marketWATCH

PROPRIETARY DATA. PROPRIETARY INSIGHT.

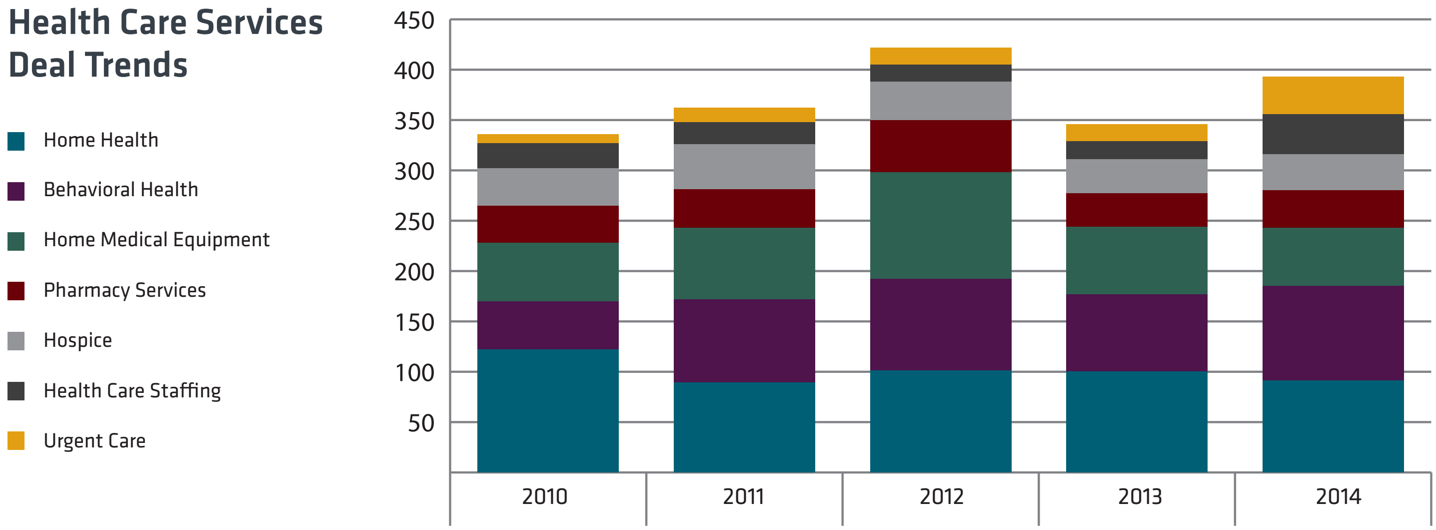
2014 M&A ROUNDUP:
RECORD DEAL VOLUME IN URGENT CARE HELPS DRIVE A 14% GAIN IN OVERALL HEALTH CARE SERVICE ACTIVITY

Based upon proprietary data collected and analyzed by The Braff Group, every sector except home health and home medical equipment recorded year-over-year gains, propelling aggregate health care service deal volume up 14% over 2013. Moreover, if we exclude 2012, a year that was artificially juiced as sellers rushed the exits to beat an 8.3% increase in capital gains, 2014 was a record year, eclipsing the tally posted in 2011.

The biggest winner – just surpassing urgent care – was health care staffing, which rocketed 150% in 2014. With reduced unemployment and more beneficiaries (care of health care reform) accessing an already under-staffed health care system, the sector recorded its highest tally, by far, in nearly 10 years.

The greatest contraction came in the home medical equipment sector, driven in large part by a marked slow-down in private equity sponsored investments in the space.

Health Care Services Deal Trends



Source: The Braff Group

Urgent Care M&A Skyrockets

On its face, 2014 was a break-out year for mergers and acquisitions in urgent care, as the sector posted 37 deals, an increase of 118% vs. 2013.

While volume increases are certainly a strong indicator, they are not enough to fully assess the relative strength of an M&A market. For example, if there are a limited number of buyers pursuing a limited variety of development strategies, there is not only greater risk of a contraction (should one or two buyers take a breather), the balance of supply and demand is likely to be in the buyer's favor.

So how does urgent care square up?

Well, the current trend is that there aren't enough sizeable, multiple unit providers available to meet acquisition demand. Quite true – if you're a private equity group, insurer, or ancillary service provider seeking an urgent care platform with the management team, operating and technology infrastructure, and development experience that can be leveraged to build the next Concentra. But if your goals are not quite that ambitious – if you're a hospital system looking to jumpstart an urgent care initiative, a local provider eyeing a regional expansion, or a PE sponsor with the bandwidth and patience to acquire incrementally (or even go the de novo route, rather than slug it out with everyone else waiting for the perfect 10 (as in centers) to come to market), there's opportunity aplenty.

And the numbers bear this out – big time.

Private Equity is Far From Done

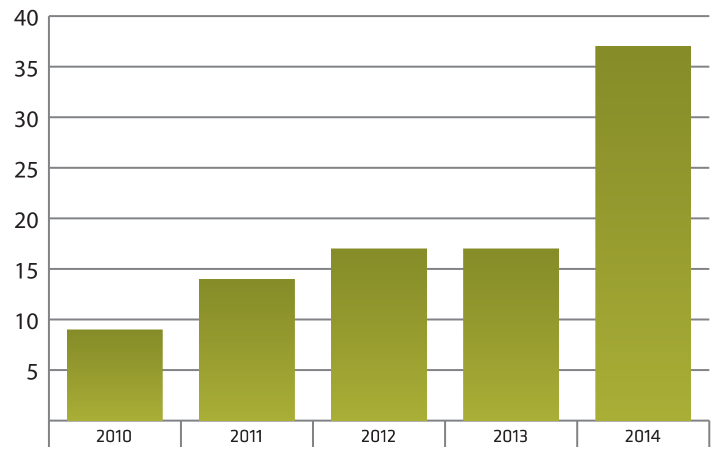
It is well known that private equity has been binging on urgent care, driving what has literally become an insatiable demand for market-entry, multi-center, platform deals. **In just the three year period ending in 2012, 13 urgent care platforms were snapped up,** making such deals harder to come by in 2013 and 2014.

After a run on the market that depletes supply and raises prices, private equity latecomers can find themselves with their faces pressed to the proverbial glass, watching impatiently for the right deal to emerge. But we note an interesting alternate strategy in urgent care. In order to fill the gap in the supply of platform opportunities, **between 2011 and 2014, there were at least nine private equity sponsored start-ups** – an extraordinary figure when you consider that, while it probably has occurred, we cannot recall a single similar such investment in all of the other health care service sectors we cover (home health and hospice, behavioral health care, pharmacy services, home medical equipment, and health care staffing).

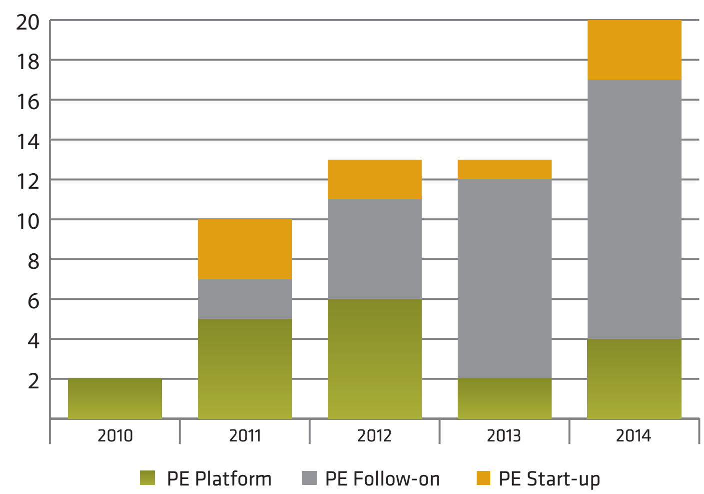
So why are investment funded start-ups viable in urgent care when they are far less apparent in other health care service sectors?

Actually, the answer is quite simple. For the most part, each of the sectors mentioned above are highly dependent on long established, zealously protected relationships with referral sources such as hospitals, discharge planners, physicians, and other providers. In such referral dependent sectors,

Urgent Care Deal Trends



Private Equity Investment Trends in Urgent Care



Source: The Braff Group

it is far more difficult to build enough size and scale in just 3-7 years – the typical PE "holding period." The dynamics are different in urgent care. Consumer driven, "retail" medicine relies far less on referral relationships than it does on location, site aesthetics, hours of operation, traffic flow, staffing models, branding, advertising, and more. While doing this right is by no means easy, it does not require cracking longstanding, often "sticky" relationships between referrers and other providers. So the de novo option is far more feasible in urgent care than in other health care service sectors – hence the PE sponsored start-up.

Finally, once platforms are in place, the PE consolidation playbook calls for follow-on transactions that can leverage the "host's" infrastructure. With almost 30 private equity groups on the prowl in the last five years alone (including the start-ups that also consider acquisition opportunities – especially late in their investment cycle where there isn't enough time to allow a start-up to mature), **the demand for "follow-on" deals has grown exponentially – and will continue to do so for the foreseeable future.**

Together then, these dynamics explain why we've seen a rise in private equity activity, followed by a hockey stick-like spike in 2014. **This will create a strong foundation to support acquisition demand in urgent care for years to come – from "one off" centers to platforms of all sizes.**

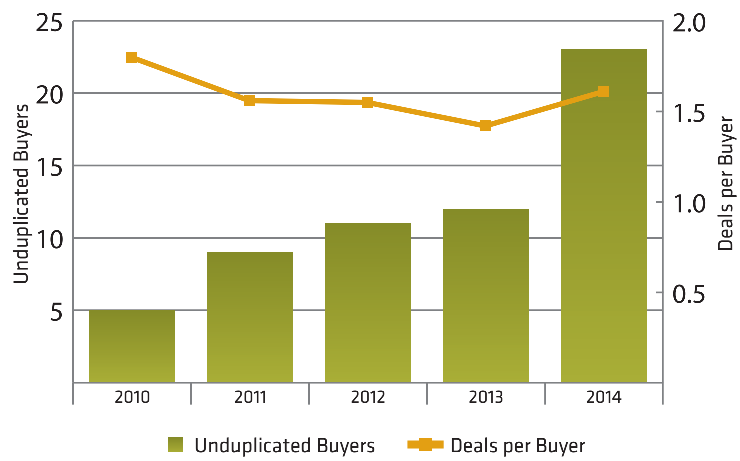
Depth and Breadth of Urgent Care Buyers – and Why They're Buying

It's not just the avalanche of equity dollars into urgent care that has catapulted acquisition demand. As we have seen repeatedly in the other health care service sectors we cover, PE money is often the catalyst that stimulates buying activity from other players to stay competitive or to become more attractive – and valuable – to buyers next-in-line in the consolidation "food-chain." This expands the buyer pool even further. Smaller, 1-5 unit operators begin to look at 1 or 2 unit opportunities that may be overlooked by the Wall Street crowd. Smaller private equity groups, or angel backed entrepreneurs, get into the mix to create the market-entry platforms that are in such high demand.

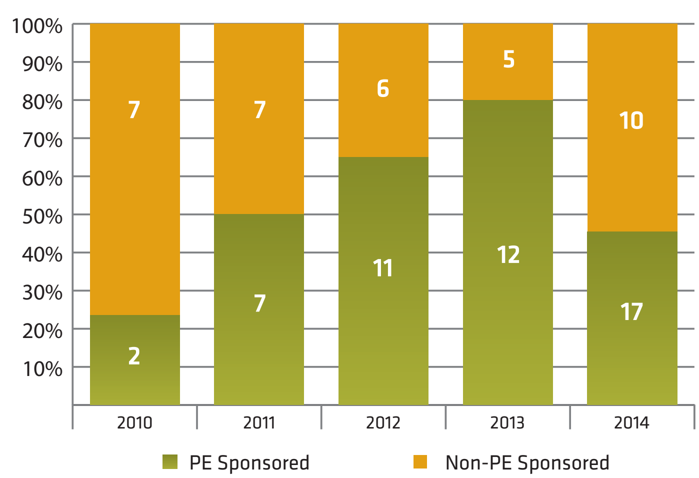
And then there is increased acquisition demand that has little to do with short-term investment returns, but more to do with strategies to adapt to a rapidly changing health care delivery system. And this brings all of the hospitals, ancillary service providers, insurers, and employers into the game. The pitch? Deploying urgent care as an alternative to the ER to treat and triage patients, beneficiaries, and employees at a lower cost, with better outcomes, and with greater patient satisfaction. The "Triple Aim" trifecta.

Turning back to the data, growth in the urgent care buyer pool just leaps off the spreadsheet. Our research indicates that while we have seen steady growth of unduplicated buyers since 2010, the numbers ballooned last year. **In 2014, we identified at least 23 different buyers completing deals during the year – nearly double the number of buyers in play in 2013.**

Unduplicated Urgent Care Buyers and Deals Per Buyer Trends



Private Equity vs. Non-PE Urgent Care Deal Trends



Source: The Braff Group

We've seen healthy movement in the distribution of deals between those financed by private equity sponsors vs. those that were not. As illustrated in the accompanying chart, while private equity was responsible for more than 50% of all urgent care deals from 2011 to 2013 (where PE accounted for 70%), the figure dropped below 50% in 2014, indicating a broader variety of buyers.

Moreover, we've seen a meaningful improvement in one of the most significant, bellwether measures of the strength of an M&A market in consolidation: deals per unduplicated buyer. In arguably a "perfect" market, the average deals per unduplicated buyer would be 1.0, illustrating the breadth of acquisition interest. So the closer to 1.0, the better. In 2010, the average number of deals per unduplicated buyer was 1.8. By 2013 this figure was down to 1.41. Although it crept up to 1.6 in 2014 with a burst of activity from NextCare, we expect this measure to decline steadily – and favorably – over the next 2-5 years.

So let's summarize:

- Private equity demand for urgent care platforms remains strong enough that over the past four years, nine firms have invested in start-ups, rather than wait for the perfect deal to present itself.
- With nearly 30 PE sponsored investments in the sector over the last five years alone, the demand for follow-on deals is accelerating rapidly.
- While growing steadily since 2010, the number of unduplicated buyers soared to 23 in 2014.
- Even as private equity sponsored deal flow has risen in raw numbers, PE accounted for less than 50% of urgent care deals in 2014 as non-PE sponsored strategic buyers haven't swelled.
- Though there was an uptick in 2014, the number of unduplicated deals per buyer fell steadily from 2010 to 2013, where it was 21% below the 2010 rate.

All of the above converged to produce an unprecedented year in urgent care M&A.

Talk about strong vital signs…

THE BRAFF GROUP DIFFERENCE

Since the firm's inception in 1998, we have closed more than 250 transactions, more than any other mergers and acquisitions advisory firm covering like sectors.

According to Thomson Reuters, The Braff Group ranked # 1 in health care mergers and acquisitions advisory services in 2009, 2011, 2012, and 2013. Four Time Winner Health Care Deal of the Year.

Call us to see how we can put our experience to work for you.

Reg Blackburn
Atlanta
866-455-9198

Ted Jordan
Atlanta
888-290-7080

Mark A. Kulik
Atlanta
888-922-1838

Nancy Weisling
Chicago
888-290-7237

Pat Clifford
Chicago
888-922-1834

Bob Leonard
Ft. Lauderdale
888-922-1836

Steven Braff
Palm Springs
888-922-1833