HOME HEALTH & HOSPICE

WITH A STRONG ASSIST FROM HOME HEALTH AND HOSPICE, HEALTH CARE SERVICE M&A RISES 34%

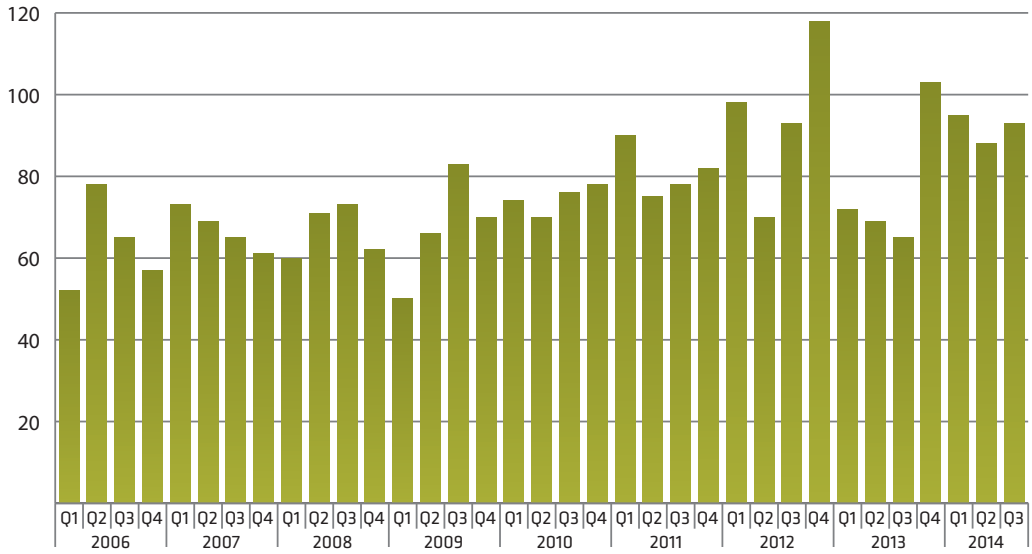
After an unexpectedly sluggish first quarter for health care service deals in aggregate – results that were consistent with other investment data points reported by other outlets – we went on record suggesting that with *"far more evidence to predict an upswing than there is to explain a downturn … we anticipate another strong year of volume and valuation."*

As it turns out, we're pretty good at reading the tea leaves.

Based upon proprietary data collected and analyzed by The Braff Group and illustrated below, despite the slow start, **aggregate deal volume through the third quarter year-to-date is up a stunning 34% in 2014 vs. the same period last year.** Notably, Q3 2014 results alone were more than 40% ahead of the same period last year.

Furthermore, the past four quarters have produced the most transactions – 379 – that we have ever seen during any previous four quarter period — far more than the then record tallies posted in 2010 and 2011 as recession weary investors turned to recession resistant health care, and just eclipsing the four quarter period in 2012 that culminated with the all-time record tally for a single quarter as sellers rushed to beat expected increases in capital gains taxes.

All Health Care Services Deal Trends



As is evident in the figures below, every sector has contributed to the M&A blowout, with home health care and hospice posting growth of 10% and 9% respectively year-to-date. But good as those figures are, they trail the other health care services we cover. Top dog thus far is health care staffing which has pulled a Rip Van Winkle and re-awakened with a bolt of 288% due to (a) a declining unemployment rate and (b) speculation that a shortage of doctors and nurses will be even shorter given reform initiatives.

While the home health and hospice M&A numbers look good year-to-date, the most recent quarterly trends appear to signal a possible change in sentiment. But in this case, we confidently emphasize the word "appear," as the buzz around these sectors is, in truth, becoming a veritable rumble.

Consider the following: The past 60 days alone have produced two of the most significant, high profile, strategically innovative, and confidence signaling deals in recent memory.

First was the completion of the months-in-the-making acquisition of Gentiva Health Services by Kindred Health care, followed shortly thereafter by the acquisition of Encompass Home Health and Hospice by once-left-for-dead HealthSouth. These deals are notable not only for the wager these buyers are making on the value of a post-acute continuum, but for their audacity of scope (a billion plus for Gentiva, three quarters of a billion for Encompass).

And these deals are not alone.

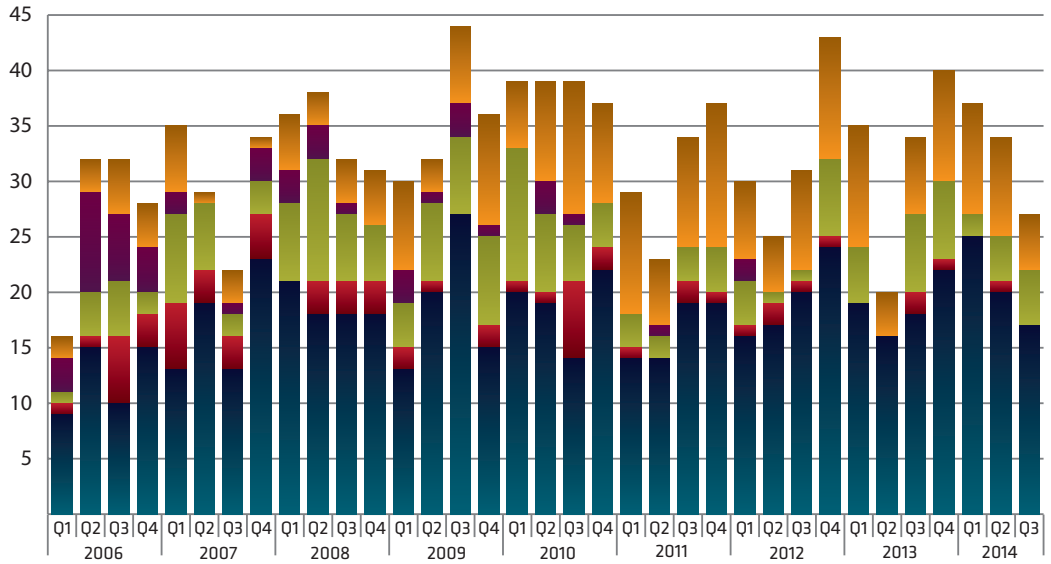
Buyers increasingly anticipate a relatively clear reimbursement runway for home health and hospice. Pair this with the demographic wave and emerging delivery – and reimbursement – models that will incent care in the lowest cost setting (i.e. at home), you have the makings of a credible investment thesis. That's why a deep dive into The Braff Group's proprietary data reveals that, after a three year hiatus, the willingness to make big bets in home care is back. And so, then, is acquisition demand from consolidators to acquire providers – small and all – in order to create the inventory for the next tier up.

So despite numbers that are trending down, the market is actually decidedly up.

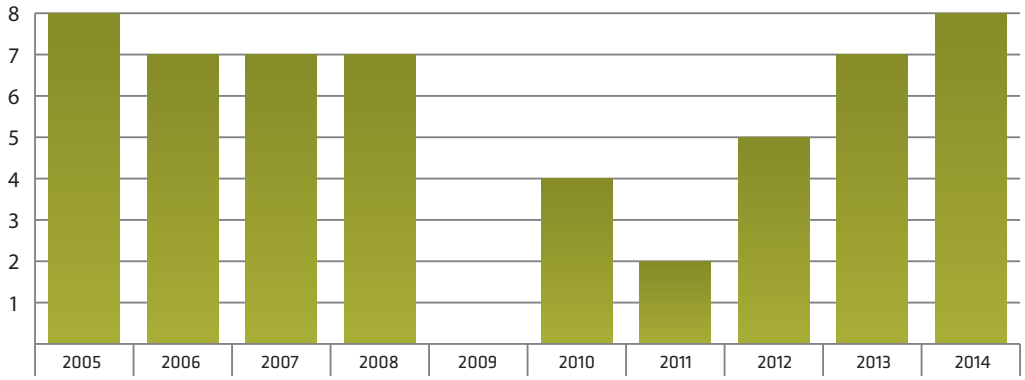
Third Quarter 2014 M&A Activity

Third Quarter 2014 M&A Activity	2014 Q2	2014 Q3	Change	2013 Q2	2014 Q3	Change	2013 YTD	2014 YTD	Change
Home Health Care	25	22	-12%	27	22	-19%	67	74	10%
Hospice	9	5	-44%	7	5	-29%	22	24	9%
Staffing	10	12	20%	5	12	140%	8	31	288%
Home Medical Equipment	18	14	-22%	9	14	56%	40	47	18%
Pharmacy Services	4	14	250%	6	14	133%	17	29	71%
Behavior Health & Social Services	22	26	18%	11	26	136%	52	71	37%
Total	**88**	**93**	**6%**	**65**	**93**	**43%**	**206**	**276**	**34%**

Home Health & Hospice Deal Trends by Segment



Large Medicare Certified Home Health Deal Trends

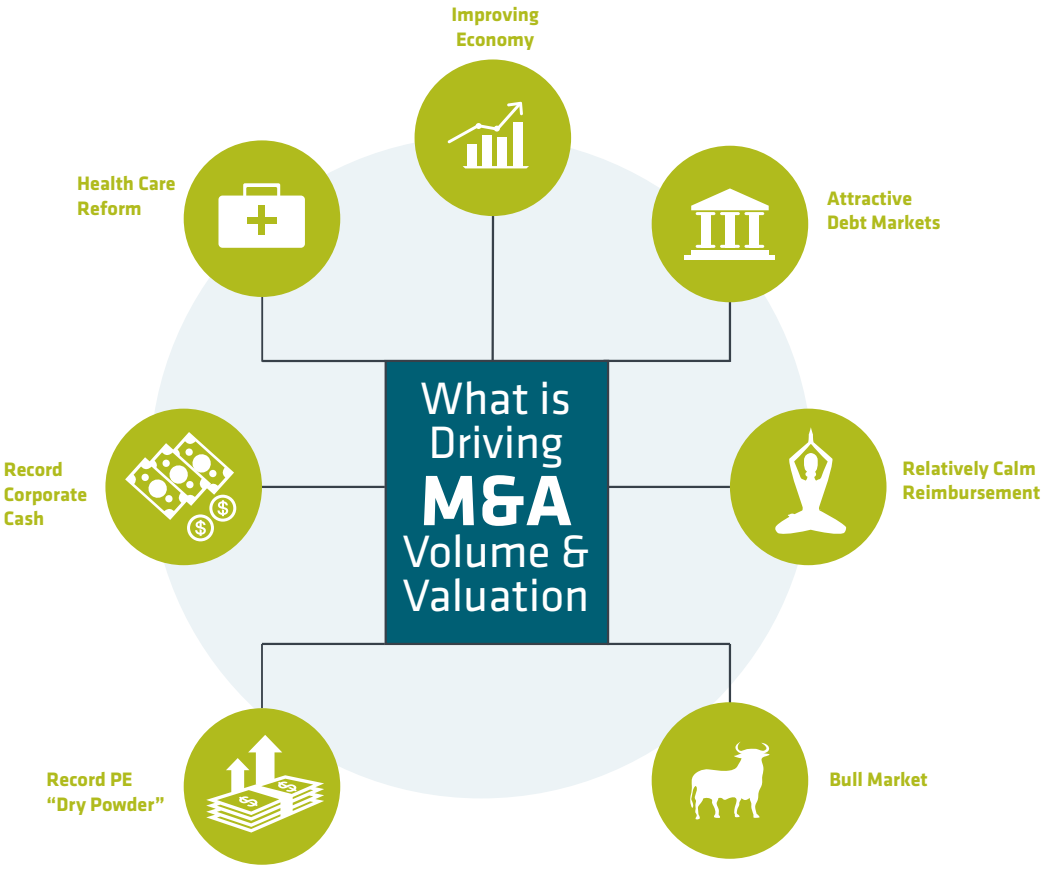


Why the Across the Board Run Up?

As we foreshadowed several months ago in our *viewPOINTS* commentary, *"Are We In the Midst of an M&A Bubble? "*, numerous factors such as a record-breaking stock market, more than 2 trillion in idle private equity and corporate cash, a relatively predictable reimbursement climate, a confidence building improving economy, and expectations of increased utilization driven by healthcare reform have converged to produce a climate ripe for extremely robust deal flow – and valuation.

Any one of these developments could create a spike in activity, but put them all together… you have a year of Black Fridays.

Factors Driving M&A Volume And Valuation



Outlook: What Will Bring It All Down?

Bubbles are fragile by nature. They rise fast – and often unexpectedly. And they deflate much the same way. Fast – and unexpectedly.

While we don't know the timing, we can guess the pressure points.

- A derailment of the stock market, possibly by external events – the middle-east, the Ukraine, domestic unrest, etc.
- A sudden and sustained reversal of the economic recovery, perhaps due to what many suggest is an inevitable rise in inflation and/or interest rates.
- A significant change in reimbursement policy. Right now, the current thinking in home health is that re-basing reductions through 2016 insulate the sector from further cuts for the time being. As for hospice, it's kind of like the X Files. A wholesale change in reimbursement methodology is "out-there", but mysterious government operatives aim to keep it hidden away. That said, sectors like home health and hospice are subject to "stroke of the pen" Medicare and Medicaid risk, and there are no shortage of pens lying around in Washington.
- Failure to deliver on the promise of healthcare reform. Right now, investors are giddy with the expectation of more covered beneficiaries, home care friendly delivery models, and the increases in utilization (i.e. revenues) that come with it. But if the promise doesn't live up to the hype (as is quite possible given the number and interplay of all the moving parts that drive health care spending), a market that's fickle can quickly become a trickle.

But the Grinch won't steal Christmas this year.

We expect 2014 to close out in record-breaking fashion.

THE BRAFF GROUP DIFFERENCE

Since the firm's inception in 1998, we have closed more than 245 transactions, more than any other mergers and acquisitions advisory firm covering like sectors.

According to Thomson Reuters, The Braff Group ranked # 1 in health care mergers and acquisitions advisory services in 2009, 2011, 2012, and 2013 and for the six year period from 2008 through 2013. Four Time Winner Health Care Deal of the Year.

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

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