



# HealthCare Appraisers

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## Buying and Selling Units to Physician Investors: An Overview of Multiples and Current Trends in Valuation

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# Presentation Outline

- Valuation Multiples
- Overview of 2010 ASC Valuation Survey (7<sup>th</sup> Year)
- Other Notable Observations
- Q&A

# Valuation Multiples

First Question:

*“What is the  $h^{**}l$  is a valuation multiple?”*

# Valuation Multiple

- A valuation multiple is appraiser shorthand for the present value of a perpetual earnings stream mathematically expressed as follows:

$$\frac{1}{(K - g)}$$

- Key components of a valuation multiple”
  - 1) Definition of the **Earnings Stream**
  - 2) Estimation of **Risk (K)**
  - 3) Estimation of the rate of earnings **Growth (g)**

# Defining “Earnings”

- Typically Measured as Earnings Before Interest Taxes and Depreciation (“EBITDA”), but can also be stated as cash flow, net income, distributions, etc.
- Single Period or Average? May be most recent year, trailing twelve months, 2-year average, etc. The appropriate measure is the one that is most indicative of future earnings capacity.
- In some instances historical earnings measures must be normalized to remove the effect of non-recurring income and/or expense items.

# Estimation of Risk

- Risk is defined as the degree of uncertainty as to the realization of investment returns (*i.e., the earnings stream*).
- Risk is measured as the required rate of return necessary for an investor to commit funds given alternative investments.
- For mature in-network ASCs the required rate of return is generally in the range of 18-22%, however, this can be significantly different if earnings are volatile or at risk.

# Estimation of Growth

- A valuation multiple is a “perpetual” valuation model.
- Because of this, there are limitations regarding the growth assumption that can be built in to a multiple.
- Generally the growth assumption should not exceed the growth rate of the overall economy, which when measured as GDP, is less than 5%.
- Because of this limitation – valuation multiples should only be applied to stable businesses.

# Valuation Multiples

Second Question:

*“Is your multiple as big as mine?”*

# Key Components of a Multiple

## 1. Earnings Stream

The next time you hear that Dr. Jones sold his interest for 5x, ask yourself “5x what?”

## 2. Risk

Not all earnings are the same! Two ASCs with \$1.0 of earnings may have completely different risk profiles.

**Higher Risk = Lower Multiple**

## 3. Growth

All things equal, **Higher Growth = Higher Multiple.**

# Valuation Multiples

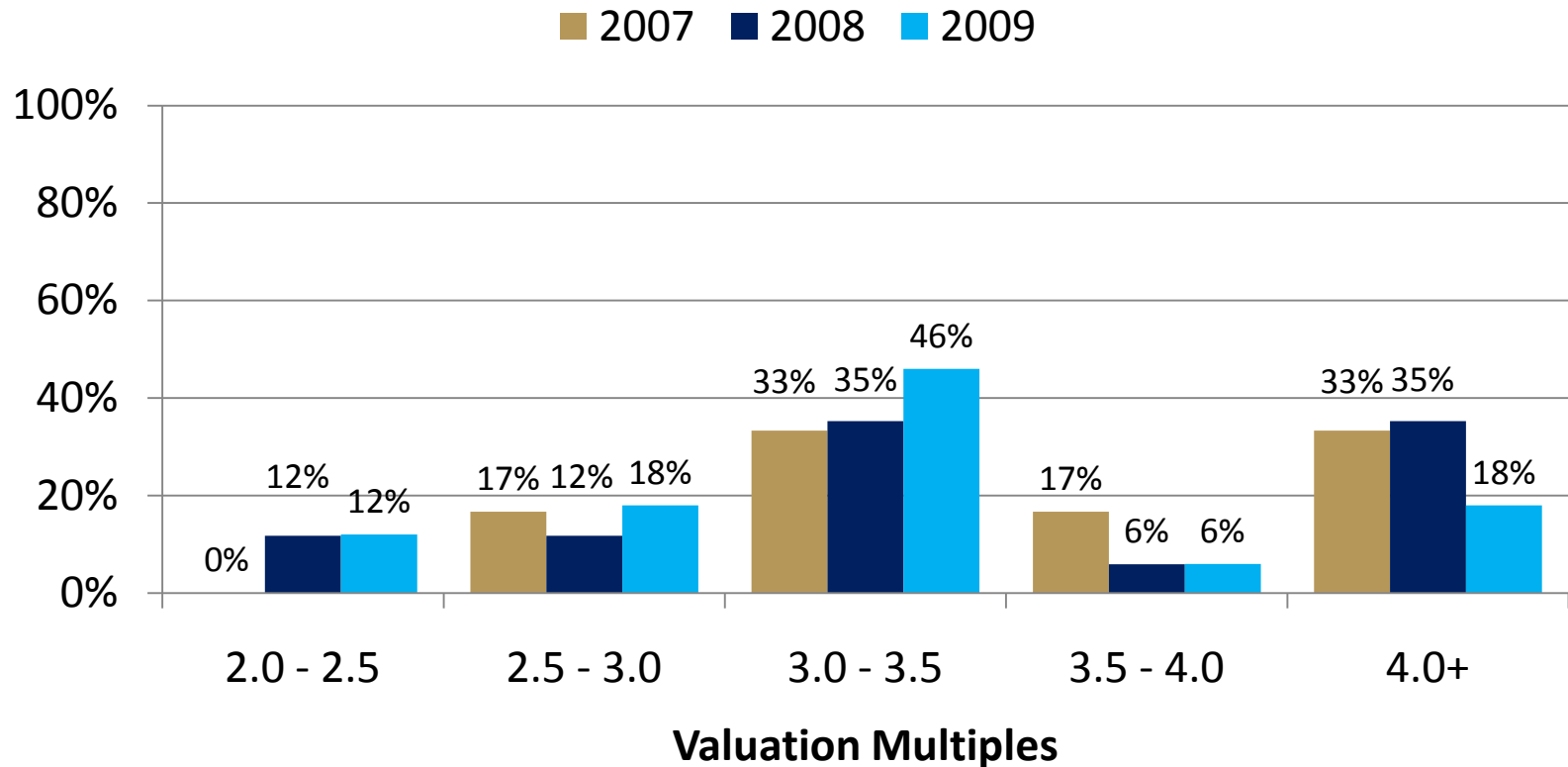
Last Question:

*“Yeah that’s all fine and good, but what are the current ASC multiples?”*

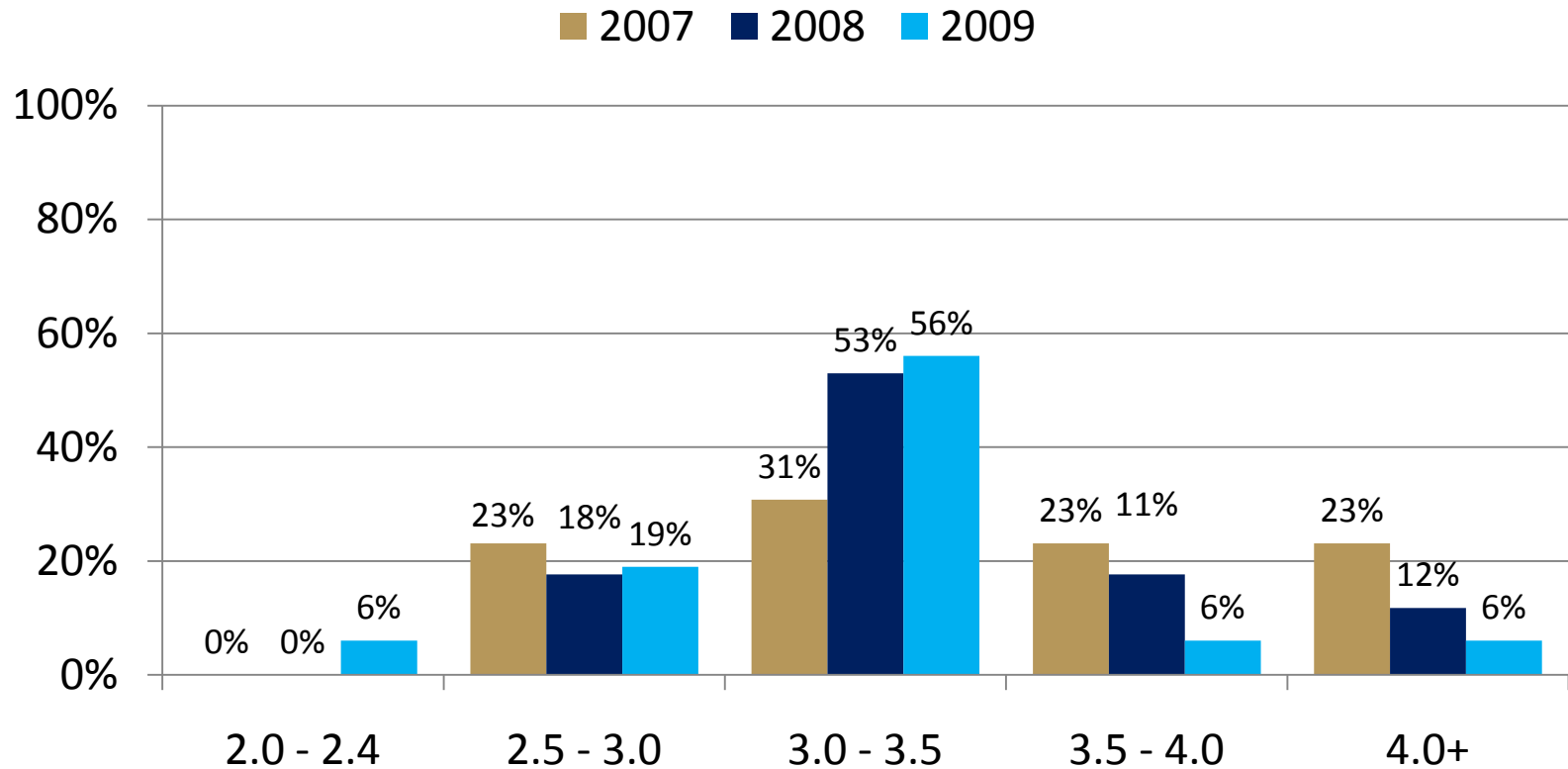
# Overview of 2010 ASC Valuation Survey

- Generally, valuation multiples have decreased during the last year
- With the exception of Plastic Surgery, all surgical specialties are viewed as desirable in an ASC
- Out-of-Network ASCs continue to be priced lower
- Survey respondents are split evenly between those who believe the acquisition activity is decreasing, staying the same, and increasing.

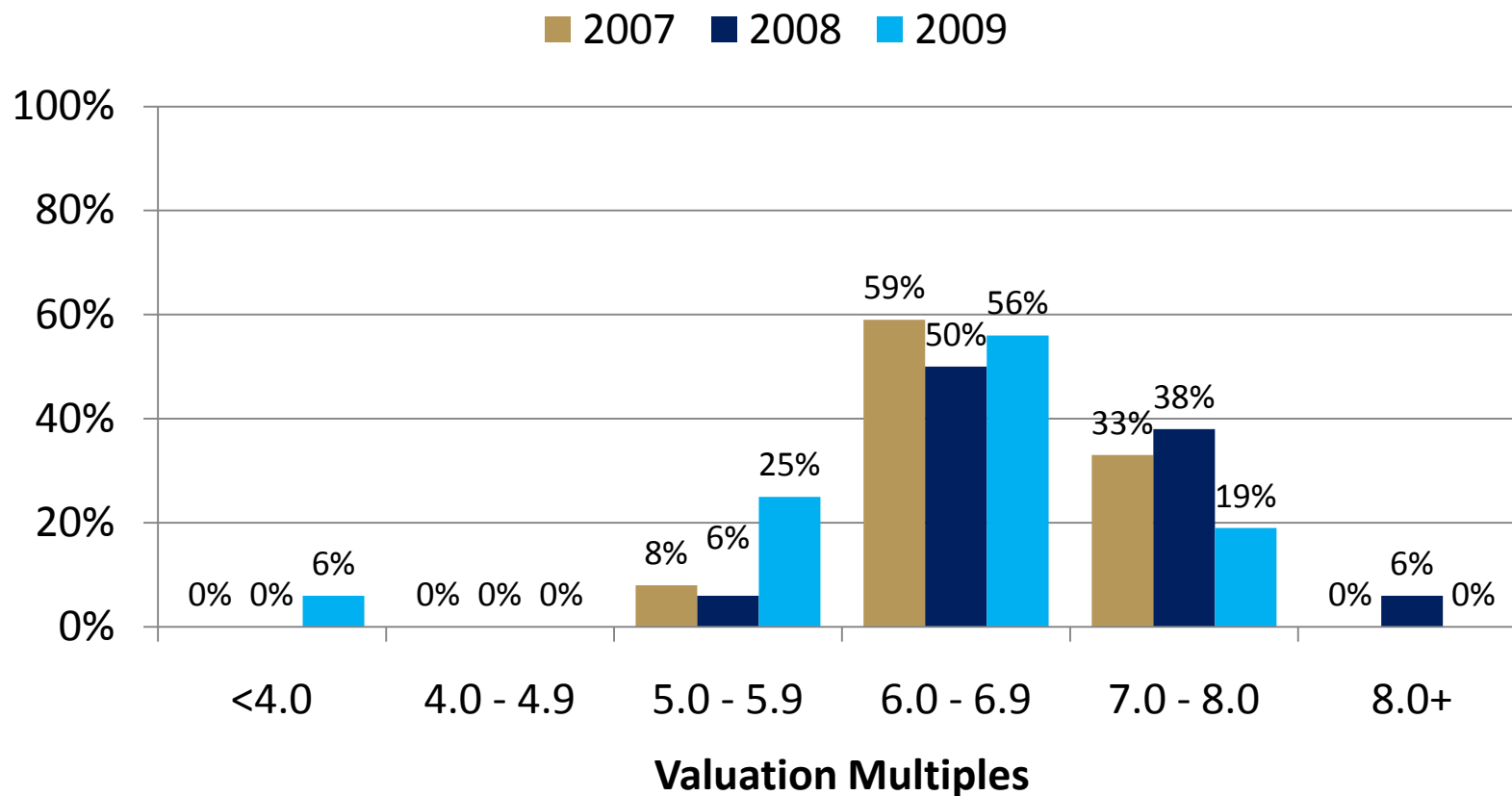
# Minority Interest Redemptions



# Minority Interest Buy-Ins



# Controlling Interest Valuation Multiples



# Preferred Surgical Specialties

Data sorted by specialty most desired to least desired

	Undesirable	No Preference	Desirable
General Orthopedics	0%	6%	94%
Orthopedic Spine	0%	12%	88%
Ophthalmology	12%	6%	82%
ENT	0%	24%	76%
Pain Management	0%	24%	76%
GI	12%	18%	70%
General Surgery	0%	35%	65%
Podiatry	12%	29%	59%
Urology	18%	35%	47%
GYN	12%	59%	29%
Plastic Surgery	82%	18%	0%

# Impact of Out-of-Network Strategy

Impact Expressed in Multiples of EBITDA	% Respondents
<0.25x	12%
0.26x - 0.50x	29%
0.51x - 0.75x	6%
0.76x - 1.0x	35%
>1.0x	18%

## Other Notable Observations

- 69% of Respondents list EBITDA as the primary earnings measure relied upon. Others rely upon Cash Flow.
- 88% of respondents report paying a premium of greater than 0.25x to acquire an ASC in a CON state; 18% report paying a premium of greater than 1.0x
- 71% of respondents indicate that new physician investors are required to personally guarantee a pro rata share of the ASC debt.

# Responding Companies

- American Surgical Centers
- ASCs, Inc.
- ASC Strategies, LLC
- Accent Partners
- Community Care, Inc.
- Covenant Surgical Partners, Inc.
- Elite Surgical Affiliates
- Facility Development and Management, LLC
- Health Inventures
- Nikitis Resource Group
- NovaMed, Inc.
- Practice Partners in Healthcare, Inc.
- Regent Surgical Health
- Surgical Care Affiliates
- Symbion Healthcare
- Titan Health Corporation
- The C/N Group, Inc.



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