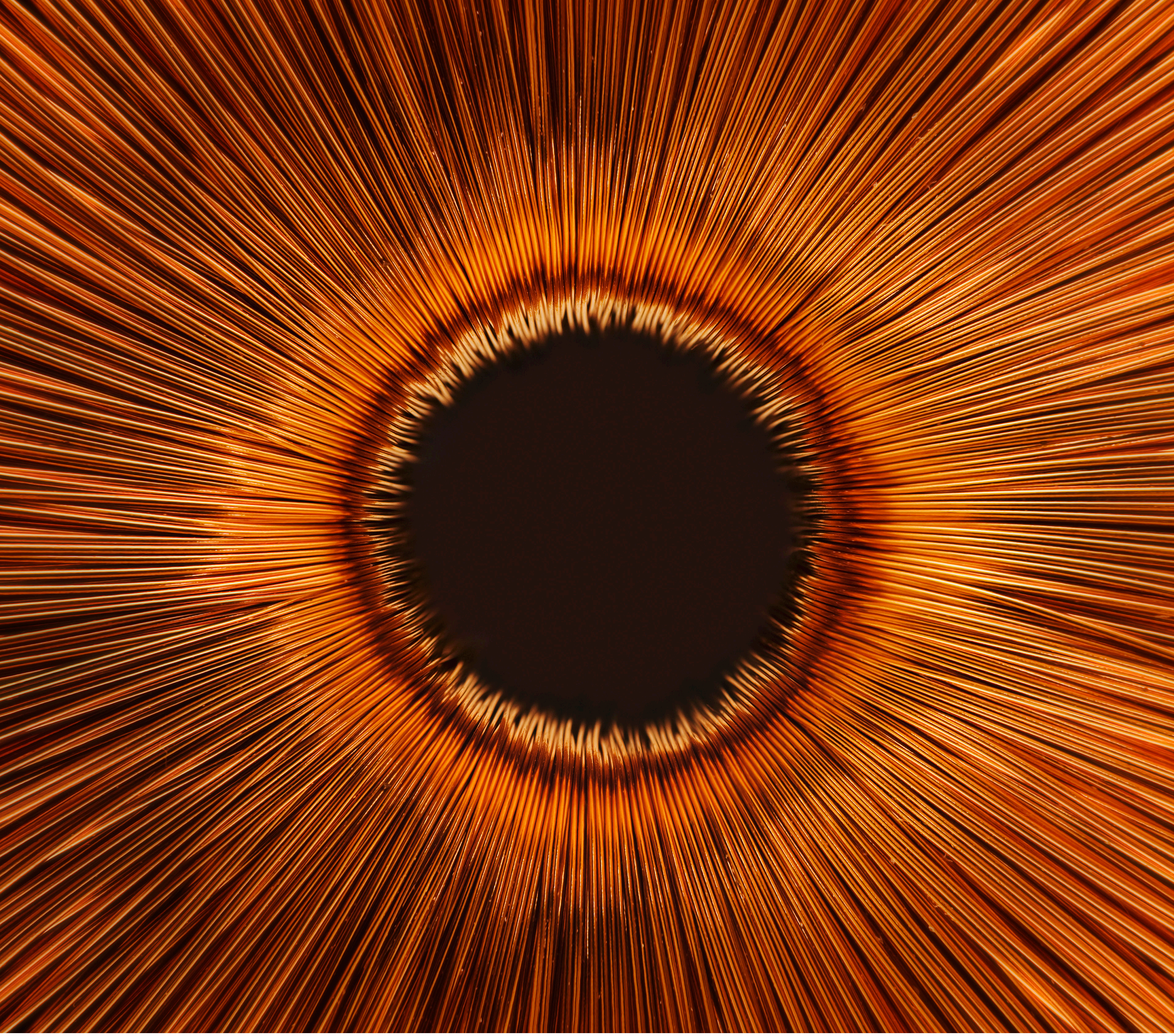


VECTOR MEDICAL GROUP

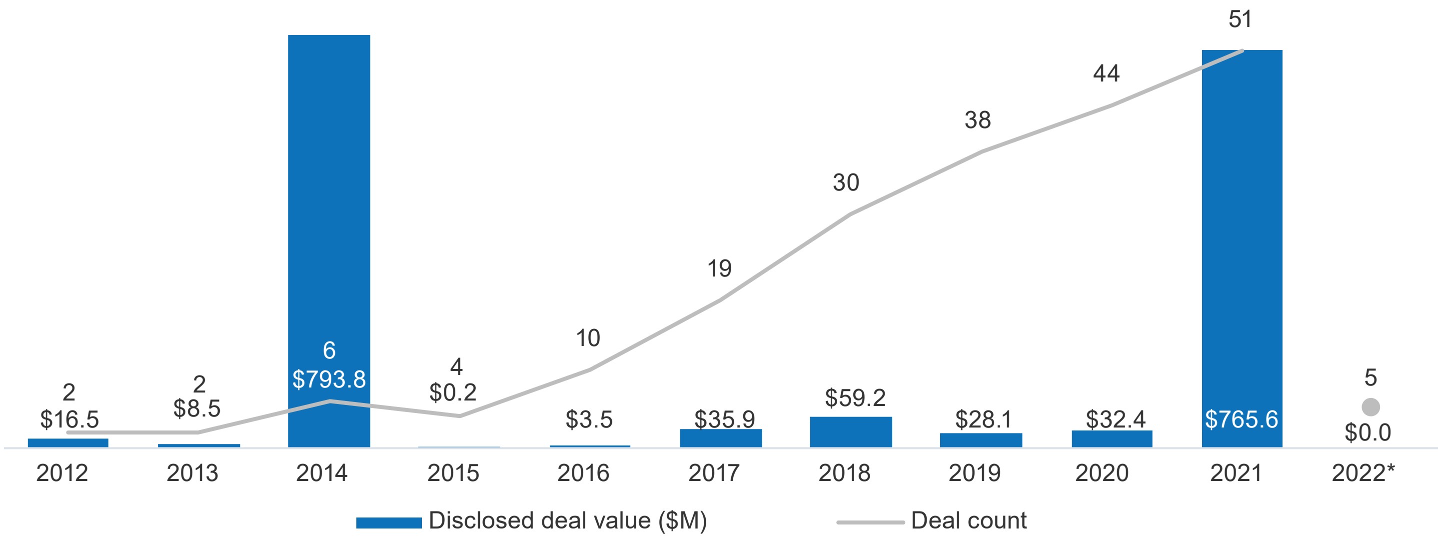
EPSTEIN BECKER GREEN

# US Ophthalmic Market: A Wave of Consolidation

Data provided by PitchBook

# Buy-and-build fueling growth

**US ophthalmic inpatient & outpatient services PE deal activity**




Source: PitchBook | Geography: US | *As of March 31, 2022

Private equity (PE) dealmaking in ophthalmology has surged in recent years. PitchBook statistics show a tenfold increase in deal flow between 2015 and 2020. Although it's difficult to collect reliable dollar amounts, large transactions are taking place. In November 2021, Cincinnati Eye Institute was purchased for $600.0 million by EyeCare Partners, an ophthalmic platform owned by Partners Group.

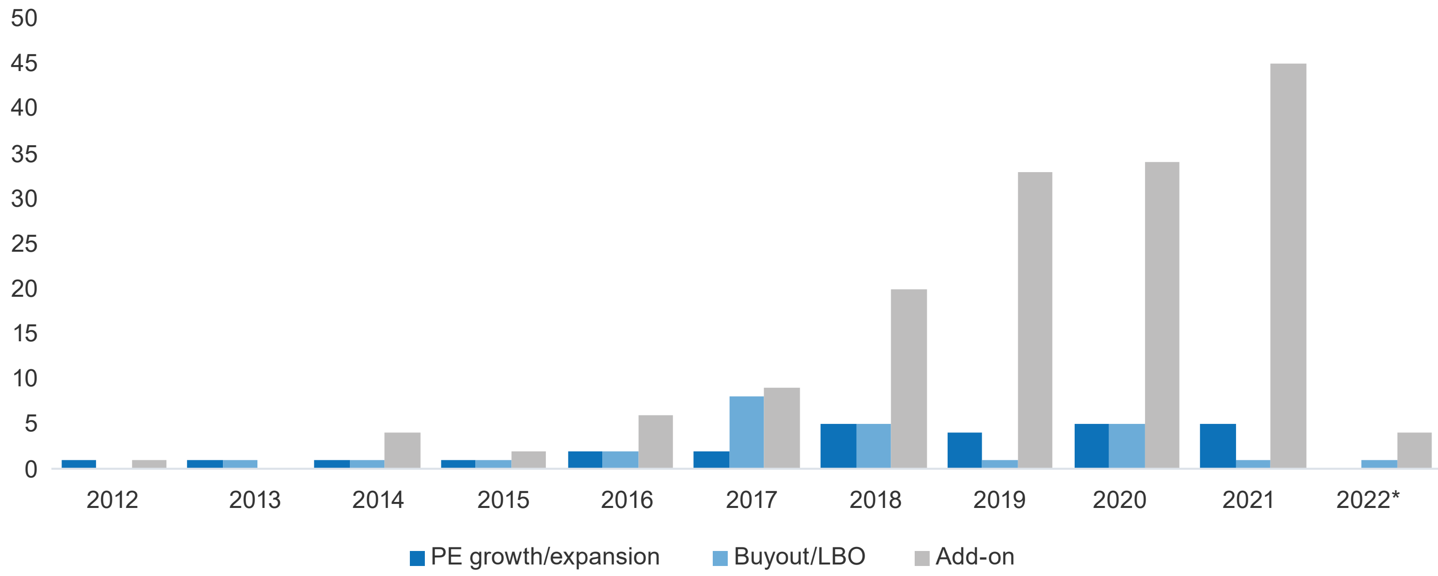
EyeCare Partners is emblematic of a larger PE trend within ophthalmology: rapid consolidation tied to regional expansion for platform companies. EyeCare Partners was acquired by Partners Group in February 2020 for a reported $2.2 billion. Over the past two years, EyeCare Partners has acquired ophthalmic practices throughout the country, building on Partners Group's effort to build a national ophthalmology brand. In a similar vein, Vision Innovation Partners, backed by Centre Partners, has made more than a dozen add-ons as it builds itself into a regional provider in Maryland, Virginia, and Eastern Pennsylvania. EyeSouth Partners, which was created from the ground up by Shore Capital Partners, is making similar moves in Georgia, Florida, Texas, and other southern states.

The buy-and-build approach is largely responsible for the wave of dealmaking since 2017. Last year, for example, 45 of 51 PE transactions—or 88%—were add-ons. In each of the past three years, add-ons have accounted for at least 75% of deal flow (see next page). Add-ons often involve smaller practices that can provide a geographic toehold for the PE-backed platform. Like other healthcare specialties, ophthalmology is a fragmented market that can benefit from a more centralized structure and future cost savings.

### *Methodology

All datasets are sourced from PitchBook, and all traditional healthcare industry codes correspond to existing industry codes for healthcare in the PitchBook Platform. Ophthalmology-specific data is derived from a combination of keywords and a primary industry code tag to identify companies within the ophthalmic space. These datasets include ophthalmic practices and platforms, surgery centers, ophthalmic rehabilitation providers, device companies, and other ophthalmic product manufacturers.

## US ophthalmic inpatient & outpatient services PE deal count by type




Source: PitchBook | Geography: US | *As of March 31, 2022

## Select PE investors active in ophthalmology practices

| Investor |
|---|
| Centre Partners |
| Shore Capital Partners |
| Partners Group |
| Chicago Pacific Founders |
| LLR Partners |
| Harvest Partners |
| Quad-C Management |
| Waud Capital Partners |
| H.I.G. Capital |
| Duchossois Capital Management |

Source: PitchBook | Geography: US

## Select PE-backed ophthalmology practices (actively expanding)

| PE-backed platform |
|---|
| Vision Innovation Partners |
| EyeCare Partners |
| EyeSouth Partners |
| EyeCare Services Partners |
| SightMD |
| Eye Health America |
| NJRetina |
| Unifeye Vision Partners |
| Sunvera Group |
| Midwest Vision Partners |
| Comprehensive EyeCare Partners |
| Atlantic Vision Partners |
| Cincinnati Eye Institute |

Source: PitchBook | Geography: US

## Select 2021 transactions

Advanced Ophthalmology Associates, alongside Clavenna Vision Institute, was acquired by Sunvera Group (Ridgemont Equity Partners) in December 2021. Based in Michigan, Advanced Ophthalmology Associates was founded in 2002, and Clavenna Eye Institute was founded in 1965.

Southwest Eye Institute, an El Paso-based practice founded in 2004, was acquired by American Vision Partners (H.I.G. Capital) in March 2021. Southwest Eye Institute marked the eleventh acquisition for American Vision Partners, which grew its footprint in Texas and New Mexico.

Cincinnati Eye Institute, a Cincinnati-based provider founded in 1945, was acquired by EyeCare Partners (Partners Group) in November 2021 for a reported $600.0 million. Cincinnati Eye Institute was already supported by PE firm Revelstoke Capital Partners before the merger.

Eye Associates Northwest, a Seattle-based practice founded in 1993, was acquired by Comprehensive EyeCare Partners (Gauge Capital) in November 2021. Eye Associates Northwest has 17 doctors across its clinical practices, optical shops, and one ambulatory surgery center.

Eye Centers of Florida, a Ft. Myers-based provider founded in 1971, was acquired by Eye Health America (LLR Partners) in August 2021. Eye Health America was formed by LLR Partners in 2018.

MidAtlantic Eye Care, along with four other ophthalmology practices, was acquired by Atlantic Vision Partners (Sheridan Capital) in December 2021.

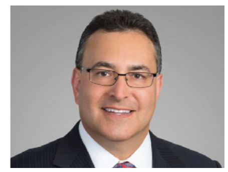
Ophthalmic Associates, a Western Pennsylvania practice founded in 1905, was acquired by Vision Innovation Partners in September 2021. Vision Innovation Partners was founded in 2017 and has expanded across Maryland, Washington DC, Virginia, and Pennsylvania.

Pacific Eye Surgeons, alongside Eye Care of La Jolla, was acquired by Unifeye Vision Partners (Waud Capital Partners) in August 2021. Pacific Eye Surgeons was founded in 2004, while Eye Care of La Jolla was founded in 1986.

Texan Eye Care, a Central Texas practice with locations in Austin and Cedar Park, was acquired by Comprehensive EyeCare Partners (Gauge Capital) in August 2021. Texan Eye was founded in 1969 and employs 17 doctors and surgeons.

# Q&A with Dana L. Jacoby and Gary W. Herschman

**Dana L. Jacoby**
*CEO*
*Vector Medical Group*



**Gary W. Herschman**
*Board of Directors*
*Member of the Firm*
*Epstein Becker Green*

**What dynamics are fueling today's ophthalmology market, especially private equity's (PE's) push to grow their portfolio companies through dozens of add-on acquisitions?**

We are seeing some fundamental changes in the healthcare financial market. Most practices weathered the pandemic only to face other economic uncertainties brought on by inflation, global instability, and an increasingly volatile market. At the same time, investors have set aside more than $730 billion of dry powder. Many of those investors view the healthcare industry as a top sector for investment because of the aging American population, the relative wealth of the baby boomer sector, and advances in medical technologies. As a result, many believe healthcare is somewhat recession-proof and that new technologies and approaches to high-quality and cost-effective care will result in increased value opportunities when properly scaled.

Specifically, the eye care market has been actively consolidating for more than10 years. Even though there are around 30 investor platforms in this space, the market remains highly fragmented because there continue to be many smaller practices across the country. Those providers are increasingly challenged by volatile reimbursement models, increased competition, and outside market forces. Keep in mind that the majority of doctors are now employed by either private equity platforms, national companies, or hospitals. Those doctors whose practices are still community-based are, on average, in their late 50s, and many of them are interested in "monetizing" their practices and taking some cash now rather than waiting for retirement (when they may not be able to sell their practices at high valuations). Consequently, the hot market and high practice valuations seem to present a perfect opportunity to transact.

PE has consolidated practices to create platforms of professionally managed eye care groups. They are looking for opportunities to build even larger platforms. Specifically, they have done the hard work of creating synergies across their acquired practices by reducing management expenses such as conducting patient billing, maintaining EMRs (electronic medical records) and combining other administrative tasks in central, more efficient operating models. In addition, PE investors may have generated increased revenues through broad-based marketing and other enhancements to increase demand. PE companies also provide capital to expand profitable opportunities such as new locations, better medical equipment, and expanded product offerings. For example, many eye care platforms are adding new specialties, such as retina (to keep referrals within the organization), as well as adding ambulatory surgery centers (ASCs) and other new diagnostic and treatment modalities. Taken together, these activities produce more profitability and arguably better outcomes for patients.

PE investors have access to a mountain of "dry powder" (capital to invest) and are interested in adding more geographies to their mix to further consolidate markets and revenue opportunities. Ultimately, those increased revenues will be shared between physicians and PE investors.

Practices that have previously passed up PE opportunities are now facing greater headwinds and lack access to professional management and financial capital that would help them successfully navigate challenges such as the following:

a. Changing reimbursement and regulatory programs may increase practice risk by creating uncertainty for future cash flows;

b. Consolidating within markets could result in larger and better-capitalized competitors that may erode a practice's market share;

c. Reducing referral sources from increasingly larger organizations such as Optum, etc., will reduce access to new patient sources;

d. Shifting from fee-for-service to value-based payment structures and establishing population health and risk programs may benefit larger and better-capitalized practices; and

e. Direct contracting with self-insured employers will become more commonplace for larger practices and platforms.

There can be no question that physician practices with extensive corporate infrastructure—including seasoned executives, substantial capital, and broad-based synergies—are best positioned to adapt and pivot based on existing and future challenges, and benefit from enhanced profitability.

The desire to monetize practices is another key factor in the highly active and growing healthcare consolidation that is underway.

Medical practices are at (or near) the height of their market value because risks such as reduced cash flow, inflation, and other factors could erode future valuation. Traditionally, in times of inflation capital markets look to other opportunities for investment that involve greater cash flow and less risk, such as real estate and precious metals. Thus, the window of opportunity for a practice to transact may be closing. If a practice misses that opportunity, the future valuation may be lower than its current valuation.

Also, many physicians recognize potential risks and uncertainties in the healthcare industry (see factor a, below) and are entering into transactions to "take some chips off the table" at the height of the market. Those physicians will receive significantly larger checks (sometimes in the multi-million-dollar range), with the ability to invest in current markets for even more net returns. Furthermore, advantageous long-term capital gain tax rates—versus 18–20% higher "ordinary income" rates—could be short-lived depending on results of upcoming mid-term Congressional elections and the 2024 presidential election.

Moreover, investor platforms that partner with medical groups in these transactions likely will be exiting their investments within 3–6 years (aka "second bite" transactions). Investors' equity—as well as the physicians' rollover equity—will normally increase 2–4 times during the initial investment period and result in a second-bite "liquidity" event for the physicians, who generally will cash out 50–75% of such increased value, which can then be invested as the physicians see fit.

**What dynamics are affecting ophthalmology practice valuations?**

Ophthalmology, like some other medical specialties, is impacted by two factors. First, baby boomers are living longer. Fewer than two decades ago, it wasn't reasonable to suggest life expectancy into the 80's or 90's. That is becoming more frequent. Second, the increasing pool of octogenarians is demanding more from its lifestyles, meaning they are more inclined to spend money for a better quality of life. In the instance of ophthalmology, the baby boomers simply want to maintain their vision capabilities for longer, and this is driving significant investment in the eye care space.

According to reported statistics, almost 60% of eye care physicians are employed by practices with three or fewer providers. What impact does that have on their operations, and why does that represent an opportunity to partner with a PE group?

Eye care physicians in solo or small practices face the increased risks outlined above. For example, the costs of new EMR programs can be spread across scores of doctors who are part of a larger platform but must be borne by just a few doctors in a smaller practice. The current transformation underway in the healthcare industry, as well as the growing competitive challenges, clearly favor larger practices with seasoned executives and other corporate infrastructure. So, it gets increasingly more difficult to remain independent.

**What factors should ophthalmology practices consider when a PE transaction becomes available?**

We would recommend that ophthalmology practices consider the following checklist of factors to help assess the benefits of a PE transaction:

a. What are the market challenges that create cash-flow risk to the practice?

b. What is the level of competition within the local market?

c. What is the desire of the physicians within the practice to monetize their equity now versus later (with less certainty on value)?

d. What are the capital requirements needed for the practice to compete and grow within the current market framework?

e. What is a potential PE partner's track record in consolidating and improving other ophthalmology practices?

f. What is the cultural fit of potential PE partners in terms of personality, approach, trustworthiness, and future vision?

## *Physician group M&A market trends*

*The emergence of investment from new buyers such as vertically integrated payers/strategic buyers and private equity firms/financial sponsors has expanded the strategic options available to healthcare providers.*

### *Hospitals/health systems*

Pros

- *Referral network*
- *Guaranteed compensation*
- *Stronger clinical operational knowledge and capabilities*
- *Geographic congruency*

Cons

- *Least favorable financial considerations*
- *Lack of equity ownership opportunity*
- *Lack of focus on physician enterprise and rates (versus inpatient rates)*

### *Payers/strategic players*

Pros

- *Increased access to strategic date and technology infrastructure*
- *Greater access to population health capabilities*
- *Risk and shared savings arrangement expertise*
- *Attractive financial considerations*

Cons

- *Decreased clinical and operational autonomy, compensation guarantee*
- *Potential lack of cultural alignment*
- *Reluctance to be employee of payor*

### *Private equity*

Pros

- *Performance incentives*
- *Entrepreneurial growth-driven model*
- *Upfront cash consideration and potential "second bite at the apple" and additional liquidity events*

Cons

- *Potential lack of operational and/or specialty-specific experience*
- *Potential decreases to guaranteed compensation in lieu of upfront cash consideration and future equity appreciation opportunities*
- *Potential lack of cultural "fit" with financial-driven investors*

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