THE
Health Care M&A MONTHLY
Inside the Health Care M&A Market

Volume 17, Issue 11
November 2012

INSIDE THIS ISSUE

ObamaCare Is Here To Stay

With Obama's Re-election, Full Implementation Comes Next

We decided to wait for the election results for the November issue because, if Mitt Romney had won, and with his pledge to repeal "ObamaCare," no matter how insincere that may have been, the landscape for health care in general, and health care M&A specifically, could have changed significantly. The level of uncertainty as to who the winners and losers would be would also have risen. Not to say that there isn't a high level of uncertainty in the market anyway.

The market greeted the election results with a resounding vote of no confidence, with the Dow plunging 312 points the next day, followed by a 121-point drop on Thursday for a cumulative decline greater than 3.1%. Within the health care sector, hospital stocks rose because investors believe the result confirmed that these providers will be getting more patients and revenues, while managed care, pharmaceutical and medical device stocks all dropped. What investors aren't focusing on is what these hospitals will be paid per episode in three, four and five years, and who will be trying to provide some of the similar services at a lower cost, putting competitive pres-

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Brisk October Follows Slow Q: 3

Heaviest M&A Deal Volume In Months Greets The Election

Just when we thought the health care M&A market was poised for a mini-recession, we had our own little October surprise with a flurry of announced transactions spread fairly evenly among the technology (51 deals) and services (53 deals) segments. It has been rare to have a single month with more than 100 transactions announced, but the overwhelming majority of the acquisitions, across both segments, were small in dollar value.

In the technology side of the business, the deal activity was pretty consistent among medical devices (12), biotechnology (14) and pharmaceuticals (18), but one of the more active sectors of the year, e-health, sort of fell flat in October with just seven deals, with revealed prices below $8.0 million. The total dollar volume for the technology sector, at just over $4.0 billion, was low compared with most months, and more than half of that came from the acquisition of **PSS World Medical** (NASDAQ: PSSI) by **McKesson Corporation** (NYSE: MCK) for $2.1 billion. McKesson is

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sure on both census and margins, even as the number of "insureds" rises.

We will play the contrarian role, since spending on hospital services represents more than 30% of total health care expenditures, and with hospital spending projected to grow by 75% in the next 10 years, that is the area where spending cuts (or reimbursement cuts) will have the most impact on potential savings. And since all the proposals for higher taxes won't put much of a dent in future federal deficits without a significant change in economic growth, the only way to slow the rate of growth in health care spending, by both the government and the private sector, is by lower reimbursement rates to providers and vendors, like pharmaceutical companies. Unfortunately, increased hospital volume alone will not make up the difference and will actually exacerbate the growing problem of rising health costs as a percentage of GDP. Yes, we know, the truth hurts. After all, the full name of what we all now call ObamaCare is the "Patient Protection and Affordable Care Act," and since we know that health care will not be any more affordable to the consumer through lower premiums, it will have to become more affordable to the government. The only way for that to happen is lower reimbursement rates or rationing, or most likely both. No one will be satisfied with that outcome.

Other than those who pay little or no income tax, no one is happy with all the taxes that will theoretically pay for ObamaCare, least of all the medical device companies, which for some reason were singled out, most likely because most of their products are not directly reimbursed so it was the only way to get them to help "pay" for ObamaCare. For four long years, President Obama vilified the millionaires and billionaires for not paying their fair share, the "fat cats" of Wall Street for not playing by the same rules that everyone else does, the 1-percenters who need to pay more, the health insurance companies for denying coverage and charging too much, the pharmaceutical companies for taking advantage of their patents to "rip off" America…in short, he has vilified you, our readers. Sorry, but demographically and professionally, that's the truth, and as we head toward the fiscal cliff in December, you will be the ones asked to pony up for the tax increases that will be coming. And some of you are okay with that, as long as the government is prudent with the extra money. To date, that has not been the case.

We found it very ironic that in a post-election story in *The New York Times*, the writers stated that "Wall Street…now has to come to terms with an administration it has vilified." Talk about the pot calling the kettle black. Just who has vilified whom? The Obama administration hasn't seen anything yet, because our bet is that one of the first "loopholes" that it will want to close, in order for the millionaires and billionaires to pay their fair share, is the tax treatment of "carried interest," something that is sacred to many on Wall Street, not to mention a few venture capitalists specializing in health care as well as owners and developers of health care-oriented real estate. We know quite a few wealthy democrats who cringe at the thought of higher taxes for carried interest, which also is ironic because higher taxes seem to be okay as long as they don't affect them. Right now, the carried interest tax treatment for limited partnerships, whether for venture capitalists or real estate developers, seems to be the most vulnerable to change in Congress. The reality, however, is that while it sounds good, it really impacts less than 1%

The Health Care M&A Monthly
ISSN#: 1091-9716
Published Monthly by:
Irving Levin Associates, Inc.
268-1/2 Main Avenue
Norwalk, CT 06851
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Annual Subscription Rate: $2,497
(Includes 50 Weekly Email Bulletins,
Four Quarterly Supplements And Special Database Access)

of the taxpayers (probably less than 0.2% and why there is little sympathy for them). Changing the tax rate from the current 15% to a maximum of 39.5% (as proposed) would only raise an additional $30 billion or so in taxes, which does not put much of a dent in the $1.2 trillion deficit. And that is based on a static analysis with no change in behavior by those paying the tax. While $30 billion may not seem like chump change, in the scheme of Washington expenditures and health care spending, it actually is.

As we head into the end of the year and the so-called "fiscal cliff," the economic environment could get even dicier as all the former tax cuts would go away and federal spending across the board would take a big hit if the leadership in Washington can't come to an agreement. That would not be good for any health care provider, and would not help the health care M&A market other than, at least in theory, valuations and prices would come down. While we may end up falling off the cliff, if it does happen, it would most likely be temporary enough to scare people into compromise and action. So what happens to the M&A market? As we mentioned last month, the third quarter was unusually slow in terms of number of announced transactions, which we concluded was because of the usual summer slowdown, combined with the continuing troubles in Europe and presidential election uncertainty here. Despite the lingering uncertainty on both sides of the pond, the deal volume surged in October to more than 100 announced transactions, something we don't see very often in one month. But despite the increased volume, the dollar value barely topped $10 billion, with only three transactions topping $1.0 billion in value. This excludes the not-for-profit mergers of hospital systems which technically have no price, and one of them would have been in that billion-dollar club.

There are often months without a large number of billion-dollar deals, but what was unusual about October, with so many transactions, was how small most of them were, with only five valued at more than $200 million each, and this includes the three billion-dollar deals. Call it timing, call it election uncertainty, call it anything you want, but this is where we believe some of the changes will take place in the M&A market, at least from now until the full implementation of ObamaCare. Acquisitions will be complementary, or "tuck-in" if you will, to fulfill a need or particular market, whether strategic or geographic, for the buyer, as opposed to the game-changing or industry-changing deals of the past. Not to say that some of these mergers and acquisitions will not occur (there is still no shortage of ego), but it will be more difficult for buyers (and their boards) to determine the financial impact of some of these multi-billion dollar acquisitions if they don't even know what the playing field will be, or even the game they are playing. (One editorial side-note: we are now reporting the dollar value of transactions that involve significant milestone payments (usually in the biotech and pharma sectors) using just the upfront payment as the base price, since it has always been impossible to really know how much of those earn-outs will ever come to pass.)

Consequently, in the technology segment we believe we will continue to see smaller acquisitions, product or licensing deals, consolidation among companies to strengthen their foothold in a certain treatment area. These seem to be safer bets with much lower risk levels, and with the IPO market still struggling, the exit strategy for these smaller companies will continue to be through the M&A market. But paying $10 or $20 billion for a large pharma company, when reimbursement for those drugs has nowhere to go but down as the reimbursement screws get tightened, just does not seem to make economic sense right now.

In the services segment, there is a different story, as the name of the game will be cost control. This will be especially true in the hospital sector, which already is under pressure from a quality perspective (readmission rates) and will be under increasing pressure from a cost perspective as more people are covered by insurance and as the baby-boomers age into more aggressive users of health care services. To deal with the former, there will be more acquisitions of or affiliations with physician medical groups, and for the latter there will be much more consolidation among not-for-profit hospitals. The problem is that unless the local or mini-regional hospital system is forced to seek a merger partner out of financial duress (and that will happen), local boards are often unwilling to give up control and maintain a somewhat parochial outlook on the future of health care delivery. We are also already seeing an increase in hospitals looking to buy local managed care companies, and managed care companies looking to buy local hospitals to help control costs and quality.

In a similar vein, small home health agencies and mom and pop skilled nursing operators will have an increasingly difficult time not only competing profitably, but also dealing with higher and higher acuity patients in a Medicare reimbursement world that will be more complicated and more miserly (which means more misery). These providers will continue to be consumed by large

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Deal Summaries—Technology — Biotechnology

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
SDIX GMO Business Washington, Mississippi	Private	**Romer Labs** Union, Missouri	Private	10/1/2012	$13,500,000

In Brief: SDIX is selling its food safety and genetically modified (GMO) businesses to Romer Labs, which is acquiring the intellectual property, current inventory and commercial contracts.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Rights to ASP 015K Northbrook, Illinois	TSE: 4503	**Janssen Biotech** Titusville, New Jersey	NYSE: JNJ	10/2/2012	$65,000,000

In Brief: Astellas Pharma is selling its rights to develop and commercialize worldwide, except Japan, its compound known as ASP 015K, which is a novel oral Janus Kinase inhibitor it has been developing for rheumatoid arhtritis and psoriasis. In addition to the upfront $65 million payment, there are milestones up to $880 million. Janssen Biotech is a subsidiary of Johnson & Johnson.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Therapeutic Nanobody Candid. Ghent, Belgium	XBRU: ABLX	**Merck & Co.** Whitehouse Station, New Jersey	NYSE: MRK	10/2/2012	$10,965,000

In Brief: Ablynx has entered into a collaboration agreement with Merck to develop Nanobody candidates to be used in conditions including neurological disorders, hypertension, diabetes, cancer and arrhythmia. There is an upfront payment plus milestones up to EUR 448 million.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
VTX-2337 Seattle, Washington	Private	**Celgene Corporation** Summit, New Jersey	NASDAQ: CELG	10/3/2012	$35,000,000

In Brief: VentiRx Pharmaceuticals formed a collaboration with Celgene for the development of VTX-2337, a novel cancer immunotherapy. In addition, Celgene has an option to buy VentiRx, which would be in addition to the $35 million upfront payment.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
NHE3 Inhibitor Program Fremont, California	Private	**AstraZeneca** London, United Kingdom	NYSE: AZN	10/8/2012	$35,000,000

In Brief: Ardelyx is selling its NHE3 inhibitor program, which is being developed both for constipation-predominant irritable bowel syndrome and for the prevention of sodium overload in patients with kidney and heart disease. In addition to the upfront payment, there are double-digit royalties and up to $237.5 million in milestone payments.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Rights to ADC Technologies Seattle, Washington	NASDAQ: SGEN	**Abbott Laboratories** Abbott Park, Illinois	NYSE: ABT	10/23/2012	$25,000,000

In Brief: Seattle Genetics is selling its development and commercialization rights to its monoclonal antibody therapies that are designed to selectively deliver cytotoxic agents to tumor cells. In addition to an upfront payment, there are up to $220 million in milestone payments.

Deal Summaries—Technology — Medical Devices

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Rhythmia Medical, Inc. Burlington, Massachusetts	Private	**Boston Scientific Corp.** Natick, Massachusetts	NYSE: BSX	10/8/2012	$90,000,000

In Brief: Rhythmia Medical is developing mapping, visualization and navigation systems for the treatment of cardiac arrhythmias, which include conducting human clinical testing outside the U.S. In addition to the $90 million, there are up to $175 potential milestone payments.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
BMEYE B.V. Amsterdam, The Netherlands	Private	**Edwards Lifescienses** Irvine, California	NYSE: EW	10/10/2012	$42,000,000

In Brief: BMEYE is developing non-invasive technology for advanced hemodynamic monitoring, primarily for use by clinicians outside the hospital. Edwards plans to integrate BMEYE's technology with its clinical platform in the hospital.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Lifetech Scientific Corporation Shenzhen, China	HK: 8122	**Medtronic** Minneaplois, Minnesota	NYSE: MDT	10/15/2012	$66,200,000

In Brief: Lifetech Scientific is developing advanced minimally invasive interventional devices for cardiovascular and peripheral vascular diseases. Medtronic is buying a 27% stake for $46.6 million cash and $19.6 million in a convertible note, with the right to increase its ownership.

Deal Summaries—Technology — Medical Devices (cont.)

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Surpass Medical Ltd. Tel Aviv, Israel	Private	**Stryker Corporation** Kalamazoo, Michigan	NYSE: SYK	10/16/2012	$100,000,000

In Brief: Surpass is developing next-generation stent technology to treat brain aneurysms, using a unique mesh design and delivery system. There are up to $35 million in additional milestone payments.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Neomend, Inc. Irvine, California	Private	**C.R. Bard, Inc.** Murray Hill, New Jersey	NYSE: BCR	10/23/2012	$140,000,000

In Brief: Neomend develops sprayable surgical sealants and anti-adhesion products. There are future contingent payments up to $25 million, through 2016, based on specific revenue-based milestones.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
PSS World Medical Jacksonville, Florida	NASDAQ: PSSI	**McKesson Corporation** San Francisco, California	NYSE: MCK	10/25/2012	$2,100,000,000

In Brief: MeKesson is paying $29 per share, for a 34% premium, and the price includes the assumption of debt. The price represents about 1.0x revenue and 12.2x trailing 12 months EBITDA.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Trivitron Healthcare Chennai, India	Private	**Fidelity India Capital** Mumbai, India	Private	10/27/2012	$74,400,000

In Brief: Fidelity Growth Partners India is buying a 35% to 40% stake in Trivitron from HSBC and ePlanet. Trivitron specializes in cardiology and implantable devices, imaging sciences, diagnostics, critical life support solutions and ophthalmology.

Deal Summaries—Technology — Pharmaceuticals

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Rights to Fareston Memphis, Tennessee	Private	**Prostaken Group Plc** Galashiels, United Kingdom	Private	10/1/2012	$21,700,000

In Brief: GTx Inc. sold its U.S. commercial rights to Fareston, a drug used for the treatment of metastatic breast cancer in postmenopausal women. Revenues had been about $7.3 million.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
ANI Pharmaceuticals Baudette, Minnesota	Private	**BioSante Pharmaceuticals, Inc.** Lincolnshire, Illinois	NASDAQ: BPAX	10/4/2012	$43,840,000

In Brief: After this merger, BioSante shareholders will own 53% of the combined company, with ANI shareholders 47%. BioSante is an integrated specialty branded and generic pharma.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
LigoCyte Pharmaceuticals, Inc. Bozeman, Montana	Private	**Takeda Pharmaceutical Company** Osaka, Japan	TSE: 4502	10/4/2012	$60,000,000

In Brief: Takeda is paying $60 million upfront plus future contingent payments for LigoCyte, a clinical stage biopharmaceutical company focused on developing novel vaccines for gastrointestinal and respiratory indications.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
HCMV Portfolio Wuppertal, Germany	Private	**Merck & Co., Inc.** Whitehouse Station, New Jersey	NYSE: MRK	10/15/2012	$143,000,000

In Brief: Merck has entered into an exclusive license agreement with AiCuris for the latter's portfolio of investigational medicines targeting Human Cytomegalovirus (HCMV) for the treatment and prevention of HCMV infection in transplant recipients. There is an upfront payment plus up to EUR 332.5 million in milestones payments.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Women's Health Business Dublin, Ireland	NASDAQ: JAZZ	**Meda** Somerset, New Jersey	NASDAQ: MDABF	10/15/2012	$95,000,000

In Brief: Jazz Pharmaceuticals sold its women's health business to Meda, a specialty pharma company, for cash.

Deal Summaries—Technology — Pharmaceuticals

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Presidio Pharmaceuticals, Inc. San Francisco, California	Private	**BioCryst Pharmaceuticals, Inc.** Durham, North Carolina	NASDAQ: BCRX	10/18/2012	$101,000,000

In Brief: Presidio is a clinical stage specialty pharmaceutical company specializing in small molecule antiviral therapeutics. Presidio shareholders are receiving 24.6 million BioCryst shares, but BioCryst's share price has plummeted since the announcement.

OctoPlus N.V. Leiden, The Netherlands	Euronext: OCTO	**Dr. Reddy's Laboratories Limited** Hyderbad, India	NYSE: RDY	10/21/2012	$35,333,000

In Brief: Dr. Reddy's is paying EUR 0.52 per share, representing a 30% premium, for the specialty injectables pharmaceutical company.

NextWave Pharmaceutcals Cupertino, California	Private	**Pfizer, Inc.** New York, New York	NYSE: PFE	10/22/2012	$275,000,000

In Brief: Pfizer paid a $20 million option in the second quarter, plus $255 million when the deal closes, and up to an additional $425 million in milestone payments. NextWave specializes in products for the treatment of ADHD and related CNS disorders.

OTC Trademarks and Assets Parsippany, New Jersey	NYSE: WPI	**The Harvard Drug Group, LLC** Livonia, Michigan	Private	10/29/2012	$117,000,000

In Brief: Watson Pharmaceuticals sold its Rugby OTC products and trademarks to Harvard Drug, a wholesale distributor and provider of private label OTC and generic prescription products.

Banner Pharmacaps High Point, North Carolina	Private	**Patheon, Inc.** Durham, North Carolina	TSX: PTI	10/29/2012	$255,000,000

In Brief: Banner is focused on softgel formulations for OTC, prescription and nutritional consumer products.

Additional Transactions—Technology

Sector	Target	Acquirer	Date
BIOTECHNOLOGY	NeoGenix Oncology	Precision Biologic, Inc.	10/1/2012
	AllergoOncology Technology Assets	Quest PharmaTech Inc.	10/2/2012
	Compendia Bioscience	Life Technologies Corporation	10/8/2012
	New Technology for Huntington's Disease	Raptor Pharmaceuticals Corp.	10/10/2012
	LymPro Alzheimer's Dianostic Blood Test	Amarantus Biosiences, Inc.	10/11/2012
	Pro 140	CytoDyn Inc.	10/17/2012
	VectorLogics, Inc.	DNAtrix, Inc.	10/23/2012
	Two TAL Technology Licenses	Cellectis Group	10/25/2012
E-HEALTH	InforMed Healthcare Solutions	Conifer Health Solutions, LLC	10/1/2012
	MED3000	McKesson Corp.	10/1/2012
	Accu-Med Technology Solutions	PointClickCare	10/8/2012
	KinLogix	TELUS	10/10/2012
	Sy.Med Development Inc.	Healthstream, Inc.	10/22/2012
	Logica Healthcare Group	Information Architects Corporation	10/23/2012
	Medrium, Inc.	AdvantEdge Healthcare Solutions	10/24/2012
MEDICAL DEVICES	Rights to Xenosure	LeMaitre Vascular, Inc.	10/1/2012
	ABT Medical	Creganna-Tactx Medical	10/4/2012
	Intermed Equipamento Medico Hospitalar	CareFusion Corp.	10/8/2012
	Spectrum Surgical Instruments	Steris Corp.	10/17/2012
	Medventure Technology	Helix Medical	10/17/2012
PHARMACEUTICALS	14 Generic Products	Par Pharmaceutical Companies, Inc.	10/15/2012
	Therakos, Inc.	The Gores Group	10/15/2012
	Covagen	Mitsubishi Tanabe Pharma Corporation	10/17/2012
	Kunwha Pharmaceuticals	Alvogen	10/18/2012
	Moksha8, Inc.	Undisclosed Buyer	10/22/2012
	RNAi Therapeutics Allinace in Asia	Genzyme	10/22/2012
	Developmnt Agreement for Linaclotide	AstraZeneca PLC	10/23/2012
	Mepha LLC	Acino Pharma Ltd.	10/25/2012

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companies or wannabes that see an opportunity. The problem is that after a while, with increased size comes a bureaucracy that becomes out of touch with the field, resulting in quality disruptions and, counterintuitive as it may be, increasing costs. The skilled nursing industry found this out when the former **Beverly Enterprises** topped 1,000 nursing facilities located in nearly every state, and then was forced to cut back to half that. While no one knows the optimal size, everyone knows it's not 1,000 buildings.

In the managed care segment, even though 2012 will go down as one of the most active years ever (in terms of M&A dollars spent), there remains the nagging question of whether ObamaCare is really a down payment on a single payer system. If so, what role would the health insurers have in the future, if any, and how do they make strategic decisions today with that thought looming? Perhaps **UnitedHealth Group** (NYSE: UNH) already did with its recently announced $4.3 billion acquisition of a Brazilian health care company serving more than 5 million people in that growing market. Is this what the market will evolve into as opportunities locally get squeezed? Perhaps. There are people who like to use Medicare as an example of efficiency (the pro-single payer people) because its administrative costs are so low relative to the private sector health insurers.

The other side of that coin is that Medicare is part of the problem because its expenditures have grown so much and the benefit received by the Medicare beneficiary (meaning the cost to everyone else) is so out of whack with what they pay (or have paid) into it, that a national system like this for everyone would definitely bankrupt the country, even though that has already happened. Regardless of what happens, consolidation will continue, and because the health care economy will continue to grow as the economy grows and as more people use the services available, there will always be opportunity, even in a single-payer world.

The Month in M&A at a Glance: Health Care Technology, October 2012

Sector	Deal Volume	Combined Price
Medical Devices	12	$ 2,617,200,000
Pharmaceuticals	18	1,241,373,000
Biotechnology	14	188,022,000
e-Health	7	7,968,000
Total	51	$ 4,054,563,000

Brisk October Follows Slow Q: 3

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paying $29 per share, representing a 34% premium, and the price comes to 1.0x revenues and 12.x EBITDA. The company markets and distributes medical supplies and equipment to office based physicians and long term care providers.

The next three largest transactions were in the pharmaceutical sector, with **Pfizer** (NYSE: PFE) agreeing to pay $255 million for privately-owned **NextWave Pharmaceuticals** after paying a $20 million option price in the second quarter. NextWave specializes in products for the treatment of ADHD and related CNS disorders, and the sellers may receive up to $425 million in milestone payments if things work out.

Netherlands-based Vion N.V., has agreed to sell **Banner Pharmacaps** to **Patheon, Inc.** (TSX: PTI) for $255 million. Banner is the world's second largest pharmaceutical business focused on softgel formulations for the over-the-counter, prescription and nutritional consumer products markets. **UBS Securities** represented Patheon. In the next largest transaction, **Merck & Co.** (NYSE MRK) is paying $143.0 million upfront to acquire the exclusive licensing agreement for Germany-based **AiCuris'** portfolio of investigational medicines targeting Human Cytomegalovirus (HCMV) for the treatment and prevention of HCMV infection in transplant recipients. In addition to the upfront payment, there are up to EUR 332.5 million in potential milestone payments.

Health Care Services

The health care services segment had an active month with 53 announced transactions for a total of $6.4 billion in disclosed prices. The real activity, however, was in just two sectors: hospitals and long-term care, with 25 deals between them. The hospital market has seen its share of potential mergers and affiliations called off (see the October 2012 issue), partly because of the rush to find a financially stronger partner without fully understanding all the ramifications of such an arrangement, and partly because they may not have made sense in the first place, not to mention other potential partners that may latently express an interest.

But as we stated last month, there are so many varieties of relationships that can be forged between not-for-profit hospitals that aren't actually mergers or acquisitions, one has to be careful in what label to use for many of these transactions. We try to be careful, but sometimes the parties themselves obfuscate things a bit, and the nature of the transaction often changes once discussions begin.

The Month in M&A at a Glance: Health Care Services, Ocotber 2012

Sector	Deal Volume	Combined Price
Managed Care	3	$4,306,000,000
Long-Term Care	12	2,014,300,000
Hospitals	13	65,000,000
Labs, MRI & Dialysis	4	6,500,000
Rehabilitation	3	1,500,000
Physician Medical Groups	4	—
Home Health & Hospice	2	—
Behavioral Health	0	—
Other Services	12	—
Total	53	$6,393,300,000

In the most significant merger of the month, and probably of the year, the boards of Michigan-based **Trinity Health** and Pennsylvania-based **Catholic Health East**, have signed a letter of intent to join as a unified health system. Combined, they will operate 82 hospitals, more than 60 long-term care and assisted living facilities, LTACs, CCRCs, outpatient clinics and a very large home health and hospice business (which may be one of the top 10 in the country post-merger), all in 21 states. Now, things can always cause a merger of this size to break apart before it reaches the finish line, but at least there is no religious issue, since both are Catholic-based, and we don't believe there will be any anti-competitive issues either since they pretty much operate in different areas. Compared with this transaction, all the other hospital mergers and acquisitions look fairly small, usually involving just one or two hospitals as the target.

One hospital, however, ventured into the managed care arena. **Detroit Medical Center** (DMC) announced plans to purchase **ProCare Health Plan**, the only 100%-owned African American HMO in Michigan (perhaps in the country). ProCare currently provides three health care programs covering more than 10,000 residents in Wayne County. DMC is the largest health care provider in southeastern Michigan. The purchase price was a relatively small $6.0 million. There was nothing small, however, about **UnitedHealth Group's** (NYSE: UNH) purchase of a Brazilian health care company, **Amil Par-**

ticipacoes S.A. (IBOV: AMIL3) for $4.9 million which, after netting out $600 million of realizable tax benefits, comes to $4.3 billion. The annualized revenue of the target is about $5.0 billion, and Amil serves more than 5 million people in the country.

Seniors Housing. It's time to put one in the win column for private equity and seniors housing, and a big win it was. Back in early 2010, **Blackstone Real Estate Partners VI** and its partners, **Emeritus Corporation** (NYSE: ESC) and **Columbia Pacific Advisors**, agreed to buy a portfolio of 144 mostly assisted living and memory care properties with 11,769 units from the bankrupt **Sunwest Management** for $1.294 billion, or $110,00 per unit. Based on "fresh-start" accounting, the pro forma revenues and EBITDA were about $349.9 million and $100.7 million, respectively, resulting in a pro forma cap rate of 7.8% and an operating margin of 28.8%. Occupancy for the portfolio at the time was just over 79%, and there was some concern that Emeritus, which was growing at a rapid pace, would have some difficulty with this portfolio because of its size, need for significant capital expenditures, the poor reputation in some of the local markets because of the previous Sunwest management and a cost structure at the local level that was assumed to be too low.

The transaction finally closed in August 2010, and by 2011, initial reports were that operating performance and occupancy were better than originally forecasted. The joint venture has invested about $42 million, or $4,100 per unit, in capital improvements during the past two years, and this may have helped occupancy increase to 86.8% year-to-date in 2012, and a reported 88% or so currently. For disclosure purposes, the purchaser of the portfolio this time around, **HCP, Inc.** (NYSE: HCP), has divided the portfolio of 133 communities it is purchasing into the "stabilized" group of 99 properties with 91.5% occupancy and the 34 "lease-up" group with 74.0% occupancy. This is important when it comes to the lease terms between HCP and Emeritus. But first, let's take a look at some of the details of the new transaction, which closed in record time on October 31.

Of the original transaction two years ago with 144 properties, it looks like two of them may have been sold, leaving 142 communities with 10,350 units. HCP is buying 133 of these for $1.728 billion, or $166,950 per unit. The price allocated to the stabilized portfolio is $1.326 billion, or $175,250 per unit and a 6.8% cap rate, and the price for the lease-up portfolio is $402 million, or $144,400 per unit and a 5.7% cap rate, for a blended in-place cap rate of 6.6%. These are obviously aggressive cap rates for what is not an "A" quality portfolio, even though there are some A- properties in there and a good share of B+ properties, from what we hear. It would be nice to know how much of the occupancy improvement came from the stabilized portion versus the lease-up, and what each group was two years ago. These properties will be leased to Emeritus with a first-year lease payment of $105.5 million (a 6.1% initial lease rate).

The remaining nine properties with approximately 1,000 units are being purchased directly by Emeritus for $62 million, or a very low $62,000 per unit, which may be why HCP didn't want them (at least not yet). HCP is providing ESC with a $52 million, four-year loan with an initial interest rate of 6.1% (same as the lease rate) to complete the purchase, with ESC using $10 million of cash for the balance.

When Emeritus teamed up with Blackstone to buy the Sunwest portfolio two years ago, it was thought to be a big win for ESC because of the $17.5 million of guaranteed management fee income (5% of revenues) plus incentive payments based on the overall return to Blackstone. Because the portfolio was operating at just a 79% occupancy rate at the time, the Emeritus management team thought an incentive payment down the road would be a no-brainer. Little did they know (or maybe they did). Emeritus received approximately $40 million for its 5.8% interest in the joint venture (a $19 million investment), plus a whopping $100 million as an incentive payment. That comes to $175 million of profit and management fees over the 26 months they managed the portfolio on behalf of the joint venture. Of this $140 million in proceeds to Emeritus, $10 million will be used for the purchase of those nine properties mentioned, $30 million will go towards capital improvements at the properties, and the rest will be used to fund the acquisition of a home health care company in Florida. If this is not a win-win, we don't know what is, but there are some future risks.

As far as Blackstone is concerned, it made a 2.4x multiple on its $225 million investment in just two years (26 months). Despite possible protests to the contrary, there is no way they expected that kind of return with this troubled portfolio in so short of a time period. While it would be nice to say the teams at Emeritus and Blackstone are geniuses, the reality is that there was a fair amount of luck and great timing involved. As we mentioned, the pro forma EBITDA of the portfolio at the time of the original

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Deal Summaries—Services — Laboratories, MRI & Dialysis

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Escalon Clinical Diagnostics Bus. Wayne, Pennsylvania	NASDAQ: ESMC	**ERBA Diagnostics, Inc.** Mannheim, Germany	NYSE: ERB	10/4/2012	$6,500,000

In Brief: Escalon Medical Corp. has sold its subsidiaries, Drew Scientific, Inc. and JAS Diagnostics, for $6.5 million cash.

Deal Summaries—Services — Hospitals

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
St. Vincent's Health System Eerie, Pennsylvania	Nonprofit	**Highmark** Pittsburgh, Pennsylvania	Nonprofit	10/19/2012	$65,000,000

In Brief: St. Vincent's has about 400 beds and has been serving the Eerie area for more than 100 years. Under terms of the proposed merger, managed care company Highmark will provide St. Vincent's with $20 million in cash, $5 million for capital projects and $40 million over the next three years to improve existing facilities and to invest in new assets. In fiscal 2012, St. Vincent's had revenues of $327 million and EBITDA of $15.3 million.

Deal Summaries—Services — Long-Term Care

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Heritage Place Fayettville, North Carolina	Private	**Meridian Senior Living** Hickory, North Carolina	Private	10/3/2012	$9,300,000

In Brief: Heritage Place has 80 independent living units that were built in 1983 and 50 assisted living units built in 1998. Revenues and EBITDA, based on 75% occupancy, were $3.95 million and $300,000, respectively. About $1.0 million of renovations had recently been completed.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Paradise Park Assisted Living New Lenox, Illinois	Private	**Focus Healthcare Partners, LLC** Chicago, Illinois	Private	10/3/2012	$9,800,000

In Brief: Focus, together with its joint venture partner Artemis Real Estate Partners, bought this community in a court-ordered bankruptcy sale. Occupancy was only 60% since it had difficulty ramping up census when it opened in 2007. In-place EBITDA was $500,000.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
18 North Carolina ALFs North Carolina	Private	**Chevalier International Holdings** Kowloon Bay, Hong Kong	HK: 25	10/11/2012	$124,000,000

In Brief: The sellers, a joint venture between Formation Capital and Smith/Packett, purchased this portfolio in December 2009 for $98 million. About 75% of the residents are funded by Medicaid, and almost half the residents are memory care. The revenue and EBITDA multiples were 3.4x and 10.4x, respectively. The transaction is expected to close by December 31.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Six Assisted Living Facilities Ohio	NYSE: ADK	**Ohio ALF Operator** Ohio	Private	10/12/2012	$22,300,000

In Brief: AdCare Health Systems is selling six of its Ohio assisted living facilities to a local operator. Revenues for the group were about $8.9 million. AdCare wants to focus on growing its skilled nursing portfolio, and will receive $7.2 million cash after paying down debt.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Portfolio of 133 Sr. Living Com. 29 states	NYSE: BX	**HCP, Inc.** Long Beach, California	NYSE: HCP	10/16/2012	$1,728,000,000

In Brief: Blackstone Real Estate Advisors, together with its joint venture partner Emeritus Corporation, sold 133 of the 144 senior living communities they purchased in 2010 for $1.294 billion. HCP will lease the properties to Emeritus for an initial lease rate of 6.1%. Emeritus purchased the remaining nine properties, financed with $52 million of debt from HCP, for $62 million. Blackstone made an approximately 2.4x return on its investment in two years. The deal closed on October 31.

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
8 Senior Living Communities Indiana, Ohio and Texas	Private	**Capital Senior Living** Dallas, Texas	NYSE: CSU	10/24/2012	$72,900,000

In Brief: Capital Senior Living is buying six communities in Indiana and Ohio for $62.5 million, and two in Texas for $10.4 million, from two separate sellers. Revenues are $20.4 million, and CSU is financing the deal with $50.2 million of a variety of debt instruments with a blended cost of 4.5%.

Deal Summaries—Services — Long-Term Care (cont.)

TARGET	LISTING	ACQUIRER	LISTING	DATE	PRICE
Palisades at Broadmoor Colorado Springs, Colorado	Private	**MBK Senior Living** Irvine, California	Private	10/24/2012	$30,500,000

In Brief: This community was built in 2008 and has a total of 124 units including independent living, assisted living and memory care. Occupancy has been averaging 85%, and revenues and EBITDA were $5.2 million and $1.4 million, respectively.

Deal Summaries—Services — Managed Care

Amil Participacoes S.A. Rio de Janeiro, Brazil	IBOV: AMIL3	**UnitedHealth Group** Minnetonka, Minnetonka	NYSE: UNH	10/8/2012	$4,300,000,000

In Brief: Amil is the largest health care company in Brazil serving more than 5 million people. The actual price was $4.9 billion, but was lowered after netting out $600 million of realizable Brazilian tax credits.

Additional Transactions—Services

Sector	Target	Acquirer	Date
HOME HEALTH & HOSPICE	Celtic Healthcare, Inc.	The Washington Post Company	10/1/2012
	Home Solutions	KRG Capital Partners	10/17/2012
HOSPITALS	Southampton Hospital	Stony Brook Medicine	10/12/2012
	First Surgical Partners, Inc.	Not Disclosed	10/3/2012
	Mountain View Hospital	St. Charles Health System	10/3/2012
	Chilton Hospital	Atlantic Health System	10/10/2012
	Halifax Regional Health System	Sentara Healthcare	10/12/2012
	St. Joseph and St. Mary's Medical Centers	HCA Midwest Health System	10/16/2012
	Harrison Medical Center	Franciscan Health System	10/16/2012
	Catholic Health East	Trinity Health	10/17/2012
	Landmark Medical Center	Prime Healthcare Services	10/18/2012
	Memorial Hospital	MaineHealth	10/19/2012
	Sherman Health Systems	Advocate Health Care	10/23/2012
	Beaumont Health System	Henry Ford Health System	10/31/2012
LABS, MRI & DIALYSIS	Clinical Diagnostics Business	ERBA Diagnostics, Inc.	10/4/2012
	Clinical Outreach Laboratory	Quest Diagnostics	10/16/2012
	Citrano Medical Laboratories, Inc.	CD Diagnostics, Inc.	10/18/2012
	OURLab	OPKO Health	10/19/2012
LONG-TERM CARE	70-Bed Skilled Nursing Facility in Arkansas	AdCare Health Systems, Inc.	10/1/2012
	Six Radius Health Care Centers in MA	Athena Health Care Systems	10/3/2012
	Family Care Center of Kingston in OK	Regional Operator	10/4/2012
	Paradise Assisted Living in MD	Shangri-la Health Care	10/10/2012
	2 Texas Assisted Living Facilities	East Coast Operator	10/31/2012
MANAGED CARE	ProCare Health Plan, Inc.	Detroit Medical Center	10/25/2012
	UnitedHealthcare's SC Medicaid Business	WellCare Health Plans, Inc.	10/31/2012
PHYSICIAN MEDICAL	Elder Medical Services P.C.	IPC The Hospitalist Company, Inc.	10/1/2012
	Beaumont Physician Organization	United Physicians, Inc.	10/5/2012
	Nautilus Health Care Group	Healogics, Inc	10/12/2012
	Medical Gastroenterology and Endoscopy Gr.	Global Health Partner	10/16/2012
REHABILITATION	Bay Area Pain, Spine Center, Brunswick Pain	Prospira PainCare	10/4/2012
	DMC Athletics and Rehabilitation, Inc.	Pazoo, Inc.	10/4/2012
	Walton Rehabilitation Hospital	HealthSouth Corporation	10/24/2012
OTHER	J.A. Thomas and Associates	Nuance Communiciations	10/1/2012
	Biltmore Surgical Center	Scottsdale Healthcare	10/2/2012
	Shoreline Colonoscopy Suites	Middlesex Hospital	10/2/2012
	Health Data Essentials	Peak Health Solutions	10/4/2012
	Promedical, Inc.	CBIZ, Inc.	10/4/2012
	Affinity Medical Technologies, LLC	Molex Incorporated	10/11/2012
	9 Urgent Care Centers in Oklahoma	NextCare Urgent Care	10/12/2012
	PDR Partners	CROMSOURCE	10/12/2012
	Medrec, Inc.	Accountable Healthcare Holdings Corp.	10/15/2012
	MedBE, Inc.	MediGain Services, Inc.	10/16/2012
	Two Urgent Care Clinics in Tx and AZ	NextCare Urgent Care	10/25/2012

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purchase was about $100.7 million. Since then, that has increased to about $113 million, plus whatever those extra nine properties are making (or losing). When the auction was held a few years ago, Sunwest's advisors were telling potential investors that at 85% occupancy, EBITDA should be about $135 million before capex, and $160 million at 88% occupancy in 2014. Obviously, the portfolio beat the projection on occupancy by almost two years, but fell short on the EBITDA number by a significant amount.

The value increase has everything to do with cap rate compression in the past 18 months or so (well, almost everything). The approximately $496 million gain on the sale (including the nine properties not purchased by HCP, to which we attribute limited cash flow), can be broken down to about two-thirds based on the 120 basis point drop in the cap rate (7.8% to 6.6%), and about one-third to the increase in cash flow. Without the drop in cap rates, this would have just been a decent investment. So, what was the rush to sell?

Since no one thinks cap rates are increasing any time soon, nor interest rates, wouldn't one of the REITs have been willing to pay a similar multiple of cash flow next year or in 2014, when cash flow would theoretically be higher, maybe by $10 million? If the lease-up group, which currently has cash flow of $8,225 per unit, reaches the level of the stabilized group (now at $11,918 per unit), that represents up to an additional $150 million of potential value. And if the stabilized group continues to improve as well, just consider the increase in value. Gordon Gekko's famous line that "greed is good" got a lot of play, but we assume the Blackstone team was not going to let an opportunity like this pass on the hope that they might achieve even higher returns in a year or two. So, a bird in hand, with that 2.4x return, will just have to do, and a wise decision it was.

With a dividend yield under 5.0%, and a cost of debt below that, HCP's initial yield on the acquisition of 6.1%, while relatively low, is still profitable and will be immediately accretive, even after the 22 million shares it sold to raise the cash for the acquisition and keep its capital structure at 60% equity and 40% debt. The initial EBITDAR lease coverage is low at 1.07x, but for the 69 Emeritus communities HCP already owns the EBITDAR coverage was just 1.13x last year, and these had an average occupancy rate of 84.4% in 2011. One could ask why HCP is not doing this as a RIDEA-structured transaction, because of the upside. The simple answer is that it is sort of a hybrid, with the upside associated with a five-year rent reset for the lease-up properties with little downside risk and a full Emeritus guarantee on the leases.

Venture Capital And IPO Market

Although not nearly as robust as several years ago (that's an understatement), venture capital is still flowing into biotech and specialty pharma companies, just not like in the past. In October, two companies trying to develop novel approaches to dermatological disorders completed Series A financings. In the larger of the two, **Aclaris Therapeutics, Inc.** raised $21 million led by **Vivo Ventures** and **Fidelity Biosciences** with a participation from **Sofinnova Ventures**. Aclaris is developing a new topical product, and it will be led by Dr. Neal Walker, a dermatologist who has been the CEO of a few other small pharmaceutical companies that have recently been sold.

In the slightly smaller deal, **Thesan Pharmaceuticals** raised $16 million in a Series A co-led by **Novo Ventures** and **Novartis Venture Funds**. Thesan has a lead drug candidate that is a topically-applied chemical treatment that is expected to enter the clinic next year. The company has been licensing products from the **University of California, Irvine**, and is also working with the **Istituto Italiano di Tecnologia** in Genoa, Italy.

Novartis Venture Funds also led a Series A1 round for **Neurovance, Inc.**, a spinout of **Euthymic Bioscience, Inc.**, that is focusing on the development of a treatment for adult attention deficit hyperactivity. Neurovance recently completed a phase 1 clinical trial of its lead product, which was well tolerated and demonstrated a wide therapeutic index. One of the things they like about this new drug is that it may have a low risk of drug abuse. Six existing investors also participated in this small round.

In some later stage deals, **Genocea Biosciences, Inc.** raised $30 million in a Series C round, which was co-led by the **Bill & Melinda Gates Foundation** and **CVF, LLC**, with eight existing investors also participating. The company has now raised a total of $76 million. Genocea is a clinical stage company working on innovative T-cell vaccines for infectious diseases. Its two lead programs include a clinical stage therapeutic vaccine candidate to deal with moderate and severe Herpes Simplex Virus type 2, as well as a drug candidate to prevent infections caused by Streptococcus pneumonia. It is also working to expand its malaria program together with the Gates Foundation.

Two companies looking at treating problems with the kidney raised significant funds to further their product development. **ZS Pharma, Inc.** raised $46 million in a Series C round led by **Alta Partners** and joined by new investors **RiverVest Venture Partners**, **3x5 Special Op-**

portunity Partners and **Salem Partners**. ZS Pharma is developing a crystal form of zirconium silicate to treat patients with kidney and liver disease. The therapy is designed to remove life-threatening toxins from patients, and clinical testing has focused on patients with elevated levels of potassium in their blood. Meanwhile, **Thrasos Therapeutics** has raised $35 million led by new investor **SR One**. The company's lead product candidate is for the treatment of acute kidney injury (AKI), which is the temporary loss of renal function that can occur following cardiac and vascular surgery, inflammatory disease and trauma. Over 1 million AKI patients are diagnosed each year in North America alone.

Last month we mentioned that two small pharmaceutical companies teed up for their IPOs in a market that has not been overly friendly. Both had happy endings, at least so far. **Kythera Biopharmaceuticals** (NASDAQ: KYTH) sold 5.1 million shares priced at $16.00 per share, and they jumped by more than 35% in what was either a well-positioned IPO or one where the pricing was just too cheap to get the deal done. Kythera is developing an injectable treatment for double chins called ATX-101. It plans to use most of the proceeds from its IPO to fund late-stage studies of ATX-101. **J.P. Morgan Securities** and **Goldman, Sachs** co-led the IPO.

In the other successful IPO, **Intercept Pharmaceuticals** (NASDAQ: ICPT) sold 5.75 million shares at $15.00 per share, which closed up 30% on the first day in another successful IPO. Intercept is a biopharmaceutical company focused on the development and commercialization of novel therapeutics to treat orphan and more prevalent liver diseases utilizing its expertise in bile acid chemistry. **BofA Merrill Lynch** was the lead underwriter on the IPO.

There have been articles written in the recent past about the death of the VC industry, or at least its sharp contraction since the bursting of the tech bubble in 2001. Specifically, biotech venture funding has seen the most dramatic fall in investing activity, and some biotech-oriented VC firms may be watching the recent spate of IPOs for future investment targets if they don't do well. The two companies above seem to not fit in that category. Perhaps it likes to play the contrarian role, but **Longitude Capital** closed its second life sciences fund in October with $385 million in commitments, or $60 million more than its first fund, which closed in July 2008 and has invested in nearly 20 companies. Longitude focuses primarily on mid-stage to commercial-stage companies with clinically "de-risked" assets and three-to-five year liquidity horizons. **Probitas Partners** was the exclusive placement agent and financial advisor to Longitude Capital.