Healthscope

Healthscope Limited
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Annual General Meeting – Managing Director and CEO's Address

19 October 2017

It is a great privilege to have been asked to lead Healthscope, one of the leading providers of healthcare services in Australia. My initial observations are of a company with strong foundations and a growth strategy that is delivering encouraging early results. However, there is no doubt that I arrive at Healthscope at the end of a challenging year.

At the core of our business is the delivery of quality clinical outcomes, exceptional patient care and support for our doctors in 45 hospitals across the country and 63 pathology laboratories across New Zealand, Malaysia, Singapore and Vietnam. This is only made possible by an extraordinary team of over 18,000 dedicated staff.

In addition to my immediate focus on improving and accelerating our performance and returns to shareholders, I also see opportunities for Healthscope to play an increasingly important role in the delivery of healthcare services in Australia.

Today, I will provide an overview of our FY17 results which reflect some industry and company specific challenges. I will then provide an update on the key initiatives which were outlined during our full year 2017 results presentation.

Turning to the financials, our continuing operations for FY17 excludes the standalone Medical Centres operations which were held as an asset for sale as at 30 June. Healthscope completed the divestment of these operations on 30 September this year.

For the continuing operations, revenue growth of 3.8% year on year translated to Group Operating EBITDA of $411.4 million, up 3.5% on FY16. Group Operating EBIT was $302.5 million, 0.7% down on last year, while Group Operating NPAT of $180.0 million declined 5.6% on the prior year. The results reflect challenges in the Hospital division combined with the impact of increased depreciation due to the opening of key brownfield sites over the past 18 months. Importantly, operational cash flows remained strong during FY17 with cash conversion of 101.6%, which is funding a substantial part of our hospital expansion program, the engine of our future growth.

Let me now take you through the performance of our operating divisions.

Hospitals

Revenue growth of 3.4% to $2.0 billion in the Hospital division was below expectations.

Victoria and Tasmania, which contribute around one third of the divisional EBITDA, underperformed with Operating EBITDA 8.7% lower than the previous year. This was due to a number of contributing factors, including increased competition at certain sites, slower than planned ramp up of patient volumes in the first few months of two of our newer facilities and higher wage costs.

The remainder of the hospital portfolio performed in accordance with our guidance provided during the year. The overall Hospital Operating EBITDA of $359.4 million grew by 1.3% year on year.

As noted by the Chairman, we are confident of the long-term private healthcare industry fundamentals. However, softer private hospital market conditions and variability in patient case mix have resulted in some margin pressures, where costs in certain areas of the business have grown faster than our health fund revenue increases.

As a result, we have a renewed focus and sense of urgency around driving improved performance during FY18 and beyond. To that end, we have identified four “Must Win” initiatives across the portfolio.

The first initiative is to accelerate profitable topline growth. This involves a site by site approach to identify measures to grow patient admissions and revenue. We have identified specific initiatives at the key hospital sites and implemented programs to optimise and grow patient case mix. Our success will be measured by achieving above market revenue growth in FY18.

The second initiative aims to drive greater operational efficiency through an enterprise-wide business improvement program. We have in progress a detailed benchmarking exercise across all our hospitals. The process has identified four main areas of improvement and, more importantly, opportunities to adopt best practice more broadly across the portfolio. Phase 2 of this project involves the rollout of the program across 12 of our largest hospitals.

The third initiative is to undertake a thorough review of our portfolio to understand the future role and growth potential of each hospital. The process is already underway with a review of the Victorian portfolio well advanced and a review of the rest of the portfolio planned to complete by December 2017.

The fourth and final “Must Win” initiative is to continue to successfully execute our brownfields expansion strategy and to deliver sustainable long-term profitable growth and shareholder return. During FY17, we invested $485 million in growth projects. Five hospital expansion projects were completed, delivering an additional 214 beds, 13 operating theatres and two emergency departments.

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We currently have seven projects under construction encompassing $1.1 billion of investment which includes around $840 million for the Northern Beaches Hospital in Sydney. As the Chairman mentioned, a further three brownfield projects have been approved and will commence construction in FY18, taking the value of capital committed to $1.2 billion.

Furthermore, on the Northern Beaches Hospital Project, I'm pleased to say that we finished the external physical structure during FY17, three months ahead of schedule. The internal fitout is progressing well and the project is on budget. Our progress against operational milestones gives us confidence we will be ready to treat patients from the planned opening date of December 2018.

New Zealand Pathology

Turning now to our pathology business, it was another successful year for New Zealand Pathology. By remaining focused on delivering high quality and cost effective community pathology services, Healthscope has retained its position as the partner of choice with the majority of District Health Boards in New Zealand.

During the year, the New Zealand operations delivered revenue growth of 8.9% on the previous year and Operating EBITDA growth of 17.7%. The strong performance reflected a number of factors. These included the full year impact of the Wellington contract and cost efficiencies from investment in new technologies.

We also expanded the scope of our commercial, veterinary and analytical businesses and established a specialised molecular diagnostics laboratory in Auckland. Healthscope is the first laboratory in New Zealand to offer non-invasive prenatal testing.

New Zealand Pathology is a great business and the team has delivered strong results year on year. In FY18, Operating EBITDA growth is planned to moderate.

Other

Given the divestment of the standalone Medical Centre operations, the Other segment now comprises the group's pathology operations across Singapore, Malaysia and Vietnam.

Each of our Asian pathology businesses generated revenue and EBITDA growth on a local currency basis. The reported results reflect adverse foreign exchange movements on translation to the Australian Dollar.

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Balance sheet

Turning to the balance sheet, Healthscope produces strong operating cashflows. The capital structure, together with the cash reserves and existing debt facilities, are designed with the capacity to deliver our brownfields program including the Northern Beaches Hospital and additional future projects.

Gearing is planned to rise to approximately 4.5x Net Debt to EBITDA as the Northern Beaches Hospital development completes. Following completion and the first 12 months of operation, the group balance sheet gearing is planned to normalise to approximately 3.0x Net Debt to EBITDA. As a result, we continue to have comfortable headroom on our bank covenants.

Commitment to clinical excellence, patient care and our people

First and foremost, at Healthscope, we recognise that clinical excellence and exceptional patient care are integral to our success as an organisation and our licence to operate in the sector.

Healthscope is an active participant in shaping industry measures to improve the quality of care and transparency of clinical outcomes. During FY18 we plan to introduce a number of new measures with the aim of continuing to be recognised as a market leader in this critical area.
I look forward to updating you of our progress on these measures during the year.

Extraordinary people and teams

It is only through the actions of our people that Healthscope can meet its standards of patient care and clinical excellence.

We recognise the importance of creating exceptional teams of people who are engaged and aspire to achieve the highest standards. We have a committed and dedicated team of over 18,000 employees including nurses, allied health professionals and non-clinical support staff. In addition, we partner with over 17,500 Accredited Medical Practitioners.

Healthscope also continued to make progress against the gender diversity objectives set by the Board. For senior roles, 50% of identified internal talent pools and 52% of short listed candidates for senior management positions were women, as outlined in our most recent Workplace Gender Equality Agency report.

I would like to take this opportunity to thank the management team, our staff and doctor partners for their hard work, dedication and efforts to ensure that we continue to deliver quality clinical outcomes and exceptional patient care each and every day.

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Conclusion

Finally, turning to our business outlook for FY18. We expect the current private hospital market conditions to continue in the short term. Four “Must Win” initiatives have been established to drive FY18 performance by developing and improving the core business while delivering on our expansion program.

For the Hospitals division, subject to there being no material change to external market conditions and barring unforeseen circumstances, FY18 Operating EBITDA for the Company’s Hospitals division is planned to be broadly similar to FY17. 1HFY18 Operating EBITDA is planned to decline year on year. The 2HFY18 Operating EBITDA is planned to deliver growth year on year, with that momentum to carry forward into FY19 and beyond.

Importantly, we are taking decisive actions to address both our short-term challenges, and to ensure we are ideally placed to take advantage of strong underlying industry fundamentals in the long-term.

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Managing Director and CEO's address

Divisional overview

Footprint across Australia, New Zealand and South East Asia[1]

45 Private hospitals

63 International laboratories

Victoria	New South Wales
17 Private hospitals	11 Private hospitals
Queensland	South Australia
7 Private hospitals	5 Private hospitals
Tasmania	Western Australia
2 Private hospitals	1 Private hospital
Northern Territory	ACT
1 Private hospital	1 Private hospital
New Zealand	Malaysia
24 Pathology laboratories	34 Pathology laboratories
Singapore	Vietnam
3 Pathology laboratories	2 Pathology laboratories

1. Healthscope's continuing operations consist of the hospital and international pathology businesses

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FY17 financial overview

Operating results from continuing operations[1]

$2.3b
FY17 REVENUE
⬆3.8%

$411.4m
FY17 OPERATING[2] EBITDA
⬆3.5%

$302.5m
FY17 OPERATING[2] EBIT
⬇0.7%

$180.0m
GROUP OPERATING[2] NPAT
⬇5.6%

1. Healthscope's continuing operations consist of the hospital and international pathology businesses
2. "Operating" results represent Statutory results from continuing operations adjusted for items of other income and expense of $17.4m (net of tax)

82%[1]

Hospitals

Hospital growth impacted by slower sector growth with mixed performance across portfolio

Segment results	FY17 ($m)	FY16 ($m)	Movement
Revenue	2,014.0	1,947.7	3.4%
Operating EBITDA	359.4	354.9	1.3%
Operating EBIT	272.6	281.4	(3.1%)

1. Contribution to Group Operating EBITDA from continuing operations

- Most states delivered good earnings growth, however, the VIC/TAS portfolio underperformed particularly in 2HFY17
- Four key “Must Win” imperatives have been established to drive performance improvement across the portfolio

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Key FY18 imperatives

Developing and improving the core whilst delivering on the expansion program

"MUST WINS"

Accelerate profitable topline growth	• Targeted growth initiatives identified at key sites in each state to improve overall admissions growth and revenue per patient day • Specific programs implemented to attract and retain the right doctors and case mix • Focus to drive above market revenue growth in FY18
Drive greater operational efficiency	• Accelerated business improvement program – Phase 1 – Detailed benchmarking completed across key hospitals. Four target areas of savings identified – Phase 2 – Commencement of implementation across 12 key hospitals
Optimise portfolio	• Review of Victorian portfolio, to be completed by end of October 2017 • Broader portfolio review to identify new areas of investment to be completed by December 2017
Continue to successfully execute brownfields	• Delivery of projects on time and on budget • Achieving target ROIC of not less than 15% for each project by the end of year 3 of the capacity being open

Hospital expansion program

Hospital expansion program will deliver profitable growth and shareholder returns

5 projects
completed in FY17

- 214 beds, 13 OTs and two EDs[1]
- Development cost $184m

7 projects
under construction

- 566 beds, 38 OTs and one ED
- Capital expenditure of approximately $1.1bn ($264m excluding NBH)[2]

3 projects
approved

- 76 beds
- Capital expenditure of approximately $52m

1. Net of Como Private (53 beds, 2 operating theatres) relocation to Holmesglen Private
2. Inclusive of capital invested in prior periods

14%[1]

New Zealand Pathology

New Zealand continued to deliver strong revenue and Operating EBITDA growth

Segment results	FY17 ($m)	FY16 ($m)	Movement
Revenue	242.5	222.7	8.9%
Operating EBITDA	59.7	50.7	17.7%
Operating EBIT	46.6	40.1	16.2%

1. Contribution to Group Operating EBITDA from continuing operations

- Strong performance driven by full year impact of Wellington contract, expanded scope of commercial, veterinary and analytical businesses and continued economies of scale being achieved with investment in new technology
- Operating EBITDA growth budgeted to moderate in FY18

4%[1]

Other[2]

Asian pathology operations generated revenue and EBITDA growth on a local currency basis with results reflecting adverse FX movements on translation to AUD

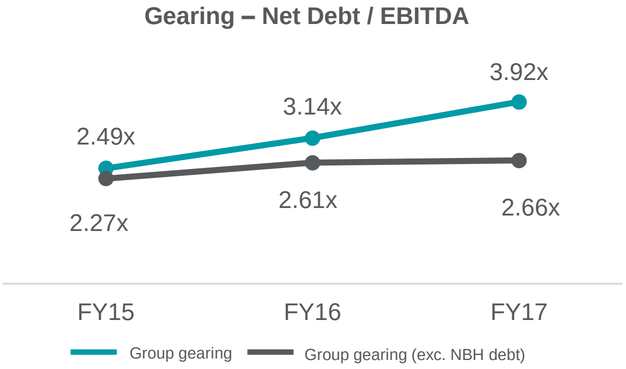
Segment results	FY17 ($m)	FY16 ($m)	Movement
Revenue	61.7	62.5	(1.3%)
Operating EBITDA	18.2	18.3	(0.4%)
Operating EBIT	14.0	14.2	(1.5%)

- Singapore pathology (revenue growth 2.3%, EBITDA growth 2.9%)[3]
- Malaysia pathology (revenue growth 6.2%, EBITDA growth 4.2%)[3]

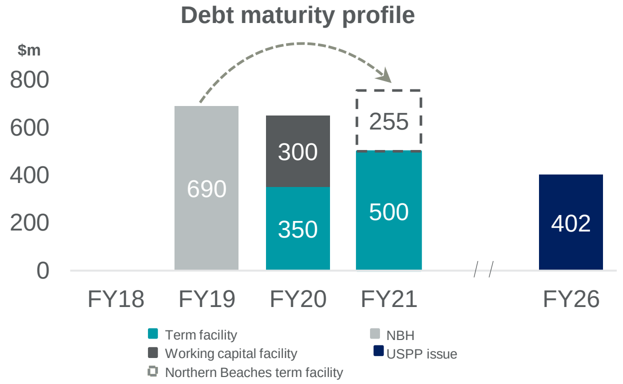
1. Contribution to Group Operating EBITDA from continuing operations
2. Medical Centres has been removed from ‘Other’ segment as business has been classified as a discontinued operation as at 30 June 2017
3. Based on results in local currency

Balance sheet and gearing

Long term funding arrangements in place to support investment program



- Group gearing increasing with NBH investment
- Capital payment for public portion of hospital and shared facilities to be received from NSW Government post transfer of patients from existing hospitals (expected early CY19)
- Following completion of NBH and first 12 months of operation, gearing expected to normalise to approximately 3.0x Net Debt / EBITDA



- Long term funding arrangements extend to FY26
- Undrawn bank facilities of $300 million at 30 June 2017
- NBH project finance facility will be partially repaid via NSW Government capital payment. Remaining balance will be converted to an already established corporate term debt facility and will form part of the debt security group

Clinical excellence, patient care and our people

Quality clinical outcomes and exceptional patient care

- Clinical excellence and exceptional patient care are integral to our success as an organisation
- Active participant in industry measures
- New measures planned with the aim of continuing to be recognised as a market leader in this critical area

Exceptional teams

- Committed and dedicated team of over 18,000 employees
- Partner with over 17,500 Accredited Medical Practitioners
- For senior roles 50% of identified internal talent pools and 52% of short listed candidates for senior management positions were women

Conclusion

- **Hospitals division**
  - Medium to long term growth for our Hospitals division continues to be supported by strong industry fundamentals
  - Ongoing private hospital market volatility and cost pressures expected to continue in the short term with four “Must Win” imperatives established to drive FY18 performance improvement across the portfolio
  - FY18 Hospitals division earnings outlook
    - 1HFY18 Operating EBITDA expected to decline yoy
    - 2HFY18 Operating EBITDA expected to deliver growth yoy
    - Operating EBITDA for the full year is expected to be broadly similar to FY17