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## Undisclosed Share Pledges Intensify Questions About True Debt Levels

Yesterday NMC issued the latest in a series of confusing disclosures about its controlling shareholders' ownership and pledges when it disclosed that 19.0 million of its shares are potentially subject to undisclosed share pledges. We note that the FCA has announced it is probing these misstatements.<sup>1</sup> In our December 2019 report, we stated that we suspect NMC has undisclosed debt.<sup>2</sup> These recent disclosures and insider share sales reinforce our view.

The numerous pledges as raise at least two possibilities, each of which is worrying. One possibility is that NMC has undisclosed debt secured by share pledges. The Financial Times December 20, 2019 report on NMC's attempted off-balance sheet debt financing hints at hidden debt secured by share pledges.<sup>3</sup> Another possibility is that these pledges were collateral for loans to related parties that transacted with NMC on non-economic terms, thereby subsidizing NMC's margins, which we called "too good to be true".<sup>4</sup> Such debt could have been taken on by either disclosed or undisclosed related parties (such as Modular Concepts, which we highlighted in our previous report). In this report, we reveal details about additional previously undisclosed related parties that appear to transact with NMC.<sup>5</sup>

In either scenario, debt would have effectively been used to pump up the value of stock, which would have in turn been used as collateral for (likely increasing) debt. To the extent our suspicions turn out to be correct, this circular symbiosis would be reminiscent of Enron's off-balance sheet debt structures in which Enron issued shares to "special purpose entities", which borrowed money using the stock as collateral, and then bought (poor) assets from Enron.<sup>6</sup> As with Enron, this circular arrangement would work until the stock value falls, which is what ultimately triggered Enron's collapse.

## The Pledges Might Secure Off-Balance Sheet Debt

One possibility we see is that the undisclosed insider share pledges enable off-balance sheet financing that disguises NMC's true financial condition. As we stated in our initial report, we believe that NMC has intentionally understated its debt balances while reporting suspiciously high cash balances and elevated operating margins. We explained that we were unable to reconcile the company's debt balance with Bloomberg's debt table, regional banks' announcements, and local reporting. We also identified hundreds of millions of dollars in lease obligations that we believe were improperly excluded from the company's reporting and noted that NMC's reverse factoring facilities do, in fact, appear to have recourse to the company,

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<sup>1</sup> <https://www.ft.com/content/c3ca5576-4bd7-11ea-95a0-43d18ec715f5>

<sup>2</sup> See Muddy Waters Capital LLC December 17, 2019 report on NMC.

<sup>3</sup> <https://www.ft.com/content/c3469f08-2231-11ea-b8a1-584213ee7b2b>

<sup>4</sup> Muddy Waters December 17, 2019 report on NMC, p. 3.

<sup>5</sup> Because we lack enough facts, we are unable to opine whether NMC was obligated to disclose these related party transactions.

<sup>6</sup> See <https://www.investopedia.com/updates/enron-scandal-summary/> "How Did Enron Hide Its Debt?"

contradicting management's prior statements. Tellingly in our view, NMC investor relations representative Mr. Yahya ceased communicating with us after we began asking more detailed questions concerning the company's debt.

Three days after our report, the *FT* reported that NMC had sought to raise €200 million in off-balance-sheet financing backed by shares in two of its existing UAE hospitals.<sup>7</sup> According to the article, NMC used Blackstar Capital, which has previously arranged supply chain finance debt for the company, to engineer the "highly unconventional" deal. While NMC issued a denial in response to the article, it did not or could not point to any specific inaccuracies in the reporting.<sup>8</sup>

The foregoing pattern of facts and events demonstrates to us that NMC insiders have a strong desire to obfuscate, coupled with a tenuous relationship with the truth. For this reason, we believe it is possible that the undisclosed share pledges were used to secure undisclosed debt financing.

### **The Pledges Might be Loans to Related Parties that Subsidize NMC's Financials**

Alternately, we believe that the share pledges might have enabled insiders to prop up NMC's margins by financing related parties, which in turn transacted uneconomically with NMC. At least one of the pledges "relate[s] to credit facilities made available... to a company associated with Dr. B.R. Shetty", which underscores our concern.<sup>9</sup> We discussed one apparent undisclosed related party, Modular Concepts, at length in our first report. Below, we identify three additional potential related parties that the company does not disclose, each of which might be utilized in such a margin inflation arrangement.<sup>10</sup> (The below list should not be interpreted as a complete and comprehensive list of potential related parties – there could be additional parties that we have not yet discovered.) To the extent this theory – that related parties borrow money in order to subsidize NMC's margins – is correct, the unraveling of the supporting web of debt would likely bring an end to the subsidies and cause reported profits to drop.

#### *BRS Catering Services LLC and Royal Catering Services LLC*

NMC's catering vendors appears to be two such undisclosed related parties. BR Shetty's BRS Ventures purchased Royal Catering in 2015 and planned to expand into healthcare catering as of

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<sup>7</sup> <https://www.ft.com/content/c3469f08-2231-11ea-b8a1-584213ee7b2b>

<sup>8</sup> <https://cf-cdn.nmc.ae/Uploads/InvestorRelations/denial-of-press-article-20-dec-2019-7778fc83-f2a5-4048-98b8-38e358af4c1f.pdf>

<sup>9</sup> <https://cf-cdn.nmc.ae/Uploads/InvestorRelations/nmc-health-plc-statement-regarding-major-shareholdings-10-feb-2020-54c90b23-f3b3-4aee-a995-0ff1187967ea.pdf>, p. 1

<sup>10</sup> Because we lack enough facts, we are unable to opine whether NMC was obligated to disclose these related party transactions.

that date.<sup>11,12</sup> No corresponding disclosures appear in NMC's reports. Less information is available regarding BRS Catering Services LLC, but its shareholdings paint a curious picture. As of the most recent ICP credit report available (dated 2018), BRS Catering Services, which is a distinct entity from Royal Catering, has 150 employees and is 49% owned by BR Shetty's daughter, Seema Raghuram Shetty.<sup>13</sup> Its headquarters are on the grounds of NMC Specialty Hospital in Dubai.<sup>14</sup> (51% of BRS Catering Services is owned by a UAE national, Abdulla Alhaj Alawadhi, who is invested in at least one other Shetty vehicle.<sup>15,16</sup>)

To deepen the confusion, though BRS Catering seems to share at least two senior finance and operations employees with Royal Catering, BRS Catering's Managing Director (CEO) is again named as Seema Shetty, not Royal Catering's then-CEO Jean-Pierre Garat.<sup>17,18</sup> Therefore, it seems to follow that not only is a BRS Ventures portfolio company, Royal Catering, providing catering services to NMC, but BR Shetty's daughter operates a distinct company, also named after her father and with approximately \$2.5 million in turnover a year.<sup>19</sup>

### *Shetty Lighting*

NMC Vendor Shetty Lighting presents another potential undisclosed relationship. Out of 22 Shetty Lighting projects enumerated on the company's site, five counted NMC as the client, while the sixth was for another Shetty business, Neopharma.<sup>20</sup>

These three apparent undisclosed related parties suggest that there is much still unknown about the web of enmeshed transactions at NMC, as well as the extent to which its key shareholders hold economic interests beyond what the company is willing to disclose. In each of these cases, undisclosed debt secured by NMC insiders' shares could be a vehicle to provide services to NMC below cost and at a loss for the vendor, which would certainly go part of the way toward explaining what we view as NMC's "too good to be true" margins.

## **Deadly Serious Concerns About NMC's Governance**

We opined that "we are unsure how deep the rot at NMC goes", and we believe that recent events have ratified that concern in spades. It is possible that NMC's independent directors

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<sup>11</sup> <http://www.brsventures.com/news/brs-ventures-acquires-royal-catering-services-2015/>

<sup>12</sup> <http://www.royalcatering.ae/about-us.php>

<sup>13</sup> BRS Catering Services LLC credit report, June 2018

<sup>14</sup> BRS Catering Services LLC credit report, June 2018

<sup>15</sup> Ibid.

<sup>16</sup> <https://www.difc.ae/public-register/brs-infrastructure-services-spc/>

<sup>17</sup> BRS Catering Services LLC credit report, June 2018

<sup>18</sup> <https://www.linkedin.com/in/gilles-corroy-8258539/>

<sup>19</sup> BRS Catering Services LLC credit report, June 2018

<sup>20</sup> <http://www.shettylight.com/portfolio.html>

could not have reasonably known of the recently disclosed share pledges, associated debt, or proxy ownership arrangements. We do, however, fault them for likely allowing a minimalist approach to disclosure of related-party transactions. Even if the related party transactions we have identified did not mandate disclosure based on the facts known to the board, we believe that a more transparent approach would have provided more warning to investors about the events that are now unfolding.

We finish on a final, related note. NMC hoped investors would dismiss our concerns about assets purchased from related parties at inflated prices. However, yesterday, NMC announced that there have been massive undisclosed share movements among BR Shetty, the Butti's, and various banks. These facts are extraordinary. They weigh heavily in favor of our conclusions.