the braff group

marketWATCH

HOME HEALTH & HOSPICE

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Generally speaking, M&A results for home health and hospice in the second quarter of 2014 remained strong.

Based on proprietary transaction data gathered and analyzed by The Braff Group and illustrated in the charts below, although Q2 figures for home health were down somewhat vs. the first quarter, through the first six months of the year, Medicare certified home health deal flow is up nearly 29% vs. the same period last year (45 deals in 2014, 35 in 2013). As for hospice, the sector is on a roll, generating 10, 10, and 9 deals for each of the past three quarters respectively. Moreover, hospice activity through June is up nearly 27% vs. the same period in 2013 (19 vs. 15).

Moreover, the nature of the transactions during the period was impressive.

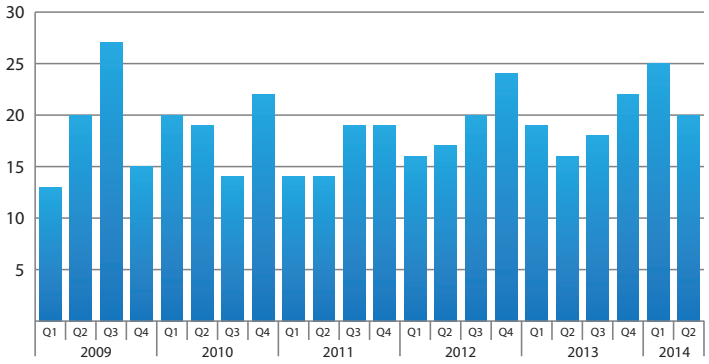
Big deals remain in vogue. The quarter saw transactions involving VNA-TIP, a statewide home care provider in Missouri (and a Braff Group client), Great Lakes Caring, a large, private equity sponsored home health and hospice company that covers much of Michigan, and Southern Care, a multi-state hospice company that was held by PE sponsor Kohlberg & Company. Additionally, while not technically a Q2 transaction, Q3 opened with the sale of Residential Home Health and Hospice, another leading provider of home health and hospice in MI and Illinois (and also a Braff Group client).

And let's not forget that Kindred is still pursuing Gentiva, which now has competition from another unnamed buyer (reported to be Formation Capital, a private equity group whose portfolio includes Genesis HealthCare, which itself recently announced its intent to merge with Skilled Healthcare Group, creating a colossus in senior housing). Whew.

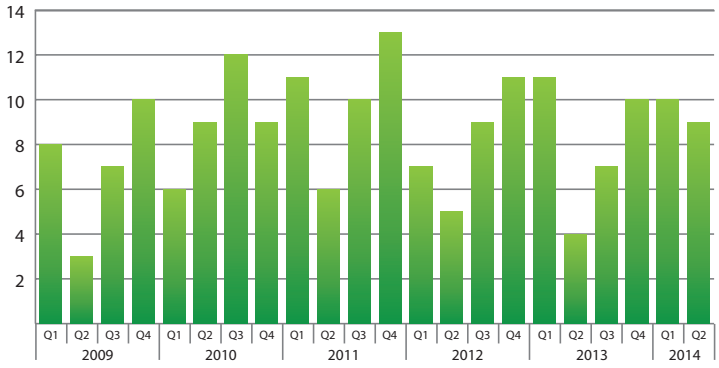
Moreover, the regulatory environment continues to be benevolently benign. In its annual rite of summer, CMS issued rules on reimbursement for home health and hospice. And the world continued to spin on its axis.

On the hospice front, hard as it is to imagine to sectors like home medical equipment that has seen cuts of up to 40% over the past 5 years, ***the lead story is that pricing for 2015 is going up 1.4%.*** While this was the primary takeaway for hospice acquirers and investors, there is an item buried below the lead that has not gotten as much attention, but could turn out to be the issue that tips the scales for some providers in favor of a possible sale. In staying true to its long-term theme of modifying reimbursement to discourage

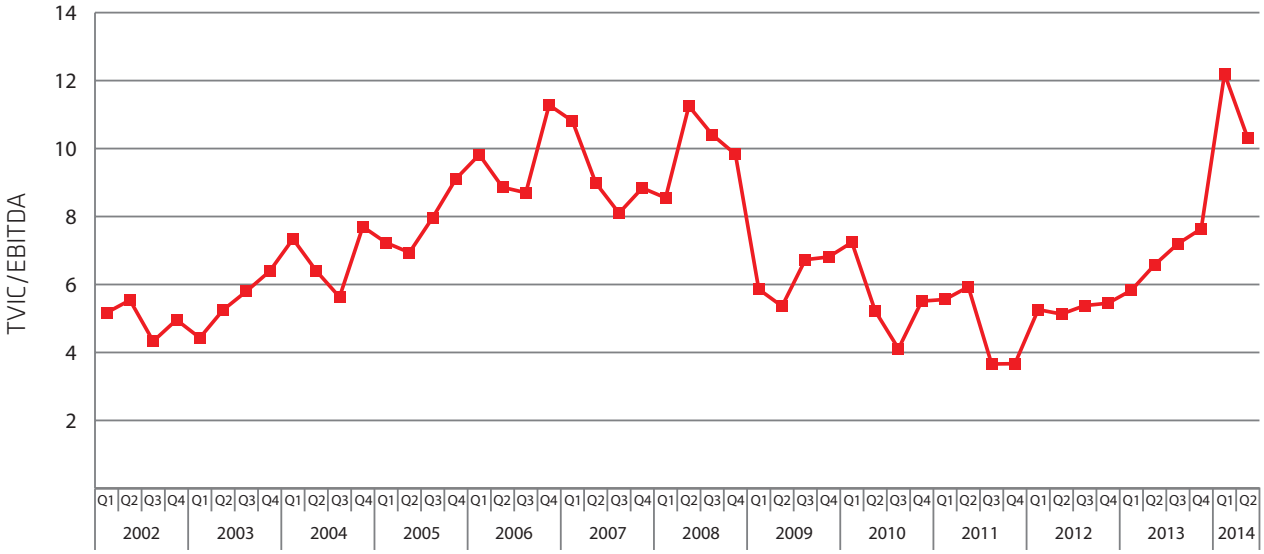
Medicare Certifies Home Health Deal Trends



Hospice Deal Trends



Median Total Value of Investment Capital/EBITDA for Publicly Traded Home Health Companies



unnecessarily long lengths of stay, in its final rule, CMS indicated that within five months of the end of the hospice calendar year, providers must complete and submit their aggregate cap determination, ***with remittance of overpayments as necessary,*** or risk suspension of future payments. Per CMS, "current practice is for the Medicare contractors to complete the hospice cap determinations about 16 to 24 months after the cap year in order to demand any overpayment." This substantial acceleration of repayments will likely make it far more difficult for providers to comply, unless they plan in advance and accumulate cash reserves if they believe they are on the cap "bubble." So in the end, the final rule is generally favorable for providers that are well within statutorily targeted lengths of stay, but less so for those that continue to struggle managing this challenge.

On the Medicare certified home health side of the ledger, after you slog your way through the tortuous labyrinth of technical adjusters, where an increase is really a decrease, and a 3.5% cut really isn't, the net effect on reimbursement amounts to a slide of three tenths of one percent. Moreover, the industry won both an administrative and psychological battle of wills with CMS as the agency walked back the depth and breadth of physician documentation requirements. Administratively, providers will find it at least a little easier to comply with face-to-face requirements. And in the battle for the regulatory moral high ground, the industry gained some ground with the relaxation by CMS of previously more onerous pronouncements – a concession that may (and we emphasize may) signal at least some softening of the body's seemingly reflexive opposition to any relief in the increasingly mind-bending gyrations an agency must go through to get paid.

These developments have only bolstered the collective wisdom that the reimbursement climate for Medicare certified home health, if not positive, is at least predictable – and manageable – and will likely remain so, at least through the end of rebasing initiatives in 2017.

Perhaps then, it should come as no surprise, that the conversion of (a) a vibrant, highly visible, and competitive M&A market with (b) a comparatively benign reimbursement climate and (c) economic conditions that are increasingly reminiscent of the pre-recession bubble (see below), that the median Total Value of Invested Capital (TVIC)/EBITDA valuation metrics for the publicly traded home health companies have returned, at least for now, to the peak levels reached in 2007-2008.

Welcome news for home health and hospice providers considering a sale.

Call us to see how we can put our experience to work for you.

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