

How Do You Value Your ASC For Sale?

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Presentation Overview

- I. Current Market Observations
- II. ASC Transaction Market
- III. Valuation Issues

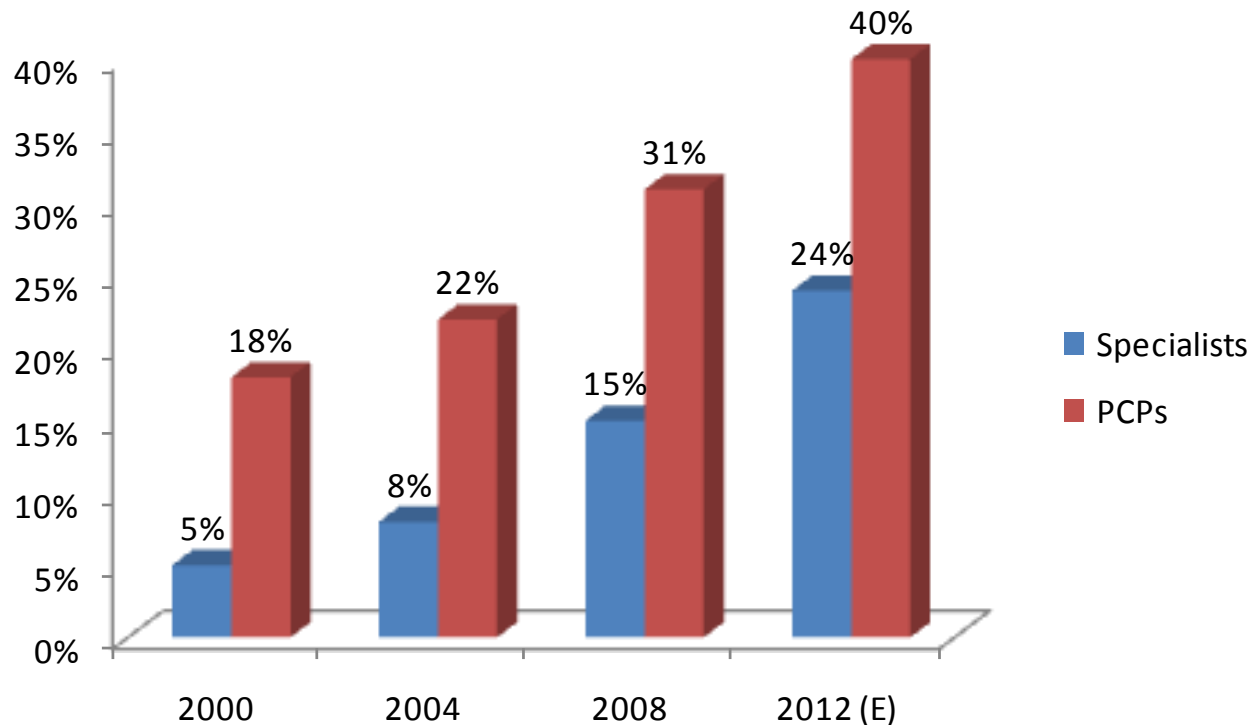
Current Market Analysis

- ∞ Observing a Maturation of the ASC Industry
- ∞ Economic Downturn / Sluggish Recovery Continues to Impact ASC Volumes
- ∞ Significant Managed Care & Medicare Reimbursement Pressure
- ∞ Uncertainty Regarding Healthcare Reform's Long-Term Impact on ASCs

Current Market Analysis

🌀 New Competition: Growth in Hospital Employment

Current and Projected Hospital Employment



Since 2000:

- *Employed PCPs has Doubled*
- *Employed Specialists has increased 5-fold*

Current Market Analysis

- What to Expect in a Mature Industry Environment?

**Attracting Physician Investment & Volume
will be the
Greatest Challenge**

**Increase in ASC
Mergers & Limited
ASC Failure**

**Increased Involvement
of Hospitals in
ASC Industry**

**Expected Return for ASC
Investors will be
Moderated**

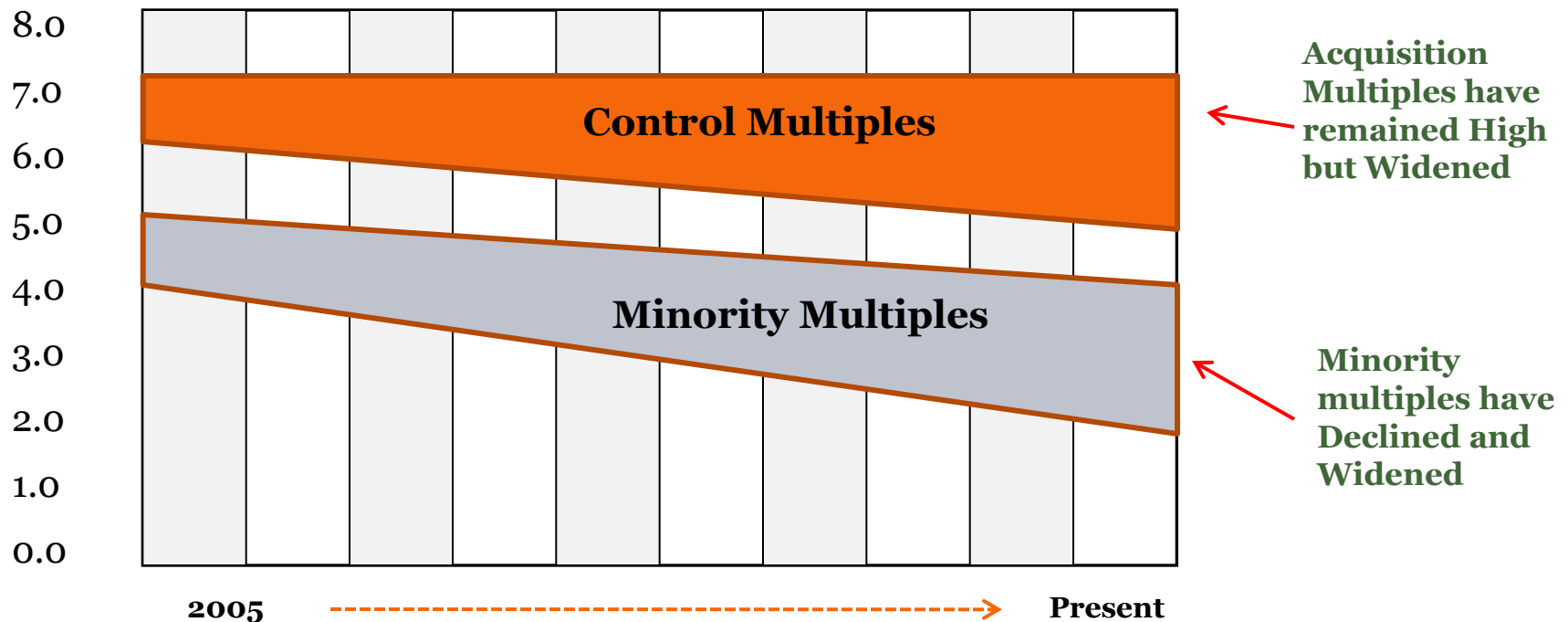
**Existing ASCs will need
to Focus Efforts on
Implementing
Efficiencies**

ASC Transaction Market

- ✎ ASC Acquisition Market – Who are the Buyers?
 - ASC Management Companies – Expanding Market Presence
 - Acute Care Hospitals – On the rise
 - Other ASCs – Consolidation Strategies
 - Physician Owned Hospitals – Niche Expansion Strategy

ASC Transaction Market

ASC Valuation Trends as Multiple of EBITDA



❖ *Key Takeaway - All ASCs are Not Created Equal with Respect to Valuation Multiples*

ASC Transaction Market

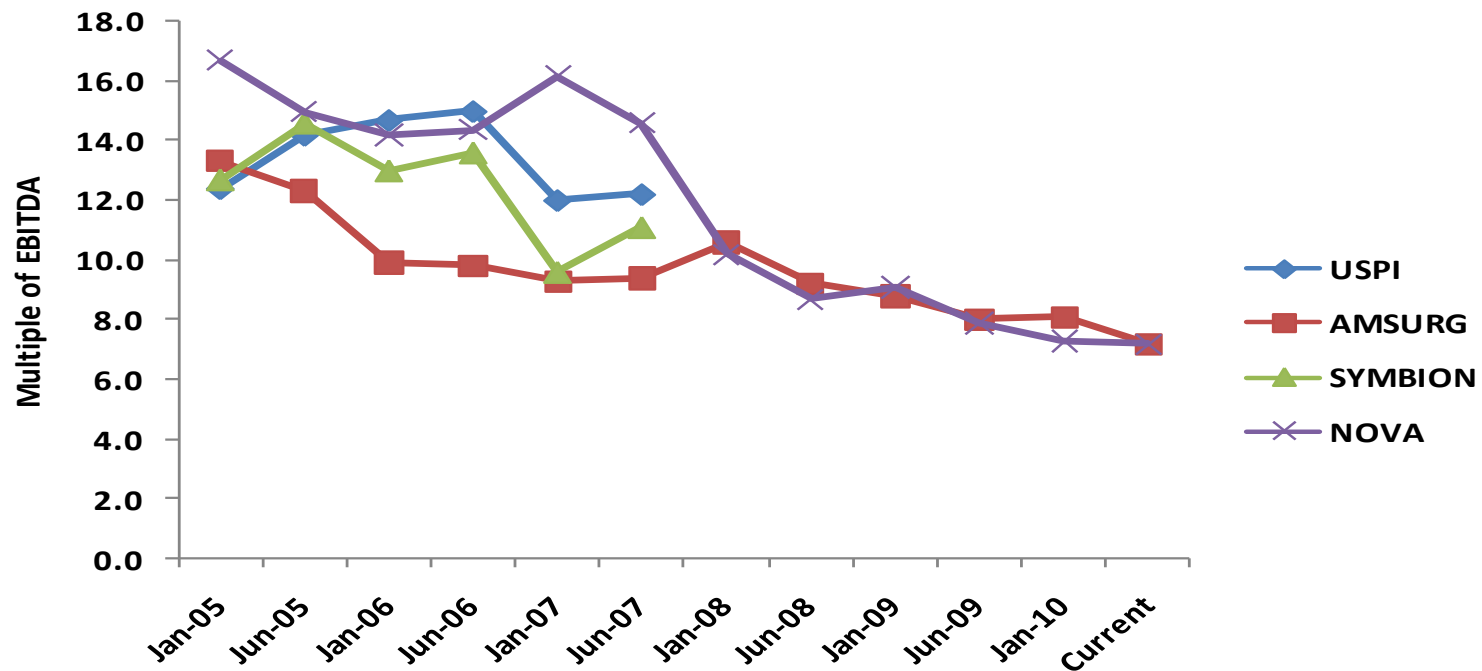
∞ Demand for Acquisitions is High

- Need for ASC Management Companies to Exhibit Growth
- Diminished Ability to do Pursue Growth through De Novo Development
- Market Consolidation Strategies are being Pursued Aggressively
- Hospitals are Joining Management Companies in the Buyers Market

ASC Transaction Market

⌘ However Buyers are Cautious

- Buyers are Keenly Aware of the Challenges facing ASCs
- Diminished Value from the Public Market



ASC Transaction Market

Acquisition Activity will
Accelerate in 2011 -
2012

Not Much DeNovo
Activity

**2011 ValueDriver
ASC Survey
Summary**

Looking for ASCs with a
Proven History of
Successful Performance

Higher Level of Due
Diligence Required

A Valuation Primer

- ∞ How Do You Value an ASC For Sale?

- ∞ Three Methods of Valuation:
 - Discounted Cash Flow Analysis (Income Approach)
 - Market Multiple Analysis (Market Approach)
 - Asset Analysis (Cost Approach)

- ∞ Two Primary Drivers of ASC Value:
 - Future Cash Flow (Distributions)
 - Volatility or Risk related to Future Cash Flow
 - Revenue and Expense Analysis

Risk Factors and Value

- ∞ The value of minority shares is lower than control value
- ∞ Risk factors usually decrease equity share values
- ∞ Measure “Risk” and “Value” the right way
- ∞ Maximize the value of shares by managing out Risk

Risk Factors and Value

∞ Market Characteristics

- Health system competition
- Freestanding surgery center competition
- Potential for new centers
- Market demographic growth
- Percentage of physicians with no ASC Investment
- Existence of certificate of need (“CON”)
- Managed care barriers
- Facility costs or availability

Risk Factors and Value

∞ Payor Profile

- Revenue contraction by payor
- Percentage of out of network business
- Commercial reimbursement relative to Medicare
- Pending legislation impacting reimbursement

Risk Factors and Value

∞ Physician Utilization

- Specialty mix
- Age dispersion
- Growth history
- Ownership by utilizers in competing centers
- Volume concentration by specialty
- Revenue concentration by specialty

Risk Factors and Value

∞ Physician Ownership

- Percent of revenue produced by owners
- Number of physician owners
- Number of non-physician owners
- Revenue dispersion among owners
- Revenue dispersion among non-owners
- Physician ownership growth and retention

Risk Factors and Value

∞ Facility Attributes

- Location in relation to acute care hospital
- Age and condition of facility
- Facility location sustainability
- Capital equipment obsolescence

Risk Factors and Value

∞ Efficiency

- Relative staff efficiency
- Relative supply cost efficiency
- Existence of labor unions
- Geographic cost index

Definitions

∞ Control Interest

- Generally, greater than 50% interest in the ASC
- The right to manage the facility
- The right to make decisions on many issues
- Not subject to repurchase provisions

∞ Minority Interest

- Generally, less than 50% interest in the ASC
- No management authority
- No decision making authority
- Subject to repurchase provisions

Standards of Value...

∞ Control or Majority Equity Level Value:

- Typical for Hospital or Management Company Buy-in
- Higher Valuation (think 5.0X – 7.0X)
- Premium value related to rights and privileges of majority owner (management control, distributing level & timing, capital structure decisions, admission of new investors, etc.)
- Buyer establishes new operating agreement with terms desired by the buyer

∞ Minority Equity Level Value:

- Typical for Physician Buy-in
- Lower valuation, typically <4.5x EBITDA
- Discounted value due to lack of specific control, rights and privileges that are available to the majority owner

Determining Physician Buy-in Price

- ⌘ How is physician buy-in calculated?
 - Pre-determined valuation multiple (stipulated in partnership operating agreement)
 - Independent Fair Market Value Opinion
- ⌘ A pre-determined multiple can be dangerous!
 - Pre-determined multiple often based on trailing financial performance
 - Future growth or risk factors must be considered
 - In today's ASC environment, future performance will not likely mirror past performance

Victims of Their Own Success

- ∞ Successful Past Performance = Expensive Buy-in
 - Valuations based solely on past performance may overstate ASC value
 - Self-fulfilling prophecy – Inability to attract new investment will result in deteriorating performance
 - ASC Partnerships have life cycles which mirror the physician investors
- ∞ What's the Solution?
 - Buy-in value must be forward looking
 - Buy-in value must consider all risks inherent in that ASC
 - Valuation must consider the actual terms related to the security interest

Summary

- ∞ Increased Hospital involvement in the ASC Industry
- ∞ Industry Participants should Expect Reduced Reimbursement
- ∞ Completely Independent ASCs will have Greater Risk Exposure
- ∞ As a Low Cost Provider, ASCs will Have a Place at the Table

QUESTIONS

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