M&A update
Consumer Healthcare

AUTUMN 2019

Corporate activity and M&A volumes have increased sharply in the private pay consumer healthcare services market

The UK's consumer healthcare services market saw 22 transactions[1] complete in the first nine months of 2019, compared to just 16 in the whole of 2018. The global obsession with health, wellness and beauty is driving growth in related sub-sectors, with consumers taking an increasingly proactive approach to their mental and physical wellbeing. Despite concerns about the sustainability of broader discretionary consumer spending in the UK, we expect the wellness and consumer healthcare space to remain stable in the face of economic headwinds.

In this attractive market, strategic and institutional investors are competing for the best businesses. This is creating opportunities for owners and management teams to secure the financial backing they need to fulfil their objectives.

Fragmented markets present consolidation opportunities

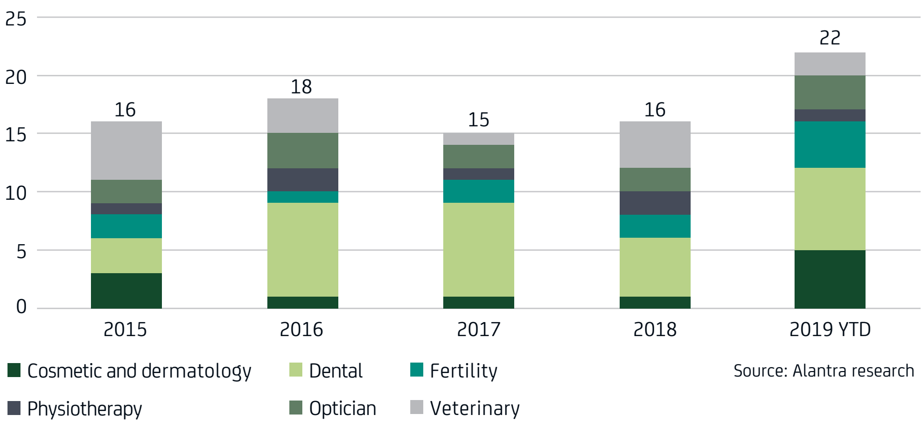
The consumer healthcare market can be categorised by both the level of medical need and the specialist nature of procedures.

Multi-site business models are comparable across an array of end-markets including aesthetics, dentistry, fertility and physiotherapy. Consolidation is an ongoing theme in these markets, many of which are highly fragmented.

Investors hope to replicate the successful consolidation achieved in the more mature dentistry and veterinary markets, where platforms have grown through acquisition before large scale buy-outs or strategic trade sales. This cycle is now being repeated in niches such as fertility (four deals in 2019 so far) and less mature areas such as cosmetics and dermatology (five deals). International strategic buyers are also acquisitive, seeking to enter new and growing markets at a time when the UK's political situation and the weakness of sterling have created opportunities.

Several value drivers support a broad range of transaction multiples. We have analysed how factors such as category, customer proposition and brand, expertise, platform, operations, strategy and financial profile are impacting valuations of consumer healthcare businesses.

M&A volumes by sub-sector



Source: Alantra research

[1]Deal volumes represent platform or transformational bolt-on acquisitions. 2019 YTD includes deals up to and including September 2019. Platform and transformational bolt-on acquisitions are defined as the acquisition of a multi-site operator, or the acquisition of a single-site or online operator that has a significant influence on the acquiring platform's business model.

M&A volumes in consumer healthcare services are up almost 40% so far this year compared to the whole of 2018. We're seeing both corporate and financial investor activity driving the market and this is creating significant opportunities for our clients.

BOBBY FLETCHER, DIRECTOR

Growth rates sustained through positive market fundamentals

In the UK, NHS retrenchment and the privatisation of some healthcare services and treatments have been critical in driving growth in the non-publicly funded procedural healthcare market. Historically, if an individual was concerned about a mole or a lesion on the body, the NHS would remove and screen it for skin cancer. Now, with public funding budgets squeezed, there is an increasing transition towards self-funding, or cover through private health insurance. This situation is similar in bariatric treatments, dermatology, breast-related procedures and many more. As a result, business models in this space are increasingly viable, as privately-funded operators offer more services that were previously publicly funded.

Funding issues have also led to a decrease in the average number of clinicians accessible to the public. According to the Nuffield Trust, a health think-tank, there are now 58 GPs per 100,000 people in the UK, down from 66 in 2009; this has been the first sustained fall since the 1960s.

This is a market featuring increased pathological awareness, education and prevalence, alongside an ageing population, rising social media usage and increased appreciation of wellness and beauty. All these factors underpin growth rates across the medical and cosmetic spectrum in non-invasive and minimally invasive treatments, as well as invasive surgery.

Attractive business models heightening investor interest

Revenue sources in this market tend to vary with the extent of treatment specialism. Companies offering less specialist services are often more dependent on patients paying out of pocket and therefore face greater competition. However, these services offered tend to generate high margins. Therefore, those businesses that can attract customers through consistently high treatment standards and employ retail best practices, make an attractive investment proposition.

To compete effectively, operators require strong digital marketing capabilities, since most customers' journeys start online when researching their options. Centralised marketing spend will benefit the operator's entire network and increased scale amplifies this effect. The ability to educate potential clients early online or through consultation, helps secure conversion through to treatment. Retention is equally important, as there is huge potential customer lifetime value for clients in consumer healthcare.

Operators that understand and exploit these dynamics will capture many more clients at the top of the funnel and minimise fall-out, reducing their cost of customer acquisition and maximising profitability. Digitally adept operators, therefore, do not rely solely on footfall to attract custom, offering more flexibility on where to locate. With increased site selection choice comes more attractive site economics. Whilst retail site contribution margins vary by end-market, consumer healthcare businesses benchmark well against other retailers.

Such characteristics can drive high returns for investors - though the most important principle of all is that patient outcomes and customer satisfaction are pivotal to success.

Private equity-owned businesses are driving 2019 M&A activity

TriSpan's acquisition of sk:n clinics from Graphite Capital, at the start of 2019, kickstarted a wave of activity in consumer healthcare. TriSpan identified a range of opportunities including digital systems enhancement, UK clinic network expansion, multi-site corporate acquisitions, international roll-out, treatment menu extension, and refinement of the skincare product strategy. The follow-on acquisitions of Destination Skin and Skin Health Spa increased the size of the combined group to a nationwide network of 75 clinics; a 50% uplift in clinic numbers since the initial TriSpan investment.

In March, BlueGem-backed cosmetic surgery provider, The Private Clinic, acquired The Cosmetic Skin Clinic. This acquisition is the fourth under BlueGem's ownership and takes it to a total of 14 premium cosmetic clinics, providing both surgical and non-surgical cosmetic treatments and generating more than £30m of combined group revenue.

More recently, Bowmark completed the sale of CARE Fertility to pan-European private equity investor Silverfleet. Since its formation in 1997, CARE has supported the conception of 30,000 babies and boasts one of the highest success rates in the UK. CARE currently operates nine full-service fertility clinics supported by a network of 13 satellite facilities. Silverfleet's growth strategy for the company involves broadening the clinic network across the UK, making acquisitions to consolidate a highly fragmented market, developing new products and services to improve patient success rates; and building an international fertility platform.

Investors seeking to replicate prior successes in adjacent markets with comparable business models

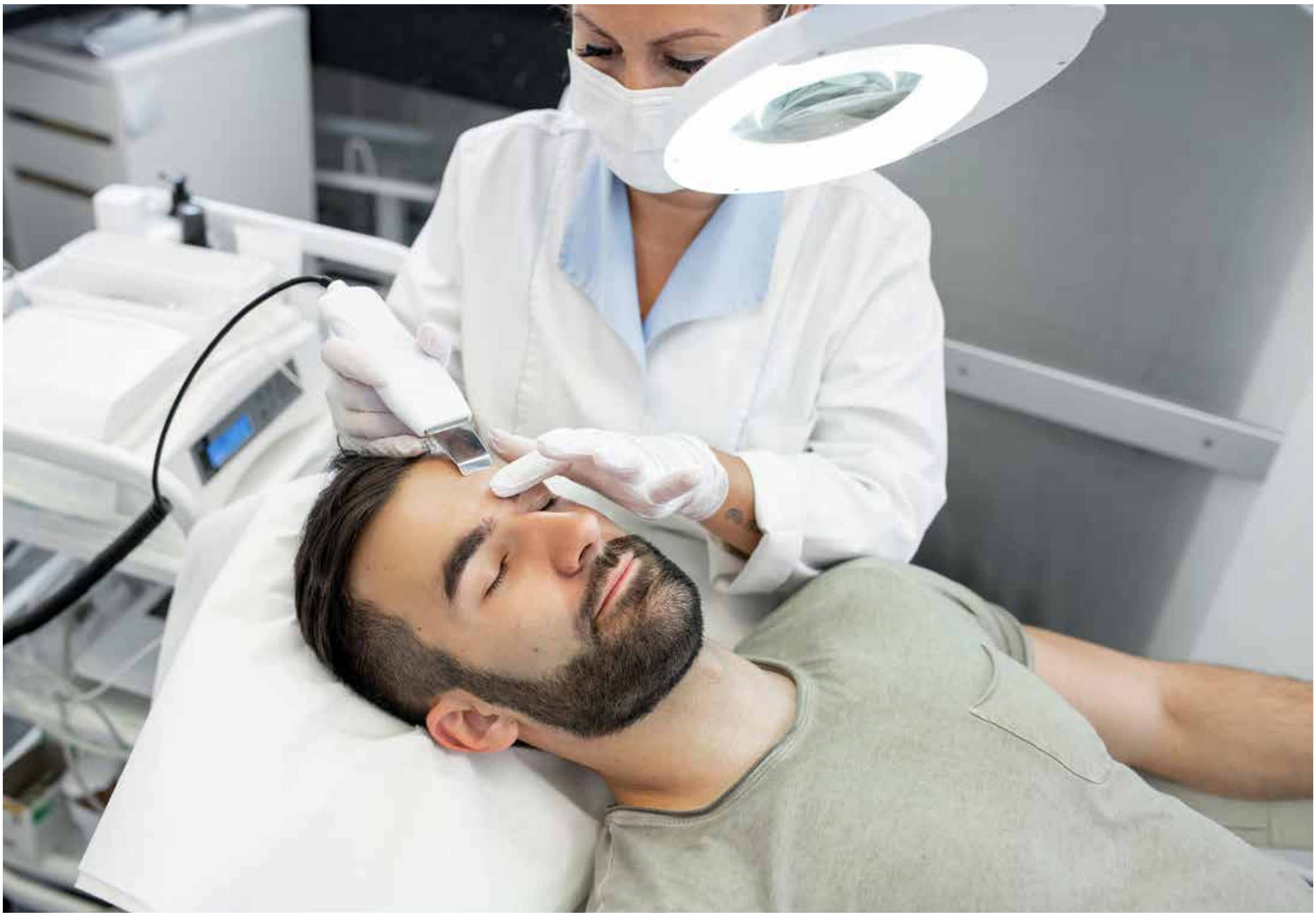
International private equity group Bridgepoint's £835m sale of Oasis Dental Care to Bupa in 2016 provides one of the best examples of a successful consolidation strategy in a fragmented market. Bridgepoint acquired Oasis for £185m in 2007 from Duke Street, which had itself acquired the business in a public-to-private transaction for £77m in 2007. Within three years of Bridgepoint's ownership, Oasis had completed the acquisition of 191 dental practices; along with various operational improvements and marketing initiatives, this tripled the company's EBITDA. Bridgepoint achieved 14x EBITDA on exit, which was a notable uplift on the 9.5x EBITDA it paid on acquisition.

There have been other examples of this type of success. In April 2019, buy-out group EQT sold a stake in Independent Vetcare Group (IVC), an operator of 1,100 vet clinics and hospitals across ten countries, to Nestlé's Purina PetCare. This followed the sale in February 2019 of a separate minority stake to Swedish institutional investors, valuing the business at €3bn. IVC is now the largest veterinary operator in Britain, having formed in 2011 through the consolidation of several large independent practices across the UK. Similarly, VetPartners, which was acquired by BC Partners for £700m in 2018, now owns more than 310 clinics across the UK. It has added an average of 80 clinics annually over the past three years, having been founded in 2015 as a platform for consolidation.

These case studies provide a glimpse of the strategy that private equity are now pursuing in similarly fragmented sectors. Dentists, dermatologists, vets and beauty practitioners have all proved they are capable of setting up and running a private practice offering their services. The complexities of running a multi-site operation can be a barrier to growth beyond a cluster of clinics, encouraging owners to sell.

Organic expansion can provide greater returns than growth through acquisition

Organic expansion can also be an effective way to generate profitable growth and attractive returns on invested capital, particularly where vendors' price expectations are high. For example, Thérapie Clinic, the Dublin-headquartered, privately-owned aesthetic treatment provider, operates 34 clinics across the UK and Ireland and is pursuing an exclusively organic growth strategy, having already opened 13 new clinics in 2019. Similarly, SISU is a doctor-led cosmetic treatment chain co-founded by Dragon's Den's Pat Phelan and doctors James Cotter and Brian Cotter. It is reported to be in talks to raise €50m in private equity funding to finance its organic expansion strategy in the UK and the US. It plans to grow from its existing five locations in Ireland to 100 within three years.



Business specific factors are the predominant driver for M&A

The synergies available to a consolidator are often plentiful, as illustrated by skin rejuvenation services in aesthetics. As scale increases, so too does buying power, and cost savings for materials such as Botox can be margin enhancing. In recent M&A discussions between two operators in this space, one business found it was paying ten per cent more for a vial of Botox than the other. Combined purchasing volumes would have contributed to a sizeable gross margin increase for rejuvenation treatments offered by the enlarged group.

Proprietary knowledge and expertise provide further synergistic value to buyers, and this can be applied across many of the adjacent sub-sectors within consumer healthcare services. Clinical efficacy is crucial to medical businesses, and it takes significant investment to create and maintain such an infrastructure. Acquisitions are a key tool for achieving expertise in relevant areas in order to extend addressable markets.

Understanding the most effective routes to market in private pay procedural healthcare is critical. A successful digital marketing strategy is now a priority for many operators. For example, one of the UK's most prominent dental chains wants to use the acquisition of a digitally-sophisticated business in an adjacent market, such as aesthetics, to expand both its current customer base and to improve its access to new markets.

In dermatology and oncology, technology-enabled businesses are using algorithms to assist clinicians in pathological diagnosis; these make attractive targets for international strategic trade buyers, particularly where there is scope to improve accuracy through increased scale. There is also consistently strong interest in UK businesses from abroad, where international expansion is a key part of the investment case.

International buyers continue to demonstrate interest in the UK market

Overseas strategic buyers are attracted to the UK market's strong fundamentals, particularly as the weakness in sterling is an opportunity to offset high valuation multiple expectations. UK and international consumers' commitment to spending on healthcare will protect the UK's consumer health sector against any potential short-term volatility in wider consumer discretionary spending, caused by the impact of Brexit. For example, cosmetic surgery tourism in the UK is growing, particularly where the clinicians are of a world-renowned standard and where there is brand heritage associated with London's most famous pockets of medical expertise, such as Harley Street.

Maximising value in consumer healthcare services

Our significant experience working with consumer healthcare services providers and our transaction record enable us to assess the key value drivers in this sector and to identify those factors generating the highest multiples:

Category

- Fit with key macroeconomic and consumer trends
- Sub-sector attractiveness
- Market growth rates
- Scale
- Resilience through economic cycle
- Competitor profile and activity, and consolidation opportunities

Customer proposition and brand

- Premium positioning
- Target customer demographics and international appeal
- Client satisfaction, trust and overall lifetime value
- Brand metrics including penetration, advocacy, customer retention, ability to lead pricing
- Trends of all of the above

Expertise

- Treatment specialism
- Breadth of treatment menu
- Medical infrastructure from a people, clinic and equipment perspective
- Depth of expertise
- Competitive differentiation
- Medical staff satisfaction, recruitment and retention

Platform

- Ability to leverage medical infrastructure
- Existing estate KPIs (LFLs, ROCE, site economics)
- Digital marketing capability
- Call centre service levels and extent of staff education
- Roll-out opportunity (green/brownfield)
- UK and international multi-site bolt-on acquisitions

Operations

- Doctor and practitioner availability and utilisation
- Treatment room availability and cross-platform visibility
- Sourcing expertise, security and volatility of technical equipment and disposable supply
- Service levels

Strategy and financials

- Top line and profit growth
- Margins and discounts
- Profit improvement opportunities
- Free cash generation
- Balance sheet
- Management and employees
- Growth opportunities/value in consolidation plays

Selected Alantra deals

Active

FUNCTIONAL WELLBEING

SELL-SIDE MANDATE

MEDICAL DERMATOLOGY

BUY-SIDE MANDATE

COSMETIC DERMATOLOGY

BUY-SIDE MANDATE

Completed

Freshtandartsen

ACQUISITION FINANCING

LIVINGBRIDGE

sk:n

SALE TO

TRISPAN

Dentego

REFINANCING

G SQUARE HEALTHCARE PRIVATE EQUITY

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