

PERSPECTIVES

A health care merger & acquisition quarterly review



Home Health and Infusion Therapy Sectors Post Record Deal Activity

Total Transaction Volume Keeps Pace with 2006

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After declining 14% from 2005 to 2006, total 2007 deal volume in the home health care, infusion therapy, specialty pharmacy, hospice, health care staffing, and home medical equipment sectors essentially kept pace with last year with 225 deals versus 227 in 2006. While aggregate transaction volume remained about the same, sector specific activity varied widely, with half the sectors we track posting gains, while the other half saw fall-offs in acquisition volume.

In this report, drawn predominately from proprietary information gathered and analyzed by The Braff Group, we take an in-depth look at the past year's M&A activity and the numbers behind the numbers, to gain a better understanding of this vibrant, yet ever-changing market.

Highlights: The Details Behind the Numbers

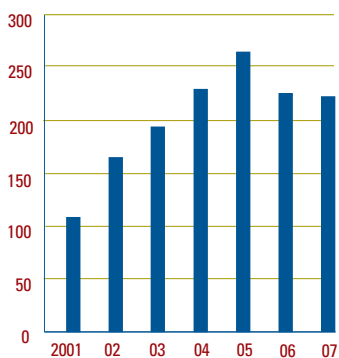
(See charts and tables throughout this document for further details)

Buyer Activity: All Sectors

- Overall, we saw an increase in unduplicated buyers with 145 in 2007, up 8.2% over 2006. With total transaction volume holding steady, transactions per unduplicated buyer fell 8.4%, from 1.69 deals in 2006 to 1.55 in 2007. From a seller's perspective, both are extremely favorable developments. As the breadth of acquisition demand rises, competition for deals escalates, nudging valuation upwards.
- In analyzing the breakdown of deal volume between public and non-publicly traded buyers, we saw a substantial proportional increase in activity from the non-publics. While publicly traded buyers represented 32.8% of all unduplicated buyers in 2006, they accounted for only 21.4% of buyers in 2007, a decline of nearly 30%. Moreover, the public accounts accounted for 30.2% of all transactions in 2007, down dramatically from the 50.2% of deals they amassed in 2006. Aided, in part, by private equity's continued interest in health care services and an increasing number of savvy private buyers jumping into the acquisition fray to capture opportunities "below the radar", non-public buyers are a force to be reckoned with – another sign of the breadth – and therefore, health, of the current merger and acquisition market.

CHART A:

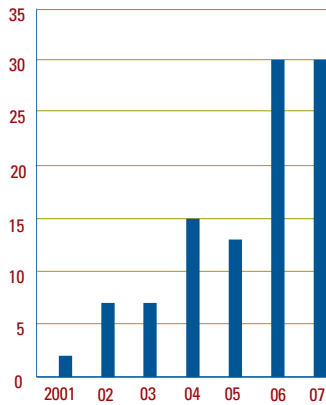
TBG Health Care Service Sector Transaction Volume



Source: The Braff Group

CHART B:

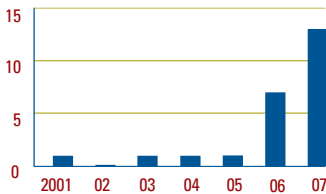
Private Equity Sponsored Home Health Transactions



Source: The Braff Group

CHART C:

Private Equity Sponsored Home Infusion Therapy M&A Transaction Volume



Source: The Braff Group

- The size and makeup of the top end of the merger and acquisition spectrum changed substantially in 2007. The total reported purchase prices of the Top 10 Deals of the Year in 2007 was \$4.01 billion, up more than 220% over the \$1.24 billion recorded in 2006. Moreover, median deal size was up 175%, from \$70.8 million in 2006 to \$194.7 million in 2007, the second highest median value posted since we began tracking the high end of the market. The makeup of the Top 10 also shifted dramatically, from a concentration in health care staffing in 2006 (four deals) to infusion therapy in 2007 (five deals). (See section on infusion therapy for more details)

Home Health Care

- Leading all sectors was the home health industry, with a record setting tally of 107 transactions, up nearly 14% over the then record 94 deals posted in 2006. Particularly noteworthy was that after a 28% fall-off in transaction volume from the second to the third quarter of the year, which we surmised could be attributable to buyer concerns regarding the potential – and as yet unknown – financial ramifications of PPS reform, the sector roared back in the fourth quarter with 27 deals representing a 59% surge in activity.
- With 107 transactions, the sector is the first to cross the 100 deal mark since we began analyzing health care service transaction activity in 2001.
- Once again, private equity was a major influence driving home health acquisition activity, accounting for 30 transactions, or 28% of total sector deal volume. That said, as **Chart B** indicates, PEG activity is flat compared to 2006. This is not unexpected. With the surge in transaction volume in the home health sector well into its fifth year, and with a more challenging reimbursement climate on the horizon, the investment window for private equity is beginning to close. Accordingly, we anticipate that PEG sponsored activity will begin to lessen in 2008, although we anticipate any slackening of demand will be taken up by increasingly aggressive strategic buyers.

Home Infusion Therapy

- In terms of year-over-year deal volume growth, infusion therapy led all sectors with a surge of nearly 32%, posting a record 25 transactions in 2007 versus 19 in 2006.
- As indicated above, five infusion transactions cracked the Top 10 Deals in 2007, led by Walgreen’s \$850 million acquisition of Option Care. Perhaps even more noteworthy is that during the six year period from 2001 through 2006, no IV deals made the list, making 2007 truly a watershed year in the sector.
- While transaction volume surged, so did the number of buyers targeting IV with 17 unduplicated buyers in 2007, up an extraordinary 42% over the 11 buyers in 2006.
- We also saw a continued surge in acquisition interest coming from the private equity community. While there were only four private equity sponsored transactions in infusion therapy during the five year period from 2001 through 2005, The Braff Group tracked seven in 2006 and 13 in 2007, a year-over-year spike of more than 85%.

CHART D:
Merger & Acquisition Transaction Trends

Sector	Deal 2006	% of Total	Deals 2007	% of Total	Change
Home Health Agencies	94	41.4%	107	47.6%	13.8%
Hospice	15	6.6%	10	4.4%	-33.3%
Staffing	24	10.6%	23	10.2%	-4.2%
Home Medical Eqmmt.	60	26.4%	43	19.1%	-28.3%
Infusion Therapy	19	8.4%	25	11.1%	31.6%
Specialty Pharmacy	15	6.6%	17	7.6%	13.3%
Total Transactions	227	100.0%	225	100.0%	-0.9%
Unduplicated Buyers	134		145		8.2%
Buyers	1.69		1.55		-8.4%
% Public Buyers	32.8%		21.4%		-34.8%
% Non-Public Buyers	67.2%		78.6%		17.0%
% Public Deals	50.2%		30.2%		-39.8%
% Non-Public Deals	49.8%		69.8%		40.0%

Source: The Braff Group

CHART E:
Detailed Buyer Breakdowns 2006-2007

Sector	Total Deals		Unduplicated Buyers (a)			Ave. Deals / Buyers			Public Buyers			% Public Buyers			Public Deals			% Public Deals		
	2006	2007	2006	2007	% Change	2006	2007	% Change	2006	2007	% Change	2006	2007	% Change	2006	2007	% Change	2006	2007	% Change
HHA	94	107	55	63	15%	1.71	1.70	-1%	8	10	25%	15%	16%	9%	33	35	6%	35%	33%	-7%
Hospice	15	10	14	9	-36%	1.07	1.11	4%	6	4	-33%	43%	44%	4%	6	5	-17%	40%	50%	25%
Staffing	24	23	17	20	18%	1.41	1.15	-19%	11	5	-55%	65%	25%	-61%	17	6	-65%	71%	26%	-63%
HME	60	43	34	39	15%	1.76	1.10	-38%	11	7	-36%	32%	18%	-45%	35	10	-71%	58%	23%	-60%
IV	19	25	12	17	42%	1.58	1.47	-7%	6	8	33%	50%	47%	-6%	10	10	0%	53%	40%	-24%
SPS	15	17	10	10	0%	1.50	1.70	13%	8	2	-75%	80%	20%	-75%	13	2	-85%	87%	12%	-86%
Total	227	225	134	145	8%	1.69	1.55	-8%	44	31	-30%	33%	21%	-35%	114	68	-40%	50%	30%	-40%

(a) Notes: Since buyers sometimes make acquisitions in more than one sector, total unduplicated buyer counts may not add up to the total by sector.

Source: The Braff Group

CHART F:
Top 10 Deals 2006 and 2007

Top 10 Deals of 2006				Top 10 Deals of 2007			
Seller	Buyer	Price	Sector	Seller	Buyer	Price	Sector
The Healthfield Group	Gentiva	454.0	HHA	PolyMedica Corporation	Medco Health Solutions	1,500.0	Supplies
ICORE Healthcare	Magellan Health Services	285.0	Behavioral Health	Option Care	Walgreen	850.0	IV
Symphony Health Services	RehabCare Group	101.5	Staffing	Oncology Therapeutics Ntwrk	McKesson	575.0	Specialty Rx
Club Staffing	Nursefinders	78.5	Staffing	Coram	Apria	350.0	IV
Trinity Hospice	Sunrise Senior Living	76.0	Hospice	Critical Care Systems	Medco Health Solutions	218.0	IV
National Home Health Care	Angelo Gordon & Co.	65.6	HHA	Deaconess Enterprises	Critical Homecare Solutions	171.3	IV
World Health Alternatives	Jackson Healthcare Staffing	53.0	Staffing	Pediatric Services of America	Portfolio Logic	121.9	HHA
Vista Staffing Solutions	On Assignment	49.0	Staffing	IntelliStaf Holdings	Medical Staffing Network	92.0	Staffing
IgG of America	Amerisource Bergen	43.5	Specialty Rx	IntegriCare	Amedisys	68.0	HHA
PSA RT & Services Business	Lincare	35.2	HME	HomeChoice Partners	DaVita	65.0	IV
Total Transaction \$s		1,241.3		Total Transaction \$s		4,011.2	
Median Deal Size		70.8		Median Deal Size		194.7	

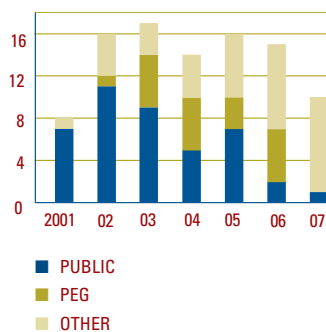
Includes only deals for which purchase prices have been made public.

Source: The Braff Group



The fall-off in hospice acquisition activity has little to do with buyers' appetite for deals... rather, there has been a dearth of potential sellers testing the market.

CHART G:
Hospice Merger and Acquisition Trends



Source: The Braff Group

Specialty Pharmacy Services

Although at first glance M&A activity in the specialty pharmacy services arena in 2007 looks quite similar to that of 2006, there were several significant developments in the sector:

- Of the 17 transactions completed in 2007, nine were completed by one buyer – Triad Isotopes – a new, private equity sponsored consolidator focusing on nuclear pharmacy, a particular niche where heretofore, we had seen little or no activity.
- Whereas in 2006, the overwhelming majority of specialty pharmacy transactions were completed by publicly traded buyers (87%), the public accounted for only two deals in 2007 – a mere 12% of the total transactions. This may be due, in part, to a general refocus of acquisition interest and demand from specialty pharmacy towards infusion therapy in order to capture greater margins.

Hospice

- 2007 was a particularly slow year for hospice M&A activity, with only ten transactions, down 33% from 15 a year ago. As **Chart G** indicates, the decline is part of a trend that began after the market peaked in 2003.
- Notable was the complete absence of transaction activity by private equity sponsored companies. This was offset, in part, by the continued increase in demand and activity from non-hospice focused buyers – particularly residential facilities and home health care providers – looking to leverage their referral source, clinical, and operating infrastructures to capture increased revenues and profits.
- It is important to recognize that the continued fall-off in acquisition activity has little to do with buyers' appetite for deals. The demand is there. However, over the past two years there has been a dearth of potential sellers testing the market, and many of those that have, have significant cost-cap exposure, all but eliminating them from acquisition consideration. We speculate that after the initial surge in hospice acquisition activity from 2001-2003, a time when for-profits accounted for only about 30% of the provider community, the "inventory" of attractive acquisition candidates was significantly depleted. However, with the surge in hospice spending, now estimated at about \$10B – triple that of 2000, – and a spike in new for-profit hospices entering the market to capitalize on this growth, we anticipate a slow, but steady increase in new acquisition candidates as these start-ups begin to mature and seek an exit strategy.

Health Care Staffing

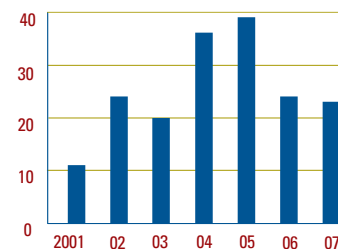
While the raw numbers would suggest that 2007 was another lackluster year for health care staffing M&A activity, with 23 transactions, down slightly from last year's tally of 24, the story behind the story is somewhat more complex.

- While transaction volume peaked from 2004 to 2005, the period was marked by a substantial number of "opportunistic" (i.e. somewhat distressed) transactions, predominately by small publicly traded companies that targeted the per-diem sub-sector to capitalize on a market facing substantial margin erosion and capture top-line growth. As margins continue to be squeezed in per-diem, several of these consolidators have faltered, notably World Health Alternatives. Furthermore, acquisition demand for per-diem has predictably slackened. Conceptually, then, if we adjust for the 2004-2005 surge in opportunistic deals that, arguably, artificially inflated transaction activity, we would get a far different picture of acquisition trends – a picture revealing a relatively consistent range of 20-25 deals per year.
- The nature of staffing transactions has changed dramatically over the recent past. Before per-diem began to be squeezed, the sub-sector accounted for a substantial portion of deal flow in the run-up from 2001-2003. Since then, acquisition demand has increasingly focused on, generally in order of preference (and relative valuation), locum tenens, allied staffing, and travel nursing.
- Health care staffing continues to be well represented at the top tier of dealmaking. While our list of the Top 10 Deals of the Year include only transactions in which purchase prices have been disclosed, if we consider the Goldman Sachs led acquisition of Nursefinders, which surely would have qualified, health care staffing would have accounted for two of the largest deals of 2007.

Home Medical Equipment

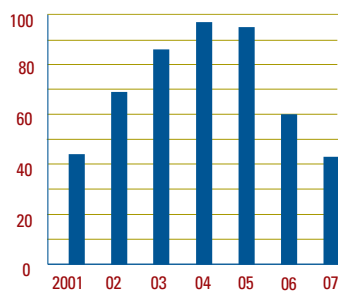
- As the **Chart I** illustrates, no other sector that we cover has experienced such a dramatic rise and fall in merger and acquisition activity over the past seven years as home medical equipment. After reaching a peak of 95 plus transactions completed in 2004 and 2005, deal volume fell 37% in 2006 with 60 acquisitions, and dropped another 28% in 2007 to close out the year with 43 deals. Concerns regarding the roll-out of national competitive bidding (NCB) and its expected, but, until recently, unknown impact on reimbursement, certainly contributed to the swoon. However, we believe that it was the introduction of a three year cap to oxygen reimbursement as part of the Deficit Reduction Act of 2006 that has done the most damage. Shortly after the 36 month cap was introduced, the President and Congress began introducing legislation to pare the cap down to as few as 13 months, creating extraordinary risk "overhang" that dwarfs the somewhat more predictable reimbursement declines likely to come from NCB. As a result, the most aggressive buyers of the past have all but withdrawn from the market – essentially adopting a "wait-and-see" position. That said, with winning bids recently awarded by CMS, amounting to an average 26% reduction in reimbursement, we may see an up-tick in activity in the initial 10 bid areas as losing bidders try to make up for their loss by acquiring a winning player, or simply decide to divest.

CHART H:
*Health Care Staffing
Transaction Trends*



Source: The Braff Group

CHART I:
*Home Medical Equipment
M&A Transaction Trends*



Source: The Braff Group

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The Braff Group is a leading middle market merger and acquisition firm that specializes in the home health care, hospice, infusion therapy, specialty pharmacy, home medical equipment, and staffing market sectors.

We provide merger and acquisition representation, strategic planning, and valuation services.



- Whereas the publics such as Lincare, Apria, Rotech, and Walgreens used to dominate M&A activity in the HME arena, they accounted for only one medical equipment transaction in all of 2007.
- In the midst of this extraordinary industry transition, local market players – most of whom sat out the bull years leading up to the heights of 2004-2005 – are collectively emerging as the most dominant buyers today, looking to complete one or two smaller, “opportunisticly” priced businesses per year as fold-ins or quasi startups. No surprise then that while transaction volume declined, as more independents entered the game, the number of unduplicated buyers ticked upwards, from 34 in 2006 to 39 in 2007, and the number of transactions per unduplicated buyer fell nearly 38% from 1.76 in 2006 to 1.10 in 2007.
- Although not an HME transaction, Apria did make a bold acquisition in 2007, acquiring infusion therapy provider Coram (one of the Top 10 transactions of the year) to add to its already formidable IV service offerings, and, we would expect, to further diversify away some of its HME risk.