Home Health Line
Regulatory news, benchmarks, best practices & executive tools for home care profitability & growth

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M&A activity: Better in home health than elsewhere

Home health mergers and acquisition activity has slowed in the past six months, but the news is better in the home health market than in many, experts say.

Other industries such as banking and technology are at a standstill in terms of buying and selling. In home health, "everything has been slowed to a crawl," says Dexter Braff, president of The Braff Group in Pittsburgh.

It's taking more time to close deals, but "it's not frozen," Braff adds. In fact, deals are taking up to 30 days longer to close, which can total as many as 150 days to close a deal in some cases.

The culprit: Investor fear. Buyers are ultra-cautious with their cash now. As credit for acquisitions has become more expensive, they're turning to their reserves rather than a bank line of credit to make purchases, Braff notes.

"There's just a psychological environment where buyers feel they have to make sure everything is picture perfect before they pull the trigger on any deal," he adds.

HHAs keeping heads above water

HHAs remain a popular acquisition target, but the economy has caused a lag in primary M&A indicators.

Mergers and acquisition activity for the overall home care market, including home health agencies, hospice and infusion, fell by 7% in 2008. For the last quarter of 2008 home health fell by 21%, hospice fell by 25% and infusion fell by 40%, according to data from The Braff Group in Pittsburgh.

At the same time, home health agency sales were up 2% for the year.

M&A activity has fallen short of experts' predictions for 2008. In late 2007, some in the industry projected "explosive growth" for mergers and acquisitions in home care.

What no one foresaw was the speed with which the credit crunch and the banking collapse would happen in late 2008, says Jack Eskinazi, senior VP for the M&A advisory firm American Healthcare Capital, Marina Del Ray, Calif.

In what's becoming a theme for home care M&A, it could have been a lot worse, experts say. Eskinazi says he handled about 40 home health transactions in 2008, which is the same as in 2007. Even as the financial world floundered, "we didn't have a single transaction crater due to a lack of financing. We feel lucky on that front," he says.

Cash is king; smaller agencies winning

With tight credit markets, sellers prefer that buyers have cash in hand rather than depend on unreliable financing. Buyers, for their part, are using cash to leverage better pricing and faster closings, say M&A experts.

It's driving ResCare HomeCare Inc., Louisville, Ky., to pursue more acquisitions – 20 deals or more in 2009 – compared with only 17 in 2008, says Brian Bruenderman, senior director of development. "There are more opportunities for us in this market" as smaller providers experience Medicaid cuts or a decline in private duty business, he says.

The cash crunch has made smaller agencies more attractive than years past when mid-sized agencies were pursued as "platform-building" acquisitions. Eskinazi says up to three-quarters of his deals in 2008 were sales of agencies under $5 million in revenue. His biggest deal in the final quarter of 2008 was only $20 million in revenue.

"The smaller transactions are just easier to do these days," because they require less financing and less time waiting for the lender to do due diligence, he says.

The major players that have left the arena, thus slowing mid-sized to big deals, are private equity investors, Eskinazi explains. Private equity firms no longer have access to cheap financing, making it more expensive for them to acquire the large, $20 million to $50 million "rollup" purchases they jumped on in the past. Private equity firm buys fell by 21% in 2008, the Braff data show.

The economic downturn has hit one other major purchasing group for HHAs – strategic buyers such as Amedisys, Gentiva Helath Services and LHC Group. These groups that typically acquire a few companies per quarter are finding their stock values down and their cash reserves strained, says Steven Braff, managing director at The Braff Group.

The buyers that are still in the market aren't willing to pay the plump prices they were in the past two years driving HHA valuations down, he says. For example, a $40 million company that might have sold for as much as eight times earnings in 2008 will probably draw closer to five times EBIDTA (earnings before interest, depreciation, taxes and amortization) in 2009.

To expedite your agency's sale, help buyers overcome fears

■ **Stabilize growth**. Buyers won't pay a premium for agencies that need to be fixed up, and they won't pay extra for agencies with 20% growth or more, which they suspect can't be sustained, says Steven Braff, managing director at The Braff Group in Pittsburgh.

For low performers, hold off on the sale until you can at least stop the bleeding, Braff suggests. For high-flyers, wait to sell until the growth has settled into a steadier pattern.

■ **Emphasize staff commitment**. Sellers should showcase the depth of their staffing and leadership now that home health recruitment and retention rates are at historic highs, Braff says.

■ **Don't spend a bundle on a new IT system or a new service line to spark buyer interest**. It's unlikely to be completed in time if you're looking to sell in the next three months and will simply reduce your reserves and perceived value, he says.

Agencies looking to sell in the next 18 months might have more time to overhaul any lagging operations and still experience results by the time buyers are at your door, Braff adds. – *Sara Jackson* [*sjackson@decisionhealth.com*]