HEALTHCARE

2Q & 3Q | 2018

Healthcare Transaction Volume Remains High, But Have M&A Valuation Multiples Peaked?

The change in control of the U.S. House of Representatives from Republican to Democrat, coupled with a slightly stronger Republican hold on the Senate, makes it unlikely any material healthcare legislation will be passed during the next two years. However, maintaining the status quo legislatively will not slow the forces disrupting how, and by whom, healthcare is delivered in the U.S.

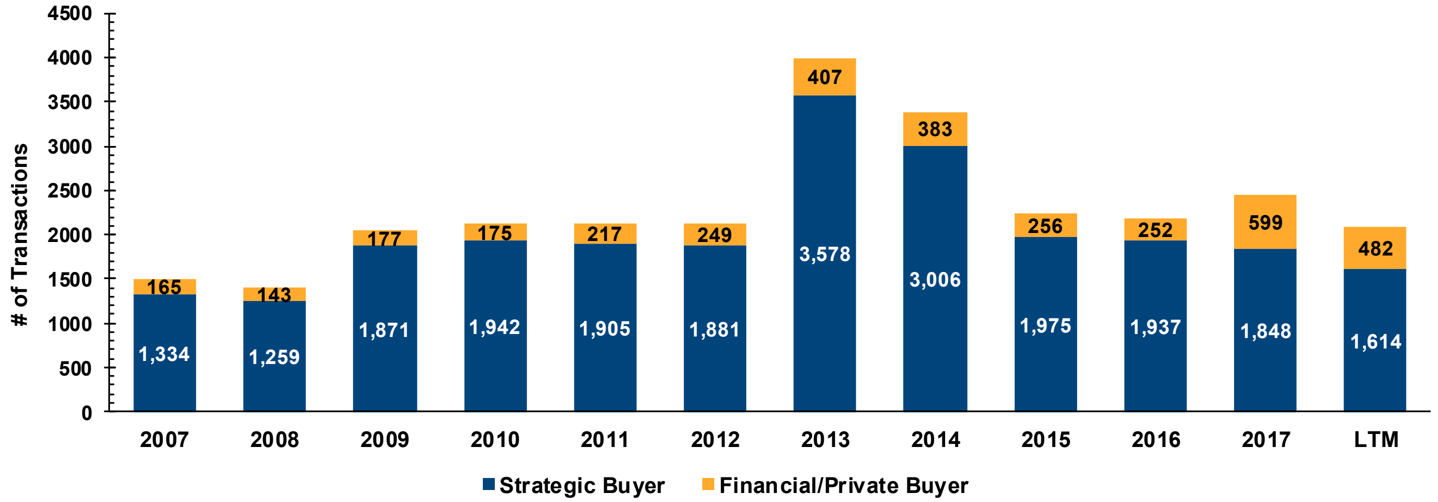
Employers continue to shift a greater share of the cost of healthcare to employees, while the demographic tide of baby boomers turning 70 threatens to swamp already strained state and federal budgets for Medicaid and Medicare. Along with a general trend toward consumerism, these pressures have payers, providers, and patients alike seeking creative ways to lower the cost of healthcare. In addition, healthcare remains highly fragmented and localized, and is ripe for technological advances. Together, these forces create an attractive market for new players—many from outside traditional healthcare sectors—to enter healthcare via mergers and acquisitions.

Large health systems and other providers participating in at-risk contracts are motivated to more fully integrate healthcare across the spectrum to assure control over the total cost of care. This will lead to increased M&A activity by strategic buyers. Financial buyers seeking strong return on investment opportunities, such as private equity groups and venture capital funds, will further accelerate the increase in M&A activity.

In summary, we expect M&A activity within the healthcare sector to remain robust, as established platform companies seek add-on acquisitions; however, as discussed on page four, we believe valuation multiples have likely peaked for most sub-sectors, albeit at an historically high level.

Healthcare Transactions by Year

(Strategic Buyers Include Private Equity Owned Companies)



Source: CapIQ. Includes M&A, Private Placement, and Public Offering

Notable Recently Closed Healthcare Transactions

Date: 7/26/2018 (Closed) | **Overview / Strategic Rationale:** | **Healthcare Services**

Target: HCR ManorCare

Acquirer: ProMedica

Key Metrics:

Implied Enterprise Value ($M)	$5,749
EV/LTM EBITDA	16.8x
EV/LTM Revenue	1.5x

ProMedica Health System, Inc. completed the acquisition of HCR ManorCare, Inc. from Quality Care Properties, Inc. (NYSE:QCP) and others on July 26, 2018, for $300 million and the assumption of $5.449 billion in debt. With HCR ManorCare being the nation's second largest post-acute and long-term care provider, this transaction makes ProMedica the 15th largest nonprofit health system in the nation.

- *The underlying real estate was acquired by a joint venture of ProMedica (20%) and Welltower (80%), a real estate investment trust (REIT) which, like ProMedica and HCR ManorCare, is also headquartered in Toledo, Ohio. Beyond the immediate benefit to the Toledo community of retaining several hundred jobs, the parties believe they can use their combined resources in the local market to incubate new models of care that can be rolled out to other communities, likely in partnership with other health systems.*

Date: 10/11/2018 (Closed) | **Overview / Strategic Rationale:** | **Healthcare Services**

Target: Envision Healthcare

Acquirer: KKR

Key Metrics:

Implied Enterprise Value ($M)	$10,615
EV/LTM EBITDA	9.9x
EV/LTM Revenue	1.3x

A fund managed by KKR & Co. L.P. (NYSE:KKR) completed the acquisition of Envision Healthcare Corporation (NYSE:EVHC) for $5.7 billion plus $4.9 billion in assumed debt on October 11, 2018.

- *KKR acquired Envision's ambulance operations last year, perhaps giving them an advantage over Carlysle, and several other competitors, for the deal. Envision's physician services division would appear to be a nice complement to KKR's acquisition of WebMD in July 2017. Less clear is whether KKR will retain Envision's surgery center operations as part of a larger strategy to amass a broad spectrum of ambulatory care capabilities, or if they will seek to spin off that division. Filings with the SEC indicate Envision had received multiple offers for the surgery center operations alone as they considered strategic alternatives leading to the sale to KKR.*

Date: 5/15 to 9/19/2018 (Closed) | **Overview / Strategic Rationale:** | **Healthcare Services**

Targets:
- Walter Barkey, MD, PLLC
- North Oakland Dermatology
- Duneland Dermatology
- Northwest Dermatology
- Skin, Vein & Cosmetic Surgery
- Spencer Dermatology Assoc.

Acquirer: Pinnacle Dermatology

Pinnacle Dermatology, headquartered in Joliet, Illinois, and backed by Chicago Pacific Founders, completed six acquisitions during the 2nd and 3rd quarters of 2018. Together with greenfield development of additional locations, Pinnacle now operates 24 dermatology offices in Illinois, Indiana, and Michigan.

- *Pinnacle is one of several PE-backed platform companies competing for acquisitions of dermatology practices. Given its comparatively low exposure to Medicaid and Medicare reimbursement, and ample opportunities for ancillary cash income, dermatology is an attractive specialty for investors.*
- *Chicago Pacific Founders (CPF) is an investment advisor that manages private funds, focusing exclusively on healthcare services. CPF's leadership team is made up of former healthcare CEOs and senior executives.*

Date: 10/1/2018 (Closed) | **Overview / Strategic Rationale:** | **Healthcare Technology**

Target: greatcall

Acquirer: Best Buy

Key Metrics:

Implied Enterprise Value ($M)	$800
EV/LTM Revenue	2.7x

Best Buy Co., Inc. (NYSE:BBY) completed the acquisition of GreatCall, Inc. from GTCR, LLC for $800 million on October 1, 2018. GreatCall provides mobile health and safety solutions for older adults and their family caregivers, including GreatCall Splash, a personal emergency response system, and Jitterbug5, a medical-alert cell phone that provides access to health and safety experts.

- *BestBuy's acquisition of GreatCall continues the trend of non-traditional players making direct investments in healthcare through an M&A transaction (e.g. Amazon's acquisition of PillBox). The addition of new, consumer-focused, technologically adept, and financially strong buyers from outside healthcare directly threatens established providers and accelerates the mandate for finding more cost-effective methods of care.*

Recently Announced and Closed Transactions *(select transactions, not intended to be all-inclusive)*

Date	Acquirer	Target	Price ($MM)	EBITDA Multiple	Revenue Multiple
HEALTHCARE SERVICES					
11/16/2018	LifePoint Health, Inc.	RCCH HealthCare Partners	$ 5,742	8.5x	0.9x
9/10/2018	1Life Healthcare, Inc.	The Carlyle Group L.P.	130		
9/7/2018	Valley Healthcare Group, LLC	Great Elm Capital Group, Inc.	66		1.4x
4/9/2018	Phillips, DiPisa & Associates Inc.	AMN Healthcare Services, Inc.	37		1.6x
9/4/2018	Four Clinic Physical Therapy Practice in Minnesota	U.S. Physical Therapy, Inc.	8		2.6x
HEALTHCARE TECHNOLOGY & CONSULTING					
8/27/2018	Cotiviti Holdings, Inc.	Verscend Technologies, Inc.	$ 5,119	17.1x	6.7x
4/2/2018	ABILITY Network Inc.	Inovalon Holdings, Inc.	1,200	16.6x	8.6x
5/8/2018	Intermedix Corporation	R1 RCM Inc.	460	9.6x	2.4x
8/13/2018	Juniper Pharmaceuticals, Inc.	Catalent Pharma Solutions, Inc.	143	29.2x	2.2x
4/30/2018	MedFORCE Technologies, Inc.	Ideagen plc	9		1.9x
HOME HEALTH & HOSPICE					
4/10/2018	Great Lakes Home Health Services, Inc.	National Home Health Care Corp.			
5/15/2018	Jordan Health Services, Inc.	Kelso & Company; Blue Wolf Capital Partners LLC			
5/1/2018	Abode Healthcare, Inc.	Tailwind Capital Group, LLC			
10/22/2018	Living at Home SeniorCare, LLC	AME, LLC	0	4.0x	0.5x
6/1/2018	Always Home Homecare Services Ltd.	Nova Leap Health Corp.	2	4.9x	0.9x
MEDICAL DIAGNOSTICS					
7/31/2018	Abaxis, Inc.	Zoetis Inc.	$ 1,995	39.4x	7.5x
6/22/2018	Analogic Corporation	Altaris Capital Partners, LLC	1,087	20.4x	2.0x
4/20/2018	Cogentix Medical, Inc.	LM US Parent, Inc.	238	94.3x	3.7x
10/1/2018	Focal Therapeutics, Inc.	Hologic, Inc.	125		7.8x
7/31/2018	Faxitron Bioptics, LLC	Hologic, Inc.	85		3.1x
MEDICAL EQUIPMENT					
6/6/2018	Advanced Sterilization Products Services Inc.	Fortive Corporation	$ 2,700		3.5x
8/13/2018	UHS Holdco, Inc.	Federal Street Acquisition Corp.	1,580	10.8x	2.9x
11/9/2018	K2M Group Holdings, Inc.	Stryker Corporation	1,406		4.9x
10/22/2018	Invuity, Inc.	Stryker Corporation	224		4.9x
7/1/2018	CoolSystems, Inc.	Halyard Health, Inc. (nka:Avanos Medical, Inc.)	65		1.9x

Sources: EdgePoint Proprietary Database, Company Filings, CapIQ, News Releases

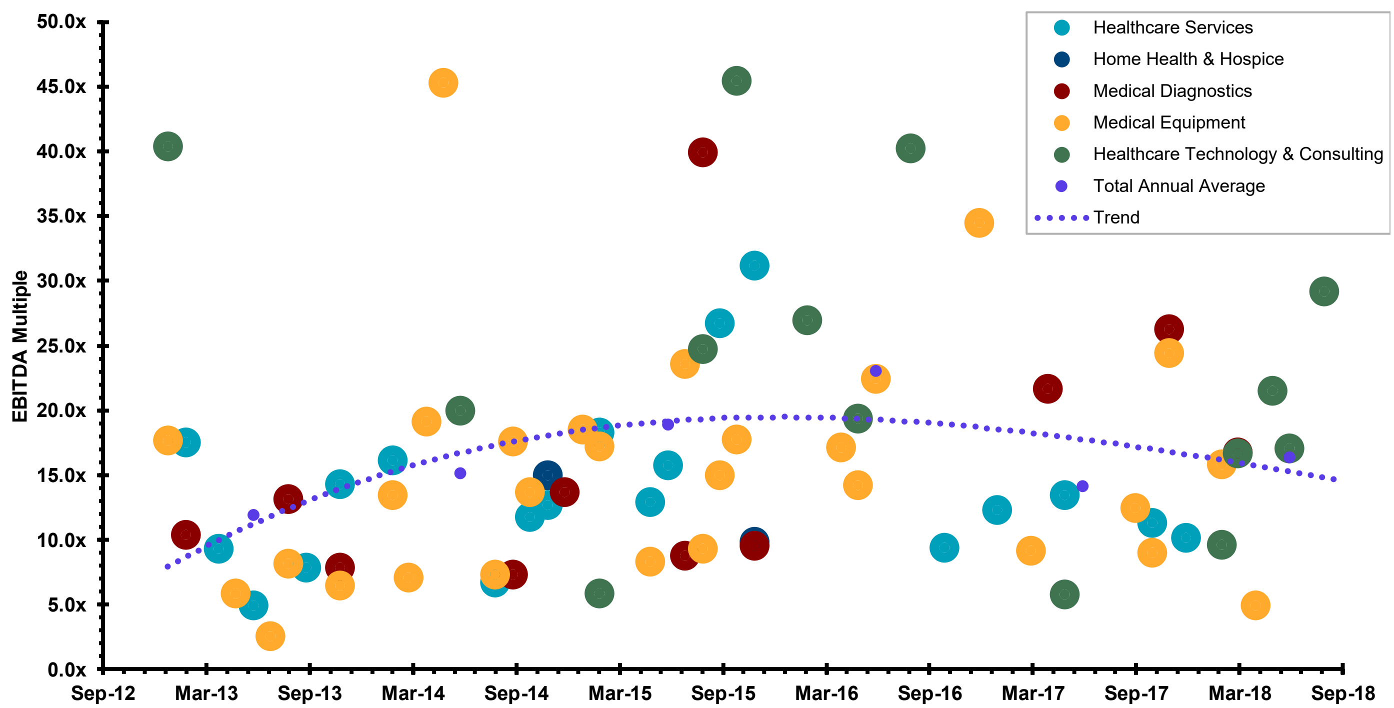
Key Metrics

The range of multiples being paid for healthcare transactions remains widely spread, reflecting the unique characteristics of each deal. The average multiple remains high, but after peaking at around 20x EBITDA in mid-2016, it appears a steady decline has begun. This is to be expected as financial buyers with established platforms shift their focus to add-on acquisitions at lower multiples. Even at 12 to 15x, these valuations are likely skewed by a disproportionate share of platform acquisitions among the limited transactions for which data is reported. We anticipate transaction multiples will trend lower until they fall below the multiples of enterprise value to EBITDA of public companies (see graph on page 8).

Healthcare Technology continues to be the sub-sector with the highest volume of transactions. Medical Equipment remains second most active; however, its share of the total has decreased by 5% in the past year, losing most of that share to Healthcare Services as sub-sectors such as Behavioral Health experience significant growth.

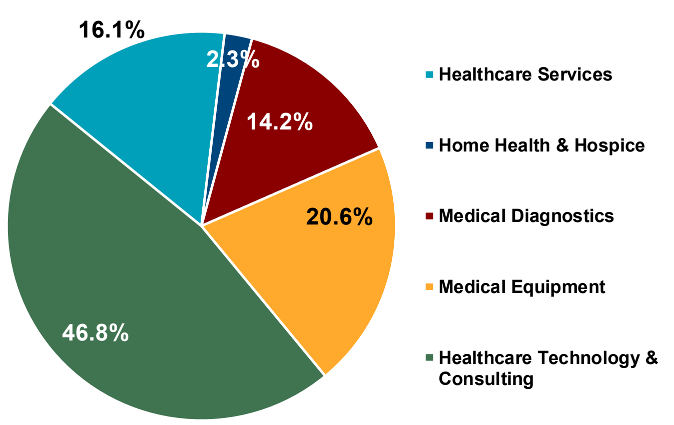
Strategic buyers continue to account for over three-quarters of transaction volume in healthcare, reflecting the highly fragmented nature of the industry and the desire of health systems, payers, and providers to more fully integrate services. In many cases, the strategic buyer is backed by a financial buyer.

EBITDA Multiples of Select Transactions

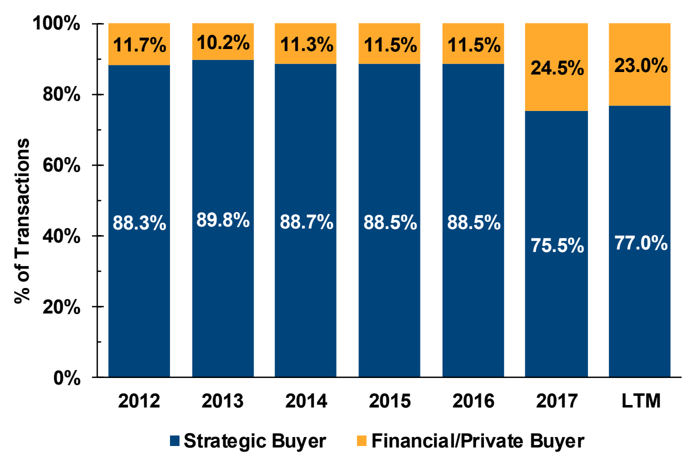


Source: EdgePoint Proprietary Database, Company Filings, CapIQ, News Releases

Transactions by Sub-Sector (LTM)



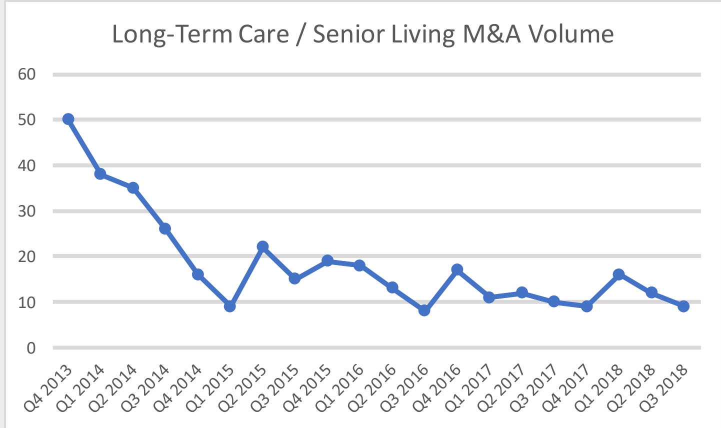
Share of Transactions by Buyer Type



Source: EdgePoint Proprietary Database, Company Filings, CapIQ, News Releases

Sub-Sector Profile: Long-Term Care/Senior Living

Merger & acquisition volume in the long-term care/senior living sub-sector dropped precipitously from its peak in late 2013 through early 2015. Increasing compliance requirements and changes to the prospective payment system reduced operating margins for skilled nursing facilities, weakening their ability to cover lease costs, and significantly slowing activity in this sub-sector by REITs. Within the independent and assisted living sub-sector—which faces lower regulatory and reimbursement risk—M&A activity also slowed as investors became concerned that development of new units had outpaced even the robust demographic changes underpinning the senior living market.



For the past three years, M&A activity in the long-term care/senior living sub-sector has been steady, averaging 13 transactions each quarter. Recent acquisitions by firms like those below, and HCR ManorCare's success in finding buyers for select divestitures, suggests strategic buyers believe the worst is over, and operating margins have stabilized. We believe REITs and other financial buyers will be re-entering the market by the end of 2019; however, we anticipate valuation multiples will remain steady.

Active Long-Term Care/Senior Living Acquirers

Select Strategic Buyers	Acquisition Activity
ENSIGN GROUP • NASDAQ: ENSG • Skilled Nursing, Assisted and Independent Living facilities (244), Home Health (22) and Hospice (21) agencies, and Home Care businesses (6) • Operates in 16 states	• Operations of Rock Creek of Ottawa (Nov 2018) • 2 Skilled Nursing Facilities in Idaho (Nov 2018) • Lake Pleasant Post Acute Rehabilitation Center (Apr 2018) • Pueblo Springs and Desert Blossom Rehab Centers (Sep 2017) • Parkside Senior Living (Aug 2017) • The Villas at Sunny Acres and Medallion Villas (Jul 2017) • Texas and Wisconsin Assisted Living Facilities (Jun 2017)
GRACE MGMT INC. A CPF LIVING COMPANY • Parent Co.: Chicago Pacific Founders • Manages Assisted and Independent Living facilities and Memory Care programs • Operates 34 developments in 18 states	• Shorehaven Senior Living (Aug 2018) • The Landon at Lake Highlands (Jun 2018) • Parkrose Estates (Apr 2018) • Camellia at Deerwood (Dec 2017) • Northgate Park Senior Living (Dec 2017) • Acacia Springs Senior Living (Jul 2017)
INSPIRIT SENIOR LIVING • Operates Assisted and Independent Living facilities and Memory Care programs • 8 locations in TN (3), PA (2), OH (2) and VA (1) • Real estate owned by various REITs	• 2 Ohio Senior Housing Facilities (Aug 2018) • Sunnington Assisted Living Community (Feb 2018) • The Palmerton and The Willow (Jun 2017) • Wesleyan Homes of Tennessee (Feb 2017) • Hilltop House, Inc. (Nov 2016)

HISTORY OF HCR-MANORCARE

1944	C.V. Wolfe acquires Lima Lumber Company
1963	Lima Lumber begins building nursing homes
1970	Lima Lumber renamed Wolfe Industries
1981	Wolfe Industries forms Health Care and Retirement Corporation of America (HCRA) to build and manage nursing homes
1984	Owens-Illinois acquires HCRA
1987	Owens-Illinois taken private by Kohlberg Kravis and Roberts (KKR)
1991	Health Care and Retirement Corporation (HCR) spun off via initial public offering
1992	HCR begins acquiring outpatient therapy clinics
1994	HCR forms long-term care pharmacy joint venture with Omnicare
1995	HCR acquires Allen Home Care
1998	HCR acquires ManorCare, Inc.
2007	HCR taken private by The Carlyle Group
2011	338 facilities sold to, and leased back from, HCP (later sold to QCP)
2018	ProMedica Health System acquires HCR; joint venture between ProMedica and Welltower REIT acquire real estate from QCP

Interview with: Steven M. Cavanaugh

President of HCR ManorCare, Inc.

In July, ProMedica Health System, and Welltower, a REIT, completed the acquisition of HCR ManorCare, the nation's second-largest provider of post-acute and long-term care.

Now part of a $7 billion not-for-profit health system, HCR begins the newest chapter of an eventful lifecycle which had its humble beginning in a Lima, Ohio lumberyard in 1944.

Since joining HCR in 1993, Steve Cavanaugh, has been an integral member of the team that led HCR through significant growth and transformation. Mr. Cavanaugh recently met with EdgePoint's Director of Healthcare Services, Matt Bodenstedt, to discuss the evolution of HCR, the role of key transactions in that evolution, and what the future holds for HCR as part of ProMedica.

EdgePoint: Thank you, Steve, for sharing HCR's story with us. HCR has been a part of several financial and strategic transactions. How would you differentiate them?

Steve Cavanaugh: A financial buyer is someone who doesn't already operate in the industry, but who is looking for an initial platform investment. The buyer targets a strong management team around which they can build a larger organization before exiting and reaping their return on investment. Venture capital funds and private equity groups are financial buyers. It's not unusual for the acquired company to then grow through subsequent strategic acquisitions.

Strategic buyers typically already operate in this, or a complementary industry. They are looking to solve a problem or take advantage of opportunities that will grow revenue or reduce expenses. The motivation may be as simple as taking out a competitor and increasing market share.

EdgePoint: How do those differ from the seller's point of view?

Steve Cavanaugh: A financial buyer doesn't necessarily have an intuitive feel for the business; therefore, they're going to focus on assessing the management team and will rely heavily on financial data. As long as results are tracking according to plan, they're happy to stay out of day-to-day decision-making, but stand ready to provide capital or strategic planning guidance. A strategic buyer will speak your language and have a deeper understanding of the challenges you face; that also means their due diligence is going to be more disruptive pre-closing, and their involvement more invasive post-closing.

EdgePoint: After becoming a public company in late 1991, HCR was faced with its own expectations for earnings growth. What were some of the key strategic acquisitions during this time?

Steve Cavanaugh: We wanted to diversify our sources of revenue in areas that were complementary to our core business, especially if they offered higher margins. One of our early transactions was a joint venture with Omnicare, the leading provider of long-term care pharmacy services. That relationship continues to this day. We also acquired an outpatient therapy provider in the local market. Additional acquisitions over the ensuing years grew that business to nearly 100 locations. In 1995, we acquired Allen Home Care, a Michigan-based home health agency. Today, our home health and hospice division operates in 25 states from more than 100 offices and generates $600 million in revenue. Then, of course, there was the merger with ManorCare in 1998.

EdgePoint: The ManorCare transaction was essentially a merger of equals and created the largest skilled nursing provider in the industry. What were some unique lessons from that deal?

Steve Cavanaugh: There's no such thing as a merger of equals. Ultimately, someone is the buyer, and the buyer is in charge. In this case, the companies had complementary cultures, and both had good properties and strong frontline management teams. Each contributed five directors to the combined board; it was ultimately the independent directors who decided which executive management team would lead HCR ManorCare long term.

EdgePoint: In 2007, the company was taken private by The Carlyle Group, a private equity group; and in 2011, sold most of its facilities to a REIT, leasing them back and continuing to operate them. What motivated these transactions?

Steve Cavanaugh: These were financial transactions. In going private, the sale cleared at about $63 per share compared to a recent stock price in the low forties; our shareholders received an excellent return on their investment. The sale-leaseback with the REIT enabled Carlyle to reap a return on its investment.

EdgePoint: Unfortunately, by 2017, decreasing reimbursement and increasing regulatory requirements made it difficult for HCR to make its lease payments, and the company sought bankruptcy protection in early 2018. That ultimately led to the recent acquisition of HCR by ProMedica. What is the plan for working as part of ProMedica? It's early yet; but how is it different being part of a large mission-oriented nonprofit?

Steve Cavanaugh: One difference is that we now hear a lot of, "We'd love to work with you!" Locally, we benefit from ProMedica's outstanding reputation and being a great supporter of the community. In other markets, our nonprofit status opens up new opportunities as well. We're excited to be working with our colleagues across the ProMedica system, including physicians, hospitals, and Paramount Insurance, to develop new models of care that improve quality and customer satisfaction, while also reducing the total cost of care. We plan to perfect the model locally, then partner with other health systems across the country where HCR has a presence.

> ***"We will redefine health care and its role in healthy aging."***
>
> *Randy Oostra, president and CEO, ProMedica Health System*

EdgePoint: Any advice for business owners considering the sale of their healthcare business?

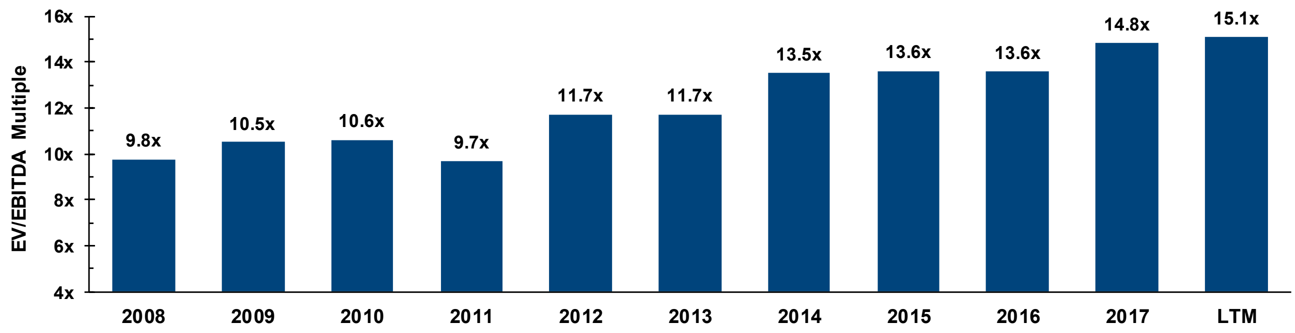
Steve Cavanaugh: Foremost, don't hold anything back or try to hide information. Credibility is key to completing a successful transaction. You can make yourself more financially attractive by having a clean ownership structure and clean assets. The fewer complications and encumbrances the better. Also, prepare yourself professionally and emotionally. Think through what you want for the future; and perhaps be open to a new career with the buyer.

EdgePoint: Finally, would you recommend use of an intermediary?

Steve Cavanaugh: A good investment banker can generate positive tension in the process. They can use their knowledge of the market to cast a wide net and create competition between prospective buyers. They can also help sellers understand what a realistic value is for the business, one that will ultimately close. The best intermediaries will help the seller prepare for the transaction and life afterward. While we may end up paying more, the transaction process should run more smoothly, and be more successful for seller and buyer.

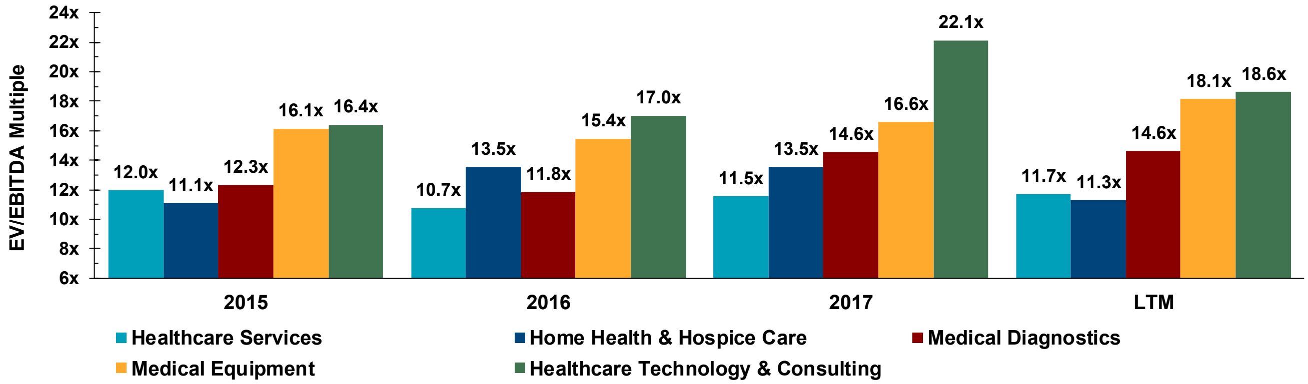
Public Company Comparisons Trading Multiples

Healthcare Industry Public Comparables: Annual EV/EBITDA Multiples



Source: CapIQ, public trading data as of September 30, 2018.

Healthcare Sub-Sector Public EV/EBITDA Multiples



Source: CapIQ, public trading data as of September 30, 2018.

Representative EdgePoint Healthcare Transactions

Sell-Side Advisory

TransMotion Medical
has sold to
Winco Mfg., LLC

Financing Advisory

The Fibromyalgia & Fatigue Center
has successfully completed a capital raise

Buy-Side Advisory

Med XS Solutions
has acquired
Health Quip, LLC

Sell-Side Advisory

Select Assets of Steris AB
has sold to
An Undisclosed Private Company

Buy-Side Advisory

Med XS Solutions
has acquired
Gar Division of Neoforma

Sell-Side Advisory

Providence Home Health Care
has sold to
A Private Equity Group

Financing Advisory

PetsDX
has successfully completed a capital raise

Sell-Side Advisory

Accu-Tube
has sold to
Washington Equity Partners

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M&A Advisory
RESULTS *with* INTEGRITY™