



# FMVantage Point™

HealthCare Appraisers' Industry Insight

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### *Monitoring Industry Activity from Quarter 4 of 2020*

As part of our ongoing monitoring of developments in the healthcare industry, HealthCare Appraisers follows reports from publicly-traded health systems, physician services providers, ambulatory surgical center management companies, and other healthcare service providers. This document summarizes important valuation-related takeaways from recent earnings calls and conference presentations, as well as supporting quotes<sup>1</sup> from publicly-traded operators. The 4Q 2020 earnings calls illustrated that while providers are certainly still focused on the ongoing disruption from COVID-19, both operators and investors have started to return their focus to their long-term operational and strategic objectives as well.



### **PROVIDERS SEE \$60 BILLION OF SURGICAL CASES MOVING TO OUTPATIENT IN COMING YEARS**

The shift of inpatient to outpatient surgical services continues its momentum with ASC operators anticipating strong growth in more complex musculoskeletal and cardiology cases in the coming years. The elimination of the inpatient only list, as well as increasing installed base of robotic surgical equipment in ASCs is spurring this growth and giving physicians more autonomy over the setting in which they perform cases. Consistent with the commentary from public operators this quarter, HAI's 2021 ASC Valuation Survey highlights the focus on orthopedics cases by operators in the space, with orthopedics

representing the most attractive specialty for respondents. In addition, Tenet's acquisition of a large ASC portfolio from SurgCenter Development was focused primarily on driving growth



<sup>1</sup> All quotes have been adapted from transcripts provided by S&P Capital IQ.



## PROVIDERS SEE \$60 BILLION OF SURGICAL CASES MOVING TO OUTPATIENT IN COMING YEARS (CONTINUED)

in this area. HAI's recent work in the ASC space suggests that large operators can benefit from significant rate lift when acquiring standalone ASCs and renegotiating total joint reimbursement with private payors. This has helped

support higher multiples in the space, as proforma EBITDA increases substantially compared to historical EBITDA achieved by the standalone operators, thereby lowering the effective multiple paid by acquirers. More broadly,

health system operators continue to focus on expansion of their ambulatory footprint, as evidenced by HCA having approximately 10-12 outpatient facilities per hospital, and Tenet Healthcare Corporation having 8-9 healthcare facilities per hospital.<sup>2</sup>

### WHAT INDUSTRY LEADERS ARE SAYING ABOUT PROVIDERS SEE \$60 BILLION OF SURGICAL CASES MOVING TO OUTPATIENT IN COMING YEARS

#### ➤ ERIC EVANS – CEO OF SURGERY PARTNERS, INC.

*"We estimate that there is over \$60 billion of cases that will shift from inpatient to outpatient over the next several years, and we estimate that over 60% of those procedures are in musculoskeletal and cardiology."*

#### ➤ SAMUEL HAZEN – CEO OF HCA HEALTHCARE, INC.

*"We are investing in our outpatient facility development. A reasonable point of reference is roughly every 1 of HCA's hospitals has 10 to 12 outpatient facilities attached to it. That's not exactly symmetrical from one institution to the other. But when you look at the total outpatient facility network capabilities we have, it's roughly 2,200 to 2,500 outpatient facilities on top of 185 hospitals. So it's roughly 10x to 12x the number of hospitals. We will continue to build on that because we believe that our patients deserve a convenient offering of facilities in our network. That doesn't require, fortunately, as much capital as the inpatient components of our spending."*

<sup>2</sup> Based on Tenet Healthcare Corporations 12/31/20 form 10-K filing.



## VALUE-BASED ARRANGEMENTS GAINING TRACTION IN DIALYSIS

The largest providers of dialysis are in discussions with payors and other providers about moving upstream into the chronic kidney disease (CKD) population and helping people before they require renal dialysis. Spurred by new governmental payment models and a focus on lowering cost of care, dialysis providers are exploring partnerships and service offerings whereby they provide treatment to patients with CKD. In addition, new value-based payment models from Medicare Advantage plans and other payors involve risk taking on the part of the dialysis providers, as well as others involved in providing a bundle of care to patients with end stage renal disease (ESRD). Under certain of these arrangements, dialysis providers partner with other healthcare providers to provide care for patients with ESRD,

and receive a fixed payment. In many cases, the ability to profitably provide these services is determined by the non-dialysis cost of delivering care to the patient, as the cost to provide dialysis is relatively fixed. This means better coordination of care outside dialysis clinics and ensuring adherence to the treatment plans prescribed by nephrologists and other physicians. We have seen an increase in value-based care models in our work in the dialysis space, with innovative providers developing high-touch care delivery models for patients with CKD, as well as working to provide manageable home-based treatment options for individuals requiring dialysis. Going forward,

there will be increased focus on preventing people with CKD from developing ESRD and lowering the percent with ESRD from “crashing into” ESRD treatment, which involves more costly hospital-based care and limits treatment options for patients. New government payment models have also increased efforts by providers to shift more dialysis treatments out of centers and into the home through higher utilization of home hemodialysis or peritoneal dialysis.



### WHAT INDUSTRY LEADERS ARE SAYING ABOUT VALUE-BASED ARRANGEMENTS GAINING TRACTION IN DIALYSIS

#### JAVIER RODRIGUEZ – CEO OF DAVITA, INC.

*“Yes, we are discussing with payors moving upstream into the CKD population. And everybody is new at this, meaning the plans are, and we’re working through what that means and what the implications are of going upstream. And then, of course, there’s some regulatory restrictions to deal with. But at the end of the day, we’re all trying to manage the patient as soon as possible to make sure that the transition is as smooth as possible.”*

#### JAVIER RODRIGUEZ – CEO OF DAVITA, INC.

*“Within these Medicare Advantage models, I would think about us making a margin on the component of the cost that is not dialysis. So think of us as a medical manager, a value-based care deliverer on the two-thirds of that \$90,000 that doesn’t go to dialysis. The dialysis cost is relatively fixed. And so I’d apply the low to mid-single digit margin number to that \$60,000.”*

#### ROBERT MAURICE POWELL – CEO OF FRESENIUS MEDICAL CARE MANAGEMENT AG

*“Our Humana contract is a perfect example of how we are already moving forward in this regard. With chronic kidney disease and transplantation, we are expanding beyond dialysis to the treatment of CKD and also looking to play an active role in the area of kidney transplantation. And with renal care innovations, we aim to be at the forefront of any industry disruption by developing our own renal care innovations as well as investing in startups and early-stage companies in our space.”*



## POSITIVE OUTLOOK FOR HOME HEALTH AND HOSPICE PROVIDERS



The COVID-19 pandemic has affected how providers practice medicine and patient preferences for care in profound ways, and many of these changes are expected to be beneficial to home health providers going forward. Recent government data show that home health was one of the only sectors of healthcare that experienced increases in spending in 2020, and operators believe these shifts in referral patterns are here to stay. There have been several large transactions in this space recently, including HCA's acquisition of a majority stake in Brookdale Senior Living's home health and

hospice business for \$400 million<sup>3</sup> in February of 2021. In addition, Bristol Hospice, a large private equity sponsored hospice organization is anticipated to sell for more than \$1 billion in the near future.<sup>4</sup> Similar large hospice platforms have transacted at mid-teens EBITDA multiples last year, while smaller, single market-focused agencies typically transact in the mid-single digit range depending on the margins and growth outlook. Hospice providers are benefitting from many industry trends including an aging population, new payment models, new coverage by Medicare Advantage, and the ability to expand

into palliative care. Similarly, home health providers are benefitting from an increased focus on moving care out of institutions into lower cost, more convenient settings. The large providers continue to develop more acute services for patients including SNF-at-home, and are increasingly receiving interest from health system operators regarding joint venture opportunities. These drivers of growth, in conjunction with disruption caused by the new home health payment model (PDGM<sup>5</sup>), are anticipated to contribute to consolidation of the industry in coming years, and support strong industry growth rates.

### WHAT INDUSTRY LEADERS ARE SAYING ABOUT POSITIVE OUTLOOK FOR HOME HEALTH AND HOSPICE PROVIDERS

#### ➤ CHRIS GERARD – COO OF AMEDISYS, INC.

*"We're seeing a decline in the length of stay across all of those segments. So for us, what we feel like is going to happen throughout 2021, and we're already seeing that so far in January and in February, is as the vaccine is getting more widely distributed, and COVID is starting to decline, we're starting to see these death rates start to decline as well. We expect that to continue through this year and then start to revert back to a normal length of stay, and you can see that illustrated in our slide deck in terms of where we see it going."*

#### ➤ KEITH MYERS – CEO OF LHC GROUP, INC.

*"Another data point I'd like to highlight is from the recent data on healthcare spending published by the U.S. Bureau of Economic Analysis. For the second straight year, it has shown the greater share of annual healthcare spending is going to home health. With the exception of prescription drug spending, home healthcare was the only category that was up in 2020. Home health was up by 2% with hospital care, physician and clinical services and nursing home care all down low- to mid-single digits. What this demonstrates is that the pandemic has resulted in a shift in referral patterns, with more patients, families, physicians and discharge planners choosing home health over more costly and potentially higher-risk concrete care settings."*

<sup>3</sup> Investment analysts estimated the transaction took place at a 20x adjusted EBITDA valuation multiple; <https://seniorhousingnews.com/2021/02/24/brookdale-to-sell-80-stake-in-home-health-hospice-segment-for-400m/>; accessed April 6, 2021

<sup>4</sup> <https://hospicenews.com/2021/01/19/webster-equity-partners-plans-sale-of-bristol-hospice/>; Accessed April 6, 2021

<sup>5</sup> Patient Driven Groupings Model



**EDITOR**

**DANIEL I. LEVIN, CFA, ASA**

**DLEVIN@HCFMV.COM | 303.566.3177**

**Daniel I. Levin, CFA, ASA** is a manager in the Firm's Denver office where he specializes in a wide variety of healthcare business and compensation valuation assignments. Mr. Levin's business valuation experience includes valuing hospitals, health systems, dialysis clinics, imaging centers, ambulatory surgery centers, physical therapy clinics, urgent care clinics and physician practices in connection with a wide range of transactions. Prior to joining HealthCare Appraisers in 2016, Mr. Levin was an Equity Research Associate performing industry research and investment analysis on publicly-traded healthcare companies. Mr. Levin graduated summa cum laude from Florida Atlantic University in 2013, and has been a CFA charterholder since September 2017.



**ASSISTANT EDITOR**

**NICHOLAS J. JANIGA, ASA**

**NJANIGA@HCFMV.COM | 303.566.3173**

**Nicholas J. Janiga, ASA** is a partner in HealthCare Appraisers' Denver office, where he leads the firm's business valuation and capital equipment valuation service lines. He has been providing his clients analysis and consultation in business valuation, litigation support, intellectual property and healthcare provider compensation relationships since 2006. His experience includes working with healthcare organizations, attorneys, administrators, providers, developers, consultants, investment bankers, and private equity groups in connection with transactions in the healthcare industry. Many of the transactions he analyzes involve Stark, Anti-Kickback, IRC 501(c)(3), and/or other regulatory implications, which requires analysis of fair market value and the determination of commercial reasonableness. He also has experience providing expert testimony in deposition and trial settings.



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