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PE Finds its Niche in Healthcare

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WITH EXPERT COMMENTARY FROM: RSM and Sterling Partners

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Investing in a Segmented Healthcare Market

As the healthcare sector strays from the traditional hospital setting, private equity has an edge in finding deals amid high valuations, says RSM's Tammy Hill



Tammy Hill

Partner, Transaction Advisory Services
RSM

Healthcare is a highly segmented sector, and to private equity, that translates into an opportunity—if you're willing to do some homework. The way private equity firms deal with companies after the acquisition lends itself to this segmentation in

healthcare, says Tammy Hill, a partner in transaction advisory services at RSM. "They will partner with operating partners who are very knowledgeable in whatever space they're thinking about investing in. Private equity investors, in general, like situations where the more you know, the better your chances of success are."

There are some healthcare sectors that exist today that were much less prevalent five or 10 years ago, says Hill, partly because healthcare services have moved farther away from the big hospital setting. The boom in urgent care storefronts and clinics that is happening now was not nearly as common even five years ago. "In many cases, people's first thought now, rather than going to a doctor or maybe even an emergency room, is to go to an urgent care center," she says. In some cases, for certain illnesses or injuries, the urgent care clinics are less expensive, it's easier to get in to see a doctor, and the reputation and quality of care has improved. "It's just so much more efficient than some of the more traditional settings for healthcare services," Hill adds.

The increased segmentation of healthcare companies has led to high

demand from private equity investors and therefore high valuations. In some cases, this immediately leads to PE firms bowing out from the bidding process as the prices go up. But one way they can work around the high valuations is by harnessing the value of their operating partners and their expertise. "They will begin discussions with a company before the seller goes to market with a broader sales effort through an investment bank," Hill says. "Maybe their operating partners have contacts. They see a good fit." If they can make their case to the seller, if there's a healthy transaction value, and if the valuation is right, going this route can result in a more streamlined process for the seller as well.

Hill says that doing the homework on a transaction up front is important, as well as making a solid bid and executing a quick close. "We do a large number of sell-side diligence projects now to help the sellers," says Hill. "That gets a lot of the detailed homework out of the way on the financial and operational diligence. And then when the seller goes to market, they can say, 'We have already done a lot of the necessary upfront work and, as a result, the buyer's process should go smoothly and take less time.'" ■

Niche in Outsourced Healthcare Services Shows Promise

Healthcare-focused firm Sterling Partners continues to keep its eye on a specific part of the outsourced services subsector



Garrick Rice
Sterling Partners

The healthcare space today boasts both fully matured subsectors and highly fragmented pockets. Successful investment in the space requires recognizing and leveraging trends early on, before they become flooded with competitors. For Garrick Rice, a managing director at Sterling Partners, one of those unique areas lies within outsourced services.

Sterling, founded in 1983, focuses

on education, business services, and healthcare. The firm has experience investing in a number of areas within the latter, including laboratories, behavioral health, and multisite-based facilities, as well as physical therapy and care services for people who have endured catastrophic injuries at work. The firm's strategy includes investing further into its portfolio companies, setting the stage for strong organic growth in approximately five years. Sterling's leadership points to its growth strategy as a differentiating factor from other firms in the healthcare space that are typically more focused on leveraged buyouts.

Asked which area in the healthcare space could be poised for significant growth, Rice points to the specialist segment within the outsourced-services subsector. Outsourced services as a whole is showing signs of maturity, but it is the underlying group of people with particular specialties and training that shows promise.

For instance, one of Sterling's portfolio companies includes Q-Centrix, a provider of data abstraction for acute-care hospitals. Q-Centrix's proprietary technology and team of outsourced employees empowers clients to make better decisions with advanced data and information gathering while ensuring cost efficiencies, according to Sterling's website. Surgical Solutions

is another Sterling investment that provides operating room support to hospitals throughout the United States. That includes technicians to assist with setup, support, and postoperative cleanup, as well as equipment procurement, equipment cleaning and sterilization, and scope repair.

Rice also points out quality-of-care management for various disease states—as well as Medicaid and payer services—as interesting opportunities.

This is not to say the smart money should ignore popular areas within healthcare. To the contrary, many firms, including Sterling, continue to keep their eyes on “population management,” for example. Going to the emergency room typically has expensive outcomes for a number of parties involved in the process. Therefore, healthcare investors are studying a variety of clinical models that focus on hands-on management of patients to prevent trips to the emergency room.

The one constant throughout Sterling's investment thesis for healthcare is to put capital to work in portfolio companies that help to increase efficiencies within the system and lower costs for patient care.

“Our goal is to drive better outcomes for the patient,” Rice explains. “That is better all around for all parties.” ■