Lead Left Interview – Rod Rivera and David Baker (Part 2)

THE LEAD | May 23, 2018

This week we continue our conversation with Rod Rivera and David Baker, Managing Directors at Capstone Headwaters. Capstone Partners LLC and Headwaters MB, LLC recently announced a strategic transaction combining the two firms. This single platform has 150 professionals, covering 16 dedicated industry groups, spanning 20 offices across the US, UK and Brazil. This combination has resulted in one of the largest independent investment banks in the US. Mr. Rivera and Mr. Baker cover healthcare for the firm. ***Second of two parts –*** ***View part one*****.**

The Lead Left: *Could you provide an example in practice?*

Rod Rivera: A good example is respiratory medicine. Many MCOs pay a premium over competitive bidding rates to include the service component. Respiratory therapy provides value to the system by ensuring higher compliance and reducing expensive trips to the ER or hospital readmissions.

We are seeing the same trend in orthopedic surgeries. Payors are beginning to bundle reimbursement to include post surgical care and outpatient physical therapy. In a capitated world, outcome management is being more broadly defined.

David Baker: I see two pieces of risk. First, there's the current landscape of disruption into a value-based model compared to whatever your company's strategy is. Second, there's execution risk. The contracts become much more important in the delivery in a value-based model.

RR: Yes, and in loan land, you need to think about what's the correct leverage point for these risk elements. Have the credit markets fully absorbed the dynamic reimbursement models.

TLL: *What about your firm's role as a sell-side advisor? What advice can you give the buy-side?*

RR: Well, that's the primary focus of what we do. We're the armed guard for our client before we present to the buyer or investor. By presenting the most accurate picture of of the business model and company strategy, we are able to optimize outcomes for the seller, and experience a higher closure rate.

DB: If there is a valuation gap, you can use structure to accommodate that. For example, using earn-outs as part of the purchase price. That way the buyer is risk-protected. Other times, the client may need to advance certain things, new line of business, new customer contracts, before presenting to private equity, there are things you need to do before they go to market. By reducing risk for the buyer, it can be an easier discussion vs. setting up post-close milestones.

TLL: *How can private equity compete against strategics in the healthcare arena?*

RR: Sponsors are at a disadvantage to strategics in a transaction where the large corporate is simply adding to an existing stable of products they can plug into their distribution network. Where the sponsor has the advantage is being able to provide the seller with a second bite; starting with a smaller company, they can improve systems, help broaden payor networks and help the company navigate the changing environment to build real value. And then of course, to ultimately be able to sell to the strategic.

Contact:

Rod Rivera
rrivera@capstoneheadwaters.com

David Baker
dbaker@capstoneheadwaters.com