



## viewPOINTS

# HOW URGENT CARE CONSOLIDATION MAY PLAY-OUT... AND PLAY-IN TO YOUR STRATEGIES

*This publication has been updated  
to reflect new information.*



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*Consolidation in health care has been more prominent than the Kardashians.*

*Over the past 35 years, we have seen massive waves of mergers and acquisitions in hospitals, skilled nursing facilities, home health and hospice, home medical equipment, rehab, pharmacy services, dialysis, home infusion, labs, physician practices, and more. Most recently, the spotlight has turned to behavioral health and addictions and substance abuse.*

*Now it's urgent care.*

Each of these roll-ups has followed a pretty consistent script.

If you understand how it's likely to play out, you can hone your development strategy, particularly as it relates to investing in – and cashing out of – urgent care.

First, we take a look at what makes a sector like urgent care ripe for consolidation.

## Markets ideal for consolidation are extremely fragmented.

The greater the fragmentation, the greater the opportunity to assemble a critical mass of acquisitions that (a) best fit a particular market's demographics, economic capacity, and health care needs, (b) are contiguous and hence more efficient to manage, support, and promote, and (c) match a buyer's ambition, investment resources, and timeline. **Given that urgent care is fundamentally a local business, often owned and operated by individual physicians, it is innately fragmented.**

## Consolidators look for sectors where the operations are relatively uniform from provider to provider.

This not only makes the business far easier to scale, but it also enhances management's ability to realize revenue enhancing and cost-saving synergies post-consolidation. Check two for urgent care. **While the quality, efficiency, and clinical capabilities of individual urgent care centers may vary widely, at their core, they all solve the same basic need – fast, convenient, affordable access to health care.**

## Consolidators must be confident that they have viable exit opportunities.

The best markets are those that are expected to undergo 10 years or more of growth and development. Such windows support multiple investment cycles, creating a dynamic environment where consolidation at one size level becomes the inventory for buyers at the next. **With health care reform creating more covered beneficiaries (many of whom do not have a primary care physician), a shortage of physicians and advanced practice providers, emerging financial incentives to keep patients out of the ER, and health care consumer behavior that increasingly values convenience and extended hours of operation, urgent care has a long runway before it.**

## Classic phases of consolidation

With sector specific variations, consolidation tends to proceed along a fairly predictable path.

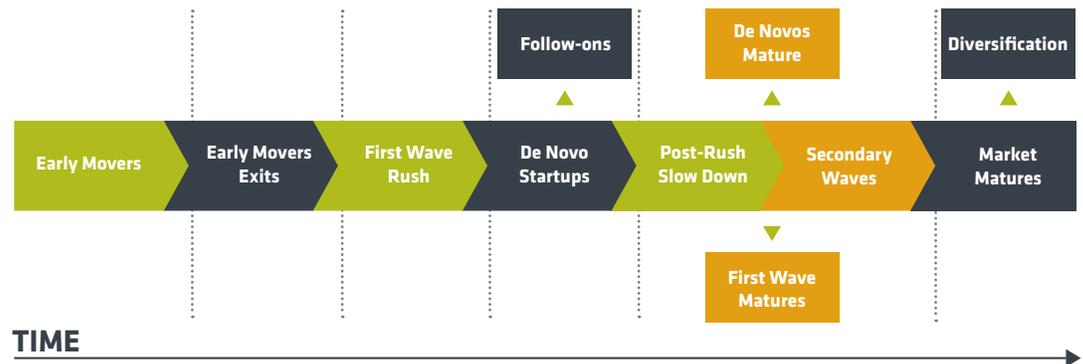
In most consolidation waves, you can find one or more **EARLY MOVERS** – investors that bring initial attention to a sector that is either just emerging (as in urgent care), or has been previously overlooked. Quite often, the early movers are maverick private equity groups – investors with a passionate belief in their, as yet, untested investment thesis, and the willingness to tread where others haven't gone.

If the **EARLY MOVERS REALIZE SUCCESSFUL EXITS**, other buyers begin to target the sector, which in and of itself, attracts even more attention. Ultimately, the acceleration of investment interest creates a **FIRST WAVE RUSH** of demand and activity – again, frequently dominated by private equity. Not surprisingly, this can also spur an increase in pricing.

Eventually, sector visibility rises to the point that it draws entrepreneurs into the space, ushering what can be an extended period **DE NOVO STARTUPS**. At the same time, acquisition demand for smaller providers begins to swell as the first wave buyers look to leverage and build upon their initial platform investments with **FOLLOW-ON DEALS**.



## CLASSIC CONSOLIDATION TIMELINE



With the first wave rush gobbling up many of the most attractive acquisition candidates, and new de novos too early in development to bring to market, the supply of potential sellers can diminish quickly. Accordingly, we often see a **POST-RUSH SLOWDOWN** where demand exceeds supply, which can further boost pricing.

Eventually, the **DE NOVOS MATURE**, and we begin to see **FIRST WAVE EXITS**, providing both the inventory and enthusiasm to support an extended **SECONDARY WAVE** that often includes more sizeable private equity to private equity deals.

At some point in the cycle, the biggest and most successful players begin to reach saturation in the markets they wish to serve. Deal volume begins to decline and valuation begins to soften, signaling the onset of **MARKET MATURITY**. During this phase, deals continue to get done, but they tend to be more opportunistic in nature. Furthermore, we begin to see forays toward **DIVERSIFICATION**, as established players look for complimentary products and services to sustain long term growth.

This phase can last many years, with peaks and valleys of deal volume reflecting changes in health care policy, utilization, or reimbursement, availability of capital, and broad economic conditions. Or it can come crashing down if any of the above renders the business models obsolete or marginally profitable (as in home medical equipment today which has seen a 40% fall-off in reimbursement)

### So how has this all played out in urgent care?

Consolidation arguably began with outpatient occupational health/urgent care hybrids. Our research indicates that at one point or another in their development, 15 different private equity firms held interests in **Concentra** and **US HealthWorks**. This was also the period during which Excellere Partners backed **MedExpress**. While there were certainly others, these were three of the first, high profile **EARLY MOVERS**.

With the visibility of so many private equity firms in these early stages, we would have anticipated at least some measurable increase in platform deal flow, even before the first mover exits. But as illustrated in the accompanying chart, it wasn't until 2011 when the deals began to churn.

Why so?

It's actually quite simple. Remember how fragmentation is one of the primary factors that supports consolidation?

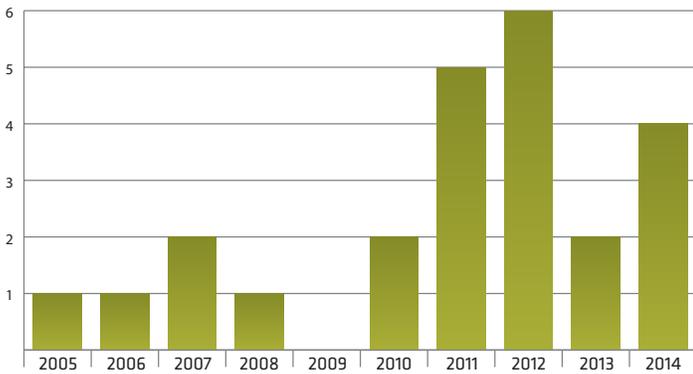
Well, unlike other health care sectors that began life extremely fragmented, when urgent care first rose to consciousness, it was dominated by two of the **EARLY MOVERS**. When they sold, Concentra had revenues of \$800M with more than 500 facilities in 42 states; HealthWorks had \$375-400M in revenues and 170 plus locations. Such blockbuster deals typically occur in the **SECONDARY WAVES** after some of the first wave consolidators consolidate themselves. But in urgent care, the market was still arguably in its infancy. So when two of its most dominant players were taken out of play, there simply weren't many traditionally sized platform companies (revenues of plus/minus \$50M) available to acquire.

This may explain why Excellere exited their investment after only three years. When MedExpress sold, it reportedly had 40 plus locations and \$110M in revenues. However when the first wave rushed MedExpress like paparazzi on deadline, the competition drove the purchase price up to a reported \$450M – a price Excellere couldn't refuse.

Back to our **EARLY MOVERS**. Each realized **SUCCESSFUL EXITS**. Concentra was acquired by Humana in 2010 for \$790M. HealthWorks was acquired by Dignity Health in 2012, and MedExpress was acquired by General Atlantic and Sequoia Capital in 2010. The Concentra and HealthWorks deals were particularly notable in that they drew in an insurer and a health system, demonstrating both the breadth of interest in urgent care, and opportunities to realize successful exits. And so began the onset of the **FIRST**



## PRIVATE EQUITY INVESTMENTS IN URGENT CARE



WAVE RUSH, a surge which has nevertheless been slowed, in part, by the aforementioned lack of supply of multi-site, regional providers, and quite possibly, a gap in price expectations driven by the extraordinary MedExpress deal metrics. Accordingly, the market has had to rely on the maturation of some of the early DE NOVO STARTUPS to meet demand. What's more, in light of these factors, we have seen an unusually high number of private equity groups eschew platform acquisitions in favor of getting into the DE NOVO business themselves, to ensure a timely market entry with lower capital outlays.

Today, **urgent care is firmly ensconced in the overlap between the first wave rush and de novo start-ups**, portending an elongated period of high demand that will be met by an equally elongated period new development. Moreover, with the pipeline of future acquisition candidates building rapidly, the sector might skip the post rush slowdown altogether.

## So how will the current pace of urgent care consolidation impact go-forward M&A opportunities?

If you are a prospective buyer, you can patiently wait for evolving platform sized acquisition candidates to come to market – and then slug it out with other investors in a bidding war.

Or, you can move “upstream” in the process by targeting the one to three location operations that are currently being overlooked to **create** the inventory that is so highly sought. With few private equity groups willing to pursue a small size - high volume consolidation play, the opportunity in urgent care is ripe for investors to swoop in below the radar and cobble together a platform relatively quickly – and with far less competition.

## From the sellers' side of the table, the timing question depends somewhat on your size, ambitions, and tolerance for risk.

If you're operating one or two centers, while your services may be urgent, your need to divest is not. Moreover, you may become more attractive – and hence more valuable – in the latter phases of consolidation when demand for follow-on acquisitions begins to rise.

If you're a prospective seller with plus/minus 10 locations, you have a more difficult choice to make. While we fully expect an elongated period of consolidation, we know that demand for multi-site operations **far** exceeds supply **today**. But we also know that there are many unknowns lurking about – mogwais that can suddenly turn into gremlins and wreak havoc in your strategic plans.

So perhaps it's worth noting that JP Morgan once said, “I made a fortune getting out early.”

Regardless, urgent care has all the makings of a vibrant consolidation play.

The race is on.

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

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