

Key Trends in Valuing ASCs



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Learning Objectives

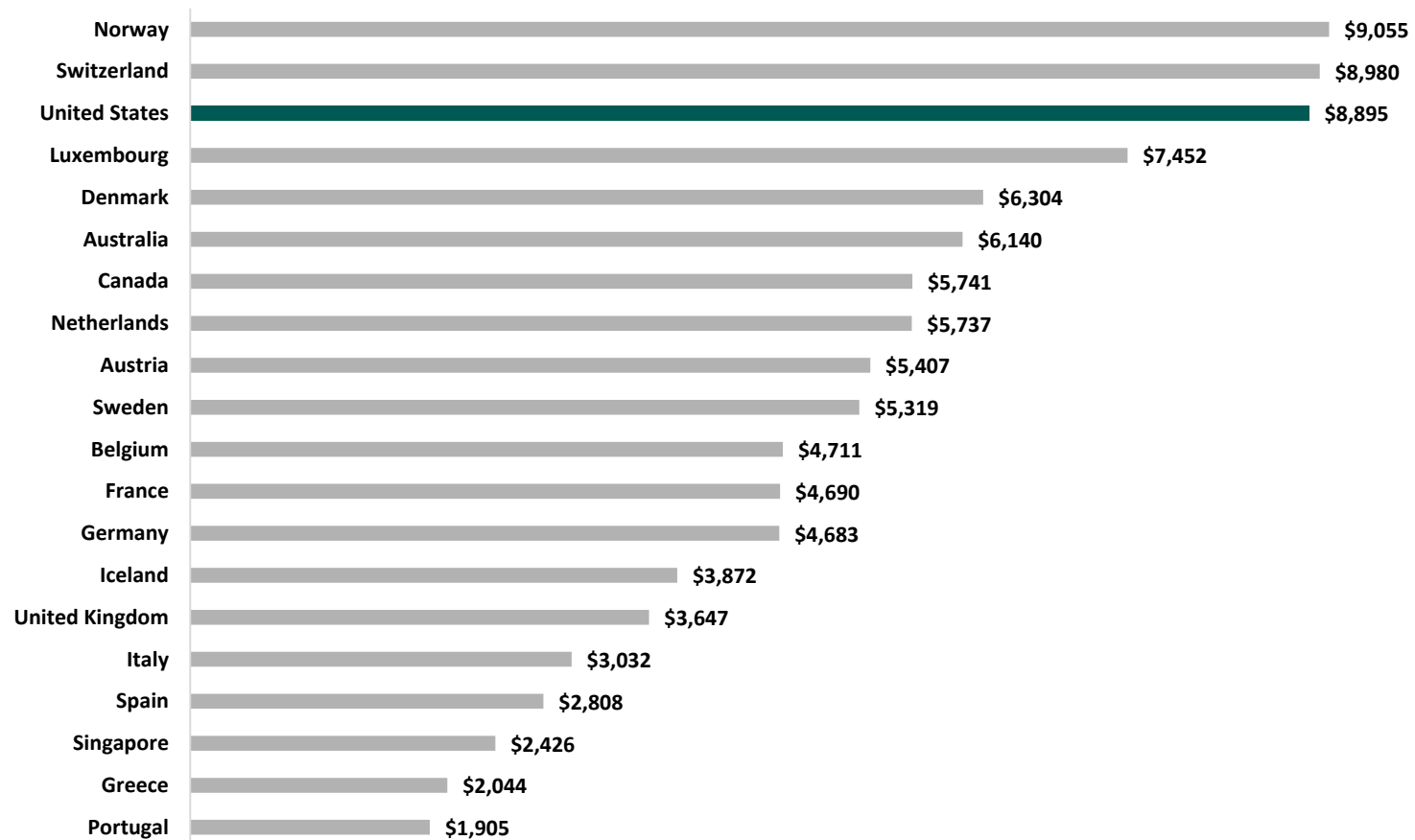
- I. Analyze the current dynamics and future expectations of the ASC industry.
- II. Describe the ASC transaction market and historical acquisition activity.
- III. Discuss the purpose and application of an ASC valuation.

I. Analyze the current dynamics and future expectations of the ASC industry.

US Healthcare Spending

- US healthcare spending per capita higher than our “peers”

2012 Health Expenditures Per Capita

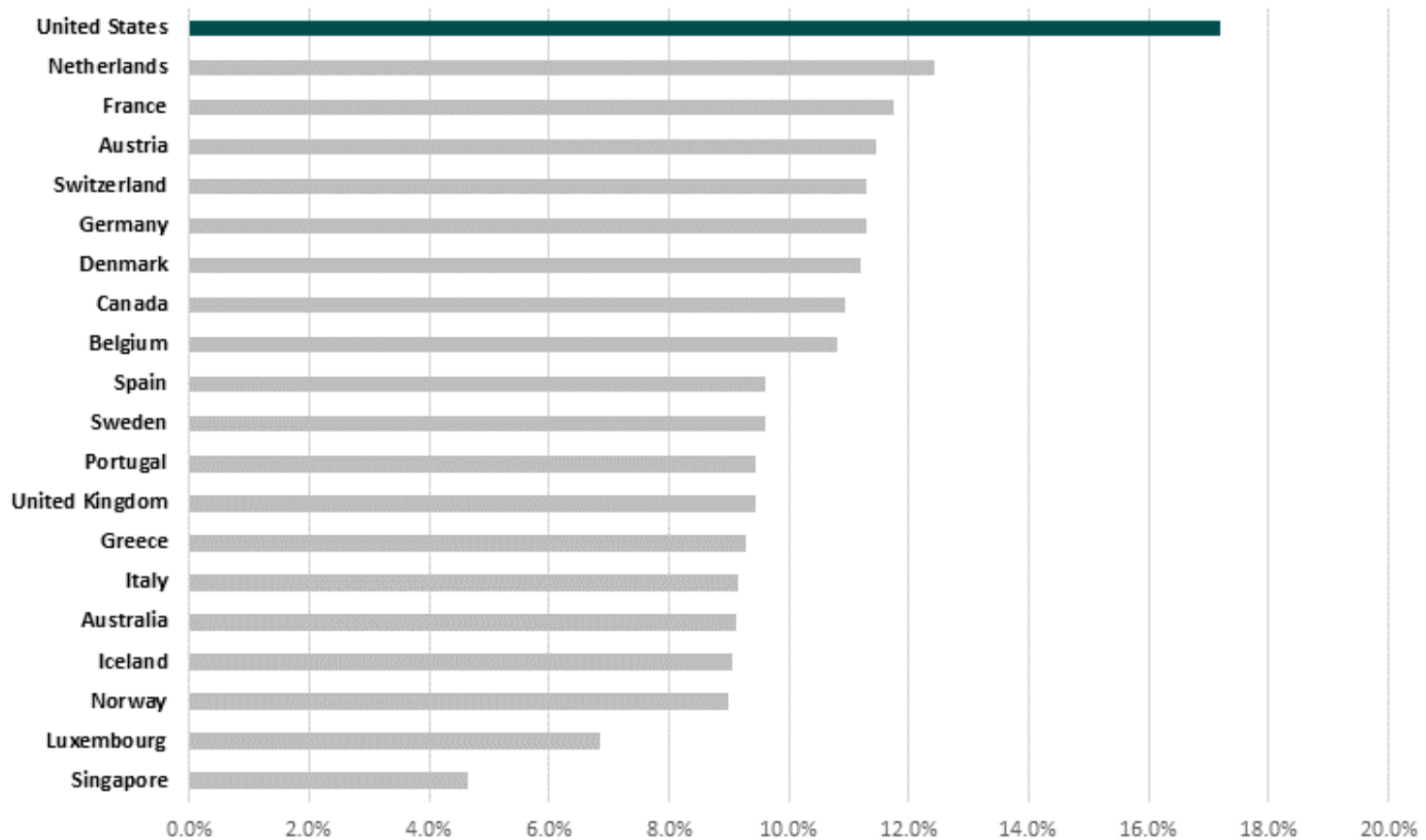


Source: World Health Organization National Health Account database

US Healthcare Spending

- US healthcare spending as % of GDP higher than our “peers”

2012 Health Expenditures as a % of GDP

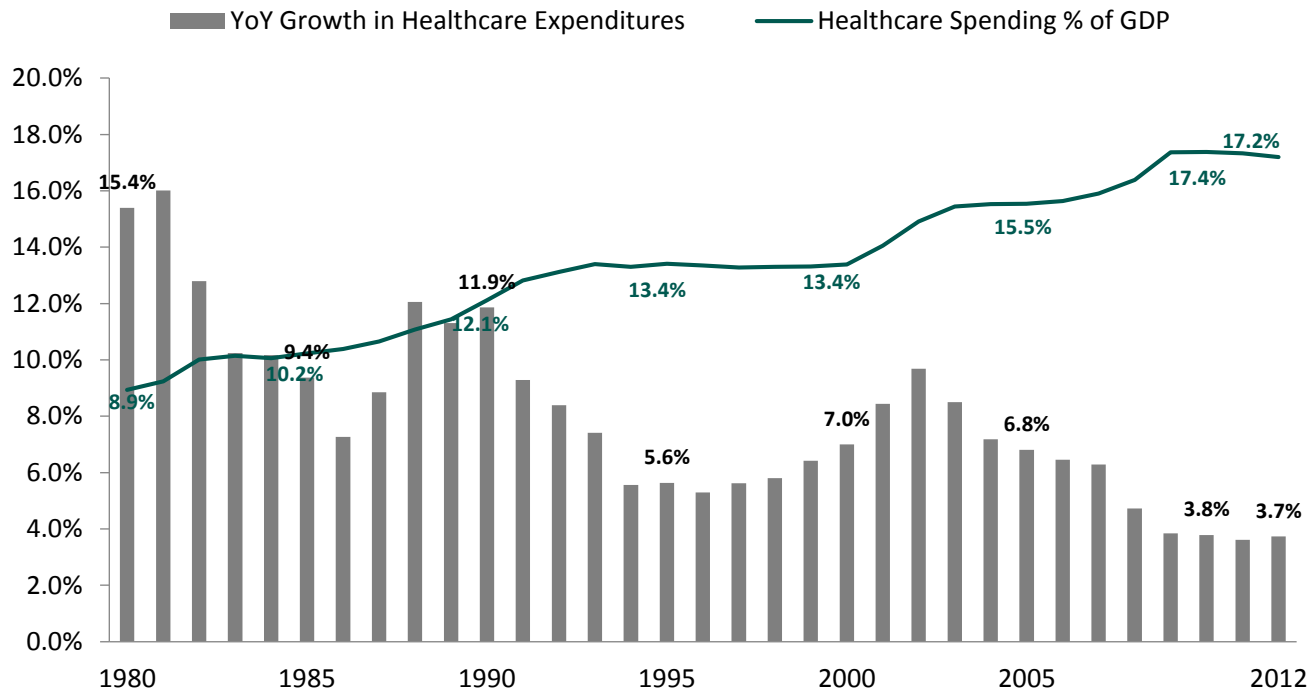


Source: World Health Organization National Health Account database

US Healthcare Spending

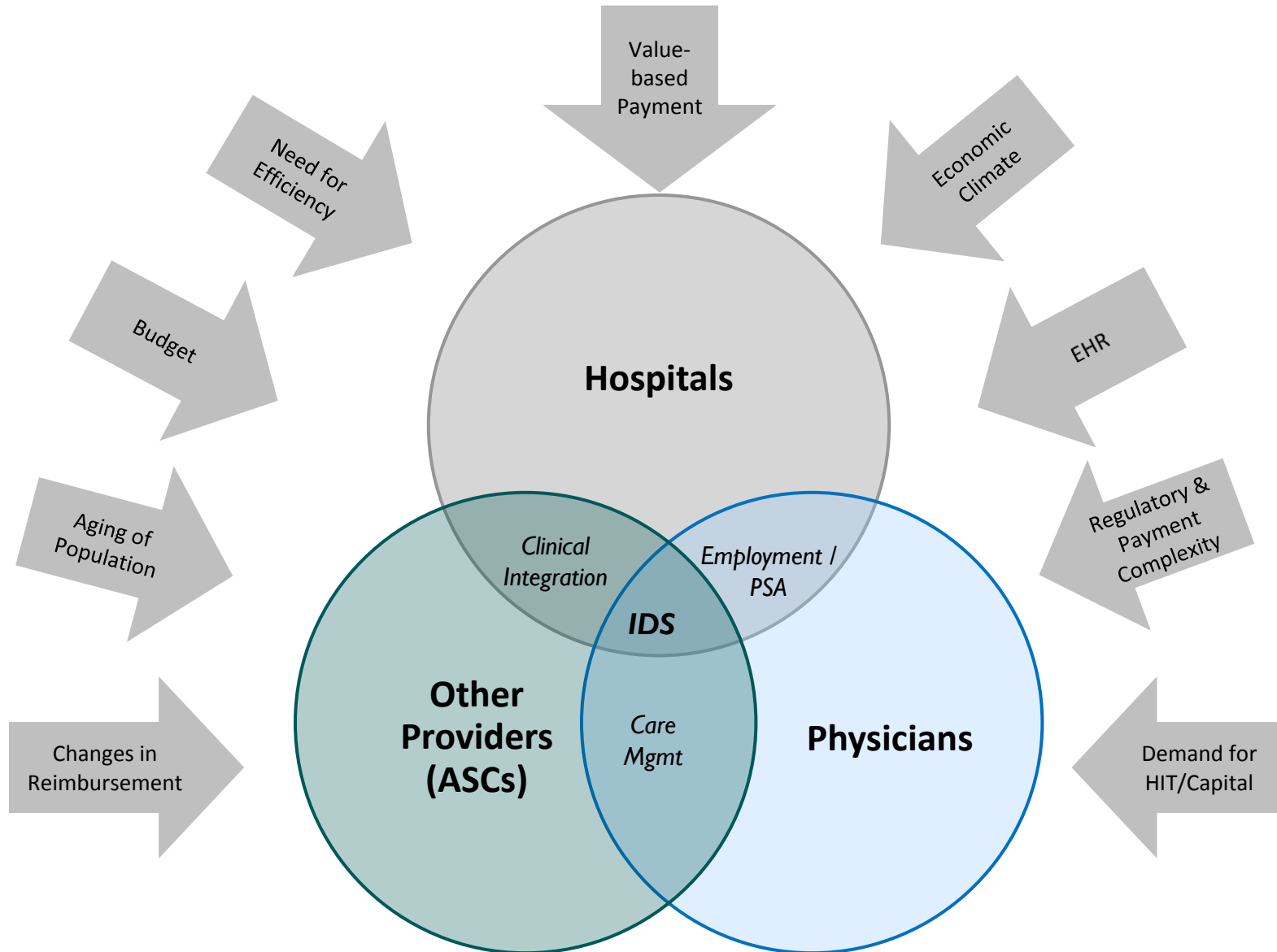
- US healthcare spending high as compared to GDP
 - ❖ Healthcare is currently 17.2% of GDP (projected to be approximately 17.4% for 2013)
 - ❖ Healthcare spending in the U.S. grew 3.7% in 2012, which is slightly greater than the increase in 2010
 - ❖ By 2020, national health spending is expected to reach \$4.5 trillion and comprise 19.2% of GDP

Healthcare Spending as a % of GDP and YoY Growth



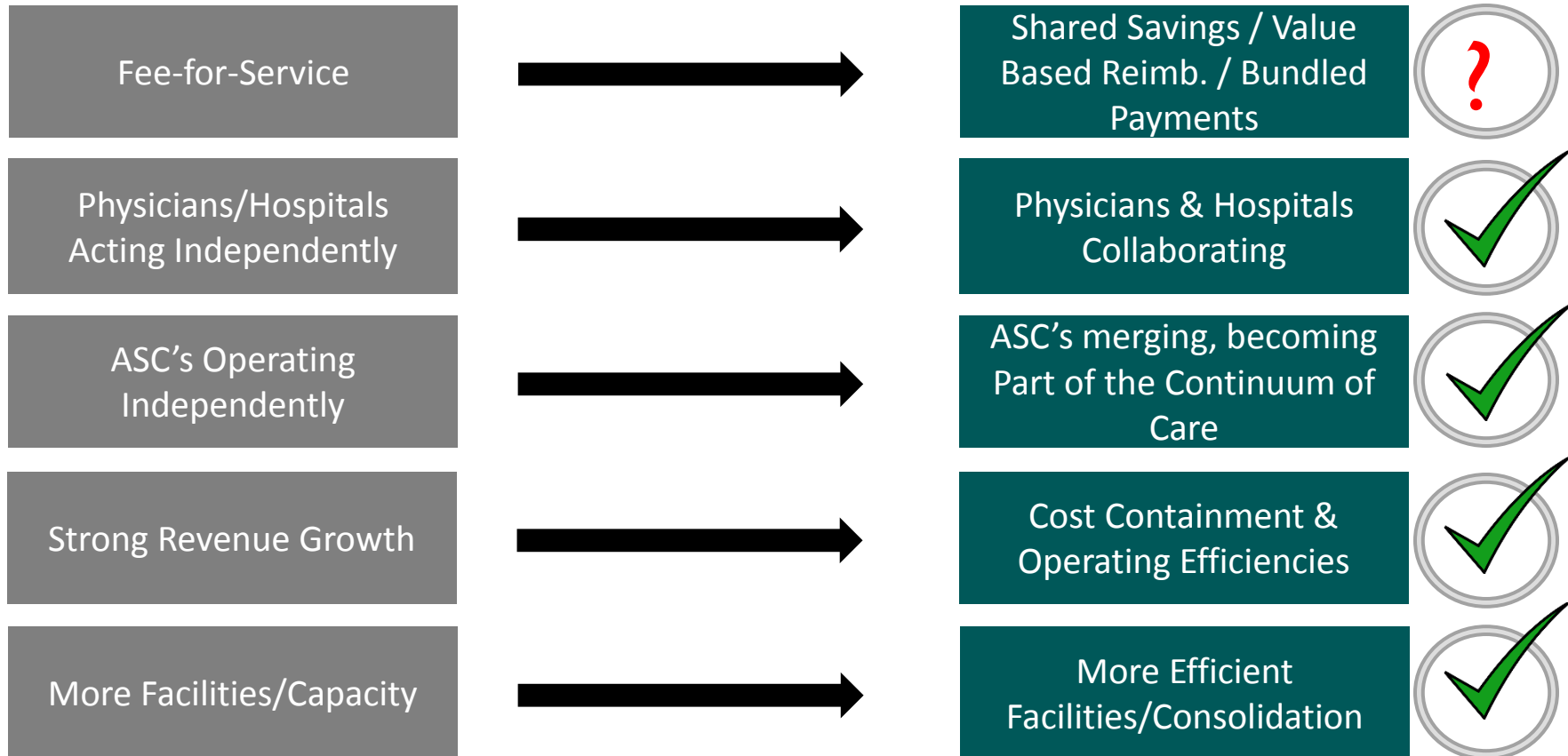
Source: World Health Organization National Health Account database

US Drivers of Greater Integration



Current Market Observations

- Healthcare is Headed towards “Accountable Care”
- Where do procedure-driven providers fit, are they positioned well?



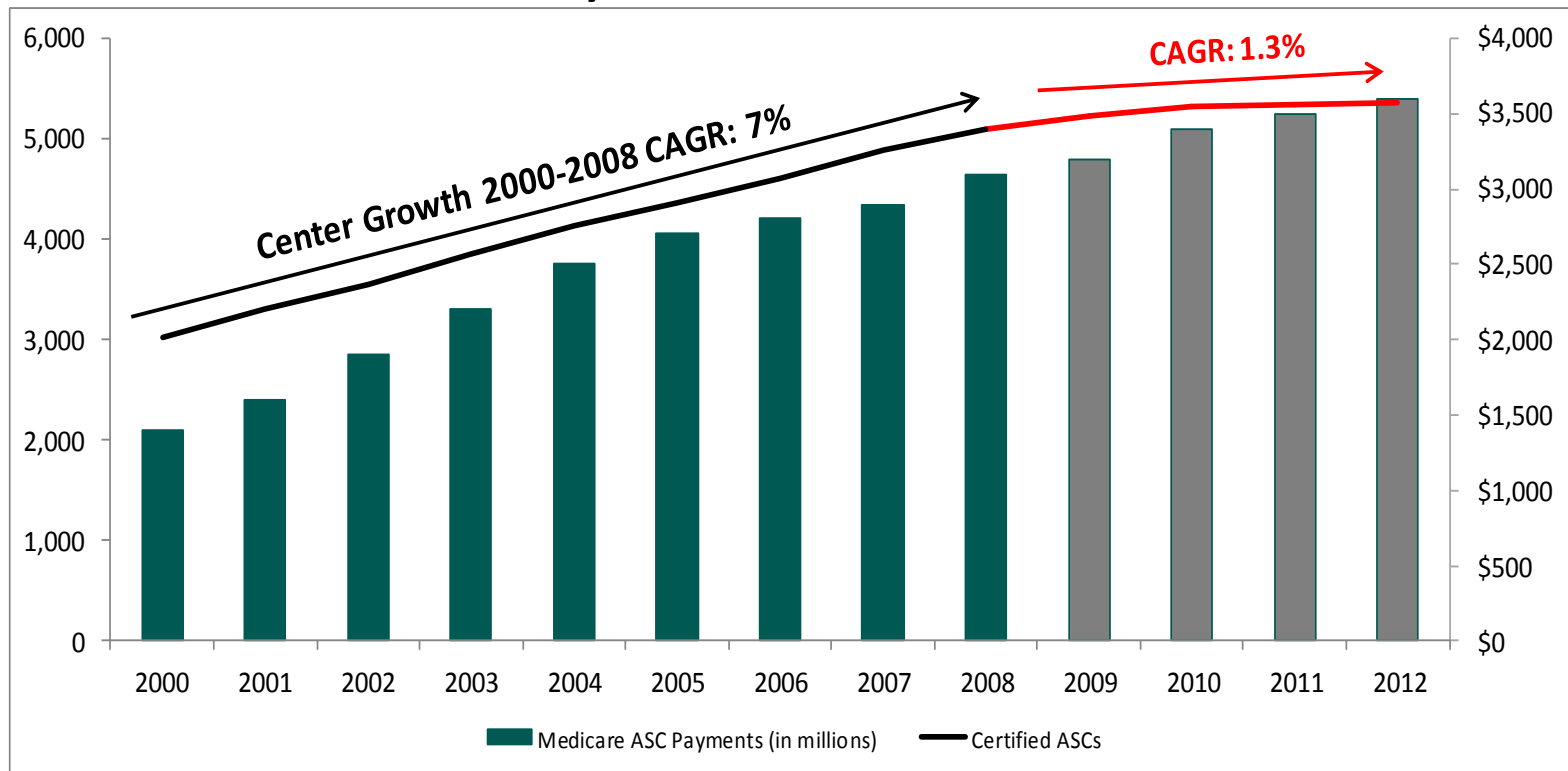
How are ASC's Positioned?

- ASC Industry is positioned well
 - Have been/will be the low cost provider
 - Deliver care efficiently/safely with high patient/physician satisfaction
- ASC's are in-demand
- Healthcare systems pursuing network development
 - Is integration into larger system a good thing for cost containment?
 - Physician alignment still important
- Independent ASC's may not have leverage with changing reimbursement models

ASC Industry

- Slowdown in government ASC payments and new ASC construction point to a mature market

Medicare ASC Payments and Certified ASCs, 2000-2012

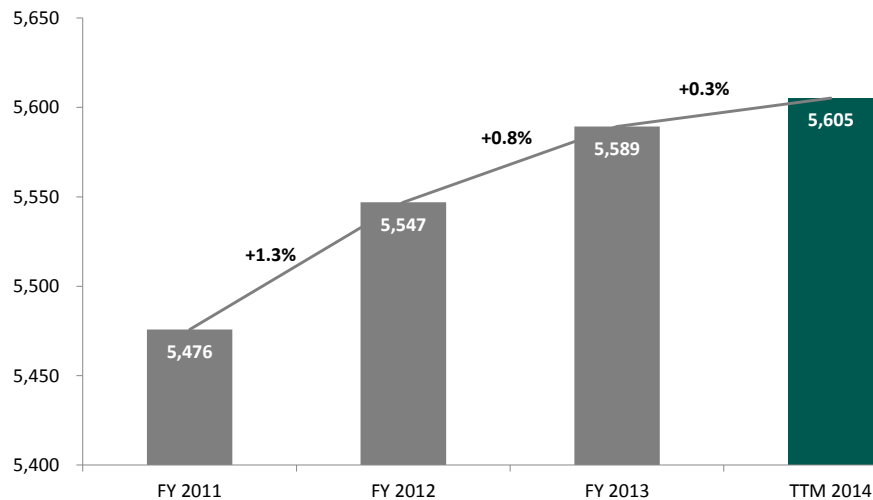


Source: The Medicare Payment Advisory Commission

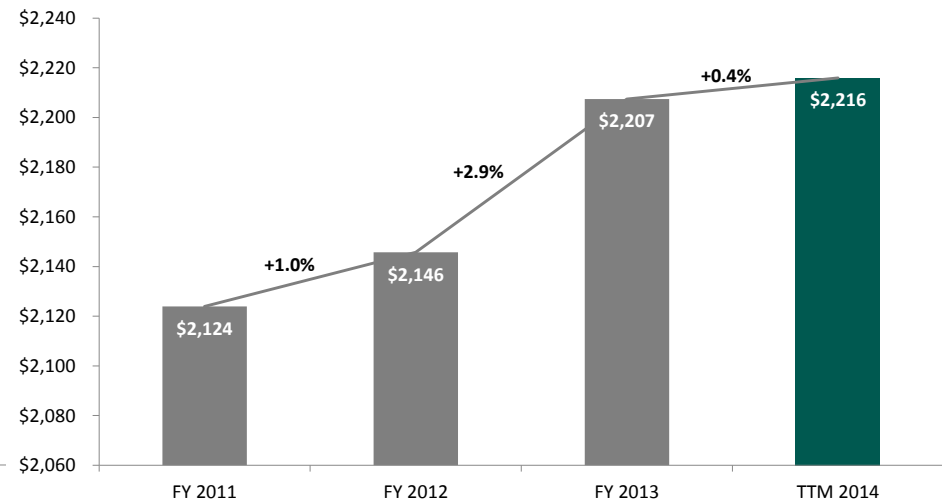
ASC Industry

- YOY Volume growth slowing down with some pricing growth

Average Surgical Case Volume Growth



Net Revenue per Surgical Case Growth



Source: VMG Health Proprietary Analysis

Mature Industry

➤ All Signs Point to a Mature ASC Industry:

Growth in ASC Development has Levelled Off

Same Center Growth has Flat-Lined

ASC Supply Exceeds Physician Demand in Most Markets

Significant Capacity at Many ASCs

Growth in Observed ASC Mergers & Consolidation

Initial Stages of Consolidation among ASC Management Companies

➤ What to Expect in a Mature Industry:

Attracting Physician Investment & Volume will be the Greatest Challenge

Increase in ASC Mergers & Limited ASC Failure

Increased Involvement of Hospitals in ASC Industry

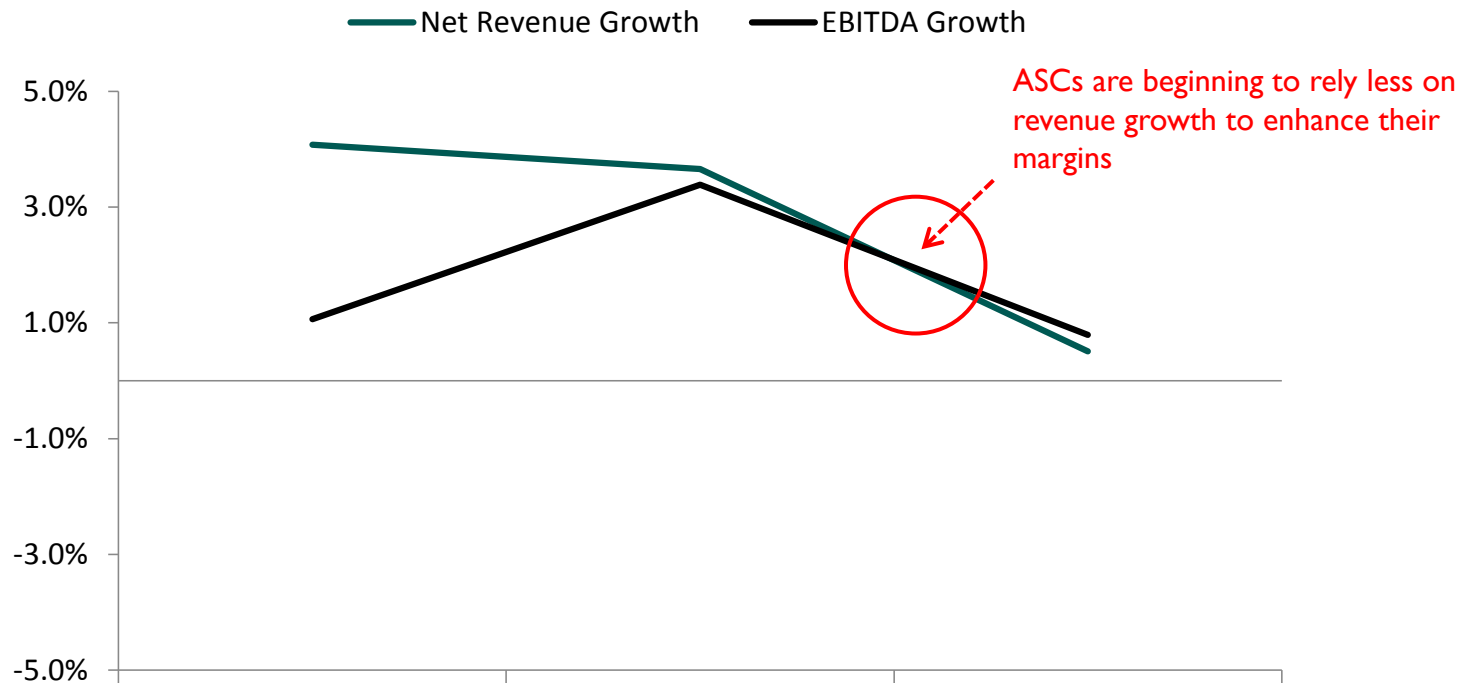
Expected Return for ASC Investors will be Moderated

Existing ASCs will need to Focus Efforts on Implementing Efficiencies

Benchmark Analysis – ASC

- Less reliance on revenue growth

Same ASC Revenue Growth (YoY)



	2012	2013	TTM 2014
Net Revenue Growth	4.1%	3.7%	0.5%
EBITDA Growth	1.1%	3.4%	0.8%

ASC Industry

- ASC industry is mature, de novo centers still developed
- Cost containment will be primary driver of profitability
- New CPT's/technology will help volume growth
- Uncertainty regarding healthcare reform's long-term impact
- Physician realignment:
 - Supply of physicians will likely no meet demand
 - Hospitals have increased physician employment to build integrated networks
- Continued managed care and Medicare reimbursement pressure, move to value-based purchasing

II. Describe the ASC transaction market and historical acquisition activity.

ASC Buyers – Control Transactions

➤ Who are the buyers, what are the motives?

Category	Hospitals / Health Systems	Management Companies / Operators	Surgery Centers	Physician Owned Hospitals
Type	Strategic	Financial / Strategic	Strategic	Strategic
Geography	In Market	In/Out of Market	In Market	In Market
Notes	<ul style="list-style-type: none"> Driven by: Physician alignment, OP network expansion, ORs maxed out, etc. Reimbursement leverage vs HOPD – but do you want it? 	<ul style="list-style-type: none"> Growth by acquisition JV's w/ Hospitals /Systems Competing models / abilities 	<ul style="list-style-type: none"> Typically Cashless Merger Target usually a struggling or at capacity 	<ul style="list-style-type: none"> Can address POH capacity constraints Difficult due to limited physician equity

ASC Buyers – Control Transactions

➤ Management Companies / Operators – League Table

Name	Center Count	Name	Center Count	Name	Center Count
AmSurg	246	Physicians Endoscopy	28	Foundation Surgery Affiliates	11
United Surgical Partners International	202	ASD Management	25	Cirrus Health	10
Surgical Care Affiliates*	185	Regent Surgical Health	25	Medical Consulting Group	10
HCA	124	Covenant Surgical Partners	19	Facility Development and Management, LLC	9
SurgCenter Development	121	Surgery Center Partners	17	Ortmann Healthcare Consultants	9
Symbion	52	Meridian Surgical Partners	17	Murphy Healthcare	8
Surgery Partners	50	Surgical Management Professionals	17	Sovereign Healthcare	7
Tenet	44	Surgem	15	Interventional Management Services	6
Ambulatory Surgical Centers of America	36	Blue Chip Surgical Center Partners	15	Global Surgical Partners	6
Community Health Systems	34	Constitution Surgery Partners	14	Surgical Synergies	5
Nueterra	30	Practice Partners In Healthcare	14	Arise Healthcare	3
					TOTAL 1,428

Equity models vary: 0%, <50%, 51%

Management Agreement terms vary, typically between 4-7%

Post-deal operational changes vary greatly

Not unusual to have >5 offers for control deal

*Note: Surgical Care Affiliates total includes approximately twenty surgery centers included in the Health Inventures acquisition, announced June 2013.

*Tenet/USPI joint venture will have ownership interests in 244 ASCs. The transaction is expected to close by the third quarter of 2015.

Sources: Company websites, press releases, and SEC filings

ASC Buyers – Control Transactions

➤ Consolidating Management Companies

Tenet announces acquisition of USPI – JV ownership in 244 Centers (March 2015)

AmSurg acquisition of Sheridan – Diversifies (July 2014)

Surgery Partners announces acquisition of Symbion – (June 2014)

Graymark acquisition of Foundation Healthcare – 21 Centers (July 2013)

SCA acquisition of Health Inventures – 20 Centers (June 2013)

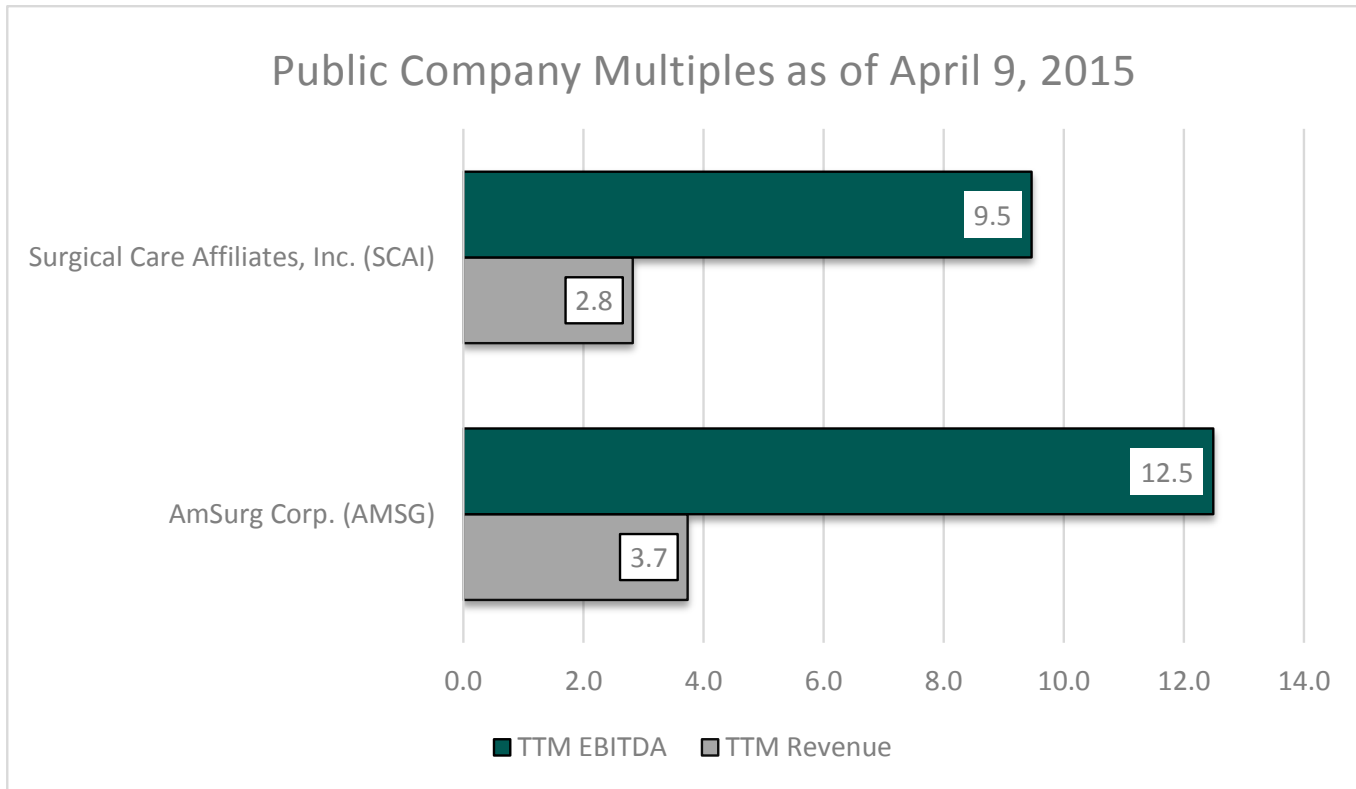
AmSurg Corp. acquisition of National Surgical Care – 18 Centers (Sept 2011)

USPI acquisition of Titan Health Corporation – 14 Centers (Sept 2011)

Surgery Partners acquisition of NOVA – 37 Centers (January 2011)

ASC Buyers – Control Transactions

- Public ASC companies trading above 9x EBITDA



Source: CapitalIQ data as of April 9, 2015

***Not necessarily FMV for single location ASCs**

ASC Buyers – Control Transactions

- Demand for Acquisitions is High
 - ❖ Need for ASC management companies to exhibit growth
 - ❖ On average, same center performance provides low single digit growth
 - ❖ Look for continued consolidation of operators
 - ❖ Hospitals are in the buyers market, but strategy driven
- Buyers and strategies are different, and make a difference
- Lots of action in ASC market = good place to be in era of HC reform

III. Discuss the purpose and application of an ASC valuation.

Why is a Valuation Needed

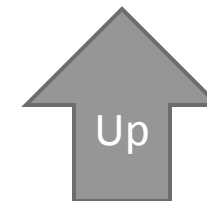
- Fair Market Value (“FMV”) – the only premise of value to meet the Anti-Kickback Statute and Private Inurement Regulations
- Both for-profit and not-for-profit health care providers that accept payments from government programs (i.e., Medicare) must ensure that exchanges between them and other providers are at FMV
- Definition:
 - ❖ The price, expressed in terms of cash equivalents, at which a property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms length in an open and unrestricted market, when neither is under compulsion to buy nor to sell, and when both have reasonable knowledge of the relevant facts.

How Value is Measured – Fair Market Value

Valuation Methodologies – All Three

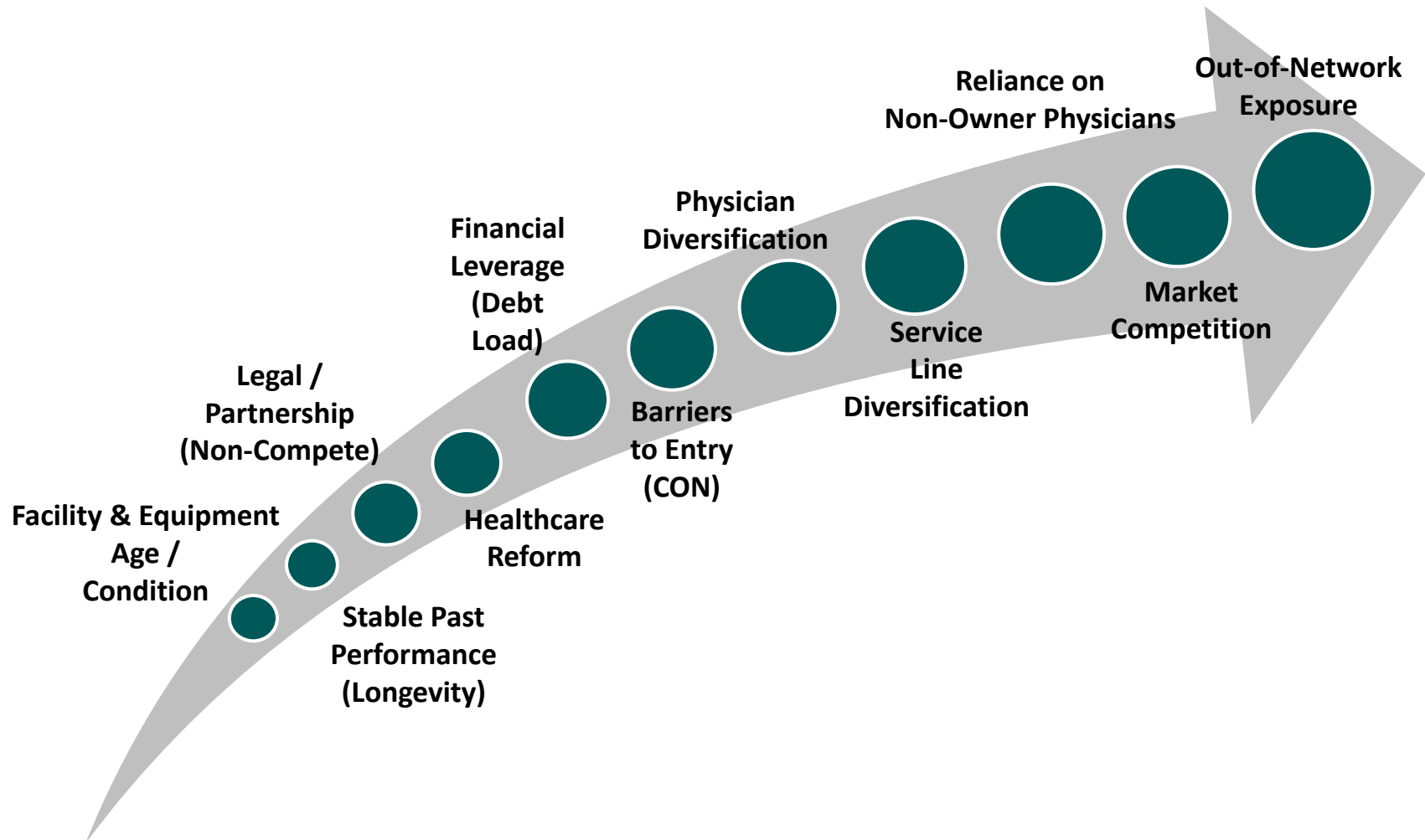
- Cost Approach
 - ❖ Provides a Floor for Value – Tangible Assets + Identifiable Intangibles
- Income Approach
 - ❖ Discounted Cash Flow Value – Measure Future Benefits of Ownership
- Market Approach
 - ❖ What are Transaction Values of Comparable Companies

Valuation Trend – LTM



Without detailed understanding of ASC benchmarks and specific ASC fact patterns, there is risk of FMV appraisals mis-valuing the transaction...

Risk Factors Affecting FMV



Control vs Minority Transactions

➤ Control Transactions

- ❖ Supply and demand: many buyers + fixed supply = higher pricing
- ❖ More buyers = almost all terms are negotiable
- ❖ Smarter sellers: highest price isn't winning deal, if strategic considerations
- ❖ Result: Seller's market

➤ Minority Transactions (Physician Perspective)

- ❖ Supply and demand: Many sellers (ASC's) + limited supply (physicians) = stable / reduced pricing trends.
- ❖ Alternative investment risk: share price vs market alternatives

How Value is Measured – Control

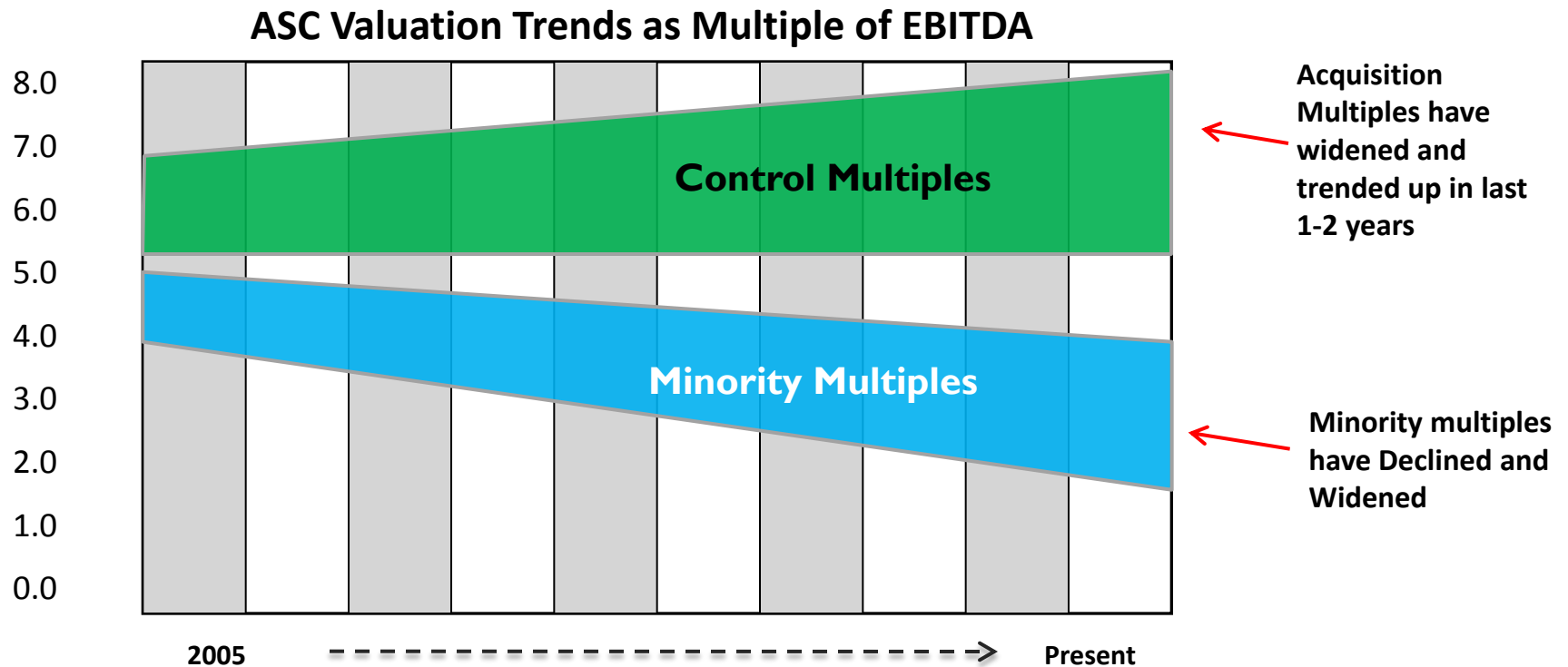
➤ Market Multiples

- ❖ Multiple of earnings applied to EBITDA (earnings before interest, taxes, depreciation, and amortization)
- ❖ Devil is in the details – which EBITDA?
 - ❖ Historical EBITDA? Normalized Historical EBITDA? Proforma EBITDA?
- ❖ Hard to understand multiples without deal knowledge: see Devil above...
- ❖ Regulatory considerations – Fair Market Value??

How Value is Measured – Minority

- Market Multiples approach, but buy/sell driven
 - ❖ Minority EBITDA multiples can range from 40% to 60% less than control level
 - ❖ EBITDA multiple, formulaic approach/stated in operating agreement
 - ❖ Return on Investment based approach – cash on cash return
 - ❖ Fair Market Value??
 - ❖ Control / minority share transactions happen at different valuations... need to document the reasons!

Observed ASC Valuation Trends



Source: VMG Health Proprietary Analysis

Conclusions & Expectations

➤ Control Transactions

- ❖ Sellers market – many buyers competing for deals
- ❖ Strategy is winning too – price isn't the whole story

➤ Minority Transactions

- ❖ Buyers market – many opportunities for physicians
- ❖ Documenting FMV increasingly important

➤ Value Drivers

- ❖ Cost containment
- ❖ New procedures?
- ❖ Affiliation, sale, re-syndication, etc...

Questions?

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