After a 2020 beset by the onset and spread of COVID, pent-up acquisition demand, the re-opening of our economy, and potential tax incentives, among other factors, led to a banner year for mergers and acquisitions in 2021 across many industries. According to PitchBook, a market research company that tracks private equity investment activity, “Middle-market private equity (PE) firms sustained the feverish pace of dealmaking activity set earlier this year: 2021’s three-quarter total has already surpassed that of the previous record year in both deal count and value.”

Such was the case in behavioral health care. Based upon proprietary data collected and analyzed by The Braff Group through the third quarter, we anticipate record breaking transaction volume for 2021. At the current pace, deal flow will be up a remarkable 21.9% over 2020.

As will be evident in our segment breakdowns below, the surge is almost entirely due to outsized growth in both substance use disorder and mental health transaction volume as buyers anticipate tremendous growth in demand, utilization, and funding due to the psychological toll attendant to COVID.

This has made behavioral health one of the most sought out sectors in all of health care mergers and acquisitions.

---

1 With fourth quarter 2021 transaction data still being compiled, to provide more timely analysis, the data presented in this report is drawn from M&A activity through the 3rd quarter of 2021 which has been annualized to estimate year-end results. While the total figures for 2021 will change, experience suggests that the trends will hold up.
HEAT MAPS

To illustrate just how dynamic the behavioral health space is, The Braff Group has developed "heat maps" specifically designed to compare the relative mergers and acquisitions activity level across various health care services and sectors.

Along the vertical axis is the total number of transactions completed over the past five years (including annualized results for 2021). Along the horizontal axis is the slope of the trend line over that period. For those of you who remember middle school math, the slope is the "m" in the formula, \( Y = m(x) + b \). The greater the "m" in the formula,

the sharper the slope – in this case, the sharper the rise in transaction volume over the five-year period. Taken together then, the highest and furthest to the right a sector is, the greater the acquisition interest in that service area.

As illustrated below, the outsized interest in behavioral health couldn’t be clearer. Not only has the sector accounted for the greatest number of deals over the past five years (including annualized results for 2021), it also has exhibited the greatest amount of annual growth in deal flow.
As discussed above, after slowing down a bit between 2019-2020, with the onset of COVID, M&A activity in substance use disorder roared back in 2021. Given the various niches comprising SUD, we created a heat map for the segment. From this, several key observations emerge. Perhaps first and foremost is the separation between high-end residential treatment programs and those that are more mid-range to value oriented. As is evident from the trend data, the high-end market is one of the few in meaningful negative territory, indicating that from an M&A perspective, interest has waned. Perhaps not surprisingly, however, the mid-range to value side of the market is growing nicely and approaching the deal volume in medication assisted treatment.

Another observation worth noting is the lack of growth in outpatient PHP/IOP/counseling M&A activity. With such an emphasis across the health care continuum on pushing services to the least costly settings, i.e., the home or community, we’ve been waiting for this niche to pop. With rising interest in mental health, particularly clinic settings, we may very well see outpatient services swept up in the enthusiasm for mental health consolidation, thereby driving increased demand and deal flow.
In the not-too-distant past, the M&A focus in mental health was psych hospitals and other facility-based programs. However, with the overall move toward community-based health care delivery combined with expectations of increased demand and utilization due to COVID, over the recent past, the emphasis has been on mental health group practices.

In projecting the M&A trajectory in a service area, one of the key leading indicators we watch is the number of private equity sponsored market-entry, platform investments in the space, as they portend a wave of follow-on deals over a typical investment cycle of 3-7 years. As we can see, 2020 and 2021 have seen a wave of such investments in mental health.

And on the heels of a successful IPO by LifeStance Health Group, which valued the company at an eye-popping $7.5 billion (a valuation of more than 13 times revenues), and the recent sale of Refresh Mental Health to Kelso Private Equity for an estimated $700M, or 17.5 times estimated EBITDA, we anticipate a sustained period of heightened investment in mental health by private equity sponsors.
While deal flow generally remains at elevated levels, we are seeing a plateauing of activity in both the residential and community-based services side of I/DD as well as autism services. This is not particularly surprising for non-autism as dealmaking in the space is comparatively mature. It’s a bit more noteworthy in autism, which is still in the nascent stages of consolidation.

So, what’s happening in the autism space?

As we first pointed out at the Autism Investor Summit in February 2020, a close examination of private equity activity in autism reveals that it has a lower proportion of follow-on to market-entry platform deals than in the other health care service markets we cover. Why? With private equity sponsors having to pay such extraordinarily high multiples to land a platform deal in autism (10 to 15 x earnings and more), they need to “arbitrage down” their total investment-to-earnings ratio. Market conditions, however, would not allow sponsors to acquire follow-on targets at 5-6 times earnings. As a result, instead of acquisitions, many have turned to start-ups instead. While the year will likely close out at approximately 30 follow-on transactions, when we consider that there are around 30 active autism platforms in the market, it’s clear that in autism, PE sponsors are not pursuing the traditional serial acquisition roll-up strategy. All of this means that demand is somewhat off the frenzied levels that characterized the period between 2017-2019.

The good news on the autism front is that despite the fall-off in demand, double-digit multiples can still be found for attractive acquisition candidates. But (and there’s always a but), they are situationally specific and hence substantially harder to find.

At Risk Youth Deal Trends

After steadily declining between 2012 and 2016, apart from 2019 we’ve seen elevated M&A activity in at risk youth over the past 5 years. Our sense is that this is due, in part, to consolidation models that recognize both the overlap of services provided in at risk youth, I/DD, and mental health programs, as well as the benefits of positioning as a comprehensive provider of behavioral health services to clients under the age of 21.

As a result, there is little room, if any, for valuation multiples to tick further upward. On the contrary, there is a far greater likelihood that valuations will fall. All it would take is a stumble from one or two high-flying consolidators, a few high profile news stories alleging some kind of fraud and abuse, or a collapse in the debt markets that are looking very much like they were before the economic collapse of 2008-2009. Now, that does not mean that one needs to sell now to maximize price. There are many providers out there with near-to-mid-term growth prospects that will more than offset any fall-off in multiples. But if you’re on the proverbial fence, you might want to heed Dickens’ alternate opening line.

If Charles Dickens was writing about behavioral health, the opening line to A Tale of Two Cities would read, “It was the best of times, it was the best-est of times.”

If you’re a seller.

If you’re a buyer, it’s a bit more complicated.

As a seller, it cannot be overstated enough that across broad swaths of the behavioral health market, COVID-inspired frenzied demand, access to capital, and sheer market momentum have pushed valuations to levels typically reserved for providers well over $100M in revenues.
OUTLOOK (cont.)

For buyers, the calculus is different. Quite often, their script relies, in part, on multiple expansion that is reserved for the largest players in the market. Players that got there in no small part through numerous lower priced acquisitions. But if valuations are already at size-premium levels, there may be substantially less room for further expansion. That’s why, as we detailed in the autism section above, we see many behavioral health consolidators rely, in part, on more start-ups than is typical. Because by doing so, they can “arbitrage down” their investment-to-earnings ratio and realize some of that lost multiple expansion. Additionally, many will focus heavily on deploying technology to reduce costs and increase earnings to build their exit value. Hence, the proliferation of tele-services, where possible, as a key part of their operating model.

Regardless, whether you are a buyer or a seller, the outlook for behavioral health is about as good as it gets.

THE BRAFF GROUP INDUSTRY EXPERTS

Steve Garbon
Managing Director
Behavioral Health
Pittsburgh
412-833-8690
sarbon@thebraffgroup.com

Ted Jordan
Managing Director
Behavioral Health
Atlanta
888-290-7080
tjordan@thebraffgroup.com

Nancy Weisling
Managing Director
Behavioral Health
Chicago
888-290-7237
nweisling@thebraffgroup.com

Deirdre Stewart
Director of Research
Pittsburgh
412-833-1355
dstewart@thebraffgroup.com

Kristin Mageras
Business Development 
& Marketing
Pittsburgh
412-283-0052
kmageras@thebraffgroup.com

Dexter Braff
President
Pittsburgh

Ted Jordan
Managing Director
Behavioral Health
Atlanta
888-290-7080
tjordan@thebraffgroup.com

Nancy Weisling
Managing Director
Behavioral Health
Chicago
888-290-7237
nweisling@thebraffgroup.com

Steve Garbon
Managing Director
Behavioral Health
Pittsburgh
412-833-8690
sarbon@thebraffgroup.com

Deirdre Stewart
Director of Research
Pittsburgh
412-833-1355
dstewart@thebraffgroup.com

Kristin Mageras
Business Development 
& Marketing
Pittsburgh
412-283-0052
kmageras@thebraffgroup.com

The Braff Group
1665 Washington Road, Suite 3 and 4
Pittsburgh, Pennsylvania 15228
888.922.5169
thebraffgroup.com

20 YEARS & COUNTING

The Braff Group is the leading mergers and acquisitions advisory firm specializing exclusively in health care services, including behavioral health, home health, home care, and hospice, home medical equipment, pharmacy services, staffing services, urgent care, digital health and ancillary services. The firm provides an array of sell-side only transaction advisory services including representation, debt and equity recapitalization, strategic planning, and valuation. Founded in 1998, The Braff Group has completed more than 370 transactions. According to Refinitiv, The Braff Group has repeatedly been ranked among the top 5 health care mergers & acquisitions advisory firms.

• Behavioral Health
• Home Health, Home Care, and Hospice
• Home Medical Equipment
• Health Care Staffing Services
• Pharmacy Services
• Urgent Care
• Digital Health
• Ancillary Services