

MANAGING DIRECTOR'S REPORT

Year in review

This has been a pleasing year for the Group, with a key highlight being the promised return to profitability.

The Company continues to grow, both through acquisition and the organic expansion of existing businesses, with operational and financial performance improving consistently year on year.



OUR VALUE STATEMENTS

In order to build and grow a successful business in New Zealand, we believe a company needs strong philosophies and guiding principles. Throughout the year, we have developed a set of five value statements which uphold our corporate and social responsibilities as New Zealand's leading listed healthcare and medical services company.

Our business objectives, management activity and performance are measured against these value statements to ensure we continue to develop Abano Healthcare Group for the benefit of all our stake holders.

- We work for the benefit of our shareholders and aim to generate superior and sustainable long term returns on their behalf
- All our clients and patients will be provided with respect, exemplary care and professional treatment
- Innovation and the search for and sharing of knowledge is encouraged for all staff
- Our people are our most important asset – we aim to provide our staff with secure and rewarding long term employment in an environment where excellence is encouraged
- Through sound management, strategic understanding of healthcare needs and support of Government health policies, we aim to improve and benefit the healthcare and medical services available in New Zealand.

These guiding principles have been implemented throughout the year and have all contributed to this year's positive result.

OPERATIONAL PERFORMANCE

The Group has shown an overall improved operational performance for the year, with a return to sustainable NPAT based on growth in core revenue and a substantial lift in EBITDA and EBIT returns. Highlights from each of our four sectors are provided below, with more detailed information available in individual sector breakouts on pages 16 to 30.

Aged Care

The Aged Care sector produced a good core performance with improved results compared to previous years. Revenue was \$23.3 million with an EBITDA before noncore/unusals of \$4.7 million. The second half of the financial year was softer than expected due to a four month drop in occupancy rates, but levels have since recovered and occupancy now runs at a sustained daily average in excess of 90 percent.

The sector has concentrated on organic growth, investing in upgrades and the expansion of facilities at our Whitianga and Takanini properties. Both projects were started in the current financial year and will be completed mid-way into the new financial year. There has also been a significant investment in staff training, as well as research, with the continuation of the successful Career Caregivers Pathways Programme, and the announcement of a joint research study with the University of Auckland. The Promoting Independent Living

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study is investigating improved wellbeing for residents in long term care and results will be incorporated into ElderCare's policies and procedures.

Systems to comply with the ISO9001 Standard have now been implemented across the Aged Care sector and certification across all facilities is well under way. With the sale of the final non-core assets, the Aged Care sector is now well positioned to grow both organically and through acquisition and is expected to show an improving performance in the 2003/2004 financial year as our new facilities are opened. As seen on page 12, this sector yields an 8.7 percent return on invested capital at EBITDA before noncore/unusuals.

Rehabilitation

Our Group results for the 2002/03 financial year include a particularly strong second half contribution from Ranworth Healthcare, the Group's business in the Rehabilitation sector, which has now shown a trend of consistently improving performance for the past four half year periods. Revenue at \$12.4 million was 16 percent ahead of last year and EBITDA before noncore/unusuals was \$2.1 million. This is a credit to general manager, Graham Menary, business development manager, John Clough and their team of clinical professionals.

Two new contracts established with the ACC have both impacted positively on operating performance in the last quarter, and the sector has continued to invest in improving the already high quality of its staff, in order to maintain its position as New Zealand's leading provider of brain injury rehabilitation and care.

Occupancy increased to over 92 percent for most of the year in our 103 bed community housing network and our out-patient clinics have benefited from new contracts, as agreed with ACC. Following these new contract arrangements, Ranworth has invested considerably in new facilities and expanded services, including new clinical staff to meet the needs and increasing demands in this area. A number of significant opportunities to expand the service are being pursued, including the acquisition of Burtons Healthcare and Health Partners as announced in July 2003.

In addition, the Group has exercised an option to acquire the remaining 33 percent of Ranworth Healthcare, effective from 1 June 2003, as provided for in the original sale and purchase agreement. As seen on page 12, this sector yields a 28.4 percent return on invested capital at EBITDA before noncore/unusuals.

Diagnostics

This is the first financial year to reflect a full twelve month contribution from the diagnostic businesses. Under the guidance of Dr Clint Teague and his partners, the sector showed steady progress, with first half results consistent with previous years. Revenue was \$17.9 million and EBITDA before noncore/unusuals was \$1.9 million. The second half performance was affected by a larger than expected decrease in patient numbers and a decrease in the yield per test through the summer months.

The sector has also invested strongly in leading edge equipment, thus improving capacity.

In preparation for the new financial year, Dr Clint Teague has stepped down as managing partner, allowing Drs Peter Bethwaite and Andy Tie to jointly fill that role. Gerry Campbell has accepted the role of general manager and Dr Teague will remain medical director on the Abano main board.

Agreement was reached on the important new national cervical screening contract with the Ministry of Health. In the last year, the District Health Boards (DHBs) in Wellington and Marlborough/Nelson have also indicated that a commercially workable settlement for community pathology laboratories, with an established history of service in the region, is possible. As seen on page 12, this sector yields a 15.2 percent return on invested capital at EBITDA before noncore/unusuals.

Dental

We entered the Dental sector in November 2002, with the purchase of Geddes Dental Group, and our Group results include seven months contribution from this business. Revenues for the period were \$4.5 million. Higher than expected transition and restructuring costs resulted in an EBITDA before noncore/unusuals slightly below break even at \$(0.2) million. While below our expectations for the period, current performance indicates the business is on target to meet its budgeted profit for the new financial year.

Since its acquisition, the focus for Geddes Dental Group has been on the transition of the business from an entrepreneurial venture to that of a committed corporate based dental company that can take advantage of the significant demand identified in existing markets. Additional dentists have been employed at the Red Beach and Mt Roskill branches, as well as the commissioning of a third mobile unit and the opening of a Geddes Dental branch on the University of Auckland campus.

A new management structure has been implemented with the recruitment of an operations manager and a financial accountant to work within the sector. Additionally, a global market research and assessment visit was undertaken in the UK and USA to identify future growth models, with investigations into successful and non-successful dental businesses. A new IT platform for Geddes Dental has been identified and is being implemented in the new financial year.

Challenging growth targets have been set for the new year, and we believe there are some positive acquisition opportunities in the North Island. Contributions from the sector are expected to improve, however, the level of profit will remain modest as investment into growth opportunities continues. As this sector generated a start up loss, its return on invested capital was negative, however, we remain confident it will produce returns above the Company's WACC in future years.

GROUP FINANCIAL PROGRESS

The following analysis looks at the Group's performance over the past four years. To simplify reporting for this annual report, we are showing consolidated EBITDA (after corporate costs and before noncore and unusuals) for each sector. Previous years' figures have been revised to provide an accurate historic trend analysis.

In addition, we have included investment returns in the form of a Return on Invested Capital (ROIC) analysis for each business sector. It is clear from these that the returns from less capital-intensive businesses have a far more attractive investor focus.

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\$ MILLION	EBITDA BEFORE NONCORE/UNUSUALS	ASSETS EMPLOYED	RETURN ON INVESTMENT
Aged Care	4.7	54.1	8.7%
Rehabilitation	2.1	7.4	28.4%
Diagnostic	1.9	12.5	15.2%
Dental	(0.2)	4.7	(4.3)%

Results for the 2002/03 financial year also include one off gains which were realised following the sale and settlement of the final non-core asset – the Regents Park retirement village development in West Auckland, as well as the recognition of the Group's deferred tax position following our return to sustainable profits.

\$ MILLION	1999/2000	2000/2001	2001/2002	2002/2003
Revenue	25.6	34.1	40.4	58.8
EBITDA before noncore and unusuals	3.8	4.5	5.5	8.5
Noncore/unusuals	5.2	(6.0)	(1.8)	0.9
EBITDA	9.0	(1.5)	3.7	9.4
EBIT	7.9	(3.9)	1.4	6.1
NPAT	5.6	(8.2)	(2.8)	2.0
No. of shares	150,771,725	157,032,387	193,681,527	194,835,832
Net debt	44.1	41.1	32.5	32.4
Total assets	87.3	76.0	80.7	81.4
EBITDA before noncore and unusuals/share	2.5 cents	2.9 cents	2.8 cents	4.4 cents
NPAT/share	3.7 cents	(5.2) cents	(1.4) cents	1.0 cents

Our focus for growth continues to be investment in medical and healthcare businesses and sectors which have proven cash flow streams and offer the best returns for our shareholders.

Like all investments, we believe a portfolio with a balance between high growth investments – rising stars – and secured returns – stable yields – offers the best investment mix for the Group. Abano Healthcare's current portfolio consists of sustainable cashflow generated by the demand for specialist medical and healthcare services in the Rehabilitation and Dental sectors, which typically exhibit low capital and high intellectual expertise, and the bond type returns of the Aged Care and Diagnostics sectors.

OVERALL FINANCIAL POSITION

The Group's financial position has improved in the past year, with an increase of over 44 percent in revenue, an expansion into a fourth healthcare sector – Dental – and organic growth across all sectors. Group debt was maintained at \$32.4 million as at year end, after investing over \$6 million in new business activities, technology upgrades, capital projects and the retirement of convertible notes. The number of potential future shares on issue has also been reduced by over 49 million shares and shareholders' equity in the Company now represents 52 percent of total assets.

FINANCIAL POSITION

\$ MILLION	1999/2000	2000/2001	2001/2002	2002/2003
Total assets	87.3	76.0	80.7	81.4
Net debt	44.1	41.1	32.5	32.4
Total equity	37.4	29.9	41.5	42.0

POTENTIAL SHARES ON ISSUE

	1999/2000	2000/2001	2001/2002	2002/2003
- Paid up shares on issue	150,771,725	157,032,387	193,681,527	194,835,832
- Options	33,034,274	33,034,274	31,034,274	nil
- Exec convertible notes	Nil	3,800,000	6,225,000	6,725,000
- Other convertible notes	9,397,328	5,398,402	22,101,025	16,451,206
Potential total shares	193,203,327	199,265,063	253,041,826	218,012,038

SOURCES OF INCOME

The New Zealand Government continues to be the largest funder of healthcare and medical services in New Zealand. Increases in Government spending were announced in the 2003 budget, with an additional \$400 million allocated each year up to 2004/05, then a further \$535 million each year for 2005/06. This is on top of funding for the first year of the phase out of asset testing for long term geriatric care.

As noted to the NBR in June 2003 by Dr Michael Cullen, Minister of Finance: "In 1993, health took 15.6 percent of Government spending; this year it will be about 18.4 percent. This is not a minor fiscal realignment. It is a massive structural shift... projections are that by 2006, health will be receiving 19.7 percent of total Government spending". He concluded by saying: "These are mind boggling numbers. I offer my sympathies in advance to the Minister of Finance in 2051."

A new distribution network has been established by the Government for the funding of primary healthcare within the community with the establishment of Primary Healthcare Organisations (PHOs). We are working closely with PHOs, DHBs and other Government funding organisations, to ensure that all our businesses offer services that are of value to the Government, and in line with current policy and support the focus on primary intervention and care in the community.

Overall, the Group's continuing financial success is reliant on positive relationships with public health funding bodies and Government organisations, with 60 percent of our income derived from public funding and Government contracts. We will always have a strong focus on, and working relationship with, Government initiatives in health, with a clear recognition that increasing private payment for health is inevitable.

	2002/2003	SHARE OF GROUP	FUNDING % GOVT/PRIVATE
Aged Care	\$23.3 million	40	60 MOH/40 Private
Rehabilitation	\$12.4 million	21	83 ACC/16 MOH/ 1 Private
Diagnostics	\$17.9 million	31	90 MOH/ 10 Private
Dental	\$4.5 million	8	25 MOH / 75 Private

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INVESTMENT IN OUR RESOURCES

At Abano Healthcare, we have identified advanced technology, leading edge equipment, quality facilities and highly skilled and experienced staff as our four key resources and our investment strategy focuses on continually improving and expanding in these areas.

As can be seen in the table below, total investment in resources for the 2002/03 financial year was \$3.3 million.

RESOURCE	INVESTMENT \$000s
Technology	\$823
Equipment	\$256
Human resources	\$460
Facilities	\$1743

Investment in technology for 2002/03 has focused on improving administration and operational performance, with the Great Plains accounting system implemented for the Aged Care and Rehabilitation sectors. This is now the Group standard and the system is currently being introduced into the Dental sector, with Diagnostics planned in the next 12 months. In addition, the Gold Care billing system was introduced into the Aged Care sector to improve billing efficiencies. A new IT platform is being investigated for the Dental sector, with implementation expected in the new financial year. This will aid in client and database management and corporate administration. The Ranworth Healthcare website was updated, with updates also planned for the Geddes Dental and ElderCare sites.

Both the Dental and Diagnostics sectors have invested in large items of equipment in the past financial year, with the commissioning of a third mobile dental unit by Geddes, and the lease of a new chemical analyser for Wellington Medical Laboratory.

Over \$460,000 has been spent on investment in our people in the past 12 months, with a primary focus on training and developing existing staff. This has all been expensed in the current financial year.

Both the Dental and Rehabilitation sectors have expanded with the addition of a new Geddes dental branch at Auckland University in May 2003, and the opening of a branch for Ranworth Healthcare in Wellington. The Aged Care sector will invest \$4.2 million over a two year period, into improving and expanding four of its existing facilities, ensuring greater efficiencies and increased profitability. Further upgrades are planned on existing sites where good development potential exists to add rooms to existing nursing homes or serviced apartments to ensure that the sector continues to meet high client expectations.

MANAGEMENT

Abano Healthcare is an operating company that creates partnerships with the clinical and management specialists in the businesses it invests in. The management objective of a new acquisition or venture is to continue to foster the successful elements of the business by continued ownership incentives and internal succession planning. We contribute support in regards to management and financial processes to help the business develop efficiencies, synergies and effective governance practices.

Each sector is led by a general manager or managing partner, with support from a senior management team

from within the business. Along with myself as managing director and Richard Keys, our new chief financial officer, the senior management team make up the sector management board. Monthly meetings are held by the management board to review performance against activity and approve activity going forward.

THE PLANNING PROCESS

Abano Healthcare has a defined planning process which runs according to the financial year. In November every year, a two-day off site planning session is attended by the board and senior management to determine the future direction of the Company and set goals for the next three years. Sector management teams undertake strategic planning and development in February each year based on the board's plan, with direct input from Abano Healthcare's management. A business plan for each sector is then prepared in April for approval by the board. These plans then form the basis for the Group's operating budget for the new financial year.

THE FUTURE

Abano Healthcare's long term business strategy is based on New Zealand's and the OECD's growing demand for healthcare and medical services. As stated earlier, Dr Michael Cullen recently acknowledged this increase in demand is due to both an ageing population as well as an expectation of improved access and higher quality healthcare and medical services in first world countries, including New Zealand, and the Government simply cannot continue to fund the growth in volume and demand.

In New Zealand, more than 23 percent of the population is expected to be aged over 65 years by 2030, a total of approximately 1.1 million people. For every five years a person lives over the age of 65 years, the demand for and use of medical and healthcare services doubles; for people aged over 70 years, demand doubles every two years. An 85 year old uses 15 times more health dollars than a 50 year old, and 85 year olds in our population will quadruple in the next five years.

Our focus therefore is on this growing demand and our clinical management teams and personnel have the experience and professionalism to ensure we maximise all opportunities and achieve our vision to be New Zealand's leading listed healthcare and medical services provider, positioned both for Government needs and a growth in private health services.

We now have four key operating divisions with track records of sustainable growth. Our priority is to achieve continued profitable growth through both the acquisition of leading healthcare and medical practices in key sectors of the market, and through the organic growth of our existing businesses.

We are confident we will experience another year of improving profitability in 2003/04, with initiatives in place to take advantage of increased public funding as well as growing demand for private healthcare and medical services.



Alan Clarke
MANAGING DIRECTOR