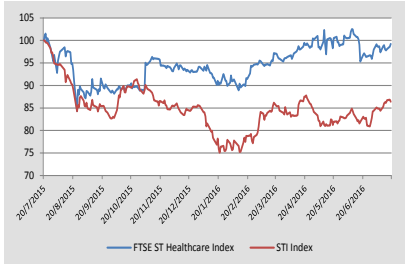


# Healthcare Services

FTSE Healthcare Index - 1 year (blue)



Source: Bloomberg, KGI Fraser

## Key Takeaways:

- ◆ Positive sector growth but current high valuations may already reflect upside potential
- ◆ Sector has outperformed STI and most other sectors over the past 1 year
- ◆ Based on P/E and Justified P/B valuation, investors may prefer to accumulate healthcare stocks at entry levels 5-15% lower than current prices. These include Raffles Medical, IHH Healthcare, Q&M Dental and Singapore O&G
- ◆ P/E Table ([page 6](#))
- ◆ P/B Table ([page 7](#))
- ◆ Singapore healthcare industry trends ([page 8](#))

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## Healthy sector but wait for price weakness to buy

Singapore healthcare stocks have outperformed the STI index over the past 1-2 years. Valuations are at their multi-year highs. Future growth potential (e.g., expansion plans locally and overseas) and healthy earnings growth over the past two years are driving their current high valuations, in our view. Healthcare stocks' current valuations may continue to be supported by earnings growth and their defensive nature amid an uncertain economic landscape. Hence, we believe that the healthcare sector may continue to outperform the general market. Investors looking for exposure to the healthcare sector may accumulate during price pullbacks.

**Sector riding on supportive long-term trends.** The healthcare sector is riding on structural changes in Singapore's population age profile. Our aging population is expected to require more healthcare services. Furthermore, medical tourism is recovering as regional currencies stabilize and as income levels continue to rise. Singapore ranks highly for its efficient healthcare system and we believe local private healthcare services can continue to tap into this growing segment despite increased competition in the region from countries like Thailand and Malaysia.

**Tapping on new and opening markets.** Key SGX-listed healthcare players like IHH Healthcare (IHH), Raffles Medical Group (RMG) and Q&M Dental (Q&M) are expanding into China, given its huge market potential. China represents a significant market for healthcare companies as the country only spends 5% of GDP on healthcare against 10% for the developed nations. Long term trend is also driven by an aging population with people in China aged 65 and older increasing to 331m by 2050 from 132m in 2015, according to estimates by the UN Population Division.

**Accumulate healthcare services stocks at 5-15% discount to current prices.** Based on P/E and justified P/B approach (page 6 & 7) and utilizing Bloomberg consensus forecasts, most of the healthcare stocks are trading inline or above their fair values, including RMG (FV S\$1.60 based on blended 34x FY16/17F P/E), IHH Healthcare (FV S\$2.11 based on 44x blended FY16/17F P/E), Q&M (FV S\$0.71 based on 32x blended FY16/17F P/E) and Singapore O&G (FV S\$0.89 based on 23x blended FY16/17F P/E).

**Key catalysts.** Short term catalysts may include spin off of subsidiaries (e.g., Q&M) or earnings accretive acquisitions given that most healthcare companies are in a net cash position.

**Key risks.** Appreciation of the SGD against regional currencies, notably the Indonesian Rupiah, may affect medical tourism. Indonesian market makes up around ~60% of medical tourism revenues. Delays in expansion in overseas markets due to regulatory hurdles.

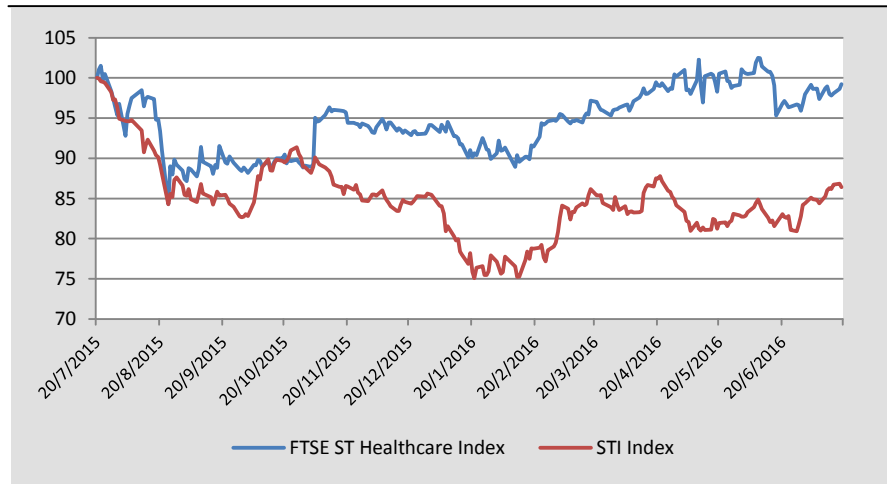
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**Singapore healthcare sector performance**

Singapore’s healthcare stocks, represented by the FTSE ST Healthcare Index, has outperformed the overall market (STI Index) over the past year by at least 10 percentage points. Investors have been shifting to the defensive healthcare sector given positive earnings growth compared to flat/negative earnings growth in other sectors. Healthcare is a necessity and thus shielded from slowing economic growth. However, healthcare companies geared towards medical tourism may be relatively more volatile given external factors (e.g., foreign exchange volatility) that may affect demand.

**Figure 1: Singapore Healthcare Index has outperformed the overall market**



Source: Bloomberg, KGI Fraser

**Figure 2: Comparison among all the Singapore indices show the healthcare sector among the top performers over 1 year**

Company Name	Price	6 Months Performance	1 Year Performance
Straits Times Index STI	2,915.70	12.36	(9.94)
FTSE ST Technology	246.02	(14.21)	(36.32)
FTSE ST Real Estate	668.98	3.75	(4.80)
FTSE ST Consumer Svcs	760.13	4.74	(2.62)
FTSE ST Consumer Goods	518.48	26.04	8.70
FTSE ST Utilities	397.79	4.46	(9.27)
FTSE ST Telecom	1,088.70	20.35	1.98
FTSE ST Industrials	686.84	5.33	(6.24)
FTSE ST Financials	768.10	11.29	(0.92)
FTSE ST Basic Materials	99.17	(0.31)	(9.93)
FTSE ST Real Estate Index	710.35	9.69	(4.86)
FTSE ST Oil & Gas Index	327.79	8.60	(2.51)
FTSE ST Mid Cap Index	685.83	10.33	(4.90)
FTSE ST Maritime Index	190.50	(1.28)	(8.81)
FTSE ST Large & Mid Index	1,014.35	11.51	(7.98)
FTSE ST Healthcare Index	1,550.96	9.90	10.55
FTSE ST Fledgling Index	686.40	(13.44)	(20.09)
FTSE ST China Top Index	162.27	4.72	(4.40)
FTSE ST China Index	192.36	3.12	(5.88)
FTSE ST Catalyst Index	447.27	(0.82)	(29.25)

Source: Bloomberg, KGI Fraser

**Outperforming stocks in hospital and healthcare services**

IHH, Q&M and Singapore O&G outperformed their peers in the healthcare sector on a one year basis, gaining between 3%-15%, compared to a 1% gain in the FTSE ST Healthcare index. These three stocks have been reporting earnings growth of 15%-36% YoY for the past two financial years. We believe this is one key factor that supports their outperformance over peers. The hospital services subsector is estimated to report earnings growth of ~10% YoY in FY16, according to Bloomberg consensus. Q&M, Singapore O&G and ISEC Healthcare are expected to be the fastest growing companies in the healthcare sector, with average earnings growth of ~30% over the next three years, according to Bloomberg consensus.

We believe the potential earnings growth is already reflected in their high valuations (30-45x FY15 P/E). However, given the healthcare sector's positive earnings growth relative to other sectors which are reporting flat/negative growth, we believe it is likely to continue to outperform the market in the coming 3 to 6 months.

**Figure 3: Singapore healthcare sector companies - hospital and healthcare services**

Company	Bloomberg Ticker	Price (Lcl curr)	Mkt Cap (US\$m)	P/E (x) (hist)	P/E (x) (fwd)	P/B (x)	ROE (%)	ROE (%) (fwd)	EV/EBITDA (x) (ttm)	EV/EBITDA (x) (fwd)	EV/EBITDA (x) (fwd 2 yr)	Net Gearing (%)	Dvd Yld (%)	Beta
<b>HOSPITAL SERVICES</b>														
Raffles Medical Group	RFMD SP	1.57	2,022	38.5	31.3	4.4	12	13	28.5	25.5	22.2	NC	1.3	0.6
Health Management Int'l	HMI SP	0.34	145	26.0	na	3.7	15	na	8.1	na	na	NC	na	0.8
IHH Healthcare	IHH SP	2.21	13,457	na	41.1	na	5	5	na	23.5	20.4	18.9	0.5	0.6
<b>HEALTHCARE SERVICES</b>														
Q&M Dental Group	QNM SP	0.71	415	43.6	29.4	6.0	14	17	26.9	21.6	18.5	26.0	1.2	0.8
Cordlife Group	CLGL SP	1.27	244	9.2	43.8	2.6	26	5	42.4	23.7	27.1	NC	0.8	0.4
Talkmed Group	TKMED SP	1.02	493	18.7	16.6	10.3	57	58	12.8	13.0	12.5	NC	4.5	0.5
Singapore O&G	SOG SP	0.96	168	35.8	23.3	8.7	30	32	31.8	20.0	17.1	na	2.1	na
Int'l Healthway Corp	IHC SP	0.06	70	13.1	na	0.5	4	na	na	na	na	166.4	na	0.9
ISEC Healthcare	ISEC SP	0.30	109	39.5	18.8	2.7	7	15	18.3	10.4	8.9	NC	1.5	na
Healthway Medical Corp	HMED SP	0.03	53	na	na	0.4	(1)	na	60.3	na	na	7.0	na	0.9
<b>Average</b>				<b>28.0</b>	<b>29.2</b>	<b>4.3</b>	<b>16.9</b>	<b>20.8</b>	<b>28.6</b>	<b>19.7</b>	<b>18.1</b>	<b>54.5</b>	<b>1.7</b>	<b>0.7</b>

Source: Bloomberg, KGI Fraser

**Figure 4: Singapore healthcare sector companies' 3 year net income and Bloomberg consensus forecasts**

Company	Net Profit (\$m)			Net Profit Forecast (\$m) - Bloomberg Consensus		
	FY13	FY14	FY15	FY16F	FY17F	FY18F
<b>HOSPITAL SERVICES</b>						
Raffles Medical Group Ltd	84.9	67.6	69.3	76.5	87.6	104.6
Health Management Intl Ltd	3.0	6.2	10.5	na	na	na
IHH Healthcare Bhd	250.8	292.1	329.9	356.9	434.0	521.0
<b>HEALTHCARE SERVICES</b>						
Q & M Dental Group Singapore	6.5	8.6	11.4	15.8	19.4	21.5
Cordlife Group Ltd	13.5	30.5	32.5	6.8	8.4	9.4
Talkmed Group Ltd	28.2	38.5	37.3	38.7	40.2	41.8
Singapore O&G Ltd	3.1	4.2	5.3	8.6	9.8	11.2
International Healthway Corp	44.5	37.3	7.1	na	na	na
ISEC Healthcare Ltd	6.0	2.0	2.8	7.0	8.4	9.2
Healthway Medical Corp Ltd	30.6	9.8	1.7	na	na	na
Company	Percentage Change (%) YoY			Percentage Change (%) YoY		
	FY13	FY14	FY15	FY16F	FY17F	FY18F
<b>HOSPITAL SERVICES</b>						
Raffles Medical Group Ltd	49.3%	(20.3%)	2.4%	10.4%	14.5%	19.4%
Health Management Intl Ltd	(1651.6%)	104.5%	68.7%	na	na	na
IHH Healthcare Bhd	(17.4%)	16.5%	13.0%	8.2%	21.6%	20.0%
<b>HEALTHCARE SERVICES</b>						
Q & M Dental Group Singapore	29.2%	32.6%	33.1%	38.9%	22.5%	10.6%
Cordlife Group Ltd	94.7%	126.3%	6.4%	(79.1%)	23.5%	11.9%
Talkmed Group Ltd	(11.8%)	36.6%	(3.1%)	3.7%	3.9%	4.0%
Singapore O&G Ltd	4.0%	36.1%	25.7%	61.0%	14.0%	14.3%
International Healthway Corp	617.6%	(16.1%)	(80.8%)	na	na	na
ISEC Healthcare Ltd	4.6%	(67.4%)	40.3%	153.6%	20.0%	9.5%
Healthway Medical Corp Ltd	302.3%	(67.8%)	(82.9%)	na	na	na

Source: Bloomberg, KGI Fraser

**Strong earnings growth may already be reflected in their current valuations**

Based on P/E and P/B valuation metrics (Figure 5 and 6), most of the healthcare stocks are currently trading inline or above their fair values. Investors seeking exposure to the healthcare sector may accumulate at 5-15% discount to their current price levels.

We believe current valuations may already be pricing in growth potential. Estimates for earnings growth, according to Bloomberg Consensus, is also expected to come in lower compared to historical trends. Consensus earnings estimates have been revised lower for FY16 and FY17, which may indicate macro headwinds and slower-than-expected growth from expansion plans.

**Figure 5: Estimated fair values based on Bloomberg consensus and P/E approach**

	Forecast Net Profit <sup>1</sup>	3 year Earnings CAGR <sup>2</sup>	3 years ROE Forecast average	P/E Multiple <sup>3</sup> (A)	P/E Multiple basis	Earnings Estimate /share <sup>4</sup> (B)	Fair Value (A) x (B)	Current Price	Upside/Price (Downside)
	\$m	%	%	x		S\$/sh	S\$/sh	S\$/sh	%
<b>HOSPITAL SERVICES</b>									
Raffles Medical Group Ltd	\$82.1	14.7%	13%	34.0	+1SD 5 yrs avg	\$0.05	1.60	1.57	2.1%
Health Management Intl Ltd								0.34	
IHH Healthcare Bhd	\$395.5	16.5%	6%	44.0	3 yrs avg	\$0.05	2.11	2.21	(4.3%)
<b>HEALTHCARE SERVICES</b>									
Q & M Dental Group Singapore	\$17.6	23.4%	17%	32.0	Peer avg + 10% premium	\$0.02	0.71	0.71	0.4%
Cordlife Group Ltd								1.27	
Talkmed Group Ltd								1.02	
Singapore O&G Ltd	\$9.2	28.0%	35%	23.0	Peer avg - 20% discount	\$0.04	0.89	0.96	(7.1%)
International Healthway Corp								0.06	
ISEC Healthcare Ltd								0.30	
Healthway Medical Corp Ltd								0.03	

1 - Based on Bloomberg Consensus; 2 years forecast average

\*We have only included Bloomberg consensus Net Profit for companies with 2 or more estimates

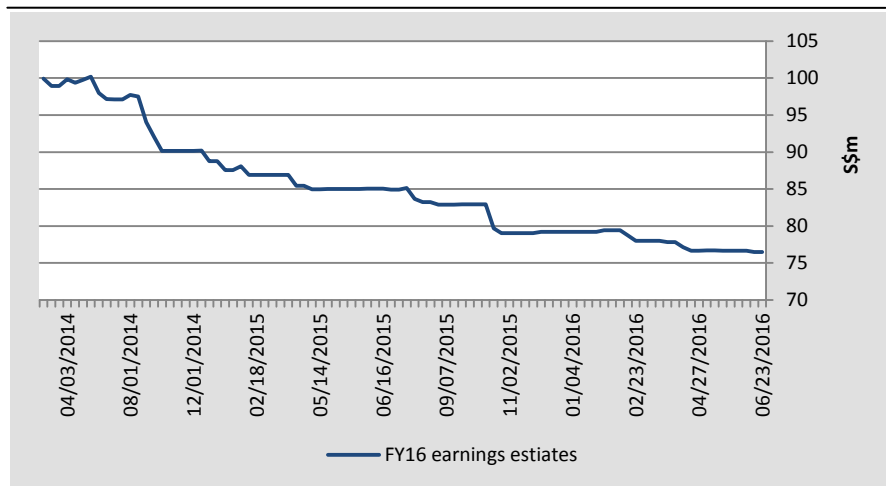
2 - Forecast 3 years CAGR

3 - Based on 3-5 years PE average or peer average adjusted for market cap and other key risk factors; premium given for short term positive catalysts

4 - Based on Bloomberg Consensus, 2 year forecast average

Source: Bloomberg, KGI Fraser

**Figure 6: RMG FY16 earnings forecast revised lower by 10-15% YoY**



Source: Bloomberg Consensus forecast, KGI Fraser

**Figure 7: Estimated fair values based on Bloomberg consensus and Justified P/B approach**

	Forecast ROE <sup>1</sup>	Req'd rate of return <sup>2</sup>	Sustainable growth rate	Justified P/B <sup>3</sup> (A)	Current P/B	Book Value Estimate <sup>4</sup> (B)	Fair Value (A) x (B)	Current Price	Upside/ (Downside)
	%	%	%	x	x	S\$/sh	S\$/sh	S\$/sh	%
<b>HOSPITAL SERVICES</b>									
Raffles Medical Group Ltd	13%	5.7%	3%	3.7	4.2	0.41	1.53	1.57	(2.0%)
Health Management Intl Ltd								0.34	
IHH Healthcare Bhd	6%	4.2%	3%	2.1	2.5	0.91	1.93	2.21	(12.7%)
<b>HEALTHCARE SERVICES</b>									
Q & M Dental Group Singapore	17%	5.7%	3%	5.3	6.2	0.13	0.68	0.71	(3.2%)
Cordlife Group Ltd								1.27	
Talkmed Group Ltd								1.02	
Singapore O&G Ltd	35%	8.0%	3%	6.5	7.4	0.12	0.78	0.96	(18.4%)
International Healthway Corp								0.06	
ISEC Healthcare Ltd								0.30	
Healthway Medical Corp Ltd								0.03	

1 - Based on Bloomberg Consensus; 3 years forecast average

\*We have only included Bloomberg consensus ROE for companies with 2 or more estimates

2 - Required rate of return based on CAPM (risk free + equity mkt premium \* Beta); KGI adjustments for company size and country risks

3 - Justified P/B = (ROE-g)/(r-g) where ROE=Return on Equity; g=sustainable growth rate; r=required rate of return

4 - Based on Bloomberg Consensus, 1 year forecast

Source: Bloomberg, KGI Fraser

### Healthcare stocks generally have low correlation to other sectors

RMG has the highest correlation to the FTSE ST Healthcare index given that it has the highest weightage in the index. Among all the healthcare stocks (including pharmaceuticals), Tianjin Zhong Xin Pharmaceutical (TZXP) has the highest correlation to the FTSE ST China Index due to its businesses that are mainly concentrated in China. Other than TZXP, which has the highest correlation to the STI and Financials index, all the other healthcare stocks have little correlation to the other sectors.

**Figure 8: Correlation of Healthcare stocks VS FTSE ST Indices**

	Straits Times STI	FTSE ST Health Care Index	FTSE ST Consumer Goods	FTSE ST Telco	FTSE ST Financials Index	FTSE ST Oil & Gas Index	FTSE ST Real Estate Index	FTSE ST China Index
Tianjin Zhong Xin	0.6	0.6	0.5	0.4	0.6	0.5	0.5	0.6
IHH Healthcare	0.4	0.2	0.3	0.5	0.4	0.2	0.4	0.5
Raffles Medical	0.4	0.8	0.3	0.4	0.4	0.3	0.2	0.3
Singapore O&G	0.4	0.4	0.3	0.2	0.4	0.3	0.3	0.3
Q & M Dental	0.4	0.4	0.3	0.3	0.4	0.3	0.3	0.3
Riverstone	0.3	0.3	0.1	0.1	0.3	0.2	0.4	0.3

Source: Bloomberg, KGI Fraser

### Key drivers of the healthcare industry

The favorable dynamics in the healthcare sector is driven by three major trends:

1. Population growth
2. Higher life expectancy and increased healthcare requirements from older people
3. Medical tourism on rising affluence and opening of new markets

In Singapore's context, the first two key drivers depend on long-term demographics trends, notably from population growth - birth rate and contribution from immigration - and an aging population. Meanwhile, medical tourism continues to ride on rising affluence in the region and Singapore's reputation of providing quality care, despite increasing competition from other countries in the region. Singapore healthcare companies are adopting growth strategies with both local and overseas expansion to tap on all three key drivers.

### Singapore Healthcare landscape (private vs public)

In Singapore, 80% of the primary healthcare services are provided by private practitioners while the government polyclinics provide the remaining 20%. The opposite is true for more costly hospitalization care, where 80% of it is provided by the public sector and 20% by the private sector.

Among the major private healthcare providers listed in Singapore are IHH Healthcare and RMG. These companies are tapping on local growth and investing in overseas expansion to ride on favorable industry dynamics. Private sector hospitals are registering faster growth rates in terms of patient admissions into hospitals. Private sector admissions grew at a CAGR of 2.9% compared to 2.3% in the public sector from 2006 to 2015.

### Singapore government spending more to meet increased demand

Looking at Singapore's government expenditure on healthcare gives us a sense of just how fast spending in the sector is growing. We estimate that cost inflation and increase in healthcare demand contributes equally to the rapid growth in spending. The government's operating expenditure on healthcare increased from S\$1.8bn in 2006 to S\$7.8bn in 2015, basically quadrupling the amount in a span of 9 years. The emphasis on healthcare spending by the government is now taking a larger share of GDP and government expenditure at 1.9% of total GDP and 11.9% of total government expenditure in 2014.

**Figure 9: Higher government expenditures to cater to both increasing quantitative and qualitative healthcare demand**

Government Health Expenditure	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15 <sup>P</sup>
Operating Expenditure (\$m)	1,840	2,020	2,379	2,920	3,258	3,489	4,066	5,044	5,872	7,773
Development Expenditure (\$m)	96	185	337	711	485	453	605	723	1,147	1,474
Government Health Expenditure <sup>1</sup> (\$m)	2,010	2,283	2,814	3,746	3,857	4,085	4,881	5,952	7,322	na
Government Health Expenditure <sup>1</sup> (as % of GDP)	0.8	0.8	1.1	1.3	1.2	1.2	1.3	1.6	1.9	na
Government Health Expenditure <sup>1</sup> (as % of Total Government Expenditure)	6.7	6.9	7.4	8.1	8.2	8.3	9.7	10.9	11.9	na

**Notes:**

1- Includes expenditure from endowment funds

p- Preliminary

na- not available

Source: MOH, KGI Fraser



**Demand for both public and private hospitals**

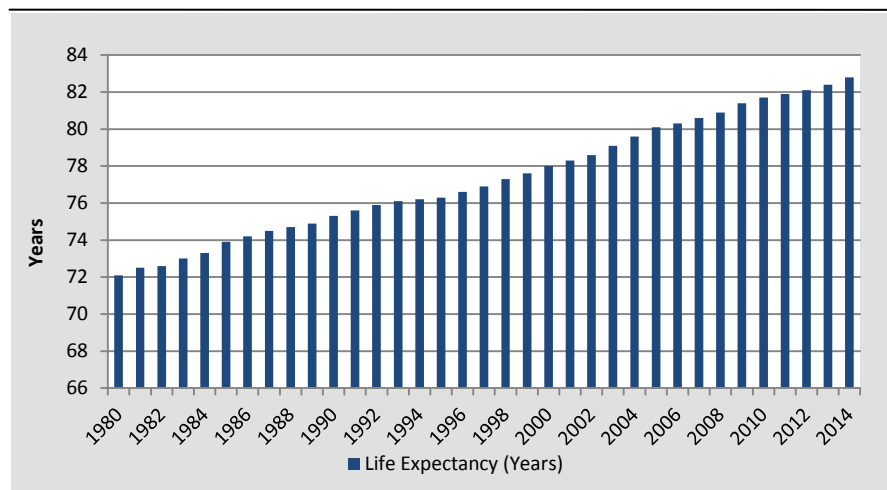
Singapore’s government has already planned one new acute or community hospital on average to come online until 2020. Although most of hospital services demand is expected to be met by public hospitals, historical trends have shown that private hospitals have seen faster growth in demand compared to public hospitals, in terms of total admissions to hospital. (Figure 10)

**Figure 10: Private hospitals are growing faster than public hospitals, based on total hospital admissions**

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015p
Total Hospital Admissions	409,490	422,534	421,606	423,249	437,529	456,461	468,795	483,001	499,025	509,079
Public	316,261	325,772	330,071	332,595	343,332	357,026	362,458	373,021	381,711	388,959
Private	93,229	96,762	91,535	90,654	94,197	99,435	106,337	109,980	117,314	120,120
Public % of total admissions	77.2%	77.1%	78.3%	78.6%	78.5%	78.2%	77.3%	77.2%	76.5%	76.4%
Private % of total admissions	22.8%	22.9%	21.7%	21.4%	21.5%	21.8%	22.7%	22.8%	23.5%	23.6%

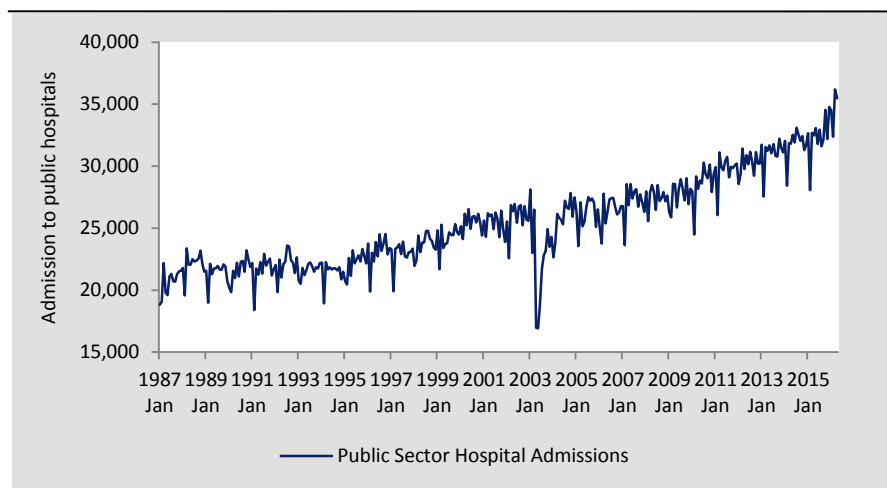
Source: MOH, KGI Fraser

**Figure 11: People are living longer, leading to increased demand in healthcare services**



Source: Department of Statistics, KGI Fraser

**Figure 12: Public hospital admissions continue to grow**

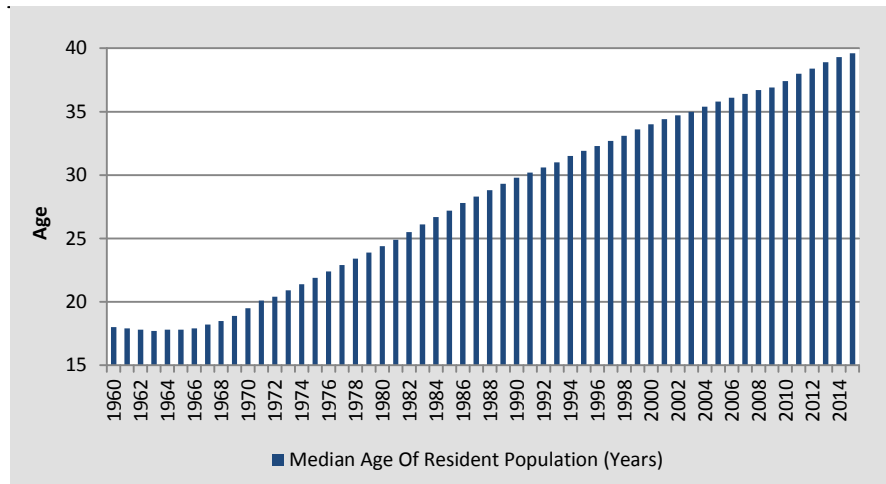


Source: MOH, KGI Fraser

**Significant increase in demand in next 10-15 years**

In the next 10-15 years, Singapore’s largest age group (50-59 year olds) is expected to reach a stage where healthcare demands increase substantially. Data provided by MOH shows that those 60 and above are twice as likely to be admitted to hospital as those that are 50 years old and younger. Singapore’s population is aging, with the median age of our resident population increasing from around 25 years old in the 1980s to 40 years old in 2015. As of June 2015, 13.1% of Singapore’s population is aged 65 and above compared to 8.8% in 2005. By 2050, almost 30% of Singapore’s population will be 65 and older.

**Figure 13: Singaporeans are getting older and require more healthcare related services**

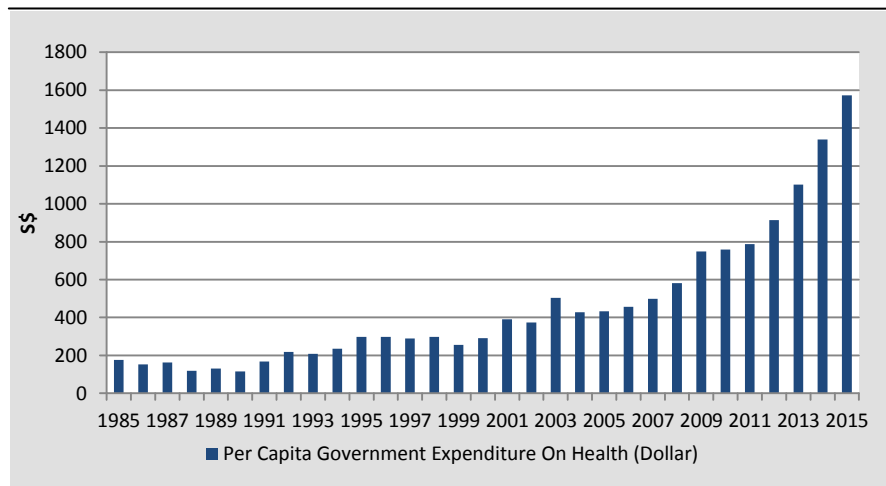


Source: Department of Statistics, KGI Fraser

**Increased care for aging population requires more spending**

Singapore’s government spending per capita in the healthcare sector has increased at 8% CAGR between 1985 and 2015 and is expected to rise 8-9% pa until 2018, according to the Economist Intelligence Unit. Total spending on healthcare in Singapore makes up around ~4.0% of Singapore’s GDP, slightly below Malaysia (4.4% of GDP in 2013) and higher than Thailand (3.3% of GDP in 2013). This is still significantly lower compared to developed nations’ spending on healthcare which makes up ~10% of their GDP.

**Figure 14: SG government is increasing spending on new hospitals and personnel**



Source: MOH, KGI Fraser

**Top 12 Medical Tourist Destinations by volume of care**

1. Thailand
2. Hungary
3. India
4. Singapore
5. Malaysia
6. Philippines
7. United States
8. Costa Rica
9. Brazil
10. Mexico
11. South Korea
12. Colombia

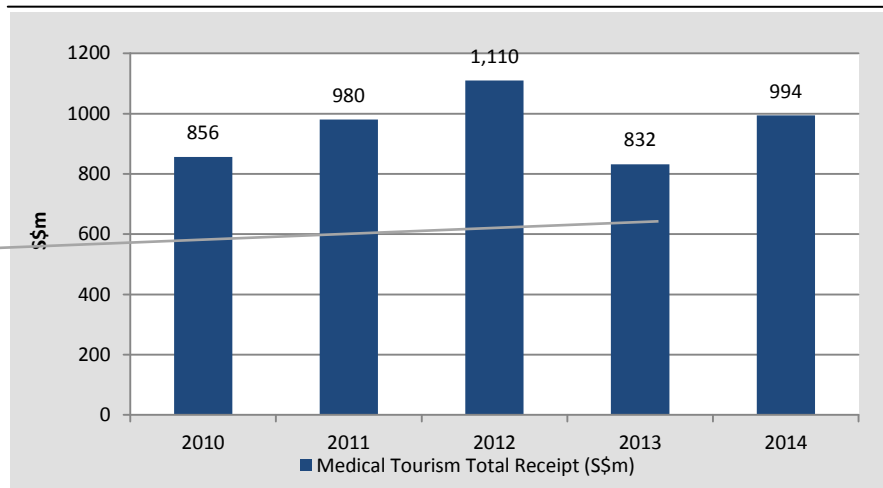
Source: Frost & Sullivan

**Singapore medical tourism**

International patients come to Singapore each year for a whole range of medical care from health screenings to high-end surgical procedures in cardiology, neurology, oncology, ophthalmology, organ transplants, orthopaedics. In 2014, medical expenditure generated from tourists was S\$994m, according to the STB. Indonesians make up 65% of total spending on medical tourism receipts, followed by Malaysians (7%) and Americans (5%). Rising affluence in the region is expected to contribute positively to future growth in medical tourism, as local governments in the region are unable to keep up with healthcare demands, in our view.

Singapore healthcare system ranks among the top in the world. In 2014, it was ranked most efficient healthcare system out of 51 countries by Bloomberg. Singapore was also ranked first as a global favourite medical tourism destination in PHD Chamber Medical and Wellness Tourism Report in 2013. According to the Economist Intelligence Unit (EIU), Singapore was ranked second in the world for healthcare outcomes in 2014. Singapore has 21 hospitals and medical centres and organizations that have obtained the Joint Commission International (JCI) accreditation, the most in Southeast Asia.

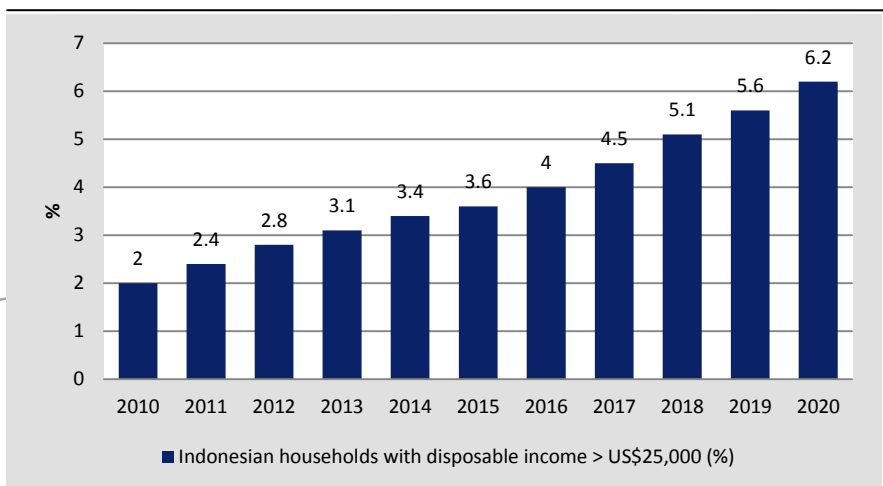
**Figure 15: Medical tourism receipts are recovering after a drop in 2013**



Drop in 2013 due to appreciation of SGD against regional currencies such as the Indonesian Rupiah

Source: Singapore Tourism Board, KGI Fraser

**Figure 16: Indonesia expected to be the growth engine in Southeast Asia**

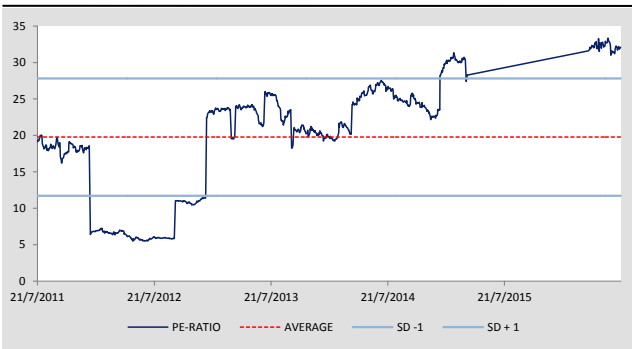


Growing affluence in Indonesia is expected to contribute positively to Singapore's medical tourism sector. Indonesia makes up 65% of medical tourism receipts.

Source: Euromonitor, KGI Fraser

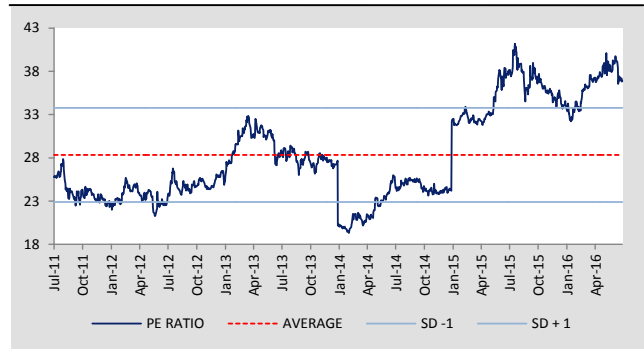
Appendix: 5 year forward P/E trading ranges

**ST Healthcare Index 5 years forward P/E**



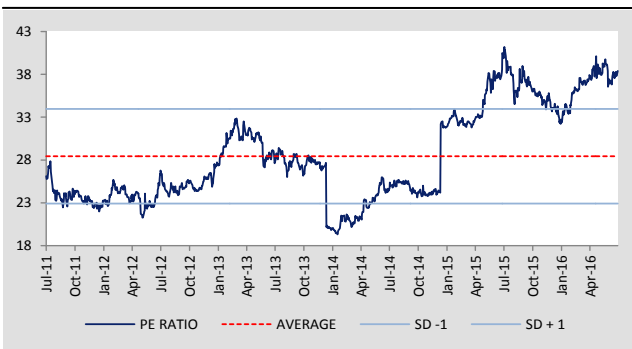
Source: Bloomberg, KGI Fraser

**Raffles Medical Group 5 years forward P/E**



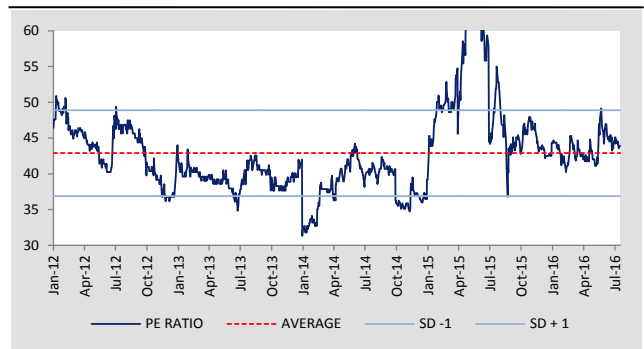
Source: Bloomberg, KGI Fraser

**IHH Healthcare 5 years forward P/E**



Source: Bloomberg, KGI Fraser

**Q&M Dental 5 years forward P/E**



Source: Bloomberg, KGI Fraser

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