Provident Perspectives:

An Update on Consolidation and Investment within Eye Care

Examining recent developments and trends in the eye care space six years into private equity investment

Provident Healthcare Partners

Introduction

It's hard to believe that less than six years ago, private equity was a foreign concept to most practicing ophthalmologists and had very little bearing in the business world of eye care. Today, private equity is one of the most focal and prevalent topics in the industry, finding its way into conference panels, board meetings, and new hire interviews. Hundreds of transactions and billions of investment dollars later, ophthalmologists today are much more versed in the language of private equity and are equipped with a wealth of resources and precedent outcomes to help navigate the waters of private equity investment.

Today, an estimated 15% of practicing ophthalmologists are affiliated with private equity; while a drastic increase from prior years, this indicates the sector is still in the very early innings of consolidation. As the industry presses forward to the next iteration of its investment life cycle, which happens to coincide with unprecedented macroeconomic conditions, Provident will reflect on the last few years and on our view of where the industry is heading. The goal of this whitepaper is to further educate ophthalmologists and other industry participants on the current state of affairs within the sector, what to expect on a go-forward basis, and on the various options and deal structures afforded to shareholders that may be considering a transaction.

Progression of Investment within Ophthalmology

Genesis of Investment within Ophthalmology:

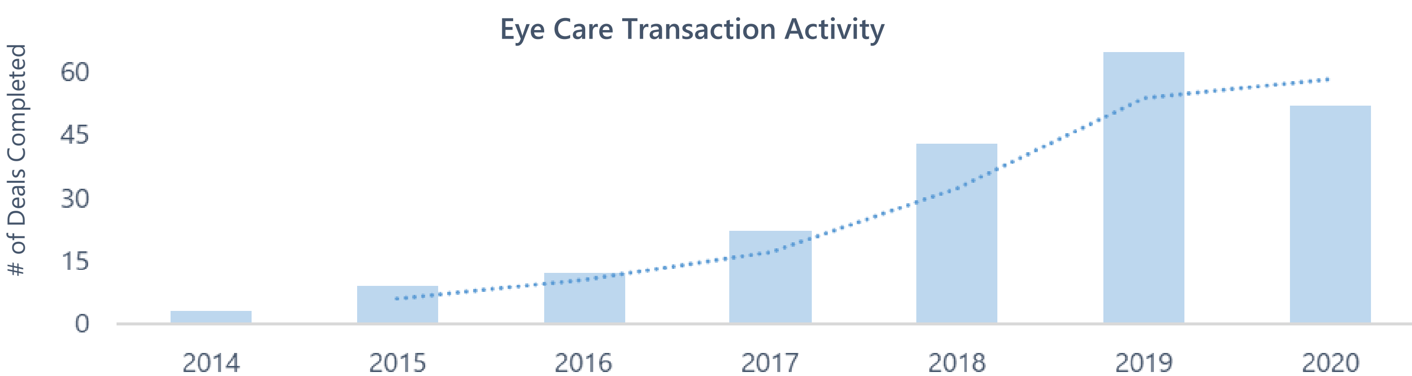
Although most transaction volume has taken place over the last four years, investment activity in ophthalmology began in the early 2010s. In 2014, Provident represented one of the first independently-owned ophthalmology practices to take on private equity investment when Varsity Healthcare Partners invested into the Katzen Eye Group to form Eyecare Services Partners (ESP), now one of the largest consolidators in the space. Less than a year later, optometric provider Clarkson Eyecare aligned with private equity firm FFL Partners to form EyeCare Partners, which has since grown into the largest vertically integrated eye care platform in the country. As these early platforms started to prove out their respective concepts, healthcare investors with prior physician services investment experience started to develop similar theses within the sector.

Surge of Private Equity Activity:

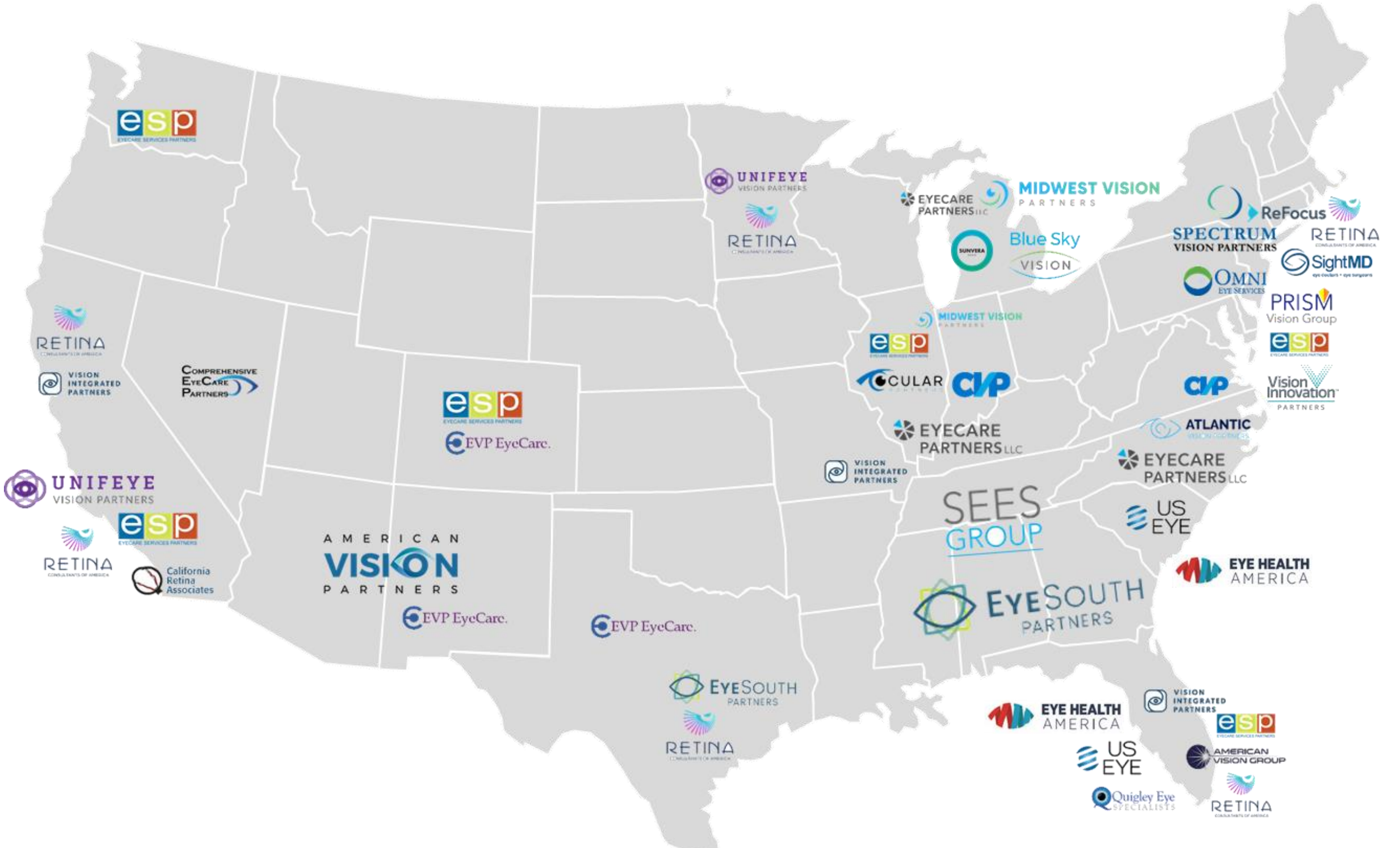
2017 proved to be a breakout year, when some of the most nationally recognized practices aligned with investment partners. Nine new platforms were created in 2017, followed by the formation of another nine platforms in 2018.. 2018 also saw the first, secondary transaction when Varsity exited its position in ESP to private equity firm Harvest Partners, resulting in a strong return on equity for the owners of ESP over its four-year hold period. Momentum continued in 2019 when five new funds invested into the sector, culminating in the $2.2b sale of EyeCare Partners to Partners Group, just the second PE-backed platform to undergo a secondary sale. Even during 2020, in the face of COVID-19, transaction volume has remained robust following delayed closings during the second quarter. In a year plagued by a pandemic, there have been almost 60 total transactions and two new platforms that have formed, bringing the total count of private equity-backed Management Services Organizations (MSOs) to 30.

The Next Phase of the Investment Cycle:

Many of those 30 platforms are likely at least half way through their expected four-to-six-year hold periods with ten groups at least three years into their investment. Provident expects several secondary deals to take place within the next 6-12 months given that a handful of platforms are rumored to currently be under LOI or approaching the market in the very near future. Larger PE-backed platforms, such as EyeCare Partners (now backed by Partners Group) and MyEyeDr. (backed by Goldman Sachs), will likely be primary strategic suitors in most secondary sale processes, along with a faction of upper-echelon private equity firms with funds large enough to finance secondary transactions and too large to invest in independently-owned practices as standalone platforms. There are dozens of firms that fit into this category and many that have precedent, secondary physician services investment experience that have been seeking out a platform in the ophthalmology space for some time.



Types of Partnership Models & Considerations



Regional Platform vs Add On Transactions:

There are over 30 strategic acquirers competing for transactions and vying for market share in their respective geographies. Each MSO has distinctly different models with similar goals of consolidating local markets, establishing new ones and expanding their addressable patient base. Some platforms focus on density in core states or regions while others have employed a regional hub model, establishing beachheads in attractive markets by way of acquisition. EyeSouth Partners, for example, stayed true to its regionally focused model, consolidating the Atlanta market before proliferating outward into contiguous states within the southeast region. CEI Vision Partners and Unifeye Vision Partners have employed a regional platform model, having established secondary hubs to serve as the foundation for further consolidation in those regions. For large, independent practices, aligning with an MSO without an existing presence in your state or market provides an opportunity to be a regional platform, which is typically accompanied by increased valuation and potentially more strategic influence through governance and management opportunities within the region. Aligning with a platform in your geography has unique sets of benefits as well, including reimbursement increases, access to new referral networks and further back-office support. Both models are prevalent in today's market and both have attractive components, depending on shareholder preference.

Platforms Historically Focused on ASC Management:

Consolidators historically focused on ASC management have also entered the ophthalmology fray as well, offering a unique value proposition to practices with physician-owned ASCs. Companies like Surgery Partners and Covenant Physician Partners have been active within the segment and have started to add practices into their respective organizations. Covenant for example, which recently unveiled a new Covenant Physician Partners name, has acquired nine ophthalmology ASCs and three affiliate practices across three separate states. The ASC-operators that have been active are well-resourced with significant financial backing, providing access to a robust set of corporate functions, including payor contracting, human resources, and revenue cycle support. Most ASC-centric models also provide supplemental compensation opportunities tied to ASC profits, such as ASC bonus pools and distributions, which are much less prevalent in the more common, multispecialty ophthalmology model.

Optometric-Focused Platforms:

Alternative models, starting on the opposite end of the care continuum within eye care, established vertically integrated platforms by first building out a primary care, optometric presence, before expanding into multispecialty and single specialty ophthalmology. Companies like AEG Vision and EyeCare Partners (ECP) have employed such models and can provide synergistic value through access to extensive referral networks of affiliated practices. EyeCare Partners began as a pure-play optometric provider before acquiring general ophthalmology practices in areas where they had a robust optometric presence. Provident represented one of the first ophthalmology practices to align with ECP, ultimately serving as the platform's surgical hub in southern Illinois. ECP has been extremely active on the multispecialty front and has also started to move into single specialty retina as well, a space that has experienced a boom as of late.

Retina Investment Activity:

Although the sub-specialty is extremely active today, retina experienced minimal transaction activity prior to 2019. In those years, retina affiliations mostly came in the form of strategic partnerships with multispecialty eye platforms in the same geography.

New private equity investment had been relatively muted due to concerns around risks associated with the sustainability of the buy and bill model, potential for drug margin compression, step-up therapy initiatives, and concentration risk in revenue among a small number of providers. As time has passed, investors and strategic acquirers have started to gain more comfort around the sustainability of retina profitability, particularly in instances where there is a clear path to multispecialty ophthalmology. Although transaction volume and multiples have increased as a result, overall valuations remain discounted relative to general ophthalmology practices due to the previously mentioned risks associated with revenue concentration and margin sustainability.

The first private equity firm to invest into a single specialty retina practice was Quad-C in 2018. Quad-C recapitalized NJRetina to form Prism Vision Group with a thesis predicated on leveraging existing referral and MSO relationships to consolidate the local multispecialty market. NJ Retina recently aligned with Retina Group of Washington to form a multiregional MSO with retina at the forefront of the platform.

More recently, the launch of Retina Consultants of America (RCA), backed by Webster Equity Partners, has contributed to a consolidation boom in the space. RCA is employing a model focused on horizontal acquisitions, dedicating over half of a billion dollars in equity capital to an all-retina platform that has resulted in partnerships with some of the largest groups in the country. The differentiated model paired with the relatively small size of the subsector has allowed the RCA platform to gain considerable traction in the nine months since inception. For retina physicians, the RCA platform provides an alternative option and model with distinctive benefits and risks outside of the traditional multispecialty archetype.

Types of Partnership Models & Considerations *Cont'd*

Key Partnership Considerations:

In considering which model or partner to align with, it's important to evaluate a multitude of factors in addition to economics, including cultural fit, clinical philosophy, operational autonomy, and influence over strategic decision-making. Most young and mid-career shareholder physicians contemplating a partnership ascribe the most weight to post-closing autonomy, influence, and a shared vision with their partner. Other important considerations that influence the go-forward success of the organization are the value-added resources that a platform can provide, outside of just capital. With $2 trillion in private equity dry powder on the sidelines, capital has become commoditized in today's market.

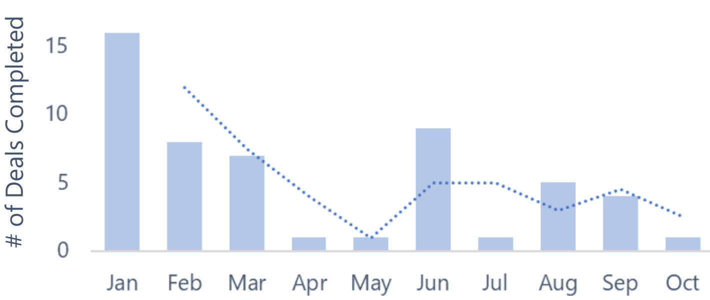
Infrastructure and back-office support, human capital investment, revenue synergies, the financial performance of the platform, as well as potential for successful rollover equity outcomes, are all areas where potential suitors can differentiate themselves from their peers. Since most transactions are structured as majority sales or recapitalizations, a meaningful amount of economic value is tied to reinvested or rollover equity post-transaction. As such, it's important to assess certain rollover equity considerations, such as platform track record to date, the hold period for the platform, private equity firm case studies and prior investment outcomes, as well the price of reinvested shares. Not all platforms and models are created equal and there will certainly be a stratified sampling of winners and losers as the market continues to mature.

Investment Activity & Structure During COVID-19

The importance of choosing the right partner has become even more pronounced in recent months due to the adverse effects of the pandemic, which has disproportionately impacted PE-backed platforms. Platforms in vulnerable markets or with less access to capital and high levels of debt have fared more poorly than groups that were well equipped to weather the storm. As a result, there is a large divide between platforms that have slowed down M&A efforts and those that have bolstered their acquisition strategy.

The organizations that continue to be aggressive and acquisitive have driven most of the transaction volume in recent months, which has already recovered to pre-COVID levels. Transaction activity has essentially moved in lockstep with the business recovery as most deals were paused during government shutdowns, followed by a surge of volume due to pent up demand. Since June there have been 20+ transactions completed across a host of markets throughout the country.

Eye Care Transaction Activity (YTD 2020)

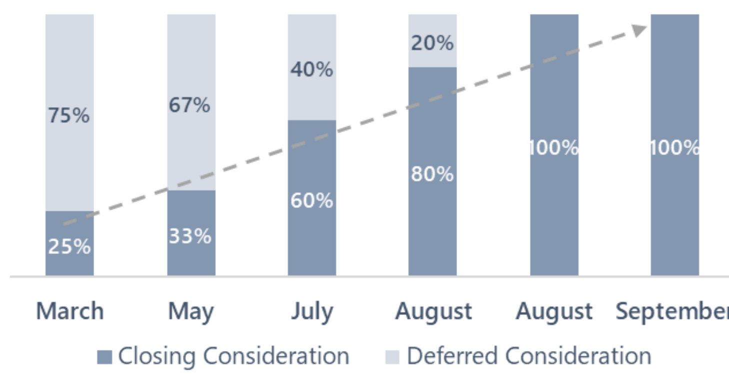


Deal Structures:

Although volume has recovered quickly, most transactions completed in the early months of COVID-19 were accompanied by deferred payment structures tied to practices achieving pre-COVID volumes post-closing. These structures were featured in most deals as a means of partially offsetting or sharing COVID-related risks between the buyer and seller as well as a way to bridge financing gaps during peak pandemic months where lending markets were less accommodative.

As businesses have recovered, contingent or deferred payment structures have become much less common in recently completed transactions. Now that practices are back to near or at pre-COVID levels, consideration at closing has trended back towards 100%, especially in competitive situations for highly sought-after practices.

Closing Consideration as a % of TEV during COVID-19 for Provident Physician Transactions*



*Based on LOI signing date

Deferred payment mechanisms prevalent in early to mid-2020 transactions also served to maintain previously agreed to valuations and helped to buoy multiples during the early months of the pandemic. Even with less structure as of late, valuations have largely remained at elevated, pre-COVID levels. With a v-shaped recovery in visits and case volume, ophthalmology businesses have proved more resilient than most alternative opportunities for investors, which has generated more interest in the sector. Many funds with existing investments within eye care and physician services have bolstered investment in the space, which has a comparative advantage to most cyclical sectors. Some private equity firms with existing investments in eye care are even targeting new stand-alone platforms using equity capital from separate funds than their original investment, which is indicative of just how attractive the space has become. Existing platforms have continued to be acquisitive as well, taking advantage of one of quickest avenues for achieving growth and expanding their footprint in advance of a secondary sale.

Investment Activity & Structure During COVID-19 *Cont'd*

Go-Forward Valuation Expectations:

With dozens of private equity firms and over 30 strategic acquirers competing for acquisitions, there remains a massive imbalance between supply of and demand for transactions in the space, which will likely keep multiples at elevated levels for some time. Seller valuations have experienced very little in the way of softening as well, which has helped sustain Enterprise Value and allowed for accounting flexibility in calculating the EBITDA base that buyers are willing to ascribe a multiple to. Most transactions completed since the pandemic have been based on pre-COVID EBITDA periods, while more recent deals have factored in COVID normalization adjustments, adjusting for pandemic-related expenses and foregone revenue during the government-mandated shutdowns. Given these many factors, Provident expects valuations to remain elevated for the foreseeable future with sizable practices garnering premium valuations.

COVID Normalization:

The accounting exercise of "normalizing" profit during peak COVID months is extremely important to ensure sellers receive proper value for their business during these unprecedented times. There are several different methodologies used to adjust the accounting in those months to reflect what the business would have produced at steady-state operations so that sellers aren't penalized by the lockdowns that were instituted from March thru May. One such method involves replacing peak COIVD month financials with the same months from the prior year, while also eliminating any COVID relief funds that were received. Because many physician practices are run on a cash basis, in most instances, this adjustment should extend through June as a portion of cash-basis collections in June would have been affected by the gradual reopening in May. For fast growing practices in competitive situations, there is also an argument to be made for applying growth rates to the "replaced" months based on year over year growth in the months preceding March 2020. Regardless of the approach taken, it is paramount for companies to track data and KPIs that will enable the practice to support and defend its "normalization" adjustment in due diligence. This exercise has become even more important given the renewed potential for further government-mandated shutdowns in the future.

Key Value Drivers & Financial Considerations

The key components of a business that ultimately drive value are consistent across the industry. Valuation multiples that buyers ascribe to the earnings of an ophthalmology business are essentially a function of two factors: the potential growth and riskiness of a business' cash flows. In paying a multiple on today's earnings, buyer analyses are predicated on the sustainability of earnings, the risk that they may contract in the future and to what degree cash flows are expected to grow.

Profile of Growth & Infrastructure:

The growth opportunities and existing infrastructure in place to support that growth are key factors that drive valuation. Practices with a track record of consistent growth by way of adding physicians, locations and acquiring practices, with tangible go-forward growth opportunities (recruiting pipeline, de novo targets, etc.) have historically garnered the highest valuations.

In a similar token, acquirers will also ascribe more value to practices with strong corporate infrastructure that have robust back-office systems and a strong management team in place to support future growth. Centralized services and a deep employee roster of support staff are key determinants of value and are viewed favorably by the buyer community, since they limit the amount of future expense the business will need to incur to scale appropriately.

Risk Profile:

There are also key elements of an ophthalmology practice that reduce the perceived risk of the business, which also contributes to higher valuations. Expansive, young provider bases with low physician turnover, extensive and defensible referral relationships, and diverse and favorable payor and subspecialty mix are all attractive elements that allow buyers to gain comfort around the sustainability of the cash flows on a go-forward basis. Groups with heavy revenue concentration among a small number of owners or with a number of near-term retirements present a riskier investment to the PE community. On the subspecialty and payor front, minimal cash pay exposure and brand name retina drug exposure are typical examples of discounted income streams due to the inherent risk in reimbursement trends.

Practices with high margin, facility fee income from ASCs, heavy commercial payor volume and sizable cash pay income streams through oculoplastic or premium conversions, typically have more diversified revenue, which has historically led to more attractive valuation multiples. For example, recent lifts in ASC rates allow practices with ownership in ASC(s) to partially offset the recent CMS reduction in standard cataract procedure rates. High premium conversion rates also provide an opportunity for price increases to mitigate the impact of the CMS professional fee reduction as well.

Value Drivers		
Robust Corporate Infrastructure	Strong Management	Track Record of Consistent Growth
Attractive Market Dynamics & Demographics	Proven Ability to Recruit & Retain Physicians	Young & Expansive Provider Base
Favorable Funding Sources & Payor Mix	Diverse Specialty Mix	Tangible Growth Opportunities

Key Risks Considered		
Aging Physician Base	Difficulty Recruiting	Heavy Medicare Concentration
Heavy Retina Drug Exposure	Competitive Market with PE Presence	Referral Attrition
High Physician Turnover	Minimal Corporate Infrastructure	Significant Key Man Risk

Key Value Drivers & Financial Considerations *Cont'd*

Competitive Landscape:

Competitive landscape and market dynamics often play a large role in valuation as well. Practices that operate in fragmented, underserved markets with limited competition, a strong reimbursement environment and attractive demographics (population age, growth and disposable incomes) typically command higher valuations than those in less desirable markets.

Overall, valuation is a variable metric based on myriad factors, but it is an inexact science at that. As one of the key factors driving consolidation in the industry, Provident is tracking macroeconomic and regulatory factors, debt markets and supply and demand dynamics to keep a strong pulse on valuation on a go-forward basis.

Economic & Financial Considerations:

Although valuations are extremely high from a historical standpoint, there are still many instances where the economics of a proposed transaction may not warrant consummating a deal. Aside from Purchase Price, there are many other financial factors to consider in evaluating offers, such as post-closing compensation, breakeven analyses, proceeds allocation methodologies and tax considerations.

In every transaction, there is an element of compensation reduction, which serves as the main source of EBITDA that buyers tie valuation to. Different platforms have varied compensation structures and methodologies, but in nearly all cases, the go-forward formula will be based on a percentage of collections model, of which the percentage varies from group to group and market to market. Some groups may also use a tiered compensation schedule based on productivity thresholds to incentivize and reward high producing physicians.

In either instance, it's important to compare pre and post-deal economics (compensation, proceeds, etc.) from a breakeven perspective, factoring in tax advantages (capital gains vs ordinary income), time value of money concepts, and potential income repair consideration. Selling shareholders should understand how many years of after-tax compensation reduction they're receiving through the proceeds from a transaction and where the breakeven point may lie, factoring in variable inputs such as return on investment for rollover equity, tax rates, and time value of money, among many others.

The entity structure and tax status may complicate decision-making as well by restricting the way a shareholder base can allocate value. S-corporations can be limited in the way they can split proceeds, but for other entity types, there are creative ways and hybrid models based on foregone compensation and ownership that may allow for an agreeable and equitable allocation of value. Communication and education is extremely important, especially with large shareholder bases, to increase the probability of closing a deal once the group has opted to seriously consider a transaction.

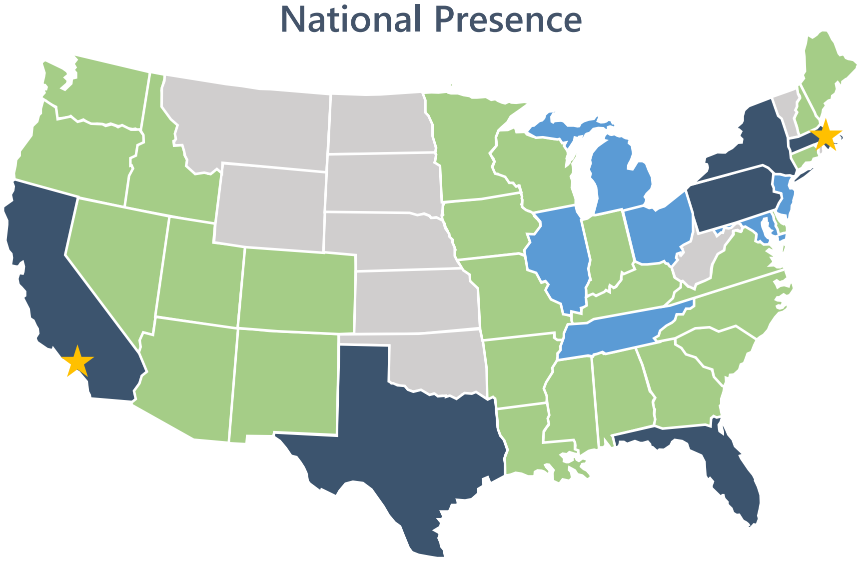
Concluding Thoughts

The eye care sector as undergone a massive transformation in recent years with the advent of private equity investment in the space. Provident expects more changes to ripple through the sector as new players enter the space and private equity-backed platforms engage in secondary transactions. As we navigate through the uncertain waters of COVID-19 and press forward to the next phase of the investment life cycle in ophthalmology, it's important to stay educated and keep a strong pulse on the market. Considering a transaction is likely the biggest business decision a shareholder can make and is a decision that warrants a tremendous amount of research, education and cost/benefit analysis.

PROVIDENT HEALTHCARE PARTNERS

Provident Healthcare Partner's investment banking team works with privately owned healthcare companies to provide advisory services related to mergers and acquisitions. Prior to formal engagement, Provident works with companies to provide the upfront education to shareholders necessary to understand the economics, structure, and motivation of a transaction. Following the education process, if formally engaged, Provident leverages their extensive knowledge of the buyer universe to find the most compatible partner and drive valuations for a company's previously illiquid stock. Driving the entire transaction process, Provident facilitates and assists with deal structuring, negotiations, exit planning/processing, counseling amongst shareholders, and due diligence.

National Presence



- 1-3 Transactions
- 4-6 Transactions
- 7+ Transactions
- ★ Provident Office

20+	Years of Healthcare Investment Banking
140+	Healthcare Deals Closed
61	Physician Service Deals Closed
9	Eye Care Deals Closed
25	Banking Professionals

Note: The above map represents states where Provident clients were headquartered. Provident has successfully closed transactions with clients operating in 45 states and Puerto Rico.

Provident Coverage Group:

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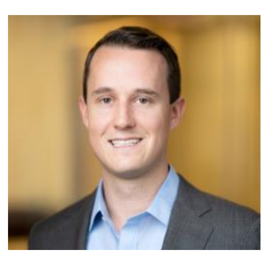

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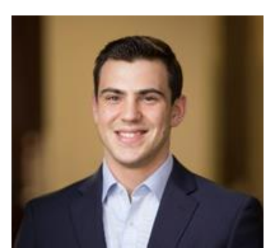

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Provident is the leading investment banking firm specializing in merger and acquisition advisory, strategic planning, and capital formation for middle-market and emerging growth healthcare companies.

The firm has a vast network of senior industry relationships, a thorough knowledge of market sectors and specialties, and unsurpassed experience and insight into the investment banking process.

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