

## The Risk of Waiting

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Many doctors that qualify as LPS clients (meaning large, profitable and growing) decide not to pursue a monetization transaction for a variety of personal reasons. There is nothing wrong with this decision in our view. We prefer to advise only clients who have definitively decided to monetize all or part of their practices with a great partner.

Some doctors consider our value estimates and point out that if they just practiced for another 5-6 years, they would get just as much cash over time. The math is pretty simple except for the Long-Term Gains vs. Ordinary Income tax differential; and more importantly, the risks of lower values in the future. There are numerous risks associated with waiting that can impact value. A few to consider:

### **#1: Synergies Can Hurt the Competition**

We recently completed an acquisition of a great orthodontist in a community of about 100,000 people. The new partner was an Invisible DSO that already owned five pediatric practices in the area. They now own an orthodontist. The other local orthodontists were receiving 1500 case referrals per year. They are now getting ZERO. This is a \$7,500,000 shift in production for the four other orthos in town. **Their practice values have been cut in half.** Keep in mind that this scenario is not limited to ortho. Imagine being an OMFS whose key referral sources are acquired by a group that also acquired an OMFS in your town.

### **#2: Your Health**

You can insure against income lost due to disability and you can insure against death, but you cannot insure the lost value of your practice due to either event. Accidents happen.

### **#3: The Weather**

Clients in Houston (floods), Santa Rosa (fires) and Gulf and Atlantic coastal areas (hurricanes) have had their long-term values impacted. It is not just damage and interruption to your practice; it is your referral sources and the buyer's views of risk in an area. You can insure against casualty loss and business interruption, but you cannot insure against value loss.

### **#4: Your Town Gains an Invisible DSO Backing Your Competitors**

As you read in our memo; Invisible DSO, Friend or Foe? if your competitors choose the Invisible DSO partner route, you will need to be prepared to fight for market share. You can probably beat the Branded DSOs with your loyal patient base, but the Invisible DSO sneaks up on you through your local competitors. They could soon be buying supplies at 30% less than you do, employ marketing talent you cannot match and charge lower fees to gain market share. Shrinking practices are far less valuable...

## **#5: The First Partner for an Invisible DSO is Paid the Most**

The Invisible DSOs pay the highest values for their first entry into a community. The local practices added later sell at significantly lower values.

## **#6 The Shrinking Practice Risk**

We only accept clients with growing practices. Shrinking practices are not attractive to the partners from which we achieve the highest values for our clients. You are probably growing right now in a booming economy, but if the economy does not continue to boom, or an Invisible DSO acquires your competition or referral sources, your practice revenue will decline.

## **#7: The Supply/Demand Reality**

LPS sent out a bulletin to all prospective clients in October 2018 predicting the top had arrived in practice values. Our logic was not based upon our expert in house economists' forecasts, but rather on our High School economics class.

Even in bubbles, the laws of supply and demand still apply. The number of practices approaching us to learn more about the Invisible DSO/Silent Partner monetization concept is up about 500% in the last 180 days. **In March we signed \$100,000,000 in new clients in Indiana, alone. We have signed \$250,000,000 in new specialty clients since September 2019.** LPS operates from Honolulu to Hartford; there were others too! Buyers now have far more practices to choose from (supply) and thus are reducing their offers below Q4 value 2018 levels. We see it every day. It is not a significant reduction yet, but it could be soon. Great practices will still achieve amazing values, but they will not be as amazing as Q1 2019.

## **#8: Long Term Capital Gains Tax Rates Will Go Up**

The majority of the consideration paid to doctors in our transactions are taxed favorably. No matter what your political persuasion is, we are looking at the lowest Long-Term Capital Gains Tax Rates in our lifetime. Taxing the rich is popular. The rich are those who pay long term capital gains taxes (in the eyes of the legislators anyway). Mark my words, these rates will go up at both the Federal and State levels in the next 2.5 years.

## **#9: The Associate Exit Strategy is Difficult Today**

Some doctors still plan their exit by bringing in an Associate to buy their interest in the practice over time. As student debt has climbed, fewer associates are interested in this approach, even at the old values of 80%+/- of collections. This might work for smaller doctors, but it will not achieve high, cash, values for larger, profitable practices in most cases.

## **#10: Dentistry is Changing Rapidly**

Pacific Dental Services (PDS) will build 100 new offices in 2019. They have 10,000+ employees now. You may disparage them as corporate or chain dentistry, but they (and dozens more like them) are coming fast and may impact you in ways you do not want to consider. If and when they and those like them come to your town, your value peaked. This is not just for GPs, but also for all specialists. PDS will generate over \$1,000,000,000 (one billion dollars) in revenue in 2020.

## **#11: Economies Change**

You may remember October 1987 and April 2000, but you will definitely remember October 2008 until 2012. During that time large practices were not sellable for “cash now” at virtually ANY price. As you saw in our Timing is Now memo from October 2018, we predicted that Q4 2018 was the top in practice values. Unfortunately, it looks like we may have been right. When economies change, practice revenues often go down and values go down.

We will be here when you are ready!