HC SURGICAL SPECIALISTS LIMITED
Incorporated in the Republic of Singapore
Registration No. 201533429G

RESPONSE TO QUESTIONS FROM SECURITIES INVESTORS ASSOCIATION (SINGAPORE) AND SHAREHOLDER ON ANNUAL REPORT 2020

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*Unless otherwise defined, all terms and references used herein shall bear the same meanings ascribed to them in the annual report issued to shareholders on 7 September 2020 (the "**Annual Report**").*

The Board of Directors (the "**Board**") of HC Surgical Specialists Limited (the "**Company**" and together with its subsidiaries, the "**Group**") refers to the questions raised by the Securities Investors Association (Singapore) ("**SIAS**") and a shareholder relating to the Company's Annual Report for the financial year ended 31 May 2020. The Company has made some editorial amendments to the questions received from one of its shareholders to ensure that the question is clear. For the avoidance of doubt, the editorial amendments do not change the meaning of the questions from the shareholder.

The Company wishes to provide its responses to the questions as follows:-

<u>Question 1 from SIAS:</u>

As noted in the chairman's statement, FY2020 had been an eventful year for the Company. The Group expanded its network of clinics to 18 and added a 25% stake in an established general practitioner clinic, Medistar Services Pte. Ltd. ("**MDS**"), in July 2019.

While the chairman highlighted that the Group achieved a 15.3% revenue growth in the first half of FY2020, revenue for the full year was down 8.7% to $16.7 million. As noted in the chairman's statement, the Group was affected by the pandemic for the last two months of the financial year and the news of Dr. Julian Ong's defamation suit and the Singapore Medical Council ("**SMC**") complaint in April 2020. The latter and the allegation of a breach of director's duty generated negative media publicity for the Group.

(i) Did the Board assess the reputational damage to the Group as a result of the defamation suit and the SMC complaint related to Dr. Ong? How much of the 8.7% drop in revenue could be reasonably attributed to the negative publicity suffered by the Group?

(ii) Specifically, has JOES and/or the overall Group experienced any significant drop in the number and proportion of female patients?

(iii) Has the senior management evaluated if the turnover of staff, especially the female employees, in the Group has increased?

In Note 5 (page 108 – Intangible assets), the Company disclosed the carrying amount of goodwill <u>before</u> impairment. However, it was also disclosed that the Group made an impairment loss of goodwill of approximately $722,000 to one of its medical services under healthcare segment. The carrying amount of such medical service, which represents a CGU by itself, was determined to be higher than its recoverable amount of approximately $1,672,000 based on its current financial performance.

(iv) Given that JOES is the only CGU that has goodwill of over $1.67 million (next highest is MLCS with $1.055 million in goodwill), can management confirm that it has impaired the goodwill allocated to JOES?

(v) For the benefit of all shareholders, would the Board clearly disclose the carrying amount of goodwill <u>after</u> impairment?

(vi) On page 109, management disclosed the key assumptions used in the value-in-use calculation, including a revenue growth rate of "-45% to 15%" for JOES. In the CEO's statement, it was disclosed that no patient had declined to see Dr. Ong after being informed of the complaint. To help shareholders understand the potential financial impact on JOES, can management disclose the number of appointments, bookings and procedures before and after the negative publicity?

In fact, the "Impairment assessment of investments in subsidiaries" is a key audit matter (KAM) highlighted by the independent auditors in their report on the audit of the financial statements (page 63). Key audit matters are those matters that, in the professional judgement of the independent auditors, were of most significance in the audit of the financial statements of the current period.

As noted in the KAM, during the financial year ended 31 May 2020, arising from indicators of impairment in certain subsidiaries, management carried out an impairment assessment and determined the recoverable amounts based on the value-in-use calculations by estimating the expected discounted future cash flow. Arising from the assessment, an impairment loss of approximately $3,683,000 was recognised on the investment in a subsidiary during the financial year.

In Note 7, it was further stated that the recoverable amount of the impaired subsidiary is approximately $2,294,000, as determined by value-in-use calculations using management-approved discounted cash flow projections covering a period of 5 years and projection to terminal year.

(vii) Given that the carrying value of only one subsidiary was impaired, it is unlikely that the reason would be the COVID-19 pandemic. Can management confirm that it has impaired the carrying value of JOES? Was the reason due to the SMC complaint and the subsequent financial and operational performance?

In addition, in Note 14 (pages 128-130), the Group recognised $1.92 million in derivative financial instruments which relates to the put option requiring the vendor of JOES to repurchase the shares and the forward purchase contracts relating to MDS, MLCS, JOES and JLES. The put option has been assessed at $549,000 using the Binomial option pricing model. Management further stated that, as at the end of the reporting period, management has assessed the probability of exercising the put option by the Company is minimal.

It was further stated that if the probability that the option is exercised is higher or lower than 5% from management's estimates, the Group profit would have been higher or lower by $549,000.

As such, it can be reasonably deduced that management has assessed that there is only a 5% probability that the option will be exercised.

(viii) Have the independent directors evaluated management's assessment that the "probability of exercising the put option by the Company is minimal"? This assessment by management was made "at the end of the reporting period". Does management still hold the same opinion in September 2020 that the probability of exercising the put option is minimal?

(ix) Given that the revenue growth rate for JOES could be as low as -45%, the written off in goodwill and the reduction of the recoverable amount to $2.294 million, would the independent directors be evaluating the pros and cons of exercising the put option with a view to protect the interests of shareholders?

(x) The put option is exercisable within the 30th month and the 48th month of Dr. Ong's employment with HCSS. The 48th month falls on 31 March 2021, or approximately six months from the AGM. Would it be opportune for the independent directors to initiate a review of the Company's options with regard to JOES (including exercising the put option) so as to safeguard shareholders' interests?

Company's responses:-

(i) The 8.7% drop in revenue of $1,595,000 was mainly due to the disposal of HMC Medical Pte. Ltd. ("**HMC**") in July 2019 and CTK Tan Surgery Pte. Ltd. ("**CTK**") in September 2019, which contributed $2,226,000 to the decrease in revenue. Excluding the disposal of HMC and CTK, the Group had in fact achieved an increase in revenue of approximately $631,000 or 4.1%.

(ii) There is no statistics on the number of female patients and the Company believes that with our new female surgeon, Dr. Goh Minghui, joining the Group in July 2020, the number of female patients may increase. The Company would like to reiterate that since the start of these events, no patients had cancelled their appointments or declined to see Dr. Ong after having had the SMC inquiry / lawsuit explained to them.

(iii) There has not been a significant increase in the turnover of female staff. The number of female employees turnover for the Group averaged 1.1 headcount per month from June 2019 to March 2020 while the number of female employees turnover for the Group averaged 0.5 headcount per month from April to May 2020.

(iv) The goodwill impairment of $722,000 is for JOES.

(v) Carrying amount of goodwill after impairment is as follows:-

Name of subsidiary	Goodwill after impairment ($'000)
LBPL	815
JOES	1,422

Name of subsidiary	Goodwill after impairment ($'000)
MLCS	640
MST	344
JLES	828

(vi) The assumptions used for the value-in-use calculations were made on a conservative approach as the Company took into consideration the negative publicity and the pending SMC outcome. The Board is of the view that it is too preliminary to assess the potential financial impact, which depends largely on the SMC outcome.

(vii) The Company has taken on a conservative approach and impaired the carrying value of the investment in JOES due to the negative publicity and the pending SMC outcome; and the assumption that these will impact the financial and operational performance of JOES. The circuit breaker measures were implemented in April and May 2020 and the restrictions imposed by the Ministry of Health on the medical services that the Group can perform affected the revenue for the entire Group.

(viii) The Board concurred with management at the end of the reporting period that the probability of exercising the put option was minimal and as of the date of this announcement, the management still held the same opinion in view of the pending SMC outcome.

(ix) The independent directors and the Company are currently evaluating the potential outcomes that may result from the SMC investigation. As and when the Company makes such a determination, the Company will make the necessary announcements in accordance with the Catalist Rules.

(x) As clarified in the foregoing response, the independent directors and the Company are currently evaluating the potential outcomes that may result from the SMC investigation. As and when the Company makes such a determination, the Company will make the necessary announcements in accordance with the Catalist Rules.

Question 2 from SIAS:

On 6 September 2019, the Company announced that it had disposed its 100% stake in the Company's subsidiary, CTK to Dr. Charles Tan Tse Kuang ("**Dr. Tan**") for $1. The net tangible asset and the net asset value of CTK as at 31 May 2019 was $49,000.

As noted in the announcement, the disposal was made following the resignation of Dr. Tan on 2 September 2019.

As set out in the Company's Offer Document dated 25 October 2016, Dr. Tan had provided the Group with a profit guarantee of $150,000 per year for a period of three years from 1 September 2016. This has been fulfilled prior to the disposal. The Company stated that the disposal has no material impact to the net tangible assets per share and earnings per share of the Group for the current financial year ending 31 May 2020.

(i) Can the Board/audit committee help shareholders understand if the carrying value of goodwill of $429,000 as at 31 May 2019 has been impaired following the sale of CTK?

As part of the Company's pre-IPO restructuring, on 4 August 2016, the Group issued to the CTK vendor 1,481,481 shares then-valued at $400,000. The vendor has an option to repurchase entire issued share capital of CTK at any time for a nominal value of $1, provided always that the vendor shall not be entitled to exercise the option for so long as he has not given notice to terminate his employment in accordance with this employment contract with the Group.

(ii) Can management disclose the revenue and profit contribution of CTK from September 2016 to August 2019 when it was part of the Group?

(iii) Given that the Company paid $400,000 in shares for CTK in 2016 and had included an option for the vendor to unwind the sales after 3 years, would the Board help shareholders understand how the deal structure would allow the Group to grow in a sustainable manner for the long term? What were the other (non-financial) benefits of having CTK in the Group from 2016 to 2019?

(iv) As disclosed in Note 14 (page 130), the Group had also granted a repurchase option to the vendor of LBPL. What assurance can management provide to shareholders that acquisitions are structured to enable the Group to grow in a sustainable manner and to meet its strategic objectives, and not only to meet short term financial objectives?

Company's responses:-

(i) The goodwill of CTK had been included in the determination of gain on disposal of CTK amounting to $48,000. This is in line with the Singapore Financial Reporting Standards (International).

(ii) The revenue and profit contribution of CTK from September 2016 to August 2019 when it was part of the Group were approximately 9.1% and 7.3% respectively for the entire period.

(iii) Although the acquisition of CTK included the option for the vendor to repurchase the shares, it also included clauses to protect the interests of the Company's shareholders. The Company is always on the lookout for opportunities and suitable partners in its expansion plans, in addition to the ongoing search for young, talented specialists to join the Group to reinforce the Group's specialist platform to support the next generation of specialists. Having CTK in the Group helped to promote the Group's market presence and built the Group's network and relationship with various parties, such as suppliers, other general practitioners and patients at that point of time.

(iv) The Company provides support to new doctors joining the Group, such as assisting in setting up their clinics, getting their clinics to be licenced by the Ministry of Health, referring patients from its clinics located all over Singapore, human resources support and other administrative functions. In addition, most of the acquisitions are structured such that the Company's shares are issued as partial consideration, and such shares are subject to a moratorium. Through this support platform and the alignment of the doctors' interests with the Group's through their shareholdings in the Company, the Group hopes to inculcate a sense of belonging and loyalty with these doctors, with a view for the doctors to continue to stay with the Group in the long term.

<u>Question 3 from SIAS:</u>

Would the Board/management provide shareholders with better clarity on the following operational and strategic matters? Specifically:

(i) Acquisition of GP clinic: The Group acquired a 25%, non-controlling interest in MDS which operates The Ming Clinic, an established general practitioner clinic, in Camden Centre. Can the Board help shareholders understand if this acquisition is synergistic to the Group which has its focus on endoscopic procedures (including gastroscopies and colonoscopies)?

(ii) Investment in SPH: Can the Company also elaborate further on the rationale for making a minority, non-controlling investment of 4.82% equity interest in Singapore Paincare Holdings?

(iii) Growth strategy: For the benefit of new and long-standing shareholders, can the Board (re)state the Group's growth strategy?

(iv) Oversight by management: How does the senior management, especially Dr. Heah Sieu Min as executive director and CEO, ensure that there is proper oversight of the Group's operations as the Group carries out its expansion plans? Already there are 18 clinics in the Group, and the CEO has to drive the Group's overseas foray to Cambodia, respond to a fast-evolving pandemic, run his own medical practice, handle queries and the allegations made against Dr. Julian Ong, and to defend himself against allegations of him breaching his director's duties.

(v) Additional fees and management time: Would the Company be charging the additional professional fees and management time to JOES?

(vi) Financial position: With the redemption of the convertible bonds, the Group recognised a loss of $417,000 on the derecognition of the convertible bond. The $5 million convertible bond was redeemed for $5.196 million as the unwinding interest was computed using an effective interest rate of 9.8%. Are the Group's growth plans affected by the unexpected redemption of the convertible bond? What is the debt headroom, if any, for the Group to support its growth?

Company's responses:-

(i) Although the Group is primarily engaged in the provision of endoscopic procedures, it is always open to strategic acquisitions and expansion plans that will increase the value for its shareholders. The acquisition of MDS, with its stable pool of patients, will increase the patient referrals to the specialists within the Group and expand the Group's existing GP network. This is in line with the Company's business strategies and future plans as disclosed in its offer document dated 25 October 2016 ("**Offer Document**").

(ii) The investment in SPH allows the Group to acquire an interest in a pain management group, potentially unlocking additional value for the Group. This is part of the inorganic growth plan of the Group.

(iii) As stated in the Company's Offer Document, the Company's business strategy includes the following:-

(a) Expansion of business operations locally and regionally;
(b) Expansion of surgical facilities; and
(c) Growing its patient base.

(iv) Dr. Heah Sieu Min, the Company's Executive Director and Chief Executive Officer, is supported by Dr. Chia Kok Hoong, the Company's Executive Director and Medical Director, and a team of key management personnel who are in charge of different aspects of the Group's operations. Efficient and effective communication such as regular and adhoc updates and discussions are held as necessary. There is monthly reporting by management to monitor the performance of the Group. The Board is also constantly being updated of any new developments. More details can be found in the CEO's Statement in the Annual Report.

(v) The Company will not be charging JOES any additional professional fees and for management time.

(vi) The redemption of the convertible bonds was made on amicable grounds, the proceeds from the convertible bonds had not been fully utilised, and the Group has sufficient working capital for its operations. Further as mentioned in the announcement dated 17 April 2020, the redemption also allows the Company to reduce its financing cost. As such, the Company believes that the redemption will not affect its growth plans.

Question 4 from Shareholder:

The Company had utilised S$2,846,712 of the net proceeds from the Convertible Bond to fund the acquisition of JOES, as disclosed in the Company's announcement dated 3 September 2019. Is this the total sum invested in the above? What are the returns from this investment? It is below expected revenue?

CEO mentioned in the last AGM that the criteria of investing into a medical practice is based on certain expected revenue from the doctors of the practice. If it is not meeting expectations, then what are the plans for this investment?

Company's responses:-

As per the Company's announcement on 3 September 2019, the total consideration for the acquisition of an additional 19% in JOES was S$3,795,000, of which S$2,846,712 was paid in cash and the balance via the issuance of 1,760,000 new shares in the share capital of the Company at an issue price of S$0.5388 per share.

In the Company's announcement dated 1 February 2017, the Company had acquired 51% equity interest in JOES for a consideration of S$2,175,000. Hence, the total investment in JOES is approximately S$5.97 million.

Under the sale and purchase agreement entered into in February 2017, the Company was to purchase the remaining 49% equity interest in JOES by 1 April 2021. However, due to JOES's better than expected performance, the Company decided to buy an additional 19% equity interest earlier in September 2019 instead.

Question 5 from Shareholder:

In respect of Heliconia's redemption of funding, has this hampered the Company's overseas plans? The CEO had mentioned in the Company's last AGM that Heliconia can provide contacts for overseas ventures.

What is the Company's business strategy going forward in view of the pandemic, global recession and the bad publicity from the law suits? The law suit and Heliconia's redemption had hit the share price badly besides the COVID-19 impact.

Company's responses:-

Due to the COVID-19 pandemic, where overseas travel is restricted, as well as the global recession, the Company's current strategy is to focus on its operations in Singapore. In July 2020, the Group welcomed its first female surgeon, Dr. Goh Minghui and it is in the midst of opening an endoscopy centre in Toa Payoh Central to extend its reach to the heartland population.

The Company would like to highlight that there is no clear evidence that its share price is badly hit by the law suit and Heliconia's redemption. The share price was 38 cents on 9 April 2020, before the law suit and prior to Heliconia's redemption. The share price was 31 cents on 25 September 2020, a decrease of 7 cents or 18%, which is relatively low compared to the share market in general.

Question 6 from Shareholder:

Have there been cost cutting measures in view of pandemic and global recession, such as salary cuts and reduction in director's fees?

Company's responses:-

As per our FY2020 results announcement on 28 July 2020, employee benefits expense decreased by S$510,000 due to lower provision of bonus, in view of the lower revenue and profits during the financial year. The Group will continue to monitor its financial performance, driving revenue post-Circuit Breaker and look to improving operating efficiencies.

Question 7 from Shareholder:

In many AGMs I attended, shareholders are given the option to request for printed copies of the AGM materials. Am I able to request for printed copies of the Annual Report for the coming AGM?

Company's responses:-

In line with the COVID-19 safety measures, companies are not required to print and send Annual Reports to its shareholders for 2020. You may go to the SGX website at https://www.sgx.com/securities/annual-reports-related-documents or the Company's website at http://www.hcsurgicalspecialists.com/en/investor-relation/news to download the Annual Report.

By Order of the Board

Dr. Heah Sieu Min
Executive Director and Chief Executive Officer
27 September 2020

About HC Surgical Specialists Limited

HC Surgical Specialists Limited (the "Company") was incorporated on 1 September 2015 in Singapore and listed on Catalist of the Singapore Exchange Securities Trading Limited on 3 November 2016. The Company, its subsidiaries and associated company are a medical services group primarily engaged in the provision of endoscopic procedures, including gastroscopies and colonoscopies, and general surgery services with a focus on colorectal procedures across a network of 18 clinics located throughout Singapore.

The contact person for the Sponsor is Mr. Pong Chen Yih, Chief Operating Officer, at 9 Raffles Place, #17-05 Republic Plaza Tower 1, Singapore 048619, telephone (65) 6950 2188.