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**HEALTHCARE IT  
SECTOR UPDATE  
1 Q2020**

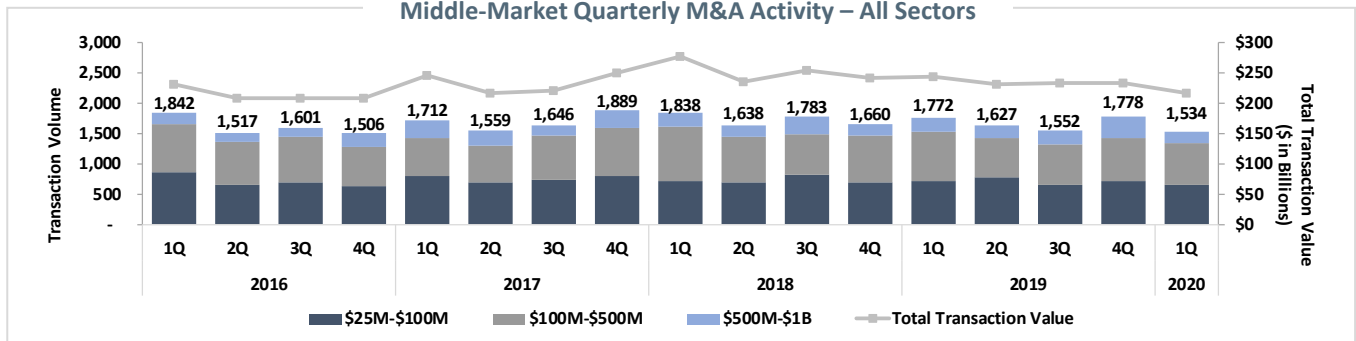
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April 2020

[www.brentwoodcapital.com](http://www.brentwoodcapital.com)

## Q1 2020 M&A Update

An M&A market that has been gradually weakening over the last two years is now on life support thanks to COVID-19. Small cracks in valuation and lending markets that appeared in March have become unbridgeable fissures in April. Most deals in the process of being closed have been delayed indefinitely. The few deals fortunate to close were significantly restructured, requiring lower purchase prices, seller notes, more onerous securities and terms and, in some cases, higher shareholder rollover.



Source: Pitchbook

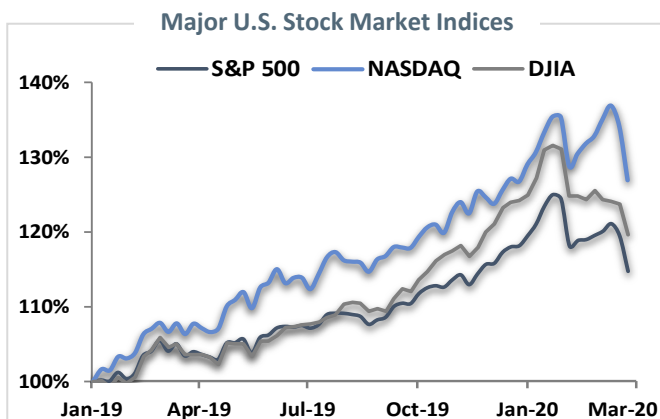
New deal flow has slowed to a trickle. If sellers don't have a significant amount of recurring revenue, an M&A process is likely to be unsuccessful. Most companies can't forecast full-year results, making it nearly impossible to value the company and to attract the requisite debt and equity financing. To bridge this valuation gap, PE firms are utilizing more structured equity that combines a preferred security and fixed return with warrants, significantly improving the risk/reward profile for the buyer.

Lenders have become more conservative overnight, dampening valuations and the chances for successful deals. Once commonplace to have deals levered at 5-6x cash flow, lenders now struggle to allow more than 2x cash flow in senior debt. Due to the previously strong economy, banks entered this crisis with solid balance sheets; however, most are dramatically boosting reserves in anticipation of higher loan defaults. Many loans underwritten at 5-6x cash flow will be leveraged at twice that level when factoring the full effects of a shuttered economy.

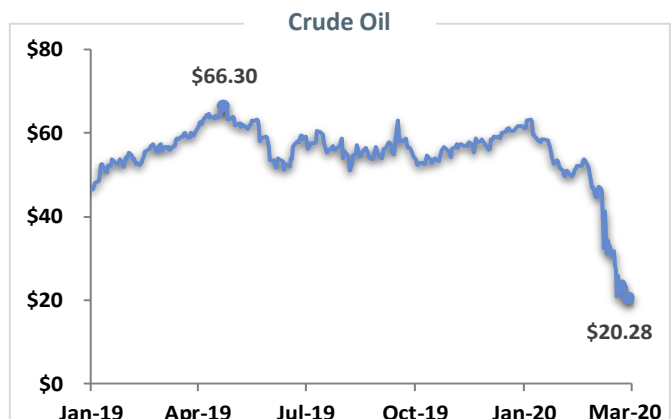
## Key Market Developments

All major market indices are experiencing volatility associated with the COVID-19 pandemic and falling crude oil prices. As the outlook for the number of COVID-related deaths in the U.S. has improved, major indices have recovered ~25% of their value. Markets have also been bolstered by plans to gradually reopen the economy beginning with six states sometime this week. The largest five states account for over 40% of U.S. GDP. Of these, California and Illinois are scheduled to be closed until May 31<sup>st</sup>, and New York may be closed longer. Without these states fully re-opened, any economic recovery will look more like a "U" than "V".

Oil prices are even more volatile. Initially, the Russians and Saudis were flooding the market trying to break the back of the U.S. petroleum industry. Although the Saudis have agreed to curtail production, crude oil prices briefly fell to -\$37.63/barrel last week on fears of global COVID-induced depression and lack of storage. With most of the world's productive capacity shutdown, there is virtually no demand for crude oil.

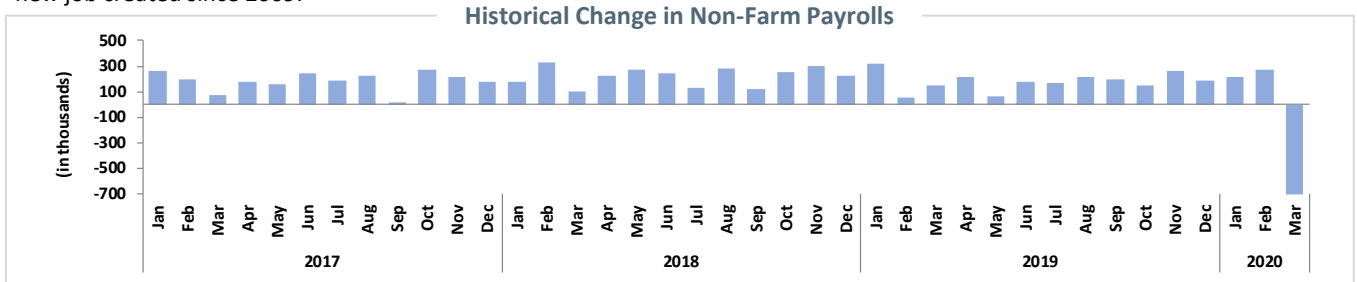


Source: Yahoo Finance



## Non-Farm Payroll

All signs pointed to a booming economy in early 2020. New job creation was setting records, particularly for this late in an economic recovery. Overnight, the situation changed when COVID-19 hit our shores and states enacted stay-at-home policies. The U.S. economy collapsed. Jobless claims that typically averaged 180-220K per month were increasing by 5.0 million per week on average. The number of people out of work now totals 30+ million and counting. Essentially, the shutdown has erased every new job created since 2009.



Source: Bureau of Labor Statistics

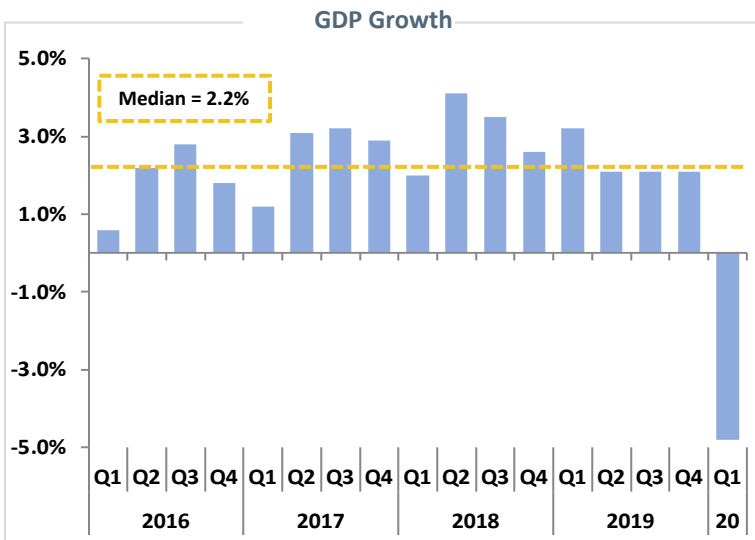
## Unemployment

The employment landscape has changed so rapidly and drastically over the last month that it is difficult to measure. Assuming 30 million unemployed out of 180-200 million workers, unemployment currently stands at 15.0-16.7%. Unemployment claims are likely to continue to rise over the next few weeks and could reach as high as 15-20% depending on consumers' willingness to reengage with a reopened economy.



Source: Bureau of Labor Statistics

## Gross Domestic Product



Sources: Bureau of Economic Analysis, Federal Reserve Bank of Atlanta

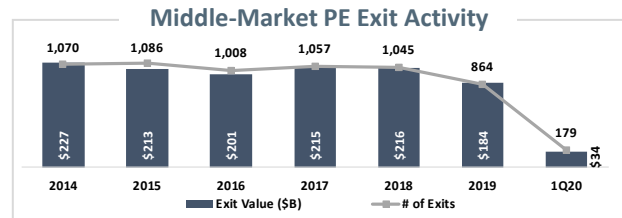
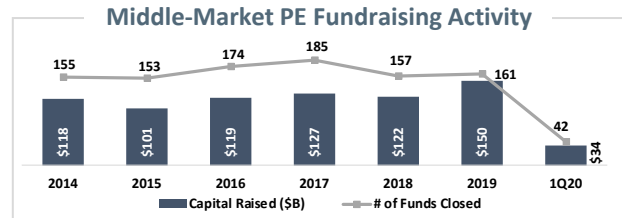
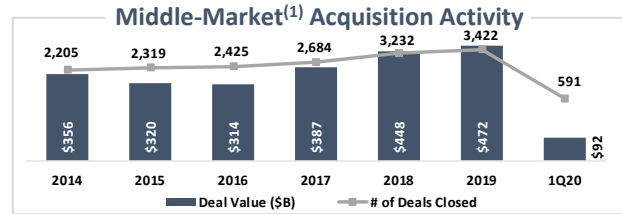
Similarly, COVID-19's impact on GDP is extremely difficult to gauge. The outlook for 3+% GDP growth in 2020 has been shattered. 1Q20 GDP was down 4.8%, including only 2 weeks of shutdown. April has been and May is likely to be a complete washout, potentially leading to huge drops in GDP, maybe as much as a 20% decline.

We are in trouble here, and therefore, so is the rest of the world. In addition to large reductions in GDP, relief bills and expansion of the Fed's balance sheet have added \$3-4 trillion in additional national debt, totaling ~\$25 trillion. This amount is likely to increase dramatically as government spending on relief pivots to stimulus. Regardless of the shape of the recovery, this pile of debt will slow the speed of our recovery.

## Private Equity Activity

- Private equity (“PE”) funds invested \$92 billion in 591 transactions in 1Q20, an 8.6% YoY increase, as 2020 began with a flurry of deal activity before COVID-19 shut down parts of the market in mid-March.
- The full impact of COVID-19 will be felt through at least 2Q20, as many PE firms focus on assisting existing portfolio companies in navigating current uncertainty, rather than evaluating new investment opportunities.
- PE firms that are actively pursuing new near-term opportunities are likely to prioritize add-on acquisitions or smaller transactions as they face obstacles in obtaining debt financing. Some may consider creative structures, such as closing with seller notes that could be refinanced when the debt capital markets rebound.
- Given these dynamics, M&A activity is expected to remain low for the remainder of 2020.
- U.S. PE middle-market exit activity declined sharply in 1Q20, with only \$34 billion realized across 179 transactions. Private equity investors are opting to hold portfolio companies until the market stabilizes. Both exit activity and fundraising are expected to remain muted for the remainder of 2020.

(1) Middle-market includes deal values of \$25M - \$1B.



Source: Pitchbook

## Leveraged Loan Market

- The leveraged loan market is under immense stress as lenders brace for higher defaults due to strain from mandatory COVID-19 shutdowns and the potential resulting recession. Many lenders are vulnerable to loans made at 5.0-6.0x pre-COVID EBITDA.
- In anticipation of defaults, large banks including JPMorgan Chase, Wells Fargo, Bank of America, Citigroup and Goldman Sachs increased reserves by nearly \$20 billion combined in 1Q20.
- A vast majority of lenders are not actively pursuing new opportunities as they (i) assess their existing portfolio, (ii) provide cash to the extensive number of current corporate clients drawing on existing lines of credit and (iii) assist smaller customers in applying for federal Paycheck Protection Program (“PPP”) loans and other borrowing options under the CARES Act.
- In an effort to soften the blow of the COVID-19 shutdown, the FOMC completed two rate cuts in 1Q20 to bring the target federal funds rate to between 0.0% and 0.25%. In addition, the Federal Reserve implemented a new quantitative easing plan that will buy at least \$500 billion in U.S. Treasuries and \$200 billion in mortgage-backed securities.
- The leveraged loan market is expected to stay fairly illiquid through 2Q20 as lenders re-evaluate market risk and their exposure.

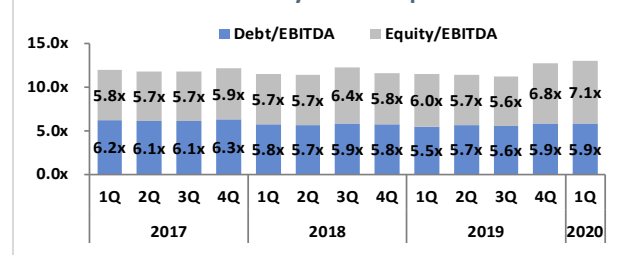
### Recent Leveraged Loan Statistics

	Leverage Pricing and Fees	
	Bank	Non-Bank
Pricing	L + (4.0 - 4.75%)	L + (5.0 - 6.0%)
Floor	-	-
Upfront Fees	50 bps	100 bps
Unused	25 - 37.5 bps	50 bps

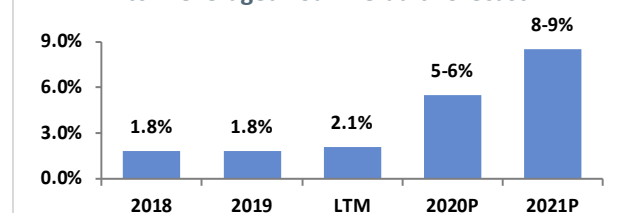
  

	Debt as a Multiple of EBITDA	
	Senior Debt	Total Debt
Healthcare Services	4.0x	5.0x
Healthcare IT	5.0x	6.0x
Non-Healthcare	4.0x	5.0x

### U.S. PE Buyout Multiples



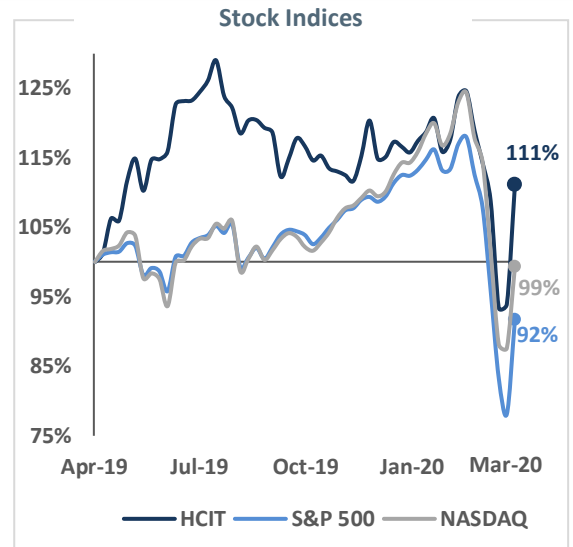
### Fitch Leveraged Loan Default Forecast



Source: Pitchbook; Fitch Ratings

## BCA Market Commentary & Stock Indices Relative Performance

- 1Q20 began with optimism for another year of steady deal volume and elevated prices for sellers of high quality HCIT assets, and ended with virtually all transactional activity grinding to a halt due to uncertainty related to COVID-19.
- As concern around the pandemic grew, operators and PE funds initially focused internally on (i) protecting cash reserves, (ii) converting to virtual work environments while also ensuring data security and HIPAA measures were in place and (iii) trying to understand the impact on the end markets into which they sold.
- BCA's conversations with financial sponsors suggest that, despite the ongoing turbulence related to COVID-19, financial sponsors remain interested in deploying capital. Almost all parties expect deal activity to remain low until the credit markets open and people are able to conduct in-person meetings again.
- Not surprisingly, telehealth and virtual care companies represent a well-performing sub-sector in an otherwise bleak HCIT environment. Telemedicine has gained broad and rapid acceptance as a viable form of care delivery. Public companies such as Livongo and Teladoc, for example, are up roughly 55% and 116% respectively, year to date.



## Select M&A Transactions

Date	Target	Acquiror	Target Business Description	TEV (\$M)
3/31/20	Carie	Emerald Organic Products	Mobile booking platform connecting users with board-certified doctors.	N/A
3/3/20	Loyale	RevSpring	Patient financial management platform for healthcare providers.	N/A
2/27/20	Duva Swako	Varsity Healthcare Partners	Practice management software for the medical industry.	Confidential
2/27/20	AlertMD	EverCommerce	Mobile platform for fee billings and revenue cycle management.	N/A
2/14/20	SimplifyASC	CSS Ormed	EHR and practice management software for the ASC market.	N/A
2/3/20	NantHealth (Connected Care Solutions)	Masimo	Patient vitals software solutions improving clinician productivity.	N/A
1/31/20	Lumere	Global Healthcare Exchange	Data and analytics platform for physicians and hospitals.	Confidential
1/13/20	SCI Solutions	R1	SaaS-based scheduling and patient access platform.	Confidential
1/8/20	CareCloud	Medical Transcription Billing	Practice management platform providing EHR and RCM solutions.	N/A

## Select Public Trading Multiples

(\$M except share prices)

Company	Ticker	Stock Price	% of 52-Week		TEV	TEV / Revenue		TEV / EBITDA	
			High	Low		LTM	NTM	LTM	NTM
Allscripts	MDRX	\$7.04	59%	154%	\$2,075	1.2x	1.2x	7.1x	6.6x
Cerner	CERN	\$62.99	78%	119%	20,731	3.6x	3.5x	12.0x	11.2x
Computer Programs & Systems	CPSI	\$22.25	62%	131%	430	1.6x	1.5x	10.3x	8.5x
Evolent	EHC	\$5.43	37%	155%	713	0.8x	0.7x	NM	NM
HealthStream	HSTM	\$23.95	80%	120%	635	2.5x	2.5x	13.5x	15.2x
HMS Holdings	HMSY	\$25.27	62%	139%	2,379	3.8x	3.4x	13.9x	12.7x
Inovalon	INOV	\$16.66	72%	145%	2,486	3.9x	3.5x	11.8x	10.6x
NextGen Healthcare	NXGN	\$10.44	49%	205%	742	1.4x	1.3x	8.3x	7.8x
Veeva	VEEV	\$156.37	88%	132%	23,721	NM	NM	NM	NM
<b>Average</b>						<b>2.4x</b>	<b>2.2x</b>	<b>11.0x</b>	<b>10.3x</b>
<b>Median</b>						<b>2.0x</b>	<b>2.0x</b>	<b>11.8x</b>	<b>10.6x</b>

Note: EBITDA includes add-backs for stock-based compensation and non-recurring expenses. Data per SEC filings and PitchBook.

## Brentwood Capital Advisors

### Industry Bankers

**John Kibler** | Managing Director  
(615) 224-3825  
jkibler@brentwoodcapital.com

**Jack Jeong** | Managing Director  
(615) 905-8032  
jjeong@brentwoodcapital.com

**Porter Meadors** | Director  
(615) 224-3821  
pmeadors@brentwoodcapital.com

### Select Recent Healthcare IT Transactions

Sell-Side  
**ORCHARD** Software  
Sell-Side Advisory to **FP** FRANCISCO PARTNERS

Sell-Side  
**CONNECTURE** Medicare  
Sell-Side Advisory to **HARRIS**

Recapitalization  
**harmony** HEALTHCARE IT  
Recapitalization Led by **PRIMUS**