Private Practice Consolidation Opportunity in the Fragmented Urology Specialty

Private equity investment and consolidation in the urology sector will provide an opportunity for independent practices to avoid the trend of hospital employment by continuing to thrive in a group practice setting.

INTRODUCTION

The urology sector has yet to see significant investment and consolidation led by private equity, but the specialty is poised to be a newer area of interest from the investor community as evidenced by Audax Group's 2016 recapitalization of Chesapeake Urology. Large group practices will be at an advantage over smaller groups as an aging U.S. population will continue to drive demand for urologic procedures, and a projected shortage of urologists will put further emphasis groups' ability to recruit new providers and increase the productivity per physician.

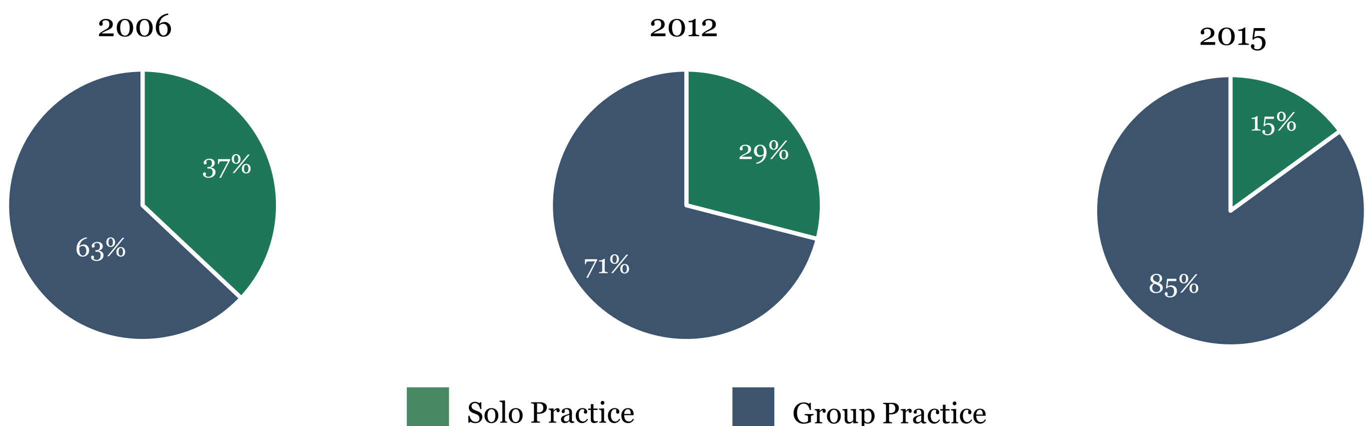
With 12,186 practicing urologists in the U.S.[1], the specialty is similar in size to dermatology and gastroenterology, but smaller relative to other actively consolidating physician services areas highlighted in Table 1. However, a high level of market fragmentation and the presence of several market-leading platforms indicates there's an opportunity for a regional or national roll-up strategy led by private equity. As seen in Figure 1, consolidation in the industry has been occurring for the last decade, primarily driven by hospital acquisitions and mergers with larger practices.

TABLE 1:
SIZING THE UROLOGY MARKET

Specialty	Number of Practicing Physicians in U.S.
Anesthesia	38,749
Dental	195,722
Dermatology	11,062
Emergency Medicine	36,607
Gastroenterology	13,014
Ophthalmology	17,413
Orthopedics	18,292
Primary Care	256,679
Radiology	24,784
Urology	12,186

Sources: Association of American Medical College's 2016 Physician Specialty Data Report, American Dental Association's Health Policy Institute, American Urological Association (AUA) 2016 Census

FIGURE 1:
UROLOGISTS IN SOLO PRACTICE

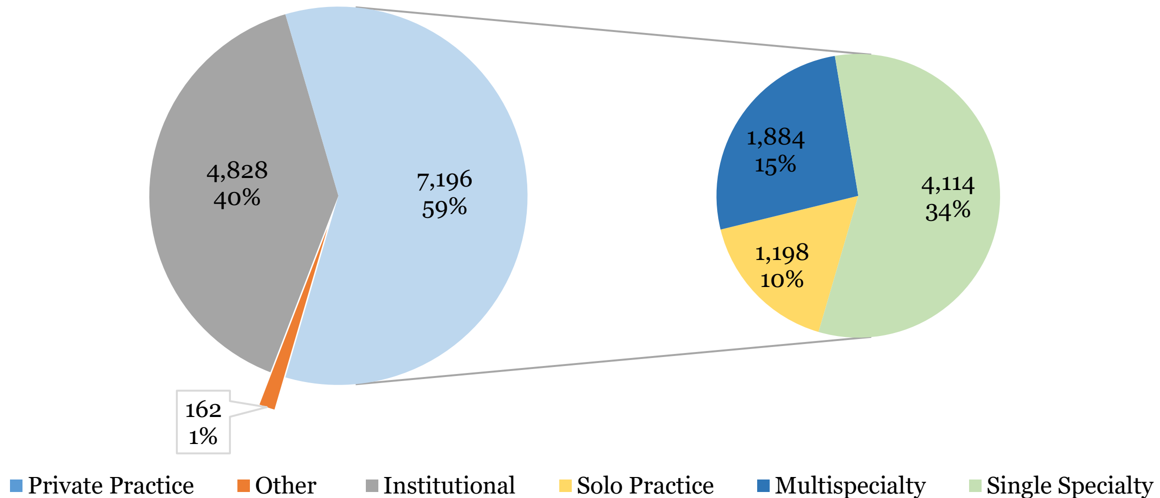


Sources: Sg2 Health Care Intelligence, Becker's

[1] *American Urological Association, The State of Urology Workforce and Practice in the United States 2016. Linthicum, Maryland, U.S.A, April 11, 2017*

MARKET FACTORS AFFECTING THE UROLOGY INDUSTRY

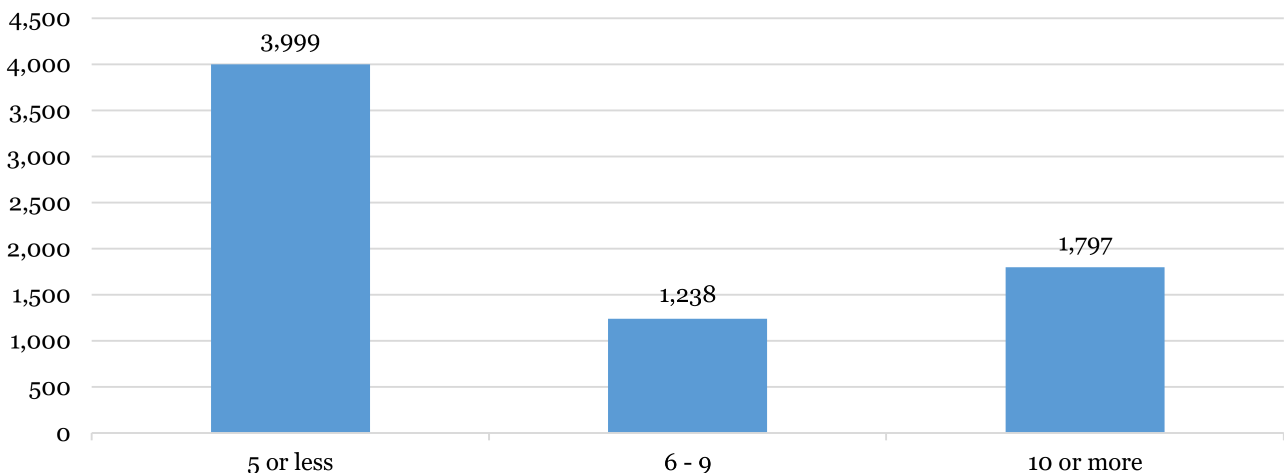
FIGURE 2:
UROLOGISTS BY PRACTICE SETTING – 2016 DATA



MARKET FRAGMENTATION

Similarly to most physician specialties, the U.S. urology industry has significant fragmentation nationally. According to data from the American Urological Association 2016 Census, nearly 60% of the 12,186 practicing urologists, or 7,196 physicians, are in a private practice setting, and about 17% of those physicians, or 1,198 urologists, are solo practitioners (Figure 2). Furthermore, over 5,000 urologists reported in the 2016 survey to be part of a practice with 10 or less total urologists (Figure 3).

FIGURE 3:
PRIVATE PRACTICE UROLOGISTS - NUMBER OF PHYSICIANS PER PRACTICE



Source: American Urological Association (AUA) 2016 Census

MARKET FRAGMENTATION (CONT.)

The single specialty urology market presents an attractive opportunity for a regional or national consolidation strategy. With over 5,300 doctors practicing as part of single specialty urology groups, fragmentation is very evident given only eight practices nationally have more than 50 total providers, which includes NPs, PAs, and physicians (Table 2). The five largest single specialty urology groups in the country employ 309 doctors, according to company websites, which is less than 6% of urologists practicing in single specialty groups nationally. Private equity groups that partner with one of the leading platforms in the sector have an opportunity to consolidate fragmented regional markets through add-on acquisitions.

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TABLE 2:
LARGEST UROLOGY GROUPS IN THE U.S. BY PROVIDER COUNT

Size	Group Name	State(s)	Number of Providers*	Number of Locations
1	Integrated Medical Professionals *(also known as Advanced Urology Centers of New York)*	NY	100	48
2	Urology Associates of North Texas	TX	81	25
3	UroPartners	IL	80	34
4	Chesapeake Urology	MD, DC	77	22
5	Michigan Institute of Urology	MI	64	24
6	New Jersey Urology	NJ	60	32
7	Georgia Urology	GA	56	29
8	Comprehensive Urology	MI	51	25
9	Carolina Urology Partners	NC, SC	44	15
10	Urology Associates	TN	44	12
11	Virginia Urology	VA	44	9
12	Urology of Virginia	VA	42	6
13	The Urology Group	OH, IN, KY	41	12
14	Kansas City Urology	MO	38	20
15	Urology of Indiana	IN	38	18

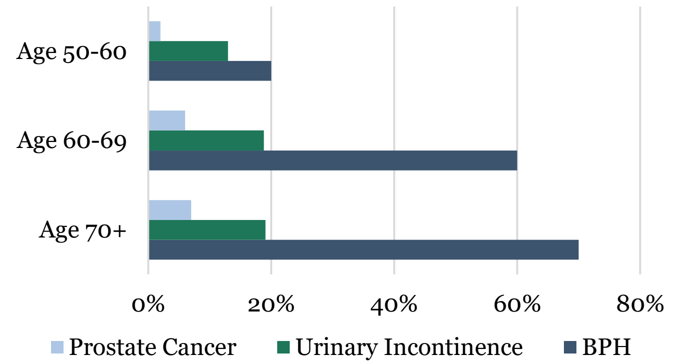
Source: Bladder Health Network, as of May 2017
** Providers include NPs, PAs, and physicians*

RISING DEMAND FOR UROLOGIC PROCEDURES WILL OUTPACE THE SUPPLY OF UROLOGISTS

Driven primarily by the aging U.S. population, demand for urologic procedures is projected to rise as the prevalence of prostate cancer, urinary incontinence, and Benign Prostatic Hyperplasia ("BPH") significantly increases in the age 60 and over population (Figure 4). Patient demand for these services is expected to outpace the supply of urologists as over 50% of the practicing urologists in the U.S., or 6,175 urologists, are over the age of 55, with only approximately 300 urologists graduating from residency programs each year (Figure 5).

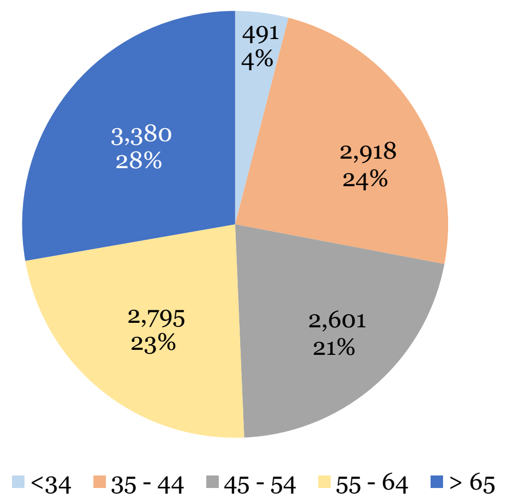
To meet the demands of the patient population, urology practices will need to be efficiently managed both operationally and clinically, leverage size and scale across multiple markets to better recruit physicians, and utilize physician extenders as their role grows within the specialty. The management capabilities and clinical protocols of a platform entity will provide an opportunity post-closing for organic growth of less efficiently managed add-on acquisitions that also lack a full suite of sub-specialty coverage.

FIGURE 4:
PREVALENCE OF UROLOGICAL CONDITIONS



Sources: The American Urological Association, The Centers for Disease Control and Prevention, Prostate Cancer Foundation, National Center for Biotechnology Information

FIGURE 5:
U.S. UROLOGISTS BY AGE GROUP



Source: American Urological Association (AUA) 2016 Census

REIMBURSEMENT ADJUSTMENTS UNDER MACRA

As the patient-to-urologist ratio increases, practices nationwide are also preparing to report value-based metrics as a result of the shift to The Merit-based Incentive Payment System ("MIPS") outlined under the Medicare Access and CHIP Reauthorization Act of 2015 ("MACRA"). Large group practices that have invested in management, healthcare information technology, sub-specialty expertise, and the implementation of practice-wide clinical protocols are poised to benefit under MIPS through their ability to qualify for bonus payments starting in 2019 and beyond (Figure 6; Figure 7). A one-stop-shop model for providing urologic services is critical to controlling the full continuum of care for the patient.

MACRA is expected to be an impetus for consolidation in the urology industry as solo practitioners and physician-managed practices look to align with larger private providers or health systems that can alleviate the administrative burden and infrastructure costs necessary to qualify for bonus payments under the new quality payment system. Private equity-backed groups will see an opportunity to scale management services via alignment with these providers.

A SHIFT FROM VOLUME TO VALUE

The passage of MACRA signifies a trend towards value-based payments in healthcare, and urology stands to be favorably impacted by MIPS; when the urology sector begins experiencing zero-sum payment adjustments in 2019 based on 2017 clinical performance data, many urology groups are poised to realize positive reimbursement outcomes. CMS estimates total bonus money to urologists of $17.9 million in 2019, with an estimated 72.4% of urologists being eligible for exceptional performance bonuses.

FIGURE 6:
MIPS PERFORMANCE CATEGORIES

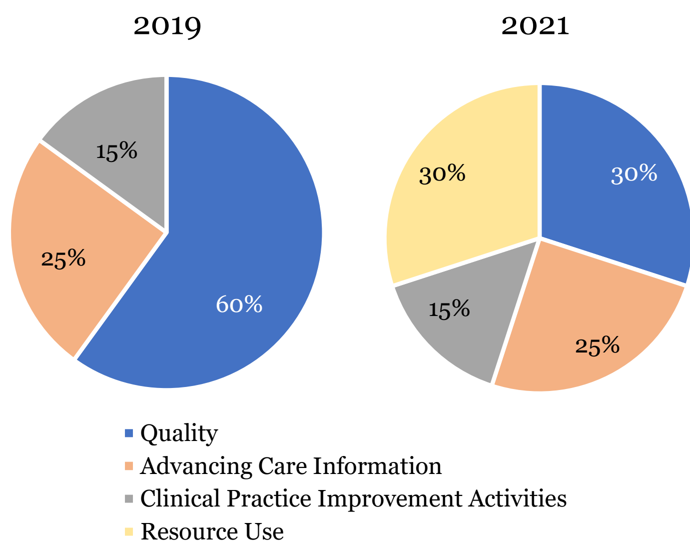


FIGURE 7:
MIPS PAYMENT ADJUSTMENT SCHEDULE

	2019	2020	2021	2022 +
Maximum positive adjustment	+4%	+5%	+7%	+9%
Maximum negative adjustment	-4%	-5%	-7%	-9%

Sources: Centers for Medicare and Medicaid Services, ModernMedicine

PRIVATE EQUITY: THE ALTERNATIVE TO HOSPITAL EMPLOYMENT

HEALTH SYSTEM ACQUISITIONS

Consolidation within the urology sector has historically been led by hospitals and health systems acquiring group practices locally. As of 2016 data, about 40% of practicing urologists in the U.S. work in an institutional setting, an approximately 6% increase since 2014[1]; financial and administrative challenges that private practices face around government regulations, reimbursement under value-based care, and the lack of leverage in negotiations with large payors have made hospital employment a more secure option with better quality of life for small practice urologists. However, hospital employment limits the autonomy and ownership that urologists sought after in their decision to practice in an outpatient setting. Additionally, the shift to inpatient care can increase healthcare costs for the specialty.

THE ATTRACTIVENESS OF PRIVATE EQUITY-LED CONSOLIDATION

Urologists in large group practices are able to enjoy the benefits of private practice. Financially, this option typically includes ambulatory surgery center ownership to access facility fees through distributions, bonuses tied to ancillary services including radiation treatments and pathology, hospital co-management fees, and compensation increases related to the overall profitability of the practice. Perhaps most importantly, private practice physicians are able to maintain clinical autonomy and work with a much more nimble organization as compared to a health system. These factors are what make private equity consolidation such an attractive alternative for urologists looking to alleviate the administrative burden of their private practices. Through partnering with a larger, privately-held entity, physicians will be able to enjoy the benefits of aligning with a management services organization while also sharing in the financial success of the enterprise through their compensation and equity appreciation.

Allowing physicians to be successful in private practice also drives down costs for payors. A 2012 *Journal of Urology* study found that 20 of 22 common urological procedures were less expensive in ASCs than in the hospital outpatient department ("HOPD") setting; the study estimated that shifting 50% of urological procedures examined from hospitals to the ASC setting would save the Medicare program $66 million annually.

For investors, post-closing growth enhancement of add-on acquisitions can be realized through providing more efficient care, driving procedural volume into company-owned ambulatory surgery centers versus hospital operating rooms, adding full sub-specialty coverage, and scaling ancillary services to practices that haven't fully invested into them.

[1] American Urological Association, The State of Urology Workforce and Practice in the United States 2016. Linthicum, Maryland, U.S.A, April 11, 2017

CONCLUDING THOUGHTS

The urology sector shares many of the qualities that are leading to enhanced investment and consolidation activity in outpatient physician areas such as dermatology, gastroenterology, interventional pain management, and ophthalmology. The specialty will benefit from the same volume tailwinds driving an increasing demand for care across all specialties treating the geriatric population. Additionally, fragmentation coupled with a more difficult private practice environment will likely result in market interest from providers looking to partner with a larger private practice organization in lieu of hospital employment. Through ancillary services and ASC ownership, private practice income margins in urology can remain attractive. Private equity groups have an opportunity to be a first-mover in the consolidation of the private practice urology sector before competition for add-on acquisitions increases.

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