Private Equity Summary Report 2014

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Benesch Health Care Market Intelligence

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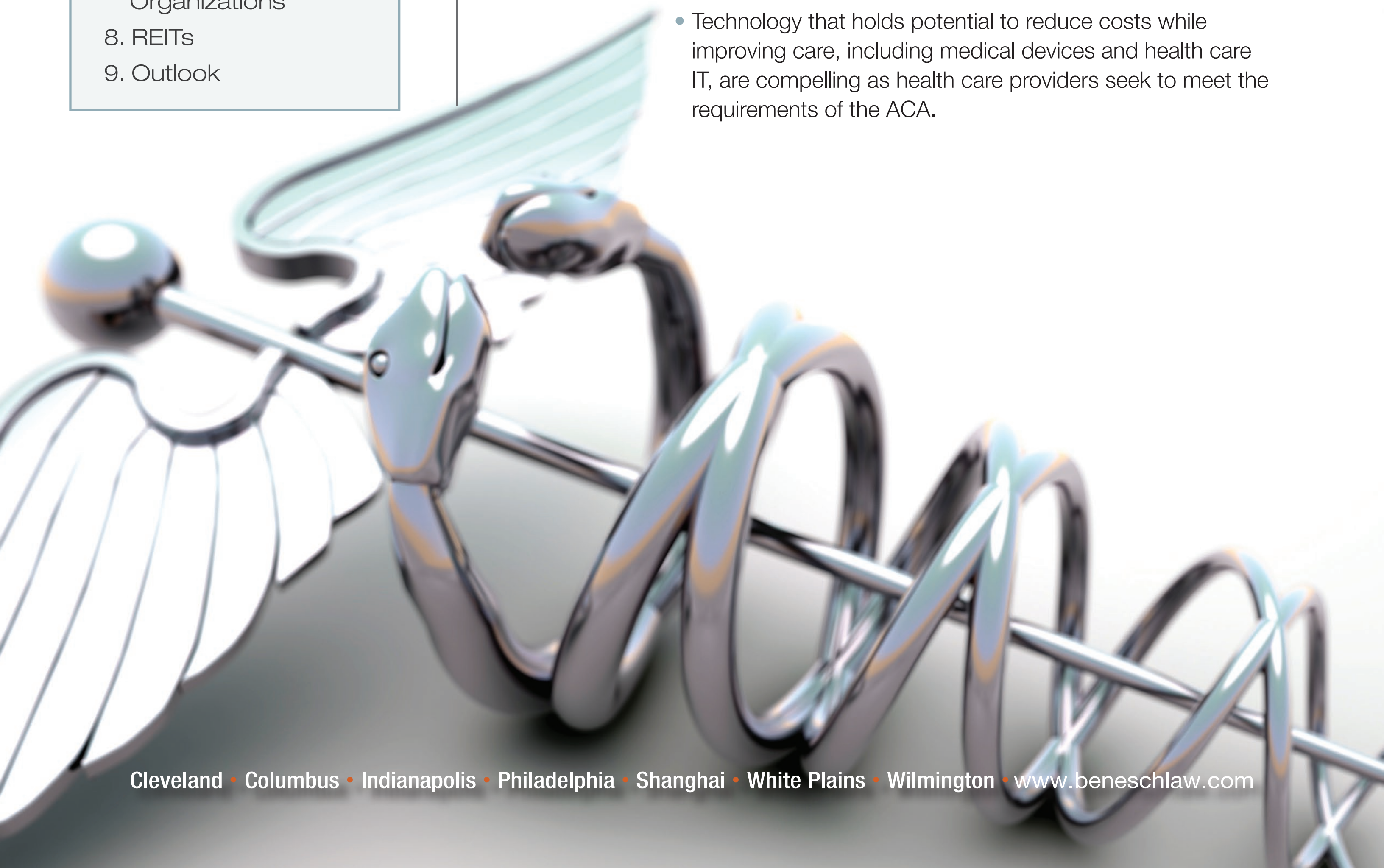
1. Key Findings

- Health care reforms and the Affordable Care Act have put the private equity sector into a period of transition, as it seeks new investment targets and health care providers reorganize their operations.
- Deal volume in 2014 has so far remained fairly consistent compared with 2013, however disclosed transaction value increased 43% in the first half of 2014.
- Strategic M&A and venture capital deals are outpacing private equity transactions in the health care sector.
- Technology that holds potential to reduce costs while improving care, including medical devices and health care IT, are compelling as health care providers seek to meet the requirements of the ACA.

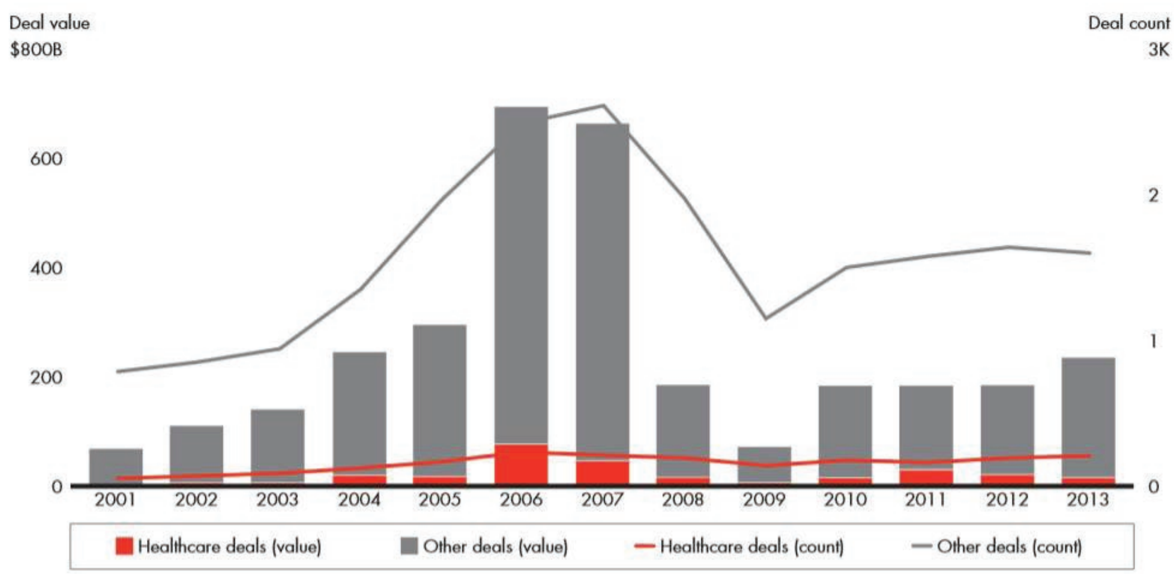


2. Disruptive Factors

- Many of the companies attracting investors' attention are in their early stages of existence and development, due to the new landscape and goals created by health care reform.
- An increase in strategic acquisitions is driving the competition for prime private equity targets.
- A strong stock market is prompting more IPOs and pricing potential acquisition targets above private equity's comfort range.
- Shift towards venture capital firms funding start-ups and early-stage companies seeking to develop new technologies that would reduce costs or improve care for health care providers to more effectively align operations with new value-based payment models.

3. Health Care Private Equity Overview

- The U.S. health care private equity industry entered 2014 amid an uncertain environment. Specifically, the implementation of the Affordable Care Act dominated the sector and influenced every corner.
- In addition to the political uncertainty, the nationwide patchwork created as some states decided to expand Medicare while others didn't further complicated the landscape, making private equity and other transactions in the health care industry increasingly complex.
- This uncertainty made private equity firms hesitant about health care transactions, even during a time when overall activity was growing.
- A 2014 U.S. Health Services market outlook by PwC shows that there were 109 announced transactions in health care involving private equity firms in 2013, compared to 112 and 124 in 2012 and 2011, respectively.



Notes: Excludes add-ons, loan-to-own transactions and acquisitions of bankrupt assets; based on announcement date; includes announced deals that are completed or pending, with data subject to change; deal value does not account for deals with undisclosed values
Sources: Dealogic; AVCJ; Bain analysis

4. Transaction Value

- There was a shortage of large-sized health care transactions in 2013, with what transactions there were “scattered broadly,” with little concentration of activity to be found in any particular subsector. No health care deals made the Top 10 list of 2013 private equity transactions, in terms of dollar value.
- A report co-authored by the Health Care Private Equity Association and Bain & Company found that 2013 was a busy year for private equity at large, with a 22% increase in total deal value over the previous year. The opposite was true within the health care industry, where buyout deal value dropped 23% to slightly more than $16 billion despite a small increase in the number of deals. This compared to $200 billion worth of strategic M&A activity in the health care sector.
- Rather than large-scale blockbusters, the year saw an increased interest in small and medium transactions, with an accompanying shift towards early-stage and middle-market targets. Large private equity firms, such as Apax Partners, KKR, CD&R and Madison Dearborn Partners, were among the most active firms involved in the bigger deals.
- There have been indications that private equity firms are again ready to consider large-scale deals in 2014. PwC reports that there were 18 in Q2 2014, compared to eight the year before, while firms selling assets are being rewarded as the appetite for deals is large and competition high.
- Among the highlights so far in 2014 are Clayton, Dubilier & Rice’s $910-million acquisition of Jacksonville, Fla. based Healogics and Summit Partners’ $550-million investment into Minneapolis-based ABILITY Networks, a health care technology company.
- Recent reports that private equity firm Apax is exploring the sale of Englewood, Colo.-based health care IT portfolio company TriZetto for as much as $3 billion is another possible sign that firms are again feeling more confident about making large-scale transactions within the health care sector.

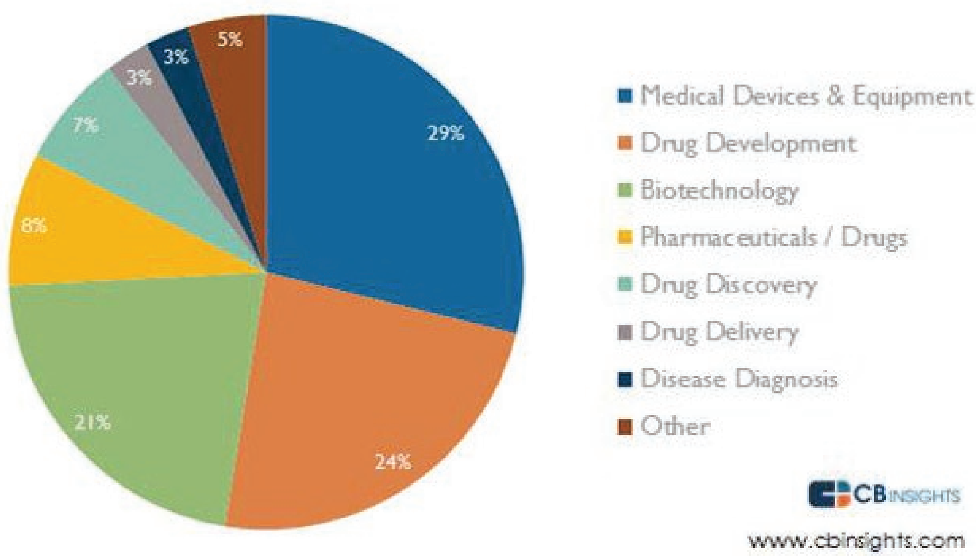
5. Subsector Activity

- The most active health care subsector in 2013 was again providers and services, and although the number of deals dropped only slightly, the total value was a fraction of 2012 levels. Breaking down the numbers even further reveals that while providers remained the most common target, there was a shift away from providers and a larger number of deals involving services during that period.
- In contrast, deals in the payer space increased both in value (primarily due to Apax’s $3-billion OCCM/Align acquisition) and in the number of deals.
- Medical device makers have historically been a common target for private equity and venture capital firms alike. However, it was believed that the 2.3% medical device tax introduced as part of the ACA would dampen that enthusiasm. This has yet to transpire, as firms are investing more in medical device makers now than before the act came into effect. This trend continues in 2014, with companies such as American Medical Systems and Johnson & Johnson currently seeking multi-billion dollar deals for their device businesses.

6. Venture Capital

- While private equity is tentatively exploring the new health care landscape, venture capital firms are extremely busy. A July 2014 report by CB Insights found a total of 974 venture capital-backed deals in the second quarter worth approximately $13.88 billion, the highest level since the first quarter of 2001. About $2.7 billion of that came from 161 deals in the health care sector.
- Venture capital firms such as Kleiner Perkins are demonstrating similarly strong venture capital activity in the health care sector.
- The report also reveals a growing shift away from early-stage deals so far in 2014. Whereas seed and Series A funding accounted for 36% of deals in Q4 2013, that has fallen to 14% halfway through 2014. Series B funding has seen the largest increase as a result, growing from 25% of deal value at the end of 2013 to 35% in Q2 2014.
- By industry, the top three areas for investment deals by volume in Q2 2014 were: medical devices and equipment (36%); biotechnology (24%); and drug development (14%), which combined accounted for almost three-quarters of all transactions.

Healthcare Corporate Venture Capital Investments by Industry
as % of deals, Q1 ‘11 – Q1 ‘14



7. Accountable Care Organizations

- The rapid creation of ACOs across the country also contributed to a shift in activity among investment firms. Buyout firms aren't directly involved with the creation of ACOs, but have been active in areas that have seen increased development as a result of their rapid rise.
- Private equity interest covered several provider and services transactions, including:
- Health care-related IT solution providers (WCAS' acquisition of GetWellNetwork; Bain Capital Ventures and Spectrum Equity's investments in MedHOK; and Summit Partners' stake in COMS Interactive);
- Consulting services (Geisinger Health System and Oak Investment Partners launched xG Health Solutions; Evolent Health received funding from TPG Growth); and
- Companies developing new care models (EDG Partners and Nashville Capital Network invested in Unity Physician Partners).

8. REITs

- Medical offices and other health care properties are increasingly attracting the interest of institutional investors, according to Mindy Berman, the managing director of JLL.
- Previously, this property segment was dominated by REITs that specialize in health care properties. Berman cites Harrison Street Real Estate Capital's sale of a 12-asset, $283-million health care property portfolio as an example of how interest in this asset class is moving beyond a niche market.

9. OUTLOOK

- Heading into the remainder of 2014 and beyond, the market is likely to see a continuation of the current level and value of transactions.
- The Health Care Private Equity Association/Bain report forecasts that "private equity funds should continue to see attractive opportunities for investment in both earlier-stage and larger assets."
- Carve-out activities, where health care companies shed non-essential units to focus on their core business, are likely to provide ongoing opportunities for private equity acquisitions. However, as they are generally mature companies, this runs against the trend of investments in growth-stage ventures, and would likely represent a longer-term investment for private equity firms.