Lakelet Advisory Group LLC

Focusing on Business Results

NEWSLETTER

Increase in M&As for Healthcare Facilities

Hospital and health systems merger and acquisition (M&A) activity is on the rise again, after years of near zero growth. Over the last four years, the number of hospital and health system M&A transactions has virtually doubled. Add to this, massive changes to physician practice acquisition and employment, and the recent consolidation becomes even more notable.

The drivers for this increase in M&A activity are:

- **Access to Capital** - Independent hospitals need more access to capital to address aging infrastructure, equipment and information technology, cash flow is stagnating and the ability to tap outside financing is diminishing. Moody's Investors Service issued a negative 2015 outlook for not-for-profit hospitals (which make up more than half of all U.S. community hospitals according to the American Hospital Association), projecting that the financial and business fundamentals of this sector will be weak over the next 12 to 18 months.

  Moody's cited three main factors likely to impact financial performance in 2015. First, little to no cash flow growth, with operating cash flow growth ranging from negative 0.5% to positive 1.5%. Second, weaker operating margins due to spending on needed capital investments and third, low revenue growth.

  With margins razor thin, hospitals are increasingly seeking transactions to achieve economies of scale and boost profitability.

- **Bureaucratic Requirements** - Hospitals are operating in an increasingly burdensome and expensive regulatory environment, and are looking to M&A to better and more affordably overcome regulatory challenges. The healthcare regulatory framework is complex and far reaching. The Affordable Care Act (ACA) and the Health Insurance Portability and Accountability Act (HIPAA) also add significant new regulatory burdens and are driving consolidation among hospitals.

- **Changing Model of Reimbursement** - The federal government has been vigorously trying to change the way doctors and hospitals get paid, focusing more on quality of care over quantity of care. The ACA expanded payment models that reward healthcare providers based on the value of the care they provide, as opposed to the amount of care they provide. And the Obama administration recently announced big changes to the way Medicare payments will be made, setting a goal to have half of all Medicare payments be based on qualitative measures by 2018.

  A shift to value-based payments has been taking place in the private sector as well. The *Washington Post* recently reported that approximately 20 percent of provider payments by Blue Cross entities "are through contracts that try to prioritize quality over quantity,"

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and that 28 percent of Aetna's reimbursements are in value-based contracts, which is expected to jump to 75 percent by 2020.

- **Urban Facilities** - Expanding market share for urban-based providers including targeting neighboring rural areas to secure patient flow, particularly for more complex procedures.

Lakelet Advisory Group ("LAG") is Expanding – Again!

LAG now has a sister entity that allows us to focus on investing in challenged entities and those entities that need capital and a partnership to achieve the "Next Level".

Lakelet Acquisition Corporation ("LAC") is a firm with a proven track record of adding value to lower middle market companies. Our model is to acquire such companies via the independent sponsor. LAC seeks to acquire companies where LAC can leverage its proven resources, cumulative knowledge, business models, and business partners to add value in the lower middle market. LAC is seeking to acquire controlling interest and provide high-level strategic and operational expertise to dramatically improve the operating results of the acquired company within our exit plan. LAC provides more than the capital for the acquisition – LAC possess the necessary strategic partnerships to take the entity to the "Next Level".

Lakelet Acquisition Corporation is seeking to invest in companies which possess a number of the following key characteristics: based in US or Canada, a proven client base, growing or flourishing industry, barriers to entry, a scalable business model and potential to financially restructure in a cost-effect manner. LAC is willing to explore turnaround / distressed opportunities.

Our Differentiators:

- LAC is powered by the team at Lakelet Advisory Group, a leading consulting firm that has driven success and operational results in over 100+ companies – see below for a partial listing of representative results;
- LAC has an extensive network of strategic and operating partners in a variety of industries – in order to foster growth and navigate any challenges in portfolio companies;
- LAC highly credentialed team also has tremendous financial contacts and experience – critical to evaluating and structuring transactions, building successful growth models, and driving to a future successful liquidity event;
- LAC team has expansive expertise with focus in the following industries: manufacturing, business services, technology, health care, distribution and consumer goods;
- Expeditious execution of deals and strategic business plans;
- Willing to explore turnaround / distressed opportunities;
- Well positioned for generational transition opportunities and assist family owned companies in continuing to prosper; and
- Opportunities for selling stockholders to acquire equity in the acquisition vehicle (and continue to participate in the success of the business post-sale).

If you are aware of any possible companies that the aforementioned pertain, please do not hesitate to contact us.

Are Special Asset Teams the Last to Know?

Too often with SMB's [Small to Mid-Size Businesses] financial institutions are not current on the financial and/or operational performance of the company in question. The financial institutions / creditors based their assessment on an annual set of reviewed or even compiled financial statements that are months old. By the time the Special Asset Team is involved, the company is literally on death row. It is not unusual to be engaged by a company where the financial institutions / creditors are unaware of the true status of the company. Why is this so?

- Entrepreneurs by their very nature are optimistic. A bad month and they wait until the next month; a bad

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quarter – well there is always next quarter; then a bad year…;

- Companies know that the Special Asset Team can become the "grim reaper" and companies will try to perform the workout under the radar;
- Prior financial statements have been overly aggressive in their accounting;
- The loss of a single customer or product line is enough in SMB to cripple the entity within weeks;
- The relationship with financial institutions / creditors was never a true business partnership;
- Loss of a key employee is enough in SMB to cripple the entity within weeks; and
- The company is hoping to sell the company before it implodes – so why put up red flags?

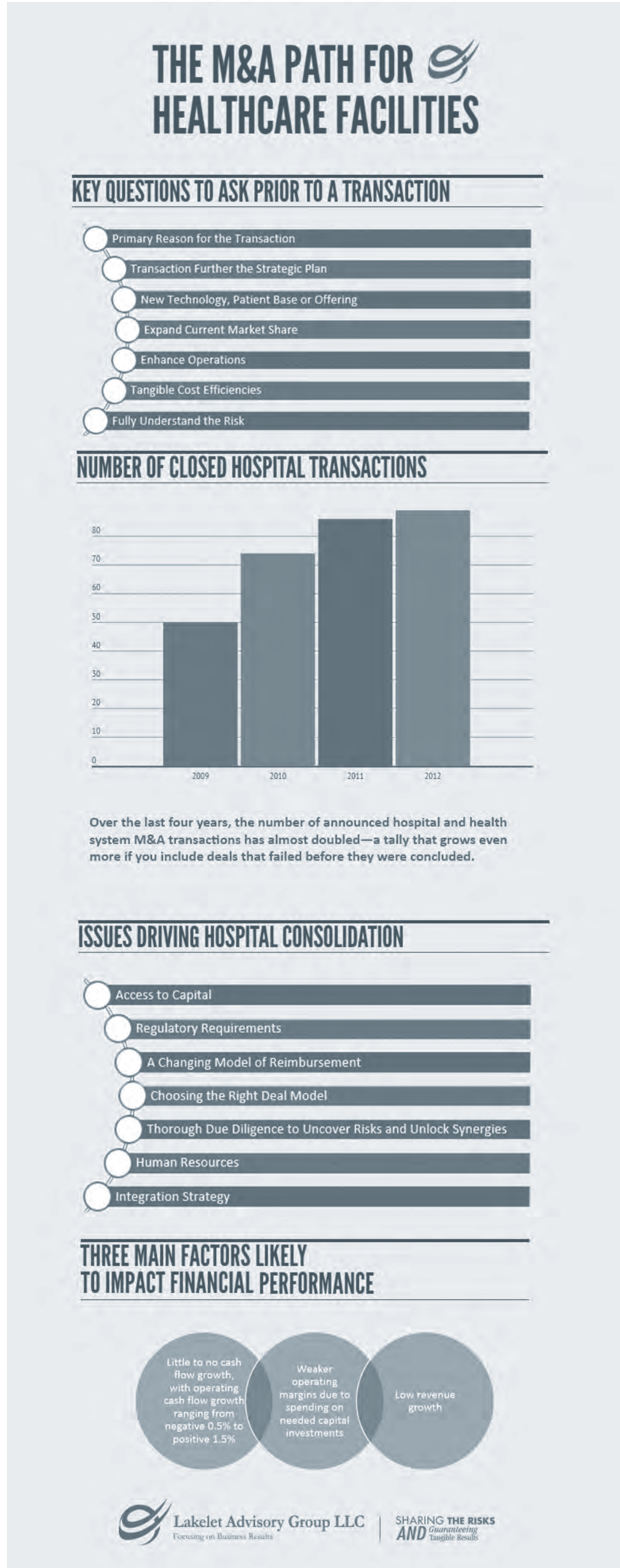
A few possible recommendations to mitigate these risks are:

- At a minimum, have the companies enter their results into the financial institutions / creditors database on a quarterly basis;
- Have the financial institutions / creditors relationship team meet quarterly with the clients, not only to sell more products, but to become aware of issues. This may require training – but what an asset this could be if properly performed; and
- Maintain vigilance on key trend industries (i.e. oil and gas, mining, etc.).

Why?

The key reasons for this situation are:

- Lack of understanding as to the specifics of the company (they miss the early signs);
- Adversarial relationship with financial institutions;
- Not requiring the business to have a true budget vs. actual. Only "after the horse is out of the barn" do financial institutions require a business plan with realistic budgets / projections; and
- Financial institutions are very departmentalized. Commercial loan officer is not in sync with the Special Asset Teams.



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"Strive not to be a success, but rather to be of value."
Albert Einstein

"Intelligence is the ability to adapt to change."
Stephen Hawking

What's Happening With Lakelet This Quarter?

- Effective January 1, 2016, Lakelet launched its healthcare business group. The healthcare industry is growing rapidly in the United States; directly correlated to this astronomical increase are the challenges of healthcare turnarounds and fraud. Lakelet has expanded its professional team to include deep industry experience and thought leadership in the areas of provider financial and operations management, health policy integration and compliance; forensics and billing management; turnaround and restructuring and medical technology assessment and commercialization.

- Lakelet welcomes David Beauregard as managing director of its healthcare initiative. Mr. Beauregard is an experienced healthcare executive and advisor, who has worked with clients and shareholders to build markets, improve operating performance and develop, align and execute strategic priorities. Through his leadership, innovative solutions and operations management skills, he has accumulated a solid track record for change management, performance improvements and increasing enterprise market values.

- In February, Tim Crino teamed up with Red Six Solutions, a strategic consulting firm, to conduct a corporate crisis training exercise for a Long Island client. This 5 hour training session employed elements of a tabletop exercise, virtual simulation and Red Teaming techniques. Corporate Red Teaming is an exciting and maturing field that incorporates both novel and time tested techniques to stave off potential business disrupters and improve operations. The purpose of this training was to provide insights into imminent threats that can significantly impact future revenue, brand reputation, valuation, resource allocation and strategic decision making of the client.