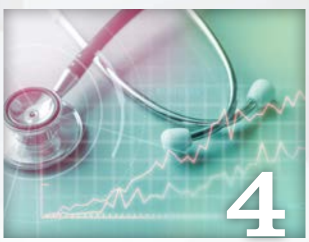
QUARTER 3 2020

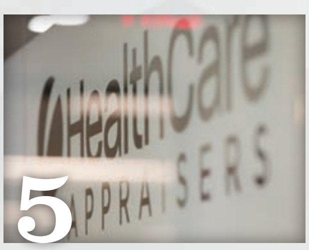
FMVantage Point™

HealthCare Appraisers' Industry Insight

QUARTERLY INDUSTRY INSIGHTS

AT A GLANCE

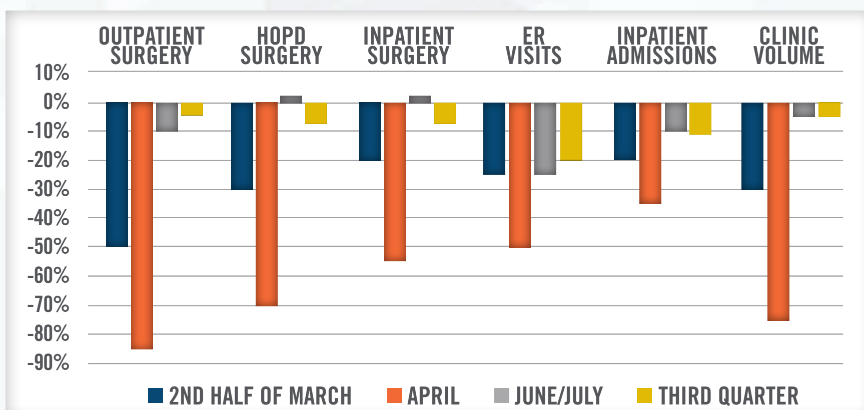




Monitoring Industry Activity from Quarter 3 of 2020

As part of our ongoing monitoring of developments in the healthcare industry, HealthCare Appraisers follows reports from publicly-traded health systems, physician services providers, ambulatory surgical center management companies, and other healthcare service providers. This document summarizes important valuation-related takeaways from recent earnings calls and conference presentations, as well as supporting quotes[1] from publicly-traded operators. While volume trends for most providers were still down year-over-year in the third quarter as presented in **Figure 1**[2], higher acuity and higher commercial mix drove positive revenue growth for many providers. Many operators also indicated that cost saving measures put in place during the height of pandemic closures, including lower or more flexible staffing levels, contributed to higher profit margins as providers learned how to be leaner business operators. At the same time, many public companies, as well as private companies that we have worked with recently, believe that some of the higher costs associated with providing care, including PPE and sanitation expenses, are likely to remain elevated into the future beyond the period directly impacted by COVID-19.

FIGURE 1 – VOLUME TRENDS



HIGHER ACUITY CASES MOVING TO ASCs

Many ASC operators continue to experience a shift of higher acuity cases out of the hospital and into the ambulatory setting, and have placed large bets that this trend is only getting started. Recent examples include Surgery Partners increasing the installed base of Da Vinci robots in its surgery centers, and Tenet's

[1] All quotes have been adapted from transcripts provided by S&P Capital IQ.

[2] Represents volume trends reported by HCA Healthcare, Inc., Community Health Systems, Inc., Tenet Healthcare Corporation, Mednax, Inc., RadNet, Inc., Surgery Partners, Inc., and other publicly-traded companies

HIGHER ACUITY CASES MOVING TO ASCs *(CONTINUED)*

acquisition of 45 musculoskeletal focused ASCs from SurgCenter Development. In the ASC setting, surgical robots are frequently used as recruiting tools to attract physicians who otherwise may feel they need to perform cases at a hospital, but also represent a further migration of cases that used to be predominately performed in hospitals to ASCs. Similarly, Tenet Healthcare Corporation's acquisition of a 45 ASC portfolio from SurgCenter Development represents a substantial bet that in the coming years, growth in the ASC space will be driven by high acuity orthopedic and MSK cases. The acquired centers have 40%+ EBITDA margins, which in our experience is not uncommon for well-run ASCs focused on high acuity orthopedic/MSK cases. Interestingly, Tenet acquired the centers for approximately 8.5x adjusted 2019 EBITDA, which represents an attractive valuation multiple given the growth profile and profitability of the centers. Our experience working with similar ASCs suggests valuation multiples for these types of acquisitions are frequently higher than 8.5x, often in the high single or low double digit range for a single center while a large portfolio could generate even higher multiples. The allocation of capital by two of the largest operators in the space suggests an acceleration of the migration to the outpatient setting.

WHAT INDUSTRY LEADERS ARE SAYING ABOUT *HIGHER ACUITY CASES MOVING TO ASCs*

RONALD RITTENMEYER – CEO OF TENET HEALTHCARE CORPORATION

"The SurgCenter Development centers are premier locations in a fast-growing segment of the ambulatory surgery market as the large majority of cases come from the higher acuity musculoskeletal procedures. The MSK market continues to develop in the ambulatory space, with more of these types of surgeries shifting to outpatient settings. This transaction ensures Tenet will essentially double down and further deepen our concentration in these high-growth areas of the future."

ERIC EVANS – CEO OF SURGERY PARTNERS, INC.

"We have also increased our installed base of robotics by 24% in 2020 and have plans to further expand in 2021... We now have 3 surgical hospitals and 2 ASCs that currently perform cardio procedures. The ASCs are early stage expansion and pilot programs, which are showing promising returns, while our surgical hospitals continue to mature and expand their high acuity cardiology capabilities. On a year-to-date basis, our cardio procedures are up 8% as compared to 2019. We are planning to more than double the number of ASCs that perform cardio procedures in 2021 and continue to evaluate surgical hospital expansion opportunities."

HOSPICE M&A ACTIVITY REMAINS ELEVATED, HOME HEALTH EXPECTED TO PICK UP IN 2021

Entering 2020, many operators in the home health and hospice space expected M&A activity to be robust. While the home health activity has been somewhat muted due to the effects of PDGM being delayed, the hospice M&A market has been very active and valuation multiples have increased as a result. As with many other sectors of healthcare, the influx of private equity money into the hospice space has caused valuation multiples to increase, with multiples for competitive bid transactions involving larger hospice providers reaching the mid-teens. Hospice activity is expected to remain robust going forward due to the fragmented nature of the market and the increasing interest in the post-acute space by a variety of potential acquirers. Home health M&A activity is believed to be delayed as government funds provided due to COVID-19 have offset some of the cash flow crunches that were anticipated as result of PDGM and elimination of RAP. In 2021, when the Medicare Advanced Payments are due to be repaid and other sources of COVID-19 funding dry up, large operators believe there will be a period of consolidation activity as smaller agencies are acquired by larger operators.

WHAT INDUSTRY LEADERS ARE SAYING ABOUT *HOME HEALTH AND HOSPICE M&A ACTIVITY*

PAUL KUSSEROW – CEO OF AMEDISYS, INC.

“We’re seeing hospice decently run hospices transact over 15x (EBITDA). So it’s gotten a little crazy, particularly when it is a PE platform. What we expect with home health is if sequestration is added back on and when the loans become due for the receivables and for payroll is that’s when we expect the shakeout to occur. If the government pushes this out further, it’s probably going to hold us back on what we anticipate as a large consolidation opportunity with PDGM, particularly as the RAP is going to be eliminated in January. But we’ve seen home health transacting around 12x, 13x EBITDA, something like that. But post synergies, it’s below 10x for us. So that’s why we’re looking and that’s where we think the market is going to be. And a lot of our competitors now, frankly, have seen what we’ve been doing in hospice and are deciding to go after hospice. So I think that’s going to push the hospice pricing up even more.”

ESTIMATING THE REVENUE IMPACT FROM CHANGES IN 2021 PHYSICIAN FEE SCHEDULE

With the recently finalized changes to the Center for Medicare and Medicaid Services ("CMS") Physician Fee Schedule, groups and organizations that bill under this fee schedule are beginning to analyze the effect on their revenue in 2021 and beyond. While the impact to Medicare revenue is understood at this point, how commercial payors will respond is of great interest to the healthcare community. The largest operator of IDTFs in the country indicated that while its Medicare Advantage contracts would reset lower as a result of the coding changes, it did not expect its private payor contracts to be materially impacted since they are not set as a percent of Medicare reimbursement. More broadly, it remains to be seen how the dramatic changes in the Medicare Physician Fee Schedule will impact the commercial reimbursement landscape, with rates potentially changing even for plans that are not directly linked to Medicare. Of note, the Consolidated Appropriations Act for 2021 (passed December 27, 2020) increased the Physician Fee Schedule conversion factor from $32.41 to $34.89; this change is expected to increase aggregate Medicare reimbursement for physician services by 3.75% relative to 2020 levels.

WHAT INDUSTRY LEADERS ARE SAYING ABOUT *2021 PHYSICIAN FEE SCHEDULE*

MARK STOLPER – CFO OF RADNET, INC.

"We have very few contracts that are tied to Medicare. When we were living through the Deficit Reduction Act and the 7, 8 years that that followed where Medicare was hitting reimbursement, we did a pretty good job of unbundling most of our commercial contracts from Medicare. We still have some, for instance, the Medicare Advantage plans that are still tied to Medicare reimbursement. So those will adjust, but it's not going to be a material amount, another couple to a few million bucks."

HOME HEALTH PROVIDERS ARE DISCUSSING A POTENTIAL RATE INCREASE IN 2022

On third quarter conference calls, home health operators discussed a potential reimbursement rate increase in 2022 from CMS. Specifically, case rates for home health have been lower than originally anticipated by CMS, which could result in an increase of approximately 2 percent in 2022 if the current trends in claims and reimbursement rates hold. The lower case rates are due to assumptions made by CMS regarding behavioral changes that were anticipated to take place as a result of the new payment model being implemented. To the extent that these behavioral changes do not play out as anticipated, the rates will be different from what CMS expected and will not fulfill the budget neutral requirements. If this continues, rates in 2022 are anticipated to increase for home health providers.

WHAT INDUSTRY LEADERS ARE SAYING ABOUT *POTENTIAL RATE INCREASE IN 2022*

DAVID KEMMERLY – CHIEF LEGAL AND GOVERNMENT AFFAIRS OFFICE OF AMEDISYS, INC.

"It's important to note and remember that the Bipartisan Budget Act of 2018 mandated that the transition to a new payment model, in this case PDGM in 2020, be budget neutral. And it even provided a mechanism for a true-up, if you will, in 2022. So thus, if the data from the early part of 2020 holds throughout the year, the remainder of this year and then into 2021, there will be a rate give-back or increase in the payment rate update for 2022. So when you see that final rule in November of 2021, there should be a rate update for 2022 if the behavioral functions are playing out like they are now."

APRIL ANTHONY – CEO OF HOME HEALTH AND HOSPICE DIVISION OF ENCOMPASS HEALTH CORPORATION.

"But I do think that we're in a very good position to have the 2022 rate be adjusted for that. And the data provided by Dobson and DaVanzo and others is very strongly in support of the fact that the assumptions were not well-founded and have not proven to be accurate, even if you try to COVID adjust them, I think their data would suggest [CMS] were way off the mark."

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Daniel I. Levin, CFA, ASA is a manager in the Firm's Denver office where he specializes in a wide variety of healthcare business and compensation valuation assignments. Mr. Levin's business valuation experience includes valuing hospitals, health systems, dialysis clinics, imaging centers, ambulatory surgery centers, physical therapy clinics, urgent care clinics and physician practices in connection with a wide range of transactions. Prior to joining HealthCare Appraisers in 2016, Mr. Levin was an Equity Research Associate performing industry research and investment analysis on publicly-traded healthcare companies. Mr. Levin graduated summa cum laude from Florida Atlantic University in 2013, and has been a CFA charterholder since September 2017.

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Nicholas J. Janiga, ASA is a partner in HealthCare Appraisers' Denver office, where he leads the firm's business valuation and capital equipment valuation service lines. He has been providing his clients analysis and consultation in business valuation, litigation support, intellectual property and healthcare provider compensation relationships since 2006. His experience includes working with healthcare organizations, attorneys, administrators, providers, developers, consultants, investment bankers, and private equity groups in connection with transactions in the healthcare industry. Many of the transactions he analyzes involve Stark, Anti-Kickback, IRC 501(c)(3), and/or other regulatory implications, which requires analysis of fair market value and the determination of commercial reasonableness. He also has experience providing expert testimony in deposition and trial settings.