Transcript:

Health Care IPO Forum 2014 Opening Remarks

Speakers: Richard Zall – Partner and Chair of the Health Care Department and the Health Care Industry Group
         Peter Marathas, Partner and Head of the Boston Employee Benefits Practice
         Frank Lopez – Partner and Co-Head of the Global Capital Markets Group
         Robin Feiner – Senior Counsel and member of the Capital Markets Group
         Bernard Cooney – UBS Investment Bank Managing Director in Equity Capital Markets Group
         Ravi Sachdev, JP Morgan, Managing Director, Health Care Investment Banking
         Peter Zippeluis – Deutsche Bank Bank Securities, Inc. Managing Director and co-head of Healthcare Services Investment Banking
         James Elrod – Vestar Capital Partners, Managing Director
         Kathrine Wolf – Rocket Science, Co-Founder and CEO
         Julie Allen – Partner and Co-Head of the Global Capital Markets Group

Zall: So let me start with a discussion about the health care landscape and the context for this. Actually health care and capital markets are a good match because the health care industry has been consuming lots of capital over the years, and is a very large sector that needs capital to grow and to thrive. And, I really think there are three elements of the industry today that I want to just cover quickly.

One is the change that’s going on. There’s really transformative change in the industry in a way that hasn’t occurred in decades and I’ve been in the industry for decades. I can attest to that. Challenge, there are certainly many challenges that industry players are facing in competing and thriving in this important sector. But they are also, lastly, lots of opportunity and that’s really capital markets hopefully will help those that are meeting those challenges and taking advantage of these opportunities will be able to use.

Marathas: There’s nothing affordable in the Affordable Care Act for employers. There is zero that is affordable, at least for the foreseeable future for employers.
This costs employers money, and it’s designed to be that way, frankly, because the employers have mandates put on them. They are also paying for a lot of the uninsured for this country through various taxes and fees. So costs will go up and taxes and fees will go up for employers and then looming on the horizon, in 2018, is a 40% nondeductible excise tax called the Cadillac Tax that will be imposed with respect to employers who offer insurance that is defined today loosely as robust. My guess is, based on the trends I’m seeing, part of that driven by all of the mandates in the Affordable Care Act. That will be pretty routine insurance so employers have to look at that as a risk and calculate those costs in.

Lopez: As you see on this slide, we’re finally back to normality as far as historically speaking for volume IPOs per year. And so if you look at this slide obviously from 2000, ’90; if you went before 2000, you would see the late ‘90s we were obviously the dot.com era, and untraditionally high volumes of IPOs. And then after 2000 there was a huge fall off and then we saw 2004, 2005, 2006, the markets came back from it. And 2008 through 2012, were historically the lowest we have seen. So finally 2013 has gotten to a place that feels a lot more like a more ordinary market and 2014 seems to be trending to be the same way. As a percentage of overall IPOs, health care IPOs are really at its highest percentages at the first half of 2014 at 35% of the overall IPOs that have closed. And as a general matter health care last year and this year has been a big part of the IPO markets.

Feiner: Let us talk a little bit about the JOBS Act and probably for the folks in the room there are different levels of knowledge about the JOBS Act. But just to give you the high level overview this was passed a little over two years ago in April 2012, so we have been living with this for two years now. The main purpose of it was to make it easier for smaller companies, which they coined the term “Emerging Growth Companies”, to go public to make it faster and hopefully less costly. So if your revenues are less than $1 billion dollars during your most recent fiscal year, you qualify as an Emerging Growth Company and then you can be an Emerging Growth Company for up to 5 years unless you hit other trigger points, which we’ve listed on the slide here. For example, if your revenue gets to a billion dollars, or if you issue a billion dollars in non-convertible debt. So what we’re seeing in the market place is that most of the companies; a very large majority of the companies – that are going public are qualifying as Emerging Growth Companies. So just to give you a sense of numbers, in our study of the 100 companies that we studied, 77 of them they qualified as Emerging Growth Companies and in the health care space, 29 of the 31 qualified as Emerging Growth Companies. So, it is definitely the lion’s share of the companies that are going public.

Cooney: Sure, testing the waters is a process where you can go out and have investor meetings after your confidential filing, and basically get a feel for investor sentiment on the story. You don’t go into valuation. It’s really an
acclimation to the story and get a feel for what investors are thinking on the name and the industry. Investors are savvy enough to know what those meeting are and the feedback they give you is usually pretty solid. On the other hand, I have almost never met a management team that did not come out of testing the waters thinking it was terrific meeting, and that the investors was going to buy, because no one asks for an order at the end.

Sachdev: I'll give just a little bit of history for a second. If you look at, at least on the health care services side, which is where Pete and I spend obviously all of our time, it was not a market that was particularly active for a long period of time in the IPO market. That generally what you were seeing was strategic sales and most of the kind of what I would describe as the next generation of health care companies hadn’t gotten to a point in their maturity cycle where they were ready to go public. But over the past 24 months or so we have seen a real uptick in the health care IPO market on the services side. We have seen a number of what I would describe as leadership oriented companies gone public. If you look at our pipeline today at JP Morgan we probably have 4 or 5 what I would describe as fast growing health care information technology or health care services companies that are in our pipeline.

Zippeluis: Health care services really moves a lot with regulation. Robby suggested that over the last 24 months there has been an increase in health care services IPOs that have come out. I think a big part of that is driven by regulation. There was basically no health care services IPOs prior to ACA being implemented. ACA, good or bad, at the very least, it provided some form of certainty for investors to price in with the environment may look like. That really ushered in a wave of IPOs. The market is shifting al little bit now, away from ACA and more towards looking to companies that add value to the health care delivery system.

Elrod: I think, pre-2007 and 2008 crash, everybody knew that going public was painful. But the question that often the investment committees that are shopping and our peers came down to, was, “can we?” The underlying thought was that 9 times out of 10 or 19 times out of 20 the public markets were going to give you the highest possible evaluation. So the gating issue was, can we pull this off? I think that has changed, and it has changed, not because the public market evaluations have gone down in an absolute sense, but some of the other alternatives available to our portfolio has risen and become much more competitive in terms of exits. The strategics out there, just by way of example, are generally in the niches that health care companies operate in and are more concentrated there. They are more well-heeled, they got more resource, so if they do want to pay up for whatever reason, they can pay up. If nothing else I think Robbie and Pete would tell you that whatever health care services this company brought to the party two years ago, their stock is worth 40% more these days. They have got that currency; they have got the ability to raise cash.
Wolf: The first thing I wrote is to make sure you the right management team in place. As Jim said the right management team for a private company is not necessarily the right management team for a company that is in the process of going public, and the management team that manages the company after it is public. So the right thing — the first thing that I put on here is to believe the CPO and the CFO. The CPO in the business and the CFO really deal with this Wall Street interface, that you don’t have prior to going public.

Allen: I think -- much like in the IPO process where the management team has to sit down with the bankers and go through the excruciating process of getting ready for Road Show and rehearsing and understanding —sort of where the tough questions are going to come and being ready for that. You have to do that obviously on an ongoing basis while you are public and it is really critically important. Again a lot of smaller companies don’t have this resource internally so you have to go out and hire somebody, but before you actually get the CEO and CFO actually get on the phone for the quarterly call, it is really helpful to go through sort of what are the really tough questions is going to be and be prepared to answer those questions in an effective fashion.

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