialist	236
9	KPJ Puteri Specialist	158
10	KPJ Pasir Gudang	36
11	Penawar Pasir Gudang	70
12	Penawar Pandan City	20
13	Medical Specialist Centre	45
	Announced New Hospitals	
14	Pasir Gudang Public Hospital	300E
15	KPJ UTM	150E
16	KPJ Bandar Dato Onn	390E
17	Thomson Iskandar	272E

Source: Company FY2016 Investor Presentation Slides

2. Regional competition

Malaysia healthcare providers face competition for medical tourism from regional players mainly in Thailand and Singapore. Besides the official government marketing effort by Malaysia Healthcare Travel Council, HMI has 17 representative offices across the region to increase HMI's cross border visibility and presence.

Cost of medical procedures is the key factor to draw medical tourists. Both HMI's hospitals have competitive pricings as compared to its neighbouring country, Singapore.

Figure 42: Representative offices targeted at Indonesian patients

Source: Company Website

Figure 43 & 44: Disparity in costs – HMI's value proposition to foreign patients

50th percentile bill sizes for certain elective procedures across various hospitals

	HMI Hospitals in Malaysia[1]		Singapore	
Procedure	**Mahkota Medical Centre**	**Regency Specialist Hospital**	**Restructured Hospitals[2]**	**Private Hospitals**
Angioplasty	**SGD 9,840** (Four-bedded) (1 ALS)	**SGD 7,865** (Four-bedded) (2 ALS)	**SGD 22,617** (Four-bedded) (2.9 ALS)	**SGD 29,268** (Four-bedded) (2 ALS)
Cataract surgery	**SGD 1,092** (Phacoemulsification)	**SGD 1,545** (1 ALS)	**SGD 3,791** (1 ALS)	**SGD 5,537** (1 ALS)
Delivery (Cesarean)	**SGD 2,164** (Double-bedded) (2 ALS)	**SGD 3,227** (Four-bedded) (2.5 ALS)	**SGD 6,007** (Four-bedded) (3 ALS)	**SGD 8,680** (Double-bedded) (3.1 ALS)
Delivery (Normal)	**SGD 997** (Double-bedded) (1 ALS)	**SGD 1,613** (Four-bedded) (1 ALS)	**SGD 3,101** (Four-bedded) (1.9 ALS)	**SGD 5,416** (Double-bedded) (2.2 ALS)
Gastroscopy (Day procedure)	**SGD 294**	**SGD 571**	**SGD 816**	**SGD 1,548**
Hip replacement	**SGD 9,003** (Double-bedded) (6 ALS)	**SGD 8,033** (Four-bedded) (5 ALS)	**SGD 19,996** (Four-bedded) (7.1 ALS)	-
Hysterectomy	**SGD 3,338** (Double-bedded) (4 ALS)	**SGD 4,167** (Four-bedded) (3 ALS)	**SGD 10,335** (Four-bedded) (3.4 ALS)	**SGD 15,003** (Four-bedded) (3 ALS)
Total knee replacement	**SGD 6,805** (Four-bedded) (3 ALS)	**SGD 7,696** (Four-bedded) (4 ALS)	**SGD 17,429** (Four-bedded) (4.3 ALS)	**SGD 16,790** (Four-bedded) (4.1 ALS)

On average, MMC and RSH bill sizes are 1/3 of Singapore private healthcare costs

Notes: (1) Based on FX of SGD 1.00 = MYR 2.93; (2) Based on private non-subsidised rates

Room charges across various hospitals

Room types	**MMC[1]**	**RSH[1]**	**Singapore Public[2]**	**Singapore Private (1)**	**Singapore Private (2)**
Deluxe/VIP or A1+ equivalent	SGD 126	SGD 130	NA	SGD 859	SGD 789
1 Bedded or A1 equivalent	SGD 85	SGD 85	SGD 428	SGD 588	SGD 609
2 Bedded	SGD 43	SGD 51	NA	SGD 308	SGD 329
4 Bedded or B1 equivalent	SGD 34	SGD 34	SGD 241	SGD 238	SGD 259

Notes:
1. Based on FX of SGD 1.00 = MYR 2.93
2. Based on private non-subsidised rates

Source: Company FY2016 Investor Presentation Slides

Investment Risks

1. **Intensifying competition with medium entry barrier**
   A high gross margin and growing demand would attract rivalry. However, a high start-up cost would deter players to enter.

   From *Figure 41*, the four new hospitals will add c.39% new inpatient beds to the existing supply of inpatient beds in Johor Bahru. However, these new hospitals require about two to three years to complete, and the supply of new inpatient beds would be increased in staggered form, which would require another five to seven years to reach full capacity. The timeline provides RSH to get a head start in capturing market share. The stickiness behaviour of a patient to hospital and doctor, i.e. a low probability of a patient switching doctor or hospital, would translate to a persistent market share in a long run.

2. **Margin compression arising from:**
   (a) **Rising operating expenses**, including rising cost of medical equipment and supplies, increasing cost of medicines, and staff cost.
   (b) **Regulation of healthcare costs and tariffs.** Domestic and regional governments may seek to restrain healthcare expenditure by regulating various aspects of the healthcare market, e.g.: regulating medical fees and pharmaceutical costs charged to patients.

3. **Foreign exchange risk: SGD against the functional currency of the Group, MYR**
   HMI's operational activities are substantially carried out in MYR in Malaysia. As mentioned earlier, a weakening MYR against SGD would increase its price competitiveness (especially for medical tourists to its hospitals), but would depress the SGD-denominated stock price.

APPENDIX

Company Background

Health Management International Ltd ("HMI") is a private healthcare provider with presence in Singapore, Malaysia and Indonesia.

HMI first began operations in Singapore in 1991 with a 60-bed HMI Balestier Hospital (formerly known as Balestier Medical Centre). HMI Balestier Hospital was then converted to the HMI Institute of Health Sciences ("HMI-IHS") by 2005 to provide healthcare education and training. It was subsequently shifted to the Devan Nair Institute for Employment and Employability in 2015.

It ventured into Malaysia in 1998 by acquiring a stake and a five-year management contract in Mahkota Medical Centre ("MMC"). Currently, HMI owns and operates two tertiary hospitals in Malaysia: the MMC in Malacca and Regency Specialist Hospital ("RSH") in Iskandar Malaysia, with total bed capacity of over 500, providing a comprehensive suite of medical and surgical services. The two tertiary acute care hospitals in Malaysia have c.200 practicing consultants with 1,600 employee strength serving more than 400,000 patients a year. To provide an extended reach to international patients, HMI has a network of 17 patient representative offices throughout Southeast Asia.

HMI is one of only two healthcare operators approved by Singapore ministry of Health for the use of Medisave by Singapore residents for overseas hospitalisations and day surgeries.

It was listed on the Singapore Exchange ("SGX") SESDAQ in 1998 with an initial public offering of 38 million new shares at S$0.27 each.

Figure 45: Company's history

Year	History and Milestones
1998	Incorporation of HMI Operated the 60 bed Balestier Hospital in SG
1999	Listing of HMI on SGX-Sesdaq Obtained agreement to manage loss making Mahkota Medical Centre
2000	Completed acquisition of 20% interest in Mahkota
2001	Achieved turn-around of Mahkota after years of losses Raised interest in Mahkota to 40%
2003	Acquired 2-year management contract for Grand Hospital Bengkalis, Indonesia
2005	Shift of core business in Singapore to healthcare education and training
2007	Acquired a 35% equity stake in Regency Specialist Hospital, an empty hospital building Raised interest in Mahkota to 49%
2008	Commissioned Regency Raised interest in Regency to 61% HMI upgraded to SGX-Mainboard
2009	Official opening of Regency
2010	HMI hospitals approved for use of Medisave overseas for hospitalisation & day surgeries
2014	Regency achieved first full year of profitability
2015	Commenced capacity expansion plans at Mahkota and Regency
2016	First in Melaka to install PET CT scan

Source: Company

Figure 46: Board of Directors

Name and Designation	Length of service as a Director (as at 30 Jun-16)	Description
Dr Gan See Khem Executive Chairman and Managing Director	17 years 5 months	▪ An active figure in public services and currently serves on the Malaysia-Singapore Business Council ▪ Received the SG50 Outstanding Chinese Business Pioneers Award from the Singapore Chinese Chamber of Commerce and Industry in 2015 ▪ Specialised in strategic planning and management during her 15-year tenure at the National University of Singapore ▪ Holds a PhD in Business Administration from the University of Sheffield, United Kingdom
Ms Chin Wei Jia Executive Director and Group Chief Executive Officer Managing Director of Mahkota Medical Centre and Regency Specialist Hospital	1 year 8 months	▪ Oversees and leads the strategic and operational activities of the Group ▪ Played a key role in the development of HMI into a SGX mainboard listed healthcare company ▪ Contributed to the start of HMI's education business via the launch of HMI Institute of Health Sciences ▪ A member of the core team that first commissioned Regency in 2008, and previously served as CEO of Regency from 2013 to early 2016 ▪ Led the establishment of HMI's Medisave accredited referral centre to enable HMI hospitals to provide overseas hospitalisation and day surgeries under the Singapore Medisave scheme ▪ Holds a Bachelor of Arts (summa cum laude) in Economics and International Relations from Boston University, USA. She also has a Masters of Arts in International Relations from Johns Hopkins University, USA ▪ The daughter of the Executive Chairman, Dr Gan See Khem and the sister of the Group Chief Financial Officer, Mr Chin Wei Yao
Mr Chin Wei Yao Executive Director and Group Chief Financial Officer Executive Director of Mahkota	8 months	▪ Responsible for the Group's overall financial reporting matters and driving the development of the Group's healthcare services business ▪ 8 years working experience in private equity and investment banking in South East Asia prior to joining HMI. ▪ Holds a Bachelor of Arts (summa cum laude) in Economics (Honours) from New York University, USA ▪ An affiliate member of the Association Chartered Certified Accountants ("ACCA") ▪ The son of the Executive Chairman, Dr Gan See Khem and the brother of the Group Chief Executive Officer, Ms Chin Wei Jia.
Professor Annie Koh Lead Independent Director Chairman of the Audit and Risk Management Committee Member of the Nominating Committee and Remuneration Committee	4 months	▪ Vice President for Office of Business Development at SMU ▪ Practice Professor of Finance holding the position of Academic Director for four university level institutes and centre - the Business Families Institute (BFI), Financial Training Institute (FTI), International Trading Institute (ITI) and Centre for Professional Studies (CPS) ▪ Chairs the World Economic Forum Global Agenda Council for Southeast Asia and the Asian Bond Fund 2 Supervisory Committee of the Monetary Authority of Singapore ▪ Member of the investment committee of i-Globe ▪ An independent director on the board of K1 Ventures Ltd ▪ Board member of the Family Firm Institute, Inc. and Singapore's Central Provident Fund Board ▪ Member of SkillsFuture HR Sectoral Tripartite Committee, HR Certification Taskforce, and MOE-WDA Skills Development Council ▪ Recipient of the prestigious Singapore Public Administration Medal (Bronze) in 2010 and the Public Administration Medal (Silver) in 2016 ▪ Holds a PhD in International Finance from Stern School of Business, New York University, USA
Dr Cheah Way Mun Independent Non-Executive Director Member of the Audit and Risk Management Committee Member of the Remuneration Committee and Nominating Committee	16 years 9 months	▪ An accomplished ophthalmic surgeon in private practice ▪ Previously the head of the eye department of Tan Tock Seng Hospital and a visiting consultant of the National University Hospital and the Singapore National Eye Centre ▪ Holds an MBBS from the then University of Singapore and is a fellow of the Royal College of Surgeons (Glasgow and Edinburgh) and the American Academy of Ophthalmology

Name and Designation	Length of service as a Director (as at 30 Jun-16)	Description
Professor Tan Chin Tiong Independent Non-Executive Director Chairman of the Remuneration Committee and Nominating Committee Member of the Audit and Risk Management Committee	16 years 9 months	▪ The Founding President of Singapore Institute of Technology and the Founding Provost of SMU ▪ Currently the senior advisor to the President of SMU ▪ A professor of marketing and has co-authored several books on marketing and business and consulted for corporations around the world ▪ An Independent Director of MYP Ltd ▪ Holds a PhD from the Pennsylvania State University, USA.

Source: HMI Annual Report 2016

Financials

Income Statement

Y/E Jun, MYR mn	FY14	FY15	FY16	FY17F	FY18F
Revenue	**293**	**345**	**398**	**449**	**494**
EBITDA	**58**	**73**	**85**	**87**	**98**
Depreciation & Amortisation	(14)	(16)	(18)	(22)	(26)
EBIT	**42**	**53**	**63**	**64**	**72**
Share of results of assoc.	5	3	2	2	0
Net Finance Inc/(Exp)	(1)	(2)	(2)	(3)	(8)
Profit before tax	**46**	**55**	**63**	**64**	**72**
Taxation	(10)	(1)	(18)	(11)	(12)
Net profit before NCI	**36**	**53**	**45**	**53**	**60**
Non-controlling interest	(20)	(26)	(26)	(22)	0
PATMI, reported	**16**	**28**	**20**	**31**	**60**

Per share data (MYR Cents)

Y/E Jun	FY14	FY15	FY16	FY17F	FY18F
EPS, reported	2.78	4.79	3.45	4.45	7.42
DPS	0.00	0.00	0.75	0.90	1.50
BVPS	19.14	25.02	29.58	38.10	40.82

Per share data (SGD Cents)

Y/E Jun	FY14	FY15	FY16	FY17F	FY18F
FX rate (SGD/MYR)	0.39	0.34	0.33	0.32	0.32
EPS, reported	1.09	1.65	1.15	1.42	2.36
DPS	0.00	0.00	0.25	0.29	0.48
BVPS	7.52	8.62	9.90	12.13	12.99

Balance Sheet

Y/E Jun, MYR mn	FY14	FY15	FY16	FY17F	FY18F
ASSETS					
PPE	143	180	178	174	231
Others	38	48	50	263	263
Total non-current assets	**180**	**228**	**228**	**436**	**494**
Accounts receivables	71	88	58	82	82
Cash	26	39	79	63	145
Inventories	5	13	14	15	15
Others	5	4	4	4	4
Total current assets	**107**	**144**	**155**	**164**	**246**
Total Assets	**287**	**372**	**383**	**600**	**740**
LIABILITIES					
Accounts payables	56	66	79	82	91
Short term loans	34	29	27	27	27
Others	3	2	6	6	6
Total current liabilities	**93**	**97**	**113**	**115**	**124**
Long term loans	22	12	14	198	262
Others	20	58	24	24	24
Total non-current liabilities	**42**	**69**	**38**	**222**	**286**
Total Liabilities	**135**	**167**	**151**	**337**	**410**
EQUITY					
Non-controlling interests	42	61	62	0	0
Shareholder Equity	**110**	**144**	**171**	**264**	**330**

Cash Flow

Y/E Jun, MYR mn	FY14	FY15	FY16	FY17F	FY18F
CFO					
Profit before tax	46	55	63	64	72
Adjustments	14	21	27	23	33
WC changes	4	17	(4)	(23)	9
Cash generated from ops	64	92	86	64	115
Others	(11)	(11)	(13)	(15)	(22)
Cashflow from ops	**52**	**82**	**73**	**49**	**93**
CFI					
CAPEX, net	(12)	(10)	(11)	(18)	(83)
Others	2	3	(11)	2	2
Cashflow from investments	**(10)**	**(7)**	**(22)**	**(16)**	**(81)**
CFF					
Share issuance, net	0	0	(1)	58	0
Loans, net of repayments	(8)	(15)	1	183	64
Dividends	0	0	0	(4)	(6)
Others	(10)	(9)	(25)	(223)	0
Cashflow from financing	**(18)**	**(24)**	**(25)**	**14**	**58**
Net change in cash	**25**	**50**	**26**	**47**	**69**
Effect of FX	0	0	1	1	1
CCE, end	**26**	**39**	**79**	**63**	**145**

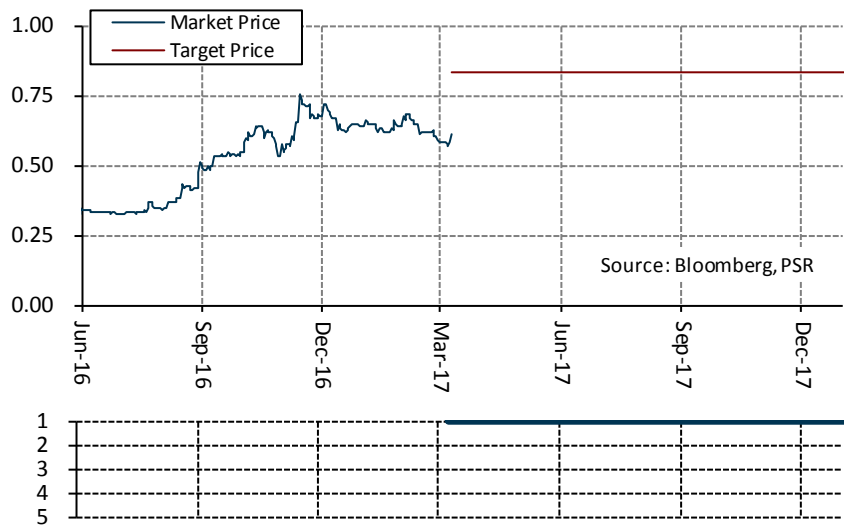
Valuation Ratios

Y/E Jun	FY14	FY15	FY16	FY17F	FY18F
P/E (X), adj.	19.0	21.5	29.3	43.0	25.8
P/B (X)	2.8	4.1	3.4	5.0	4.7
EV/EBITDA (X), adj.	5.2	8.1	6.9	17.9	15.8
Dividend Yield (%)	0.0%	0.0%	0.7%	0.5%	0.8%
Growth & Margins (%)					
Growth					
Revenue	19.4%	17.9%	15.2%	12.9%	9.9%
EBITDA	26.8%	26.3%	15.4%	2.6%	12.9%
EBIT	25.7%	25.8%	18.7%	1.5%	12.4%
Net profit, adj.	111.6%	72.5%	-28.0%	54.9%	94.4%
Margins					
EBITDA margin	19.8%	21.2%	21.2%	19.3%	19.8%
EBIT margin	14.5%	15.4%	15.9%	14.3%	14.6%
Net profit margin	5.5%	8.0%	5.0%	6.9%	12.1%
Key Ratios					
ROE (%)	15.7%	21.7%	12.6%	14.2%	20.2%
ROA (%)	5.8%	8.4%	5.3%	6.3%	8.9%
Net Debt / (Cash)	29	2	(37)	162	145
Net Gearing (X)	19.3%	0.7%	Net Cash	61.6%	43.9%

Source: Company, Phillip Securities Research (Singapore) Estimates

*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
<-20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

Contact Information (Singapore Research Team)

Research Operations Officer
Mohamed Amiruddin - amiruddin@phillip.com.sg

Consumer | Healthcare
Soh Lin Sin - sohls@phillip.com.sg

Property | Infrastructure
Peter Ng - peterngmc@phillip.com.sg

Macro
Pei Sai Teng - peist@phillip.com.sg

Transport | REITs (Industrial)
Richard Leow, CFTe, FRM - richardleowwt@phillip.com.sg

REITs (Commercial, Retail, Healthcare) | Property
Dehong Tan - tandh@phillip.com.sg

Technical Analysis
Jeremy Ng - jeremyngch@phillip.com.sg

Banking and Finance
Jeremy Teong - jeremyteongfh@phillip.com.sg

US Equity
Ho Kang Wei - hokw@phillip.com.sg

Oil & Gas | Energy
Chen Guangzhi - chengz@phillip.com.sg

Contact Information (Regional Member Companies)

SINGAPORE
Phillip Securities Pte Ltd
Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel +65 6533 6001
Fax +65 6535 6631
Website: www.poems.com.sg

MALAYSIA
Phillip Capital Management Sdn Bhd
B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel +603 2162 8841
Fax +603 2166 5099
Website: www.poems.com.my

HONG KONG
Phillip Securities (HK) Ltd
11/F United Centre 95 Queensway
Hong Kong
Tel +852 2277 6600
Fax +852 2868 5307
Websites: www.phillip.com.hk

JAPAN
Phillip Securities Japan, Ltd.
4-2 Nihonbashi Kabuto-cho Chuo-ku,
Tokyo 103-0026
Tel +81-3 3666 2101
Fax +81-3 3666 6090
Website: www.phillip.co.jp

INDONESIA
PT Phillip Securities Indonesia
ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel +62-21 5790 0800
Fax +62-21 5790 0809
Website: www.phillip.co.id

CHINA
Phillip Financial Advisory (Shanghai) Co Ltd
No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel +86-21 5169 9200
Fax +86-21 6351 2940
Website: www.phillip.com.cn

THAILAND
Phillip Securities (Thailand) Public Co. Ltd
15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel +66-2 6351700 / 22680999
Fax +66-2 22680921
Website www.phillip.co.th

FRANCE
King & Shaxson Capital Limited
3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel +33-1 45633100
Fax +33-1 45636017
Website: www.kingandshaxson.com

UNITED KINGDOM
King & Shaxson Capital Limited
6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel +44-20 7426 5950
Fax +44-20 7626 1757
Website: www.kingandshaxson.com

UNITED STATES
Phillip Capital Inc
141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1-312 356 9000
Fax +1-312 356 9005
Website: www.phillipusa.com

AUSTRALIA
Phillip Capital Limited
Level 10 330 Collins Street
Melbourne, Victoria 3000, Australia
Tel +61-03 9629 8288
Fax +61-03 9629 8882
Website: www.phillipcapital.com.au

SRI LANKA
Asha Phillip Securities Limited
2nd Floor, Lakshmans Building,
No. 321, Galle Road,
Colombo 03, Sri Lanka
Tel: (94) 11 2429 100
Fax: (94) 11 2429 199
Website: www.ashaphillip.net

INDIA
PhillipCapital (India) Private Limited
No.1, 18th Floor, Urmi Estate
95, Ganpatrao Kadam Marg
Lower Parel West, Mumbai 400-013
Maharashtra, India
Tel: +91-22-2300 2999 / Fax: +91-22-2300 2969
Website: www.phillipcapital.in

TURKEY
PhillipCapital Menkul Degerler
Dr. Cemil Bengü Cad. Hak Is Merkezi
No. 2 Kat. 6A Caglayan
34403 Istanbul, Turkey
Tel: 0212 296 84 84
Fax: 0212 233 69 29
Website: www.phillipcapital.com.tr

DUBAI
Phillip Futures DMCC
Member of the Dubai Gold and
Commodities Exchange (DGCX)
Unit No 601, Plot No 58, White Crown Bldg,
Sheikh Zayed Road, P.O.Box 212291
Dubai-UAE
Tel: +971-4-3325052 / Fax: + 971-4-3328895

CAMBODIA
Phillip Bank Plc
Ground Floor of B-Office Centre,#61-64,
Norodom Blvd Corner Street 306,Sangkat
Boeung Keng Kang 1, Khan Chamkamorn,
Phnom Penh, Cambodia
Tel: 855 (0) 7796 6151/855 (0) 1620 0769
Website: www.phillipbank.com.kh

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