



# HEALTHCARE FOCUS



## Outlook for 2010 Transaction Activity—Healthcare Reform or Not

With the passage of the Senate Bill (H.R. 3590) and the House Bill (H.R. 3962) in 4Q 2009, a unified healthcare policy framework appeared imminent. However, the recent Democratic Senate seat loss in Massachusetts and declining public support make the passage of healthcare reform less likely. The demise of the “public option” has highlighted the commonality of the two proposals in certain key provisions, namely, expansion of access to coverage, expansion of Medicare and Medicaid, mandates related to employers and individuals, and new and increased taxes. These areas, as well as the overall cost of each bill (\$871 billion for H.R. 3590 and \$894 billion for H.R. 3962) are widely discussed in the mainstream press. Whether or not any compromise bill legislation is passed eventually, we would like to focus on several provisions of the two bills that we believe would likely remain as part of any compromise bill, and which may have a significant effect on the capital flows into and within the healthcare sector going forward. In our view, the inclusion of these provisions in the bills reflects a recognition of a debate that precedes the proposed legislation, rather than any revolutionary ideas. The proposals, however, do solidify and confirm the implications of these ideas on future transaction activity.

Each bill contains distinct provisions for improving the quality, outcomes and overall performance of the healthcare delivery system, instituting prevention and wellness programs, and establishing a framework for the use of information technology. The evolving legislation is likely to unify these ideas into an “integrated” system for achieving unprecedented efficiencies and quality in overall care delivery. We believe that fears of a system based on rationing are overblown, partly because the push (mainly by the private sector) to reshape the delivery model to achieve these goals of efficiency and quality is likely to outpace any such rationing efforts, and rationing of any kind would be politically unpalatable. The chart on Page 2 shows a summary comparison of the relevant provisions of each bill.

Providers will continue to face severe capital constraints, and this situation is likely to be exacerbated by both bills’ provisions to recover part of the cost of reform by limiting payments to a wide spectrum of providers. While limited capital availability and lower future reimbursement will constrain providers’ investments in new initiatives related to efficiency and quality, the bills do provide some subsidies to encourage them to invest, thereby enhancing the demand for such services.

### Sectors to Watch

Regarding reimbursement trends, the past, beginning with the Balanced Budget Act of 1997, is the best predictor of the future, particularly given the mounting federal deficit. While it is important to understand the specifics of the emerging policy, reimbursement is not a primary factor in our outlook, and sectors that we believe will enjoy increasing favor primarily will be those that are fundamentally consistent with the efficiency/quality idea discussed above.

Areas of particular interest are care management and continuum of care, revenue cycle management, electronic medical records, document management (particularly paperless processing), remote patient monitoring technologies, workflow solutions, and enterprise systems integration. The highest valuation multiples will be commanded in transactions where there are proprietary (as opposed to commoditized) technologies and processes involved. Notwithstanding ongoing reimbursement pressure and capital constraints faced by providers, demand for the above areas will be strong from across the provider spectrum, ranging from small physician practices to alternate-site providers to inpatient care providers, including senior living. The chart on page 4 shows current trading multiples for a variety of healthcare subsectors compared to levels one year ago. The outsized change in multiples enjoyed by Healthcare IT supports the fundamental value proposition discussed above.

An area of equal importance will be diagnostic labs and related subsectors. In particular, the pathology related lab sector has shown tremendous appeal lately. The recent \$230 million acquisition of Spectrum Labs by Welsh Carson, Spectrum’s acquisition of Carilion, and PathGroup’s \$100 million recap with Primus validate the expectation of strong capital flows into the lab sector. On Page 2, we highlight the fundamentals of clinical labs and provide a snapshot of both Spectrum Labs deals and the PathGroup transaction.

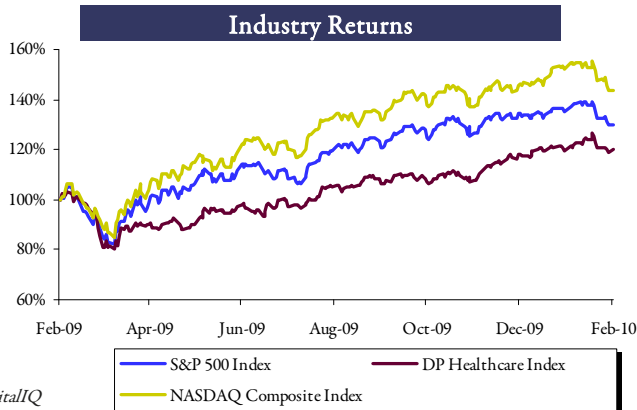
Secondary areas of heightened transaction activity we believe will be skilled nursing, assisted living and potentially hospitals. While this may appear to be a contrarian view regarding facility-based care, the main driver here will be distress, or the expectation thereof. This is evidenced by several transactions in 2009, namely Redwood Capital’s acquisition of Erickson following Erickson’s bankruptcy, Blackstone’s acquisition of financially distressed Sunwest Management and Omega’s acquisition of CapitalSource’s senior living portfolio. Also of potential interest is behavioral health which is showing increased interest partly as a result of the Mental Health Parity Act that provides a refinement (and reduced uncertainty) of reimbursement policy related to this sector.

Interest from strategic buyers will remain strong. However, private equity investment is accelerating due to the enormous overhang of approximately \$400 billion of investable capital and a semblance of recovery in the credit markets. Additionally, our current transaction portfolio is enjoying a high level of interest from cross-border buyers that are eager to enter the US healthcare market.

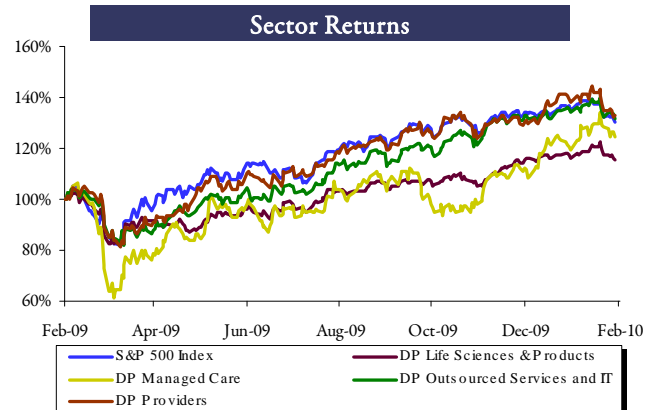
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### Healthcare Public Market Trends



Source: CapitalIQ





# HEALTHCARE INDUSTRY DEVELOPMENTS

## Recent Transactions & Regulatory Changes and Developments

### Healthcare Reform Legislation Overview (Cont. from page 1)

	Senate Bill (H.R. 3590) (Passed by the Senate on December 24, 2009)	House Bill (H.R. 3962) (Passed by House on November 7, 2009)
<b>Improving Healthcare Quality</b>	<ul style="list-style-type: none"> <li>- Establish a research institute to identify research priorities and compare the clinical effectiveness of medical treatments.</li> <li>- Award grants to states to develop, implement, and evaluate alternatives to current tort litigations; focus on patient safety and reducing medical errors.</li> </ul>	<ul style="list-style-type: none"> <li>- Establish an institute to conduct, support, and synthesize research on outcomes, effectiveness, and appropriateness of health care services and procedures.</li> <li>- Provide funding to states to change medical liability laws with a focus on dispute resolution, disclosure of health care errors, and affordable liability insurance.</li> </ul>
<b>Disease Prevention and Wellness</b>	<ul style="list-style-type: none"> <li>- Establish a public health council to develop a national strategy to improve national health</li> <li>- Create a public health fund to expand funding for prevention and public health programs.</li> <li>- Create a task force to study and make recommendations on the use of clinical and community prevention services.</li> <li>- Establish a grant program to support prevention and wellness services with a focus on reducing chronic disease rates and addressing health disparities.</li> <li>- Improve disease prevention through increased funding for proven preventative services and requiring health plans cover basic preventive services.</li> </ul>	<ul style="list-style-type: none"> <li>- Develop a national strategy to improve national health through prevention and wellness activities.</li> <li>- Create a task force to study and make recommendations on the use of clinical and community prevention services.</li> <li>- Provide wellness grants for up to three years to small employers for up to 50% of costs incurred for a qualified wellness program.</li> <li>- Improve disease prevention through increased funding for proven preventative services and increased Medicare payments for preventative services.</li> <li>- Establish a grant program to support prevention and wellness services with a focus on reducing health disparities, preventing obesity, and training health workers in underserved communities.</li> </ul>
<b>Healthcare IT</b>	<ul style="list-style-type: none"> <li>- Set up electronic systems in order to enable: electronic matching against existing federal and state data, submission of electronic documentation, reuse of stored eligibility information, online management of information, expansion of the enrollment system to integrate new programs to expand volume and functionality, and communication of eligibility information electronically.</li> <li>- Award grants to develop new, and adapt existing, technology systems to implement the HIT enrollment standards and protocol</li> </ul>	<ul style="list-style-type: none"> <li>- Increase use of electronic health records (EHR) by small health care providers through: higher reimbursement rates, low-cost software, and training assistance.</li> <li>- Standardize electronic records, and use them to: determine patient eligibility, submit claims, allow electronic funds transfer (EFT), and store health records.</li> <li>- Provide funding for the implementation of electronic systems with a focus on rural and underserved markets.</li> </ul>

### Select Recent Transactions \*

On January 6, 2010, **Kandu Capital** acquired **Belfair Retirement Community**, a 79-unit independent living retirement community, from Sunwest Management, Inc.

On November 17, 2009, **Omega Healthcare Investors Inc.** signed an agreement to acquire 80 long-term care facilities from **CapitalSource Inc.** for \$530 million. Omega will also receive a purchase option to acquire an additional 63 facilities from CapitalSource.

On November 2, 2009, **Abbott Laboratories** acquired the remaining 90% stake of **Evalve**, a manufacturer of devices that enable the repair of cardiac valves, from a group of private equity firms for **\$410 million**.

On October 30, 2009, **Warner Chilcott** acquired **the global pharmaceuticals business of Procter & Gamble**, a manufacturer and marketer of pharmaceuticals, from Procter & Gamble for **\$3.1 billion (1.4x revenue)**.

On October 20, 2009, **Dainippon Sumitomo Pharma** acquired **Sepracor**, a research-based pharmaceutical company, from Wellington Management Company, Fidelity Management, and Barclays Global Investors for **\$2.9 billion (1.8x revenue, 7.7x EBITDA)**.

On October 19, 2009, **Redwood Capital Management** signed an agreement to acquire six **Erickson Retirement Communities** subsidiary companies and **Novi Campus** from Erickson Retirement Communities for approximately \$610 million.

*\*Source: CapitalIQ, MergerStat & Dresner Partners estimates*

## Diagnostic Laboratories

The \$59 billion clinical lab industry in the United States consists of three broad segments: commercial labs, physician-owned Labs, and hospital labs. Federal and state regulations govern clinical lab operations for facilities serving Medicare and Medicaid patients. The two largest commercial labs, Quest and LabCorp, account for annual revenue of over \$11 billion, which represents approximately 20% of total billings in the industry. These two companies have been active consolidators, ultimately closing many smaller regional and rural labs that they acquired in an effort to maximize operating efficiencies. Since 2000, the clinical lab industry has grown at a 6.4% CAGR from \$32.9 to \$57.3 billion in revenue. The fastest areas of growth within the lab sector have been anatomic and molecular pathology, as well as certain niche subsectors.

The in vitro diagnostic ("IVD") products industry, which includes instruments, related reagents, and test kits used in the detection and monitoring of diseases and disorders, is a growing \$17 billion industry. Advances in diagnostics, especially the increase in diagnostic capability at the molecular level, are beginning to deliver on the promise of the genomics

revolution. The IVD industry is currently positioned to grow in the years to come as better screening technologies enable earlier detection, treatment and potential prevention of diseases and medical conditions, increasing the quality and efficiency of the healthcare delivery system.

### Recent Transactions

On January 27, 2010, **Triad Laboratory Alliance, LLC** (Spectrum Labs) acquired **Carilion Labs**, a provider of clinical, anatomic pathology and esoteric testing services.

On January 12, 2010, **Primus Capital** sponsored a \$100mm leveraged recapitalization of **PathGroup, Inc.**, a provider of clinical and anatomic pathology services.

On December 11, 2009, **Welsh, Carson, Anderson & Stowe** acquired **Triad Laboratory Alliance, LLC** (Spectrum Labs), a provider of clinical, esoteric and anatomic pathology testing, from Apax Partners.

*Source: Wall Street and Dresner equity research*

# HEALTHCARE SECTOR SPOTLIGHT

## Diagnostic Laboratory Statistics

### Public Company Trading Statistics - Clinical Labs

(\$ in millions, except per share data)

Company Name	2/1/2010			LTM			Enterprise Value to:				
	Stock Price	Market Cap	TEV	Revenue	EBITDA	EBIT	Revenue		EBITDA		EBIT
							LTM	2009E	LTM	2009E	LTM
Bio-Reference Laboratories Inc.	\$37.24	\$531.9	\$539.3	\$362.7	\$48.1	\$38.3	1.5x	1.5x	11.2x	11.5x	14.1x
Laboratory Corp. of America Holdings	\$71.00	\$7,666.6	\$9,093.4	\$4,648.7	\$1,105.4	\$947.6	2.0x	1.9x	8.2x	8.0x	9.6x
Quest Diagnostics Inc.	\$56.11	\$10,363.3	\$12,958.1	\$7,455.2	\$1,600.3	\$1,343.6	1.7x	1.7x	8.1x	8.0x	9.6x
Sonic Healthcare Ltd. *	\$14.43	\$5,605.0	\$6,845.9	\$3,008.2	\$584.4	\$483.1	2.3x	2.5x	11.7x	12.7x	14.2x

\* Traded on the Australian Securities Exchange

High	2.3x	2.5x	11.7x	12.7x	14.2x
Low	1.5x	1.5x	8.1x	8.0x	9.6x
Mean	1.9x	1.9x	9.8x	10.1x	11.9x
Median	1.8x	1.8x	9.7x	9.8x	11.9x

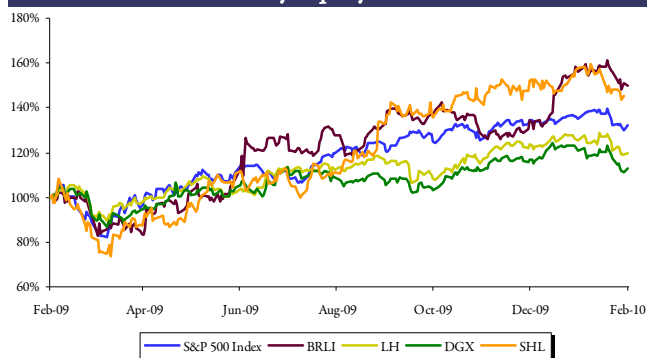
### Public Company Trading Statistics - Specialty Labs

(\$ in millions, except per share data)

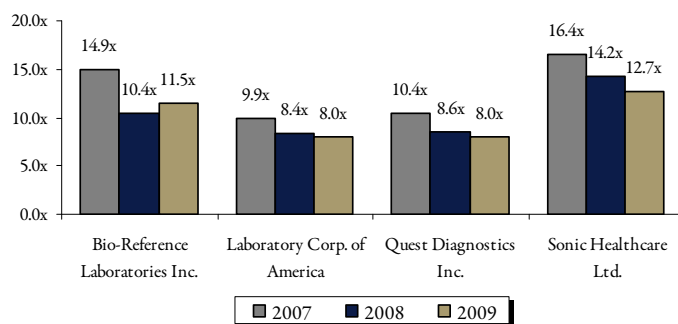
Company Name	2/1/2010			LTM			Enterprise Value to:				
	Stock Price	Market Cap	TEV	Revenue	EBITDA	EBIT	Revenue		EBITDA		EBIT
							LTM	2009E	LTM	2009E	LTM
Clariant, Inc.	\$2.31	\$189.0	\$226.0	\$90.3	\$3.0	NM	2.5x	2.5x	NM	NM	NM
Genomic Health Inc.	\$16.70	\$485.0	\$426.6	\$141.2	NM	NM	3.0x	2.8x	NM	NM	NM
Genoptix, Inc.	\$30.42	\$518.0	\$380.2	\$169.3	\$51.7	\$48.6	2.2x	2.1x	7.3x	6.6x	7.8x
Cepheid	\$14.37	\$871.2	\$827.4	\$159.3	NM	NM	5.2x	5.0x	NM	NM	NM

High	3.0x	2.8x	7.3x	6.6x	7.8x
Low	2.2x	2.1x	7.3x	6.6x	7.8x
Mean	2.6x	2.5x	7.3x	6.6x	7.8x
Median	2.5x	2.5x	7.3x	6.6x	7.8x

### Clinical Laboratory Equity Market Performance

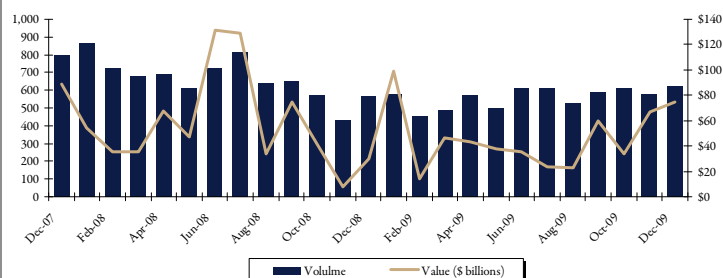


### Clinical Laboratory EV / EBITDA Multiples

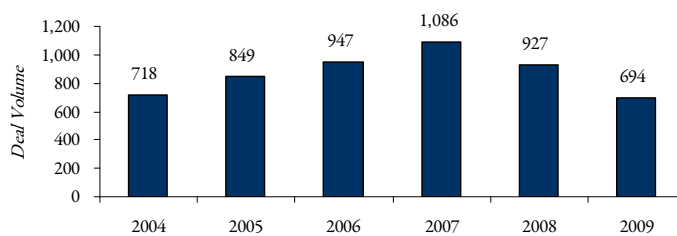


## Capital Markets

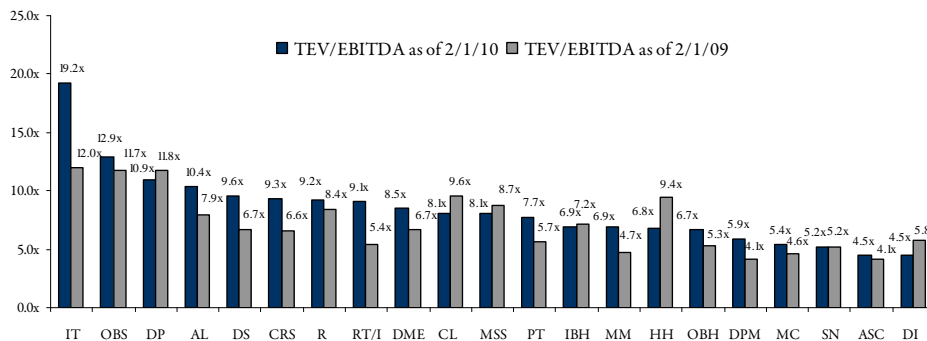
### U.S. M&A Activity



### U.S. Healthcare M&A Volume



# DRESNER PARTNERS HEALTHCARE GROUP



IT - Healthcare IT	DS - Dental Supplies	MSS - Medical & Surgical Supplies	HH - Home Health	ASC - Ambulatory Surgery Centers
OBS - Outsourced Business Services	R - Renal	PT - Physical Therapy	DPM - Dental Practice Mgmt	
DP - Diagnostic Products	RT/I - RT/Infusion	MM - Medical Management	SN - Skilled Nursing	
DME - Durable Medical Equipment	CL - Clinical Labs	IBH - Inpatient Behavioral Health	MC - Managed Care	
AL - Assisted Living	CRS - Clinical Research Services	OBH - Other Behavioral Health	DI - Diagnostic Imaging	

*Source: CapitalIQ*

## Dresner Partners Healthcare Service Offering



## DEAL SPOTLIGHT

Dresner Healthcare - A Leader in Investment Banking Services to the Senior Living and Home Health Sectors

**The Carle Foundation**  
Urbana, Illinois  
has sold its skilled nursing and dementia care businesses to:  
**TRADITIONS MANAGEMENT™**  
HOME HEALTH AND SENIOR LIVING  
Dunedin, Florida

**DRESNER PARTNERS INVESTMENT BANKING**

**CareCollaborative**  
HOME HEALTH SERVICES, INC.  
has formed a strategic partnership with:  
**HOME HEALTH GROUP, LLC**

**DRESNER PARTNERS INVESTMENT BANKING**

## Current Transactions

Project Terrapin	- Sale of leading renal care provider	Project Sample	- Growth capital for a rural focused diagnostic laboratory company
Project Workflow	- Sale of a healthcare IT company focused on image management and workflow solutions	Project Tiger	- Buy-side advisory for a critical access hospital owner/operator
Project Quality	- Sale of a healthcare IT company focused on credentialing and care management	Project RCM	- Sale of revenue cycle management company

## Dresner Partners Healthcare Group

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Our role as a financial advisor requires independent and objective advice, and seasoned execution. Please contact one of our Healthcare Group leaders to discuss how our experience can help you.

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