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Healthscope announces results for six months ended 31 December 2013

27 February 2014

Healthscope Notes today announced half year results for the Healthscope Group for the period ended 31 December 2013.

Financial results for the period include:

- Revenue of $1,163.6 million, an increase of 4.4%;
- Operating EBITDA of $177.1 million(1), an increase of 13.7%;
- Net profit after tax of $20.7 million;
- Cash inflows from operations of $192.1 million, an increase of 9.3%;
- EBITDA cash conversion of 108.5%.

(1) Excludes other expenses (non-operating) of $6.8 million

The strong 1H14 performance was driven by strong results from the Hospitals and International Pathology divisions, and a much improved performance from the Australian Pathology division.

In summarising the interim results, Healthscope's Executive Chairman, Mr Robert Cooke, said "The 13.7% increase in 1H14 EBITDA clearly demonstrates that momentum continues to build across the businesses. It is now over three years since Healthscope was acquired by TPG and Carlyle, and the success of the strategies and initiatives put in place during this period are reflected in these results."

In commenting on the performance of the Hospitals division, Mr Cooke said "The Hospitals division continued its strong track record of performance, delivering EBITDA growth of 9.8% and EBITDA margin uplift of 60 basis points, reflecting the significant operating leverage in the business. Furthermore, this excellent result largely reflects organic performance, with minimal impact from brownfield projects in 1H14."

"The impact of brownfields projects is expected to ramp up from FY15 and beyond, as we deliver on the strong project pipeline that is in place. We are close to securing Development Applications for a number of major facilities and are confident these will be secured in the coming months, with construction commencing soon after. We also recently signed a new lease to extend Melbourne Private Hospital's tenure at its current location until 28 May 2020," Mr Cooke said.

"Another key element of the growth strategy for the Hospitals division is to relocate existing facilities to new, expanded facilities. Construction has commenced on the new Gold Coast Private Hospital, scheduled to open in 2016." Mr Cooke said.

In relation to Healthscope's market leading position for quality and clinical excellence, Mr Cooke said "Healthscope launched another innovative quality initiative during the period, Healthscope Never Events. In an Australian first, Healthscope has agreed with a major health fund to forgo payment for defined

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Never Events – events that should never happen in relation to the provision of healthcare. This reflects Healthscope's commitment to delivering best in class healthcare across its facilities."

"Healthscope's relationships with key health funds have continued to strengthen, with a number of contracts successfully renegotiated in recent months. Contracts and pricing are agreed until September 2015 for over 80% of our revenue base, providing funding certainty into the future. The innovation underpinning the MyHealthscope website and Never Events has attracted the attention and support of all major health funds. Healthscope is pioneering the link between quality and funding, with some health fund contracts now including quality payment components," Mr Cooke said.

"Healthcare is a relationships business, and the stability and ongoing investment in training programs for hospital executive teams is contributing to stronger relationships with doctors at the local level," Mr Cooke said.

In commenting on the growth prospects for the private hospital industry, Mr Cooke said "Health fund membership has continued to grow since the introduction of the means testing of the private health insurance rebate in July 2012, reflecting the importance of the private health sector to the overall health system and the strong value consumers place on the private health insurance product. This continues to provide a solid foundation for future growth of the private hospital industry."

"An ageing population and increasing prevalence of chronic disease are continuing to drive demand for both private and public hospital services. As the public system comes under increasing pressure, there will be opportunities for private operators to play an increasing role in delivering high quality and efficient public healthcare services."

"An example of this is the Northern Beaches Hospital project, where the NSW Government will partner with a private hospital provider to deliver the new 423 bed hospital, with the private operator to run the hospital for at least twenty years. Healthscope is excited to be one of two shortlisted parties for this exciting project," Mr Cooke said.

In relation to the International Pathology division, Mr Cooke said "Healthscope's International Pathology business continued its excellent performance, and the Malaysian and Singaporean businesses provide a strong platform for further growth in South East Asia."

Turning to Australian Pathology, Mr Cooke said "The successful turnaround of the Australian Pathology business is now evident in the results, with EBITDA increasing more than twofold compared to the prior corresponding period. Focus on profitable growth and tight cost management has underpinned the significant improvement in the performance of this business."

"Medical Centres also reported solid earnings growth in 1H14, and strategic links to Healthscope's other divisions are strengthening. An example of this are benefits for Bupa members that visit a Healthscope medical centre, which form part of Healthscope's broader, value-adding partnership with this key health fund," Mr Cooke said.

In summarising Healthscope's recent performance, Mr Cooke said "The last three years has been all about developing a strong platform for the future. We have put in place the strategies to deliver sustainable growth into the future and the 1H14 results demonstrate that these strategies are starting to

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deliver. Importantly, we are only part way through delivering on key operational initiatives, and the Group is now entering an exciting growth phase."

Group results

	1H14 $m	1H13 $m	Movement %
Revenue	1,163.6	1,114.8	4.4%
EBITDA (1)	177.1	155.8	13.7%
Depreciation	(47.2)	(46.7)	-1.1%
EBIT (1)	129.8	109.1	19.0%
Other expenses (refer below)	(6.8)	(123.3)	n/a
Net finance costs	(94.4)	(92.3)	-2.3%
Profit / (loss) before tax	28.6	(106.5)	n/a
Tax	(7.9)	(2.9)	n/a
Net profit / (loss) after tax	20.7	(109.4)	n/a
EBITDA margin %	*15.2%*	*14.0%*	*+120bp*
EBIT margin %	*11.2%*	*9.8%*	*+140bp*

(1) Operating EBITDA and Operating EBIT excludes other expenses (non-operating) of $6.8 million. EBITDA and EBIT excluding operating expenses (Operating EBITDA and Operating EBIT) is presented as it provides an understanding of the underlying trading performance of the business

The Healthscope Group recorded revenue growth of 4.4% to $1,163.6 million in 1H14, driven by the Hospitals and International Pathology divisions. EBITDA increased by 13.7% to $177.1 million, driven by solid growth in earnings across all divisions.

Note 1: Other expenses (non-operating)

	1H14 $m	1H13 $m
Restructure and other costs	(6.7)	(7.5)
Onerous leases and related costs	3.8	
Impairment of assets	(3.9)	
Impairment of goodwill - Australian Pathology		(120.0)
Profit on sale of operations		4.2
Total other expenses	**(6.8)**	**(123.3)**

Other expenses (non-operating) amounted to $6.8 million in 1H14. The restructure and other costs of $6.7m relate predominantly to Australian Pathology, and the impairment of assets of $3.9m relates to

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Brisbane Waters Hospital which is subject to a conditional sale agreement with Healthe Care Australia (Healthe). The $3.8m relating to the onerous contract results from a re-assessment of the provision as a consequence of re-negotiated lease terms.

Divisional results

Hospitals

	1H14 $m	1H13 $m	Movement %
Revenue	883.1	837.4	5.5%
EBITDA	149.5	136.2	9.8%
EBITDA margin %(1)	*16.9%*	*16.3%*	*+60bp*

(1)EBITDA margin includes prosthetics revenue and costs

Revenue growth in the Hospitals division was driven by a combination of volume and casemix.

Revenue growth was predominantly organic, with no new beds opened in 1H14, following on from the 54 beds opened in FY13. Following the change in ownership in October 2010, a full review of the brownfields pipeline was undertaken to refocus on projects at large, acute facilities. Given the timing from project conception to completion, new bed and theatre openings will continue be modest in FY14 before ramping up in FY15 and beyond.

Strong growth in earnings was recorded across acute, psychiatric and rehabilitation hospitals. The Hospitals EBITDA margin increased by 60 basis points, reflecting operating leverage and cost control. Key labour and procurement KPIs continued to trend in the right direction, which contributed to the robust margin uplift achieved by the Hospitals division.

In November 2013, Healthscope entered into an agreement with Healthe for the sale of Brisbane Waters Private Hospital in NSW. The parties have also agreed that Healthscope will purchase Healthe's Brunswick Private Hospital in Victoria.

Brunswick Private is a 128 bed rehabilitation and general medical facility, with outpatient and community based services, which will complement the surgical, medical and emergency focus of John Fawkner Private Hospital.

Finalisation of the transaction will require regulatory approvals, including from the ACCC. The ACCC's separate review of each of the Brunswick and Brisbane Waters potential transactions is continuing.

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Australian Pathology

	1H14 $m	1H13 $m	Movement %
Revenue	172.5	183.7	-6.1%
EBITDA	12.1	5.0	n/a
EBITDA margin %	*7.0%*	*2.7%*	*+430bp*

The Australian Pathology business had a significant improvement in profitability in 1H14 on the prior corresponding period, driven by a focus on profitable growth and tight cost management.

Revenue decreased by 6.1% in 1H14 reflecting the divestments undertaken in FY13, and the restructure and downsizing of the New South Wales pathology business. Excluding revenue from divested / closed operations, Australian pathology revenue growth was 4.8% in 1H14. All states contributed to this revenue growth.

The New South Wales business reported a significant increase in EBITDA in 1H14, reflecting the successful restructure of this business. The cost out initiatives implemented in FY13 combined with a focused marketing strategy, are delivering sustainable improvements in this state.

The Victorian, Queensland and South Australian businesses all delivered sound results.

The industry association is pushing for tighter regulation on market rents, and this matter will be the subject of further discussion with the Department of Health.

Medical Centres delivered solid earnings growth in 1H14, as focus continues to be on filling capacity at existing centres and cost management.

International Pathology

	1H14 $m	1H13 $m	Movement %
Revenue	108.0	93.7	15.2%
EBITDA	24.4	21.0	16.3%
EBITDA margin %	*22.6%*	*22.4%*	*+20bp*

International Pathology reported another strong result driven primarily by New Zealand and Singapore.

New Zealand delivered strong revenue growth which was partly driven by recent acquisitions and new contracts. The acquisition of the clinical pathology business of Diagnostic Medlab (DML) was completed in October, further cementing Healthscope's market leading position in this market. The strong revenue growth, combined with cost initiatives resulted in further margin uplift.

Labtests Auckland successfully secured an extension to its contract for Clinical Pathology services with the Auckland Regional District Health Boards for an additional three years. The original term of the

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agreement ended in September 2017 and the extension takes the contract through to the end of September 2020.

Singapore achieved strong revenue and earnings growth in 1H14, which was attributable to volume growth, favourable revenue yield and cost control.

The Malaysian business delivered an improved performance achieving solid volume growth in 1H14 after a period of softness in FY13, with good cost control.

Cashflow and balance sheet

Healthscope recorded cash flows from operations in 1H14 of $192.1 million, which compares to $175.8 million in the prior corresponding period. The Group continued its strong cash generation performance with EBITDA to cash flow conversion for the period at 108.5%.

The Healthscope Group had a net debt position of $1,540.1 million as at 31 December 2013, with a gearing ratio (net debt / net debt + equity) of 65.2%.[1]

The Total Leverage Ratio as at 31 December 2013 is 4.6.

Covenants

As at 31 December 2013 the Healthscope Group continued to meet all of its covenants.

Banking covenants December 2013:

Covenant	Actual Covenant Dec-13	Covenant limit Dec-13 quarter
Senior Gearing Ratio (Debt / EBITDA)	3.20X	<4.15X
Debt Service Cover Ratio	1.40X	>1.05X
Interest Cover Ratio (EBITDA / Net Interest Expense)	1.97X	>1.80X

Strategic review

The strong performance and growth profile of Healthscope's businesses has encouraged the owners of the Healthscope Group (who are also the owners of Healthscope Notes) to begin a strategic review process. It is expected that this process being undertaken by the owners of Healthscope Notes will take some time. Healthscope Notes will not make any further announcements in relation to this review unless there are developments which it determines ought to be announced immediately.

Further enquiries:

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[1] Net debt calculation excludes capitalised loan establishment fees in accordance with the definition of net debt in the Group's syndicated banking facility.

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NOTE 1: BACKGROUND

Healthscope Notes Limited was incorporated on 8 November 2010 as a special purpose vehicle to issue publicly listed debt instruments and on-lend the net proceeds raised from the issue of the debt instruments to Healthscope Finance Pty Ltd, a member of the Healthscope Group. As a result of its listing on the ASX, Healthscope Notes Limited is required to lodge annual and half yearly financial reports in accordance with the ASX Listing Rules and the Corporations Act. In addition, it will lodge with the ASX annual and half yearly financial reports for the Healthscope Group, which aggregate the financial performance, the financial position and the cash flows of:

- Healthscope Hospital Holdings No. 2 Pty. Ltd ACN 145 126 094 and its controlled entities;
- Healthscope Pathology Holdings No. 2 Pty Ltd ACN 146 342 832 and its controlled entities; and
- CT HSP Holdings (Dutch) B.V. registration no. 34308383 and its controlled entities;

(together the 'Healthscope Group') to provide the holders of Healthscope Notes with an understanding of the financial position of the Healthscope Group, which was referred to as the 'Security Group' in Healthscope Notes Ltd's prospectuses dated 24 November 2010 and 12 March 2013.

NOTE 2: RECONCILIATION TO NET PROFIT / (LOSS)

The following table reconciles the net profit/loss for the period to EBITDA before restructure and acquisition costs.

	Period ended 31 December 2013 $'000	Period ended 31 December 2012 $'000
Net profit/(loss) for the period	**20.7**	**(109.4)**
Add back:		
Income tax expense	7.9	2.9
Net finance cost	94.4	92.3
Depreciation and amortisation	47.2	46.7
Earnings before finance costs, income tax depreciation and amortisation, (EBITDA)	**170.2**	**32.5**
Add back:		
Restructure and other costs	6.7	7.5
Onerous leases and related costs	(3.8)	-
Impairment of assets	3.9	-
Impairment of goodwill – Australian Pathology		120.0
Profit on sale of operations		(4.2)
Total other expenses	**6.8**	**123.3**
Corporate costs	**9.0**	**6.4**
Operating EBITDA before other expenses (non-operational)	**186.1**	**162.2**