

MARLIN & ASSOCIATES
Healthcare IT Review
May 2013

Dear Clients and Friends,

Welcome to our May issue of H.I.T Greatest *Hits*.

When we hear that hospitals who make the most errors are more profitable, it makes one wonder if we have made much progress in improving our healthcare system. At times it might be difficult to imagine a world where we can offer better care, with less money, for more people.

Whether or not you are a fan of government intervention, it is clear that the incentives that came with the passage of the Health Information Technology for Economic and Clinical Health (HITECH) Act provided "seed money" intended to improve our broken healthcare system. These incentives, coupled with the support and funding from our venture capital community, helped launch the first wave of next generation HIT companies.

These are indeed exciting times in our industry and we share that excitement and enthusiasm. We are confident that these innovative companies will lead us down a path where we can have better care at lower cost. The confluence of advanced technologies, government mandates, social imperatives and availability of capital, make this time a prime time for our industry.

Sincerely,



Afsaneh Naimollah
Partner

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"Let's begin your exam with a simple coordination test. Swipe your credit card."

Marlin & Associates is one of the most active investment banking and strategic advisory firms providing strategic and financial advice to worldwide buyers and sellers of middle-market technology firms. Our firm is headquartered in New York, NY and has additional offices in San Francisco, CA; Washington, DC; Toronto, Canada; and Hong Kong, China serving companies that provide information and technology to a wide range of communities including those that serve the banking, capital markets, insurance, marketing and healthcare arenas.

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HEALTHCARE INVESTMENTS

We speak to some of the smartest and largest financial investors in America who often ask us to help them identify HIT companies that are growing at 50% on the top line YoY, have EBITDA margins of at least 25%, with little reimbursement risk and minimum EBITDA of \$15-20M. Clearly there are very few companies that meet this criteria and where they do, it is difficult and expensive to buy them. There are, however, many exciting investment opportunities in the industry but we note some key observations on how the investment landscape is changing.

- 1. Strategic buyers are acquiring companies at earlier and earlier stages.** This is why the average price of HIT M&A transactions has remained stubbornly low at around \$45-50M. As a result, the inventory of deals available for financial buyers may not be as strong as before.
- 2. For HIT investments, mega funds need to reduce their minimum investment threshold.** Transactions with price tags of \$250M+ seldom come to market and when they do, they fetch strategic multiples which may not be suitable for financial buyers. Mega funds need to get comfortable with smaller deals.
- 3. Financial buyers need to write bigger equity checks.** The traditional use of leverage of 4-6x EBITDA in the majority of HIT transactions yields very little, hence the equity checks need to be upwards of 70% of transaction value.
- 4. Consequently, financial buyers should be looking for Alpha returns.** The thought process has to shift from “we make our companies more efficient” to “we buy and build to create new platforms on proprietary investment theses.” In the HIT industry, the era of dependency on certain growth trajectories to generate Beta returns is slowly fading away. Success is about being disruptive and doing things in new ways.

M&A SECTOR TRENDS

We expect investments and M&A activity in those companies that focus on clinical applications to continue, but at a slower pace. With increasing penetration of EHRs and dwindling government incentives (U.S. government has paid \$10Bn of incentives to date), the administrative side of healthcare, i.e. RCM will see increased activity. The acquisition of MED3000 by McKesson and the Gores Group's acquisition of GE Healthcare Strategic Sourcing are just a few examples of the growing interest in the RCM industry. We see impressive innovations on the administrative end such as analytics, billing automation and point of service patient payments to name a few.

Another emerging area that holds much promise is the comingling of clinical and administrative data. There are a number of companies that are aggregating and analyzing data from disparate systems across the enterprise. Health Catalyst and Apixio are amongst the companies that are leading that effort. These technologies automatically report patterns, trends and correlations for eliminating waste of unnecessary care, population managements, care transformation, revenue optimizations, etc.

In observing how horizontal workflow technologies have developed in other industries, we see an important difference with healthcare technology companies. In industries such as finance or manufacturing, technology giants like SAP and Oracle were able to build seamless back-end to front-end workflows under the same architecture. HIS companies such as Cerner and McKesson have not followed the same path and have missed that opportunity. The next generation HIT companies are now building innovative offerings for the front office providing administrative point solutions which have been developed on top of legacy infrastructure systems.

As competition in the RCM sector intensifies amidst declining reimbursements, the larger vendors need to offer more integrated back-end to front-end offerings. To us, it sounds like a busy M&A market ahead.

IMPORTANT INDUSTRY NEWS

UnitedHealthcare (NYSE:UNH) forms joint venture with Dignity Health, Baylor Health Care System, and Advocate Health Group

United joined three provider groups to launch an initiative that will independently measure the effectiveness of certain medical devices. The new company will be known as SharedClarity. Devices covered by SharedClarity include pacemakers, knee and hip implants, stents, heart valves, etc.

The game of benchmarking medical devices has shifted from having independent firms measuring quality to providers and insurers joining the foray. At the end of the day we believe the main reason behind this alliance is to put pricing pressure on medical device manufacturers through the formation of purchasing groups. The goal of evidence-based decisions has just taken a step forward.

A case for private Insurance Exchanges

Mercer, a well-respected consulting company, announced that 10 insurers are joining its private exchange to provide health coverage. The list includes who's who of the insurance sector; namely, Aetna, Humana, Cigna, UnitedHealth and Blue Cross Blue Shield plans. Aon, another top consulting firm, is also opening its private exchange this fall.

The battle between the government and private exchanges will run its course, but we believe there is room for both. What will be interesting to watch is the insurers themselves who plan to start their own exchanges. Clearly, the market will be crowded for some time. What is encouraging are the similarities in the evolution of this market and how financial exchanges evolved from their early days. We may not be exchanging stocks or bonds but we have available a market that gives us the tool to select the plans right for us with the hope that price competition brings in lower premiums.

NOTABLE TRANSACTIONS / INVESTMENTS

Although April was a slower month than usual, some deals of note are:

Roper Industries (NYSE:ROP) agrees to acquire Managed Healthcare Associates

Roper, the diversified manufacturer whose products include radio frequency products, energy systems, and medical imaging products, agreed to acquire Managed Healthcare Associates, which provides products supporting alternate site healthcare providers and specialty pharmacy solutions. The acquisition price of \$1Bn implies a 10.5x Enterprise Value / forward EBITDA multiple. Roper expects that Managed Healthcare Associates will earn \$95M in EBITDA over the next 12 months and be cash accretive to earnings. Roper's management cited the technology tools and customer-service model of Managed Healthcare Associates as contributors to their decision to acquire the Company, as well as the recurring revenue stream and high customer retention rates.

This is Roper's second healthcare acquisition in eight months. In July 2012, the Company bought Sunquest Information Systems for \$1.4Bn. Sunquest is a laboratory information systems company. Roper may become a good example of how larger companies, while focused on their horizontal competencies, will transform themselves through sizable investments in the healthcare industry.

WorldOne raises \$35M

WorldOne, one of the largest providers of healthcare data collection and research, raised \$35M from new investor Deerfield Management Company. WorldOne's management plans to use the investment to make strategic acquisitions and to expand Sermo, the online community for physicians that the Company acquired in Summer 2012.

After this capital raise, we believe WorldOne will be THE leading survey platform for the healthcare industry. The Company has 1.8 million healthcare providers in its network globally.

ShanghaiMed Healthcare raises \$100M

ShanghaiMed, which provides healthcare management services, including disease assessment and medical treatment, raised \$100M from investors including Goldman Sachs and the Government of Singapore's Investment Corporation. ShanghaiMed's management plans to use the proceeds to accelerate expansion of its medical entities in China's major cities.

Healthcare is a bright spot in a number of international markets. We foresee increased investments in Australia, China, India, and Japan.

RedBrick Health raises \$14M

RedBrick Health, a healthcare engagement platform that helps employers drive ROI on their health and wellness programs, raised \$14M. The Company has raised nearly \$75M since being founded in 2006. Early investors include Highland Capital, HLM Venture Partners, Kleiner Perkins, Split Rock, Versant Ventures, and Volition Capital.

RedBrick has successfully blended financial accountability and clinical / behavioral insights with social and gaming platforms. We view the Company as one of the leaders in the next generation consumer health engagement market.

Carl Icahn acquires 9.3% stake in Nuance Communications (NASDAQ:NUAN)

Nuance Communications provides voice and language solutions, including dictation and transcription solutions which enable clinical documentation and medical speech recognition technologies. Although the transaction value was undisclosed, the 30-day average price when Carl Icahn's investment was announced implied an Enterprise Value of \$7.5Bn. Since the announcement, the stock price has decreased by 6.0%.

It remains to be seen if this transaction turns out to be another successful investment for Carl Icahn.

lifeIMAGE raises \$35M

lifeIMAGE, which provides a secured network for universal e-sharing of diagnostic imaging information, raised \$35M from existing investors Cardinal Partners and Galen Partners.

This is lifeIMAGE's largest round since the Company was founded in 2008.

Healthspot raises \$10.4M

Healthspot, which develops and owns technology that connects health-care providers and patients at retailers and other facilities, raised \$10.4M from 18 investors, including Cardinal Health. This telemedicine company provides private kiosks for two-way communications links between healthcare patients and providers. Healthspot hopes to raise an additional \$10M of funding during this same financing round.

E-visits are gaining ground and have exhibited good momentum. We believe opportunities will be plentiful both in the at-home e-visits (therapy sessions) market as well as the more comprehensive kiosk offerings.

"We are at the beginning of what we believe will be the fastest transformation of any industry in U.S. history."

-Glen Tullman, Former CEO of Allscripts, Jun 2010

"The ability to interface in healthcare offers the possibility of unbounded opportunity for discovery. But without standards, that effort is going to fail. Currently we have a cacophony of data that needs to be managed, integrated, massaged, and distilled. It will only confuse us if we don't take the next steps."

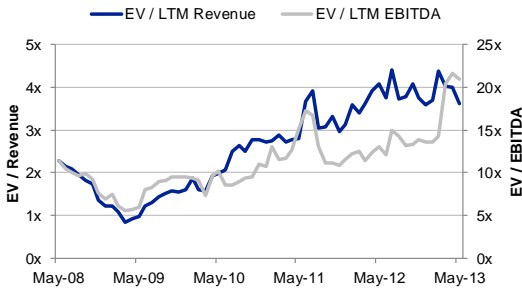
-Kevin Fickenscher, M.D., President and CEO of the American Medical Informatics Association, Nov 2012

"There's nothing wrong [with healthcare] we can't fix ... But we have all these horse-and-buggy systems, and you can change all that."

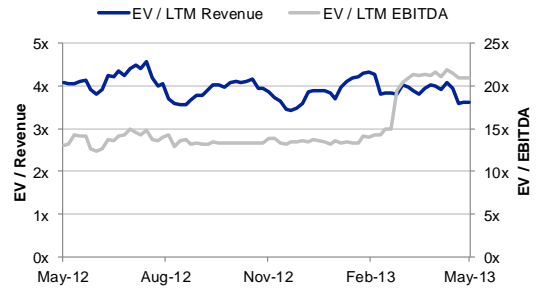
-Bill Clinton, Former President, HIMSS 2013

Healthcare Information Services & Analytics

5 Year LTM Revenue & EBITDA Multiples

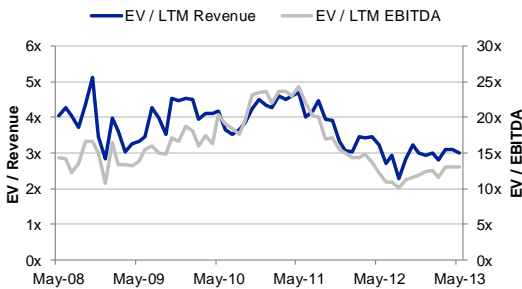


1 Year LTM Revenue & EBITDA Multiples

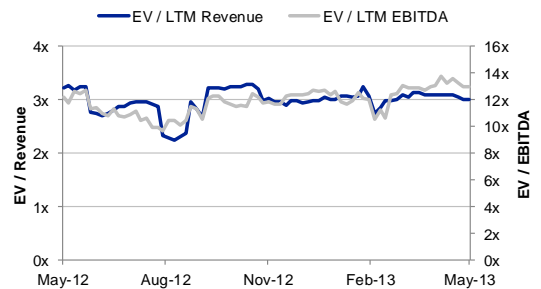


Healthcare Provider Systems & Solutions

5 Year LTM Revenue & EBITDA Multiples

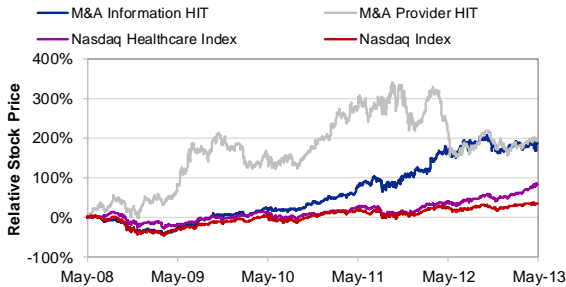


1 Year LTM Revenue & EBITDA Multiples

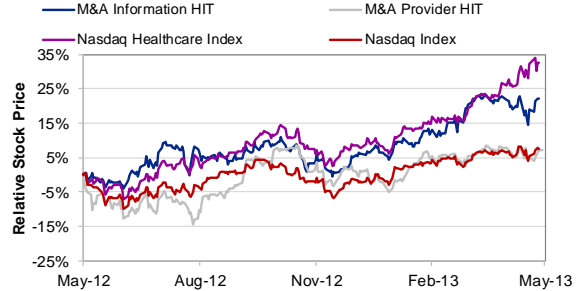


HIT Stock Price Performance versus Nasdaq Healthcare Index

5 Year Indexed Stock Price Performance



1 Year Indexed Stock Price Performance



PUBLIC MARKET TRENDS

It is no surprise that Healthcare Information Services & Analytics companies enjoy higher multiples as compared with the Healthcare Provider Systems & Solutions sector which includes many RCM companies. The former group has demonstrated a substantial rise in multiples in the past five years reaching 20.0x EV/EBITDA multiple. Over the last 12 months, HIS companies have continued to outperform the Provider HIT sector.

The performance of both sectors have substantially exceeded the NASDAQ Healthcare Index over the past five years; however, this trend has reversed in the past year. The Provider HIT Index has been tracking the NASDAQ Index, while HIS Companies have enjoyed a rise similar to that of the NASDAQ Healthcare Index. This may in part be based on investors' views that RCM companies should be valued similarly to the BPO sector.

Marlin & Associates' Healthcare IT Indices include the following companies

Healthcare Information Services & Analytics

Company (USD millions)	Enterprise Value	Market Cap	EV / Revenue		EV / EBITDA		Revenue Growth		EBITDA Margin		
			2012	2013	2012	2013	2012	2013	2012	2013	
The Advisory Board Company	\$1,557	\$1,655	4.2x	3.5x	26.7x	19.3x	31%	21%	16%	18%	
Cerner Corporation	\$15,654	\$16,477	6.0x	5.2x	22.0x	16.1x	21%	15%	27%	32%	
Healthstream Inc.	\$503	\$599	4.9x	4.0x	24.2x	21.4x	26%	22%	20%	19%	
Healthways Inc.	\$719	\$453	1.1x	1.0x	12.5x	8.3x	-2%	8%	8%	12%	
McKesson Corporation	\$26,015	\$24,262	0.2x	0.2x	9.0x	8.3x	10%	1%	2%	3%	
National Research Corp.	\$402	\$398	4.7x	4.1x	14.7x	12.8x	14%	15%	32%	32%	
WebMD Health Corp.	\$953	\$1,144	2.0x	2.1x	41.0x	12.4x	-16%	-4%	5%	17%	
			Mean	3.3x	2.9x	21.4x	14.1x	12%	11%	16%	19%
			Median	4.2x	3.5x	22.0x	12.8x	14%	15%	16%	18%

Healthcare Provider Systems & Solutions

Company (USD millions)	Enterprise Value	Market Cap	EV / Revenue		EV / EBITDA		Revenue Growth		EBITDA Margin		
			2012	2013	2012	2013	2012	2013	2012	2013	
Accretive Health, Inc.	\$781	\$978	0.8x	0.7x	14.6x	8.9x	15%	11%	6%	8%	
Allscripts Healthcare Solutions, Inc.	\$2,775	\$2,434	1.9x	1.8x	22.3x	9.8x	0%	4%	9%	19%	
Athenahealth, Inc.	\$3,296	\$3,489	7.8x	6.1x	nm	29.9x	30%	28%	12%	20%	
CompuGroup Medical AG	\$1,470	\$1,127	2.4x	2.3x	10.8x	9.2x	15%	5%	23%	25%	
Computer Programs & Systems Inc.	\$565	\$583	3.1x	2.8x	12.7x	10.6x	6%	10%	24%	27%	
Craneware plc	\$149	\$177	3.6x	3.3x	13.2x	11.0x	8%	10%	28%	30%	
EMIS Group PLC	\$676	\$683	4.8x	4.5x	12.8x	13.1x	23%	7%	38%	34%	
Greenway Medical Technologies, Inc.	\$448	\$475	3.6x	3.1x	nm	26.2x	38%	17%	6%	12%	
MedAssets, Inc.	\$1,958	\$1,077	3.1x	2.9x	10.0x	8.9x	11%	6%	30%	32%	
Merge Healthcare Incorporated	\$500	\$287	2.0x	1.9x	16.2x	8.4x	7%	7%	12%	22%	
Quality Systems Inc.	\$965	\$1,072	2.2x	2.1x	7.7x	8.0x	22%	9%	29%	26%	
			Mean	3.2x	2.9x	13.4x	13.1x	16%	10%	20%	23%
			Median	3.1x	2.8x	12.8x	9.8x	15%	9%	23%	25%

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