NETCARE LIMITED
(Registration number 1996/008242/06)
JSE ordinary share code: NTC
ISIN: ZAE000011953
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("Netcare")

UPDATE ON H1 2018 TRADING AND UK RELATED MATTERS

The primary purpose of this announcement is to provide shareholders with an update on Netcare's trading in South Africa ("SA") and the United Kingdom ("UK") for the first half of its 2018 financial year ("H1 2018"). Shareholders are also updated on matters related to Netcare's investment in the UK.

SOUTH AFRICA

Hospitals and Emergency Services

Continuing the trend of positive patient day growth experienced in Q4 2017, there has been an overall improvement in year-on-year activity in H1 2018. As of yesterday (27 March 2018), patient days have grown in excess of 3.0% against H1 2017. However, the remaining days of the month are expected to be quieter than usual due to the Easter public holidays falling over the month-end. Full week occupancy levels of 63.7% were experienced up to 27 March 2018, improving from 63.2% reported for H1 2017. Revenue per patient day increased by 5.2% to the end of February 2018. The specialist base has grown by a net 50 doctors. In line with our guidance in November 2017, underlying trading EBITDA margins are expected to remain broadly flat against H1 2017, although there will be some minimal dilution in the overall margin due to costs incurred in respect of the Akeso acquisition and UK advisory fees.

In terms of Netcare's "asset lighter" approach, aimed at leveraging our existing capacity, no new beds were added during the period. Twenty-one under-utilised beds were transferred to a hospital with high demand and ten under-utilised beds were converted to higher demand disciplines during H1 2018.

Netcare 911 has been restructured and losses from this division have been curtailed during this trading period. The closure of its Mozambican operations was completed as of 31 December 2017.

As announced on 19 March 2018, we are delighted at the successful completion of the Akeso acquisition. Akeso Clinics is a group of 12 dedicated mental healthcare facilities, comprising 811 beds, located in various parts of South Africa, including Cape Town, George, Johannesburg, Pretoria, Nelspruit, Umhlanga and Pietermaritzburg. Netcare recognises that there is a growing demand for the treatment of conditions related to mental health. The acquisition of Akeso provides Netcare with an excellent and established platform from which to expand its mental health offering. As the acquisition is effective 27 March 2018, and has only just completed, there will not be any impact on trading results in H1 2018.

Primary Care

The Primary Care division opened three new Medicross clinics in H1 2018. The new day clinics in Kimberley and Upington are ramping up in line with expectations and, along with improvements in the performance of the sub-acute facilities, there has been a reduction in the start-up losses of these new operations. EBITDA margins are expected to improve against the margin of 12.9% for H1 2017.

UNITED KINGDOM

Trading conditions have remained difficult across the private healthcare market, characterised by National Health Services ("NHS") demand management initiatives, weaker Private Medical Insurance ("PMI") demand and a continuing change in case mix in favour of more day cases.

As a consequence, the H1 2018 performance of BMI Healthcare has been poor, with the market trends experienced in the second half of 2017 being carried through into the first half of this financial year. Inpatient and day caseload for the 5 months to February 2018 has declined by 2.2% year-on-year. Total NHS caseload for the 5 months ended 28 February 2018 declined by 4.4% year-on-year affected by stringent demand management strategies implemented by the NHS. PMI caseload to the end of February 2018 has reduced by 5.7%. Self-pay activity to the end of February 2018 grew by 3.0%, driven by longer NHS waiting times. As compared to H1 2017, the EBITDA margin has been weaker and is expected to be between 0.8% to 1.2% as compared to the prior period EBITDA margin of 5.2%. The business continues to be affected by onerous lease payments and has also incurred a series of one-time costs associated with restructuring related activities.

ACQUISITION OF MINORITIES' INTERESTS IN GHG

In September 2017 Netcare announced that it intended to acquire its partners' 43.1% interest in GHG. A condition precedent to the completion of the acquisition was the conclusion of a long-term financing arrangement between BMI Healthcare and its lenders. This condition was not satisfied by the longstop date of 28 February 2018 and the transaction did not complete. Accordingly, there has been no change in the shareholding of GHG, Netcare's interest in the business remains unchanged at 56.9%, and no consideration (which was anticipated to be settled in the form of Netcare warrants) is payable.

NETCARE TO EXIT FROM THE UK MARKET

Following lengthy consideration, Netcare has made a strategic decision to exit the UK market and pursue the disposal of its interests in the GHG group in due course. The background and rationale informing this decision are as follows:

Netcare acquired GHG in May 2006 as part of a consortium. Shortly after the acquisition, GHG was restructured into an operating company (“OpCo” or BMI Healthcare) and a series of property companies (collectively “PropCo”) that held the hospital properties and leased them to BMI Healthcare under long-term leases.

At that time, the lease arrangements, as concluded, were considered market related and provided for a fixed escalation in rent of 2.5% per annum. Given the global financial crisis of 2008, and its effect on the UK economy as well as the declining PMI demand, and the sustained period of exceptionally low inflation since that time, BMI Healthcare’s rent obligations have grown to be unaffordable. Moreover, the continued escalation in rent is, in Netcare’s view, unsustainable. In FY 2017 rent represented approximately 20% of revenue impacting on the company’s ability to fund ongoing investment needs.

Netcare has spent considerable time and resources pursuing a rent reduction transaction with BMI Healthcare’s largest landlord (“Theatre PropCo”) on 35 of its 59 hospital properties. However, after more than five years of negotiation, Netcare has concluded that a rent reduction transaction under which the UK business will have the resources necessary to invest in the estate, remain competitive and simultaneously generate an appropriate risk adjusted return, is highly unlikely.

In addition, with the acceleration of demand management initiatives implemented by both the NHS and PMI providers, market conditions have become further constrained and are expected to remain challenging in the medium to longer term. These pressures, and the resulting lower levels of patient activity, have required the business to respond and implement efficiency measures. However, BMI Healthcare’s ability to adapt sufficiently to the changing market continues to be impacted by its onerous long-term leases and its limited capital.

Netcare has always ring-fenced its respective businesses in SA and the UK. As such, the debt obligations of BMI Healthcare (and those of PropCo) do not have recourse to Netcare and its South African operations.

Netcare also has no obligation to provide additional funding to GHG and has previously indicated that it would not invest further capital into BMI Healthcare in the absence of a rent reduction transaction.

The short-term funding solution concluded with BMI Healthcare’s lenders in December 2017 expires on 31 March 2018. The lenders have conditioned any further short-term funding on existing GHG shareholders relinquishing effective control of the boards of directors of BMI Healthcare. Netcare has agreed, in the interests of the business, to accede to this demand. This has allowed BMI Healthcare to conclude a further short-term funding arrangement with its lenders and it will continue to pursue a longer-term funding arrangement.

As a result of these factors, in accordance with accounting standards, the UK operations will be deconsolidated from Netcare’s accounts with effect from 28 March 2018 and Netcare will pursue a disposal of its interests.

Additional announcements will be made as and when appropriate.

The information provided in this trading statement has not been reviewed or reported on by Netcare's external auditors.

Netcare will be releasing its unaudited interim Group results for the six months ended 31 March 2018 on Monday, 14 May 2018.

Johannesburg
28 March 2018
Sponsor
Deutsche Securities (SA) Proprietary Limited