Conference call transcript

25 May 2023

INTERIM RESULTS

Operator
Good day, ladies and gentlemen, and welcome to the Life Healthcare unaudited group interim results. All participants will be in listen-only mode. There will be an opportunity to ask questions later during the conference. If you should need assistance during the call, please signal an operator by pressing * then 0. Please note that this call is being recorded. I would now like to hand the conference over to Peter Wharton-Hood. Please go ahead.

Peter Wharton-Hood
Good morning, ladies and gentlemen, and welcome to the executive management presentation for the six months ended March 2023. We're delighted to report a strong business performance during the six months underpinned by exceptional performances both in South Africa and internationally. Our Southern African business grew revenue by 11.6% to just short of R11 billion, normalised EBITDA up 13.5% to R1.8 billion, off the back of a strong improvement in our paid patient days during the period under review, which increased by 12.5% and will be explained in more detail by Adam later on.

From a strategy perspective in South Africa, we are starting to see that the promises we made delivering our 2026 strategy take shape. We concluded some impressive new network deals in Southern Africa. Our energy program continues. We're delighted to announce the acquisition of TheraMed Nuclear. And on the back of our diversification away from acute revenue, we're also entrusted with the care of Fresenius Medical Care's renal dialysis patients across 51 clinics in South Africa, Eswatini and Namibia.

Internationally, our Alliance Medical Group grew revenue by an impressive 15.5% to just over R4.4 billion, with a normalised EBITDA of nearly 11% at just short of R1 billion. This was underpinned by strong PET-CT volumes in the United Kingdom and an impressive growth in Irish volumes that were nearly 17% up. From a strategy perspective, we continue to deliver on our community diagnostic centre roll-out programme, and we now have seven CDCs in operation and a healthy pipeline against which we can deliver, and Mark will explain that a little later on.

At a group level, revenues are up nearly 13% to just over R15 billion. Normalised EBITDA is up 13.5% to just short of R3 billion—or R2.8 billion, to be precise. We have declared an interim dividend up 13.5%, in line with the operating performance of the company, to give shareholders a payback of 17 cents per share. At a group level, from a strategy perspective, we are seeing positive news flow on LMI, which I will expand on a little bit later.

The R3 billion question in Life Healthcare currently is how our capital allocation procedures work. We have been asked this a number of times. It falls under the sub-committee of the board's responsibility, our investment committee, which is both sophisticated and detailed in its approach. You can break the R3 billion down into two broad categories—that which is to seek to grow and sustain the existing business, which we call maintenance capex, and that money which is deployed to organic growth in the existing business and other innovation opportunities. In Southern Africa, the maintenance capex is all around organic volume growth, improving occupancy levels, and optimising the arrangement of the bed portfolio across the footprint. Internationally, it's bolstering our strong partnerships with the public health service and the necessary replacement of old scanners as and when the replacement becomes due.

From a growth capex perspective, domestically, you'll see that we're investing in renal and other value-based care products, our oncology centre of excellence, further imaging services and very exciting opportunities in radiopharmacy. Whilst our growth capex internationally is around expanding our partnerships with CDCs, exploring new markets. We will talk about selected acquisitions in due course. And of course, there is the ever exciting prospect of growing our investment in NeuraCeq. All told, for the full year that will come to R2.9 billion.

If one thinks about acquisitions, we have announced during the course of the six months under acquisition of TheraMed and the assumption of responsibilities and implied acquisition of Fresenius Medical Care in South Africa. Internationally, we've had some small bolt-on acquisitions of community-based diagnostic clinics in Italy and opportunities being pursued in the United Kingdom and Spain. All told, if excess cash is presented inside the business after our capital allocation process and the deployment thereof is concluded, it of course will be returned to shareholders, whether it be by ordinary dividends, special dividends or share buybacks, as would be appropriate under the circumstances.

As I alluded to earlier, we have had some very positive news flow on Life Molecular Imaging during the course of the six months under review. By way of a recap, NeuraCeq is an approved injectable radioisotope used in PET scans to detect beta amyloid deposits in the brain. It's an important medical term to understand because Alzheimer's has been proved to be attributed to the accumulation of beta amyloid in the brain, and clearly being able to detect it is our way of being able to diagnose whether a patient has Alzheimer's or not. There are other ways that you can detect beta amyloid in the human body, in the brain. They could be by a spinal fluid test, a blood test, or what we believe to be the highest accuracy test, being that of a PET-CT scan. We aren't the only player around the world that has an approved amyloid-detecting isotope. Lilly and GE Healthcare also have approved F18 isotopes in production.

We've been blessed with having a significant market share in all the global clinical trials to date, but of course what we're really saying is the reality is we couldn't sustain that market share over time. We'll probably end up with about one-third of the market share, and we've already got the capability to produce NeuraCeq around the world. The key point to commercialisation, then, is at what particular point will the demand for NeuraCeq go up? Clearly, we've explained the care pathway for Alzheimer's for some years now. And what we do understand is if a patient has a treatment pathway to cure Alzheimer's, we think the demand for the diagnostic will go up on the basis that if you know you can be cured, you can be diagnosed, and on that basis, we think that the demand for NeuraCeq will go up.

There are two drugs currently in various phases that are seeing significant support internationally. We have had accelerated approval by the FDA on the 18th of January of this year for Leqembi from the Eisai / Biogen stable. It is clear that, by the 6th of July, as far as we are concerned, we think that these will be formally and finally approved. Eli Lilly also has a drug under review, and we think that they will get approval later in late in 2024. So, we therefore think that an approved drug for Alzheimer's is highly likely.

What does that mean for us as a company? We've done some very high level numbers and made some assumptions. We think there are about 36 million patients possibly suffering from Alzheimer's or dementia in the US, the EU and the UK. We have excluded the Asian analysis at this stage because we do not have enough data at our disposal. Of the 36 million, we think 17 million, or roughly half, of the patients will be eligible for a PET-CT scan. And conservatively, we think that gets us to somewhere between 1 million and 2 million patients per annum who will actually go for a PET-CET scan.

If our assumptions up front are correct and we have one-third of the global market share, it means that we’re probably lined up to produce somewhere between 300,000 and 400,000 doses of NeuraCeq every year. We think the analysis is conservative. We think our logic is sound. We are very optimistic about the way forward for life medicine, as and when the big medical aids in the United States agree to reimburse for the treatment of Alzheimer's on the back of approved drugs.

The last point that I would like to mention, which has also been newsworthy during the past six months and more recently, concerns the cautionary announcement on the Life Healthcare company and, more specifically, around the unsolicited expressions of interest in Alliance Medical Group. I do maintain strongly that these were unsolicited. We were not seeking to sell our interest in Alliance Medical. Our external advisers have been appointed and are in the process of assisting the board in assessing the attractiveness of the proposals which have been submitted.

In line with our fiduciary responsibilities and under the guidance of the board, management are formally engaging with these third parties regarding their expressions of interest, and this engagement is ongoing as we update the market more recently. I must confirm that management and the board is taking these approaches seriously and is working hard to ascertain the viability, the execution risk and the potential to unlock value that has been contained in these approaches. As a result, the cautionary will remain in place until further announcements are made. I'd now like to hand you over to the Chief Executive of our Southern African Operations, Adam Pyle, to take you through the overview and detail of his results.

Adam Pyle
And I apologize for my croaky voice. My colleagues here are concerned that I'm going to give them a Louis Armstrong rendition. But you can rest easy because I assure you that's certainly not the case. Just in terms of our SA business, the recovery post-COVID is, continues to gain momentum. We have had a really good half in terms of our volume recovery. And if you look at the graph on the bottom right, you'll see that our occupancies for the half finished at 65.9%, which is a good recovery from a 58.5% in H1 2022. In addition to the good growth

in activities, we've seen a normalisation of our case mix, which is important. And our case mix now is more reflective of what we see in 2019.

Coming out of COVID, the surgical admissions and PPDs recovered at a much faster rate than medical. And we've always said before that as a group, we've always had a higher medical PPD percentage. And what we've seen in this last half is a strong recovery on medical PPDs. And as I said, the case mix now is more reflective of what we saw in 2019. Pete mentioned the new network deals and they became effective in January 2023. And they're starting to contribute to our increased activities, but this is really early days. They are three year deals and we expect to see continued improvement in activities from these networks.

I will talk a little later on our renal dialysis business as well as the SA imaging business. In terms of the challenges in SA, working in SA is not for the faint-hearted. We are all impacted by load shedding. The last six months we spent roughly an additional R40 million on diesel compared to prior year. One hospital in Queenstown got flooded twice in three weeks due to heavy rainfall and also just because of infrastructure issues in the town. And of course, there's been a lot said in terms of the issue around nurses over the last few days. It's very frustrating. But we remain hopeful that we can reach some form of agreement which allows us to train more nurses, which the country desperately needs.

Just in terms of business, we continue to invest in our underlying infrastructure. Last year, we spent R1.6 billion capex on our infrastructure, and this year we'll spend roughly R1.4 billion. And in addition to investing in our facilities, although we look to drive our occupancy percentage primarily, there are certain hospitals where there's an opportunity of adding additional beds. For example, you'll be adding ICU beds at Life Vincent Pallotti, additional beds at Life Westville and Life Wilgeheuwel. And there's additional projects we're currently working on at Life Peglerae and Life Hilton, which will add bed capacity. We're very careful in terms of adding the bed capacity, and we only do it in those hospitals where we see good growth opportunities.

In addition to investing in our facilities, we have now completed the modernisation of our underlying IT infrastructure network, and this will give us a platform for which we can move forward. We continue to invest in the IT platform and systems, and we've made good progress in our cloud migration. And, of course, we continue to invest in our data analytical capabilities. We continue to look at our SA portfolio, and over the last six months we have closed one stand-alone birthing unit. And we've also closed a stand-alone acute rehab unit. We still feel very positive about acute rehab as a business line, and we'll continue to grow that business line, but we closed this unit because of particular issues around this unit.

In addition, we've said that we look to grow our non-acute part of our business, and so we've recently announced the acquisition of TheraMed Nuclear, which I'll touch on later, as well as the acquisition of the assets and operations of the renal dialysis clinics from Fresenius Medical Care. This transaction is still subject to competition commission approval.

If you look at the segmental breakdown of our numbers, we grew revenue by 11.6% to R10.5 billion. And within that you see that hospitals and complementary services grew revenue by 13.1%. And this revenue growth is off a strong PPT growth of 12.5% for the period. Normalised EBITDA grew by 13.5% and we're starting to get some benefit from operating leverage as well as some cost controls. And within that you see that at an operational EBITDA line, hospitals and complementary services grew by 13.7%. And healthcare services, which consists of Life Nkanyisa and Life Health Solutions, grew the operational EBITDA by 16.9%. Life Nkanyisa had a really solid six months. And we spoke about Life Health Solutions last year, which is our occupational health and wellness business, and we are busy going through a restructuring and the benefits of that are not coming through. So, although we saw a decline in our revenue in healthcare services, the improvement in EBITDA is a reflection of the work that's being done by management. And finally, you see that the normalised EBITDA margin increased from 17.1% to 17.4%.

Just breaking down [the Southern African results] I'll touch on the acute hospitals and complementary services and then renal dialysis and imaging. So, starting with acute hospitals first, you'll see that there's a revenue growth of 12.1% for the half, off the back of a 13.1% PPD growth, which is really strong PPD growth. If you look at the graph on the top right, you'll see that the red line is, certainly for the months of February and March, really close to 2019. That has resulted in occupancy moving up to 65.5% from 57.7% in the prior year. And if you look at the graph at the bottom right, where you show the quarters, you see that Q2 2023, our occupancy for acute hospitals was 69.8%. So, touching on 70%, which is good to see. And certainly, the occupancy in hospitals for the months of February and March was above 70%.

In terms of the case mix, you can see that we've now switched back to a 51/49 percentage medical-surgical case mix for the hospitals. And if you combine the complementary service lines as well, we're back into a sort of 55/45 percentage split, which is what we were in 2019. As a reflection of the change in case mix, you can see with a 13% increase in PPDs, but only a 6.3% increase in theatre minutes. It shows the faster rate of medical PPDs we saw over the last six months. As an aside, I just want to show you that our cath lab activity in the cardiac side of the business has done exceptionally well over the last six months, with a 22% growth. And our revenue per PPD was now down 0.9% on prior year, and that's a reflection of both the change in case mix, as well as the discount on our network deals.

Moving on to our complementary lines of business, a really excellent performance, revenue up 26%. That's off a base of an 8% PPD growth with mental health growing by 11.4%. Rehab a little slower, just under 3%. That's also impacted by the closure of one unit. You know, if you're closing a rehab unit, which has a length of stay of between 25 and 30 days, you have to start working on that closure over a period of months. So, that had an impact on the overall acute rehab PPD numbers. But they still have high occupancies across that business. And you can see occupancy levels for the half finished at just over 70%. And again, if you look at the graph on the bottom right, in Q2 2023, our occupancies were 74%. And certainly, for February and March, the occupancies for mental health and acute rehab were in the late 70s, which is very pleasing to see.

And the other lines of business within complementary services outside of imaging: oncology, we saw good growth with a 10% increase in treatments, and renal dialysis treatments increased by 8% in the prior half. So, I just want to talk a little bit about renal dialysis. We announced the acquisition of Fresenius Medical Care's Southern African renal dialysis business. So, there's 45 clinics in SA, five in Namibia, and one in Eswatini, and roughly 2,500 patients with chronic kidney disease. This transaction is supposed to go to the Competition Commission (Comp Com), but we are very excited with this transaction and our ability to roll out our value-based care platform to a broader base of patients. Our aims sound very simple. They are quite difficult to do. But certainly, to provide improved clinical outcomes, improved patient experience, and with a decreased overall cost in terms of the treatment of these patients. And that's why we talk about Fresenius entrusting the care of their patients to us, the quality of care we will provide these patients going forward.

I just want to have one quick slide in terms of our imaging business in SA. The existing SA imaging practices are continuing to perform well and ahead of business case. You can see there's an improvement in the facility numbers. The seven and the eight, the seven relates to H1 2022, and the eight facilities is H1 2023. So, good activities coming through, which is to be expected because in the prior year we only had East Coast Radiology from February onwards. And in addition to that, the good performance, we will be looking at other potential acquisitions for the remainder of this year.

And I suppose you could say that we've added a new line of business within our imaging in SA through the acquisition of TheraMed Nuclear, which adds PET-CT and SPECT-CT to our existing imaging business. TheraMed Nuclear consists of three outpatient nuclear medicine sites in Gauteng. And we've explained before that we are in a JV. We are busy building two cyclotrons, and those cyclotrons will produce a radioisotope which you need for a PET-CT. So, this complements the cyclotron business. And then the PET-CT business will complement our oncology strategy. So, we feel that it's all aligned and the building blocks are slowly coming into place.

And finally, I'd like to just touch on our value-based care strategy, which we put a lot of emphasis on. Value-based care is a term which is quite loosely used, but it's actually very difficult to do. And so, we're basically talking about coordinated patient-centric journeys which we design. And to do that, you need to have a unified patient engagement and clinical management system to enable this. And Life Healthcare has the first Salesforce health cloud installation in Africa in this regard. You then obviously have to leverage your data analytics to design and manage these products to ensure that you have clinical excellence and efficiency.

Then outside of that, you have to have your network of facilities that provide that care. And of course, you have to have the value-based reimbursement models in place to ensure that you're aligned with the funders as provider and of course, as patients are aligned. This is a complicated journey and it's one we started off with renal dialysis in terms of the rollout of our renal product across our business, and we have a range of other products that are in the pipeline.

So, I just want to finish off by thanking the SA staff and doctors for an excellent six months. And I'll now hand over to Mark Chapman, who you'll be pleased to know doesn't have a croaky voice.

Mark Chapman
Good. Thank you, Adam, and good morning, everybody. I'm pleased to say that H1 has produced a very solid set of results with the revenues up 15.5% which resulted in a 10.8% growth in EBITDA whilst operating in a high inflationary period across the eurozone which presented its challenges. So, it's been a strong start to the year. The core business, we increased revenues across all geographies, which you'll see shortly. We continue to negotiate with multiple public sector partners on contracts and also tariffs in the inflationary period that we see ourselves in. And the PET-CT continuation strategy is firmly ongoing within a work stream.

There's always lots of opportunity in diagnostics and in the business. And you'll see the diagrams to the right, the opening of one of our CDCs [Community Diagnostic Centres] with the PM in the UK. So, we continue to grow this pipeline of CDCs, in discussions with the NHS, and the focus is also on ensuring that we grow and establish the existing CDCs that we have already contracted out, of which I will come on to shortly. We are developing four new sites in Ireland, which goes hand in hand with the volume and growth and the opportunities that they are seeing. And we continue on the strategy of growing bolt-on acquisitions across the region.

We also continue to invest in our current footprint. We have a scan replacement programme in place. We want to maintain the average age of our scanning portfolio at just below seven years overall. We continue to invest in the cyclotron maintenance programme, the refurbishment to ensure that with the future growth of PET-CT we have the capacity within the cyclotrons. And we continue to invest in more efficient fleets for the mobile staff and the staff across the board, while investing in electric vehicles, obviously supporting our ESG agenda.

To deliver those results has had its challenges in the past six months. The obvious one is that we have been operating across the eurozone at the highest levels of inflation in decades. There has been some limited tariff relief in parts, and we've also had some resources assisting with the due diligence relating to the expressions of interest that Pete spoke about previously.

So, we've had a strong operational result. The 15.5% has been driven by the continuing growth in the PET-CT scans across the UK, along with the growth in Ireland and Northern Europe. And we've had some benefit from the FX movement, which you'll see on the left. I think it's also worth noting that the EBITDA margin has been well managed to 20.3%, as we've seen increasing energy and staff costs across the six months, increased headcount as we ramp up for the benefits of the CDCs. And there's been some case mix with some new contracts, as an example, the programme of lung cancer screening in the UK, which is strategically the right thing to do, but sometimes comes in at a slightly lower margin, by way of example.

So, to break down into the three main geographies, the UK, good volume growth in DI. And when I say DI, that's MRI, CT, and other, and molecular imaging is the PET-CT part of the business. The mobile assets have had a slower start to the year than was anticipated. This is linked a little bit to the NHS spending cycle, and I'm pleased to say, come April, we're seeing the utilisation of the mobile fleet increase. There have been pressures, as I have continued to talk about, around the NHS, although we are expecting some tariff increases. If you look at the last four years within the NHS, tariff increases have gone up 8%. And we need to manage our costs accordingly to support the mobile fleet with the fuel costs. And I'm also pleased to say that we've had two large CDCs go live in the first half of the year in Taunton and also in Oldham.

You'll see in the chart we continue to be a main supplier and partner to the NHS with 92% of the services in the UK with the public sector. And you'll see the split between molecular imaging and diagnostic imaging moving back to the pre-covid levels where molecular imaging is now at 55% of the revenues in the UK. So, just to break the UK down into those two parts, molecular imaging, PET-CT growth at just shy of 10%. There was some seasonalised weakness over December and a number of bank holidays as well, which seem to be more this year than previous. Margin expansion comes with that volume growth as the marginal economics continues to kick in. We do have the inflationary protection mechanisms around that contract and we will see the tariff increase for the scans increasing by 4% from April 2023. We continue with the PET-CT continuation. I'm pleased to say that the CDCs provide an opportunity where we can co-locate PET-CT and to advance the services within the community for that offering.

If we look at diagnostic imaging, up 4.1%, there has been a little bit of a lag with diagnostic imaging in the UK compared to the other regions. But I'm pleased to say that in the last quarter that started to increase. And you'll also see that's against the backdrop of increasing waiting lists in the UK with the NHS. And then the CDCs continue to be a very strong opportunity which I detailed previously in the last presentation. But you'll see that we have seven up and running. We do have a strong pipeline going forward. The target from the NHS is around 160 imaging centres over the medium term. I think it's fair to say there's very positive signalling from the NHS to work with the independent sector to provide these solutions. More recently, in the last couple of weeks, both Conservative and Labour parties have been talking very encouraging about working with the independent sector to support the NHS.

The final slide just to look at Italy and then Ireland. You will see that the Italian volumes are down 4.4% for H1. That is against the previous year, when there were spot awards from the ASL budget, which was favourable last year. However, please note that the revenues are still up 7.1% and the EBITDA follows that as well. So, there's been positive growth in the revenues. This is due to increasing some of the self-pay tariffs in the region of 10% to 15%, which has obviously helped support not only the volume declines against that like for like, but also the inflationary pressures of the salaries and the energy increases that we're seeing in Italy.

And then finally in Ireland you'll see it's been very strong growth in Ireland. This is being supported by new contracts with the HSE, which is the public services supporting the increased need of diagnostics. And Malcolm and the team have taken the opportunities. You can see there's four new sites being developed this year, and you can see the growth since 2017. So, I foresee that to continue going forward. Okay, thank you for that. I'd now like to pass you over to Pieter to go through the finances.

Pieter van der Westhuizen

Thank you, Mark. Good morning, everyone. The company had strong operational result for the six months, driven by PPD growth of 12.5% in SA and good growth in the AMG business with scan volumes up to 7.1%. 12.9% growth in Group revenue over the last year translated into a normalised EBIT and normalised EBITDA at 13.5% and 14.9% respectively. Earnings were however impacted by the higher interest rates, and the interest rate cost has gone up. The settlement of a tax matter in South Africa resulted in normalised earnings per share going up 1.1%.

We did experience an IT outage at one of our service providers that impacted our ability to collect cash in the month of March. And hence our cash from operations is down to R1.1 billion where we would have expected it closer to be about R2.2 billion. Capex spend for the six months has been R1.2 billion. This IT outage also then increased our net debt to normalised EBITDA slightly to about 2.17x as measured in terms of the bank covenants. I am pleased to say that this position has normalised at the end of May and we have declared an interim dividend of 17 cents per share.

Just looking at the income statement, what I want to highlight is that you can see revenue up 12.9% and translating into EBITDA at 14.9%. Operating profit up 11.1%. There is an impairment in our international business of R33 million where we've closed one of our clinics in London and we had to impair the goodwill on that. Interest cost, as I said, has gone up. And you can see the breakdown. Interest on the SARS VAT matter, R47 million. And then in the Alliance business, we do have intercompany loan accounts that are denominated in different currencies. And with the exchange differences between the Pound, Euro and Dollars, resulted in a loss of R66 million. The attributable profit for the year at R547 million, 9% down against last year.

Earnings per share, as I said, normalised earnings per share up 1.1%. You can see the adjustments that we made. Once-off items are really the interest on the SARS VAT matter that had a 3.3 cents impact. And then included in other a few transaction costs. So, normalised earnings per share is 44.6 cents. On the right, showing you the impact of the interest rates. Both in South Africa as well as in international, the base interest rates have all gone up from last year March to this year by between 200 bps to 400 bps in the period. And hence, although our net debt hasn't really moved, the interest cost has gone up substantially.

On the balance sheet, net debt to normalised EBITDA at 2.17x. And you can see the main impact or the reason for that is the movement in our current assets, moved up from September at around R5 billion to R6.6 billion. That's largely the movement of R1.2 billion in debtors due to the IT outage. We still have available R3.8 billion in facilities. On the cash flow, maintenance capex, although lower than last year for the same period, is largely impacted by some logistic issues in the international business where we have placed the order for machinery. Those will be delivered in the second half, and we do expect to spend our full allocation that we've estimated for this year of about R2.9 billion in both maintenance as well as in growth capex. And I now hand you back to Pete.

Peter Wharton-Hood

Thank you very much, Pieter. It remains for me to take you through the outlook for the next six months. Off the back of our positive start to the year, I'm delighted to say that we can forecast a PPD growth in Southern Africa approaching 10% for the full year. And as a result of the change in our business mix, we're expecting a margin expansion at the EBITDA level. We will be very busy completing the integration of the current acquisitions and the deployment of the capex of R1.3 billion anticipated for the year.

Internationally, we see volumes growing by between 6% and 8%, and we will concentrate on growing and establishing the volumes through the CDCs, to which we are already contracted. On a similar vein, we will continue to build the CDC partnerships with the NHS and deploy the capex estimated at around R1.6 billion for the full year. All in all, for the group, that implies a revenue growth in the region of somewhere between 10% and 12% and a significantly improved cash flow generation during the second half of the year as we recover from the situation of the IT failure that impacted us in the first half of the year.

We will conclude the evaluation of the AMG proposals, and in the light of the positive news flow of Life Molecular Imaging, we will also continue to build out the required capabilities, principally in the United States of

America, to collect the benefits that we anticipate going forward. That concludes our presentation. We're now in a position to answer some of the questions that some of you may have.

Operator

Thank you. If you would like to ask a question, please press * and then 1 on your touchtone phone or on the keypad on your screen. If you however wish to withdraw the question, you may press * and then 2 to remove yourself from the question queue. For those on the webcast, you may use the textbox at the bottom of your screen to submit your questions. The first question is from Alex Comer of JPMorgan. Please go ahead.

Alex Comer

Hello. I've got a couple of questions, please. You haven't really given much margin guidance for the second half, and yet we're looking for some operational gearing to come through from the extra volumes in SA. So, I was wondering if you'd just like to comment on whether or not you think margins will be up in the second half in SA, similar in the UK. Secondly, you gave some guidance for I think 300,000 to 400,000 scans for NeuraCeq. I think historically you've indicated maybe $1,000 per tracer. So, does that still hold, and therefore does that point to a $300 million to $400 million market? And then I think also you said the margin there would be around about 30%. So, does that still hold? That's my second question. And then the third question, obviously you have these unsolicited approaches from people to purchase AMG. I'm just wondering what your thinking there is. I think total assets on the book are about £1 billion. I would assume that you're not prepared to sell this at a loss. Would that be a sensible assumption to make?

Adam Pyle

Hi Alex, Adam here. I'll talk about the SA side. So, we would, with the underlying PPD growth that we said of 10% for the year, expect a further improvement from operational leverage, which should translate into better margins. You know, I think we had indicated that there'd be a little bit of pressure in the first half because what happens with these network deals is you give the full discount up front across the whole business, and then it takes a while for the volumes to come through. So, there is a bit of a lag, but we would expect to see some operational improvement coming through off the base of the increased volumes.

Peter Wharton-Hood

In the context of the life molecular observations that you make, yes, our high level and very conservative estimates around 300,00 to 400,000 doses is correct. That's as per the slide. Insofar as the market carrying price of NeuraCeq is concerned or any other competitor radioisotope going forward, it's quite difficult for us to predict that because the market and the pricing is, as you would appreciate, completely immature. In the clinical trials that were conducted, NeuraCeq was going for $2,000 a dose. Insofar as how that market plays out as it matures relative to demand and supply, we'd have to keep a watching brief on it.

So, at this particular point, I would submit the $2,000 a dose is probably top-ish, but I'd be hesitant to be able to say where the market clearing price actually plays out going forward. And I think you'll find different price levels present themselves in different markets, cyclotron production capacity being one of the core components in the production cycle that you have to take cognisance of. And market pricing regulations also vary across different countries. So, apologies, a vague answer, but I'm telling you with the best knowledge that management has at the moment. And the only real price that we can point to is where it was in the clinical trials.

Insofar as your questions around Alliance Medical are concerned, I reiterate the way that we expressed it in the cautionary announcement we issued to all shareholders more recently. Of course, we're taking the approaches seriously. And at this particular point, the steps we are taking, in answer to one of the questions on the webcast, is we need to ascertain the viability of the approaches that have been made. We need to be able to interpret and understand any possible execution risk that comes by way of these interests. And of course, when it comes to price, we said that we have to understand the potential to unlock value. So, we've given no indication on price and we'll continue to remain silent on that topic. But we do know that we will do what's in the best interest of the company.

Alex Comer
I'll ask one more question if that's okay. Would NeuraCeq be going with AMG or would you retain an interest in that?

Peter Wharton-Hood
We specifically said in answer to expressions of interest in an Alliance Medical Group that LMI is excluded by way of these interests. Any other questions?

Operator
The next question is from Roy Campbell of RMB Morgan Stanley.

Roy Campbell
Good morning. Thanks for the time. Yeah, our first question has just been answered. That's just whether LMI would form part of the discussions that you're having. Second question, please. The 4% increase in your PET scans, is this the first time that you've got an inflationary increase on those? And then perhaps you can just give us a feel for what the current inflation is in UK and Europe relative to what the potential recovery in that inflation could be. And then last one is just the interest on the VAT for Pieter. Is that for the full six months, or can we expect that to be a recurring fee into until the settlement is settled? Thank you.

Mark Chapman
Hi. Good morning. Yeah, regarding the PET and the contract for the PET wave one, there's inflationary protection that's in the contract. So, it's reviewed every year. If inflationary goes ahead of the 3.5%, then there's a calculation that's performed and that's shore up is the following year. In answer to… sorry just remind me of the second question.

Roy Campbell
Just in terms of the inflation that you're seeing now. So, we've seen the H1 performance and now you're going to be getting obviously an inflationary increase for the PET scans. But if you can just give us an indication of current inflation or cost inflation.

Mark Chapman

Yeah, so the current inflation at the moment in the UK, it was ahead of 10%. I think yesterday it came in at 8.4%, so we can see it coming down. Some of the challenges that we see are still within the utilities and the costs, which there's certainly a lag. I think the wholesale market is coming down across Europe, but we're not seeing this at site level at the moment. I think also to answer Alex's question about the margin, I think with the inflationary pressures that we have, wage salaries are now being settled at broadly around 5%. We foresee the second half to be similar to the first half. But I think that at the beginning of the next financial year we will start to see inflationary come down. I will now pass you over to Pieter for the tax question.

Pieter van der Westhuizen

It's a very short answer. That's actually the final number. We have settled that matter now with SARS. So, we won't be a recording charge coming through in the next half.

Roy Campbell

Thanks, Pieter.

Operator

The next question is from Anuja Joshi of SBG Securities. Please go ahead.

Anuja Joshi

Good morning, everyone. Thanks for the presentation. Two questions on South Africa and two on AMG. I missed some of Adam's commentary, so I'm not sure if Adam already covered it. So, in South Africa, your revenue for PPP declined by 0.9% in the first half. What's the split for tariff increase and case mix impact? And the second question is, what's your South Africa hospital occupancy in April and May?

Adam Pyle

There was a 0.9% decrease in the acute revenue per PPD. What is the split between the discounts and the case mix. That's your first question.

Anuja Joshi

Yes. What's the split tariff increase and the case mix in that?

Adam Pyle

I think roughly the split is if you look at what we're seeing elsewhere in terms of revenue PPD numbers because of the case mix, I suspect we would probably have had a revenue PPD of 1% increase without the discounts. And so, it's probably two-thirds is case mix and one-third is the discounts coming through, roughly.

Anuja Joshi

Okay, thanks. And what...

Adam Pyle

Well, April's a little bit quieter because of the holidays, but we're expecting May to be back at March levels. So, above 70%.

Anuja Joshi
Thanks, Adam. And just two questions on AMG. So, what sort of volume and pricing impact do you anticipate if or when your long-term contracts with NHS in the UK expire or get renewed? And can you perhaps comment on the capex profile for AMG in FY24 and beyond?

Mark Chapman
Okay, thank you. So, regarding the tariffs, we expect because the tariff is, as I say, the NHS currency, the impact of the inflationary pressures is across all sites and hospital trusts. We are getting some guidance that the tariff will increase. And again, at renewals, the currency we operate in around scanning is the tariff. I think there is some protection around that. We do not see it going further down in new contract renewals and certainly in new contracts. The capex going forward through to 2024, I think from a maintenance point of view, the guidance in Sterling is probably around the £20 million to £25 million. And then for the growth capex, it really depends on the level of CDCs that will come through the pipeline. And the CDC ranges from £4 million to £5 million up to circa £10 million, depending on the size and maturity of it, how many scanners go in from day one. And they are generally 10 to 15 year contracts at the moment that we're seeing.

Anuja Joshi
Thank you.

Operator
Thank you. I would now like to hand over for webcast questions.

Peter Wharton-Hood
If we go through the list of questions on the webcast, the first one that one would like to look at is the diesel cost for this year. We've estimated in our SENS announcement to be somewhere around about R40 million additional cost. And we see that as part of continuing operations. We've not normalised for that figure because we don't see it going away, and we think we've got load shedding with us for some time to come. Insofar as protection against higher finance costs going forward, our hedging policy is intact and we see probably the rate cycle with a small increase going forward but not in the context of worth hedging the next piece of the increase. So, we're expecting the rate cycle to turn in our favour going forward.

Adam Pyle
The question on the diesel costs. So, there's additional R40 million roughly spent, around about R48 million on diesel costs in the first six months. And we expect that to probably increase in the next six months as we go through winter. What that number looks like, we are not sure. But we expect it to be higher than the R48 million we spent in the first six months.

Peter Wharton-Hood

Insofar as the question that came for us as to the contingency plans for a potential grid failure in South Africa, our risk function under the supervision of our board risk committee has carried out a detailed evaluation on a site-by-site basis. And at this particular juncture, it's absolutely clear we can't make all our hospitals completely energy independent. And we are therefore reliant on double backup diesel generation during the moments of load shedding, in after hours or when the sun goes down. We have complementary sources of solar power during the day, but at this particular point the technology doesn't exist on a cost-effective basis to go to inverter-driven battery supplementation for entire hospital complexes. So, potential grid failure does place our infrastructure at risk once the diesel generation capacity runs out. And at that particular point in time, we'll have to make every effort on a best efforts basis.

There's a question on the capital investment that would be required to boost NeuraCeq production. We don't need to invest in more cyclotron capacity. We've actually concluded arrangements between Life Molecular Imaging and Alliance Medical on an arm's length basis for sufficient production capacity to take care of the anticipated demand in Europe. And we've completed a number of sub-licensing and manufacturing deals with other cyclotron owners around the world in anticipation of the increase in demand.

In the context, there's a question here as to why health insurers would prefer PET-CT scans versus spinal fluid tests. And that goes back to the slide which says the three options available for the detection of beta amyloid in the body have varying degrees of accuracy and the ability to identify where the beta amyloid deposits are concentrated. So, a blood test can give you a generic outcome as to the presence of beta amyloid in your body, as can a cerebral spinal fluid test. A PET-CT scan will tell you the concentration of beta amyloid in the brain specifically. And that is, in our consideration, exactly why the PET-CT scan is the most reliable form of testing. In our analysis on page 10 of our presentation, that's why we've noted that not every person that has Alzheimer's will necessarily go for a PET-CT scan. And that's why we've said, perhaps in the region of 10% would be sent for a PET-CT scan. I think that has covered the questions on the webcast. Any other questions before we close?

Operator
We have no other questions on the conference call.

Peter Wharton-Hood
I'd like to thank everyone for attending the presentation. And thank you from the executive to all our staff through our hospital complexes around the world, and to our doctors for a considerable effort under difficult circumstances, and a very pleasing result. Thank you very much.

Operator
Ladies and gentlemen, that concludes this conference. Thank you for joining us. You may now disconnect your line.

END OF TRANSCRIPT