

Singapore Healthcare

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Second time lucky?

- Economic Times reported that IHH is set to launch a voluntary open offer for Fortis Healthcare, potentially competing with TPG-Manipal Hospitals
- We do not rule out this possibility given i) Fortis Healthcare's share price has fallen some 23% since IHH walked out on the previous negotiations, and ii) IHH has secured a warchest of USD2bn multi-currency bonds and issued USD500m of perpetual securities
- If a takeover is successful, the buyout offer for RHT could likely go through (RHT's current price at 77.5 Scents vs offer price of 90 Scents). On a combined basis, we estimate the acquisition to be at 18x FY19F EV/EBITDA
- Market could be sceptical given unresolved issues within Fortis and the promoters. Integration costs could moderate IHH's near-term earnings growth potential but we note that IHH has successfully turned around Global and Continental Hospitals within one year of acquisition

What's New

Economic Times reported IHH is set to acquire Fortis Healthcare, potentially competing with TPG-Manipal Hospitals. Economic Times reported that IHH is set to launch a voluntary open offer to buy the non-promoter shares of Fortis Healthcare. This offer could be in competition with a TPG-Manipal Hospitals, who has expressed interest to acquire Fortis for INR6,500 crores (~INR125 per share) in early Mar 2018, according to news reports.

Just to recap on the events surrounding Fortis Healthcare, the promoters (Malvinder and Shivinder Singh) resigned from the board of Fortis Healthcare on 8 Feb 2018 in light of the recent Delhi High Court judgement to uphold Daiichi Sankyo's rights to enforce the arbitration award of INR3,500 crores. The resignations were accepted by Fortis' board on 13 Feb 2018. On 15 Feb 2018, the Supreme Court allowed financial institutions to sell the pledged shares of Fortis Healthcare by the promoters. The five lenders are Yes Bank, Axis Bank, RBL, ECL Finance and Indiabulls Housing Finance. Fortis Healthcare's share price fell 4% to INR137.50. According to news reports, we understand that Yes Bank had acquired 17.3% stakes in Fortis Healthcare following this.

Do not rule out the possibility given Fortis Healthcare's valuation looking more attractive and IHH secured a warchest. We do not rule out the possibility that IHH could still be interested in Fortis Healthcare despite walking out on the negotiations in mid-2017, as Fortis Healthcare's share price has fallen some 23% from close to INR200 to the last closing price of INR152.55 and after having secured a warchest of USD2bn multi-currency bonds and the issuance of USD500m of perpetual securities in 2017. At the current price, it is trading at forward EV/EBITDA of 19x, below the historical average of 40x and close to -1SD of 14x.

Buyer should keep in mind of RHT's buyout offer by Fortis Healthcare. However, the potential buyer should keep in mind of the RHT's buyout offer from Fortis Healthcare of S\$0.90 per share made previously. On a combined basis (RHT+Fortis), we estimate the potential acquisition (at Fortis' current price + RHT's offer price) is at an FY19F EV/EBITDA of 18x, which is still attractive compared to its historical EV/EBITDA trading band.

If a takeover is successful, the buyout offer for RHT could likely go through. If the acquisition of Fortis Healthcare goes through, the offer to acquire all assets of RHT will likely be carried through as well. RHT's last closing price is at 77.5 Scents vs an offer price of 90 Scents.

Reiterate our view that integration costs could moderate IHH's near-term earnings growth potential but IHH shown strong track record with the acquisition of Global and Continental Hospitals. We reiterate our view that while the acquisition may elevate IHH's position to be the 2nd largest hospital operator in India and leapfrog its presence in India with some 30 hospitals (45 including pipeline hospitals), we believe the integration costs could potentially moderate its near-term growth potential.

While the market could be sceptical given the legal issues and news on the promoters siphoning money have yet to be resolved, we note that IHH has demonstrated its ability to integrate and turn around hospitals as seen in Global and Continental Hospitals, which turned EBITDA positive within one year after the hospital groups were acquired.

IHH – Maintain BUY, TP RM6.81. We maintain our BUY rating on IHH with a TP of RM6.81. We remain positive on IHH's growth plans, with a pipeline of new hospitals in China and a potential turnaround in India. We believe the ramp up in Gleneagles HK could offset some start-up losses in China and lead IHH into its next phase of growth. IHH's medium-term outlook is bright while it rides out its near-term gestation period for the new hospitals.

The key catalysts are i) shorter-than-expected gestation period for Gleneagles HK and other new hospitals, ii) better-than-expected organic performance, and iii) positive developments in new markets such as India.

RHT – Maintain HOLD, TP S\$0.85. We maintain our HOLD rating on RHT with a TP of S\$0.85 despite the latest developments, as the news has yet to be confirmed and there are legal issues surrounding the promoters or Fortis which have yet to be resolved. However, if the probability of a takeover increases, we believe there could be an arbitrage opportunity at the current share price vs the offer price.

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

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

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

Share price appreciation + dividends

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