

DENTAL MARKET REVIEW

2019

INTRODUCTION

The dental sector continues to be one of the most active in which Christie & Co operates.

One of the undoubted 'green light' sectors for lenders, there is a plethora of established and new challenger banks keen to support the sector which should underpin activity in the medium term. In a less certain political landscape, investors and bank money tends to follow regulated, needs-driven sectors where levels of business impairment have historically been low. Dentistry certainly delivers on that criteria, as well as offering business owners opportunities for organic growth through the introduction of private dentistry and a flexible skills mix at practice level.

Our expanding specialist team reports encouraging levels of activity across the UK and has been involved in some of the highest profile projects, from a valuation and consultancy perspective.

In an increasingly sophisticated and rapidly evolving sector, the need for accurate advice backed up by market leading data, has never been more important.

Welcome to the latest edition of Dental Market Review 2019

There is a plethora of established and new challenger banks keen to support the sector.

c. 3,000

Total number of registered applicants looking to buy a dental practice.

The need for accurate advice backed up by market leading data has never been more important, creating high demand for our consultancy services.

The UK Dental Landscape and Workforce



UK DENTAL MARKET COMPOSITION

KEY OBSERVATIONS

Despite considerable M&A activity across the market, corporates still only account for around 13% of the total practices in the UK.

A 'mid-market' is emerging as companies such as Dentex, Dental Partners and Perfect Smile move towards (or through) the 50 site mark.

There has been a surge of start-ups, with the aim of growing rapidly to become a significant platform size in order to be attractive for acquisition in the future.

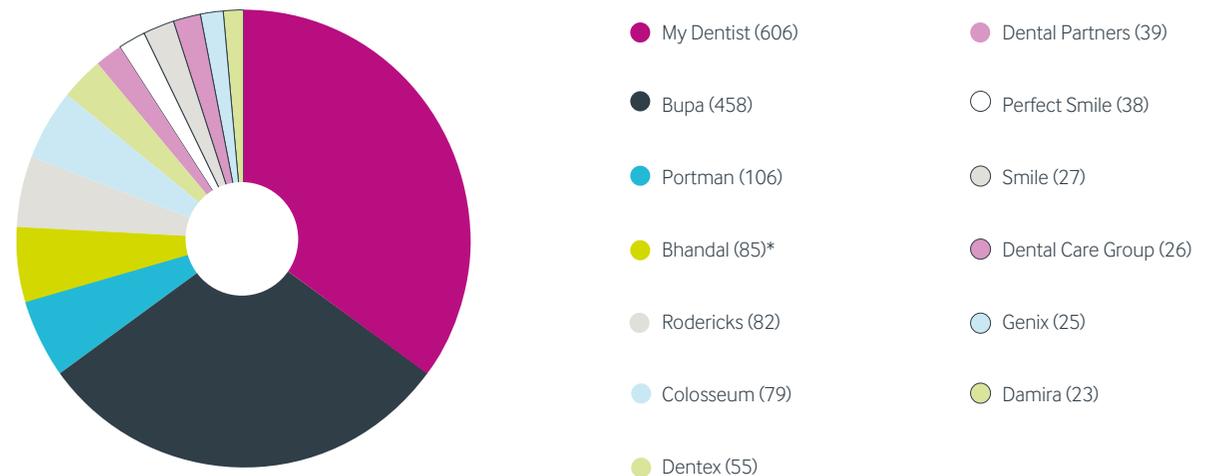
Further private equity activity in the sector emerges with Apposite Capital and G Square Capital making recent investments in the sector.

The sector continues to consolidate although it is still highly fragmented

MARKET COMPOSITION BY NUMBER OF PRACTICES



CORPORATE OPERATORS BY OWNERSHIP



*Estimate

THE UK DENTAL WORKFORCE

The majority of the 116.2k registered dental professionals in the UK are dental nurses (49%) with the next largest group being dentists (36%).

In total there are 41,705 dentists registered in the UK, which represents an average of one dentist per 1,600 of the UK population as at 2016.

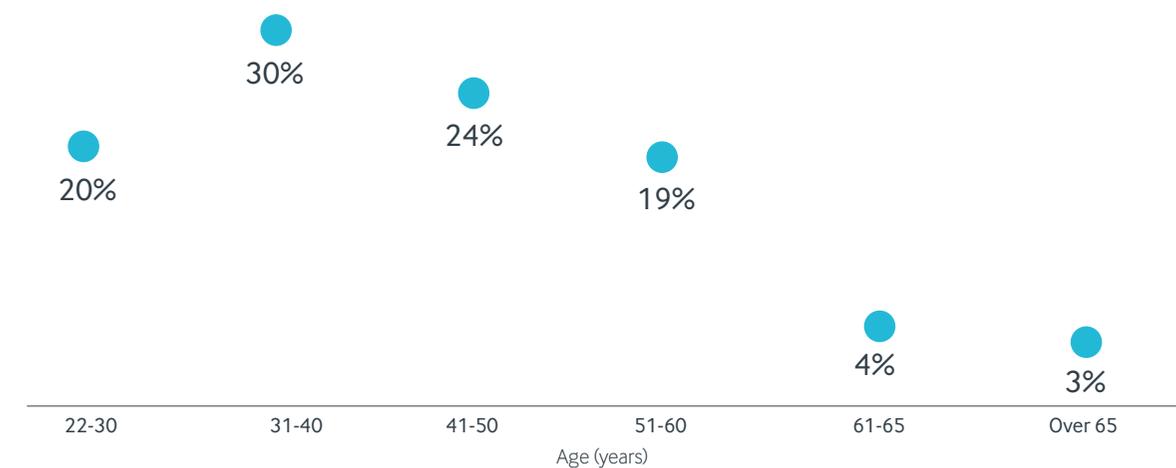
92% of non-dentist dental care professionals (DCPs) are female, and 8% are male.

The majority of dentists are aged 31- 40 years with only 7% aged 61 years and over.

GDC REGISTRANTS BY DENTAL GROUPING 2017



AGE PROFILE OF UK DENTISTS



51%
of dentists are male

49%
are female

Key Features of the UK Dental Market



THE DENTAL MARKET OVER THE LAST 12 MONTHS

The market is increasingly quality driven and geographically sensitive

Continued challenges with associate recruitment and retention, particularly amongst corporate purchasers, has driven demand towards urban locations. Independent buyers are less sensitive to this as they are generally working principals.

Average price increases level out although better quality practices command premium prices

In the NHS sector, offers are increasingly based on actual contract performance as opposed to baseline contract value. Both buyers and lenders are more sensitive to claw back and breach notices. Local area teams are taking an increasingly hard line when the 4% performance threshold is breached.

Sector consolidation continues in the mid-market

The last 18-24 months have seen an increase of dental start-ups. We estimate that there are now in excess of 400 multiple practice owners in the UK (2+ sites) which is an increase of some 50% from 2015. The very keen interest in the dental sector from private equity, family trusts and other investors is encouraging the growth of these groups, who anticipate an opportunity to exit at enhanced value.

Key highlights

Recruitment and retention of associates is directly impacting the performance of NHS contracts

A two-tier market is emerging in the NHS sector. Well located and/or run practices demonstrating consistent UDA performance are selling for a significant premium. Whereas those in remote locations with a history of underperformance are now being sold based on actual performance rather than baseline contract values. An increase in running costs is compressing net profit margins.

A shift in demand towards private dentistry

There has been a discernible shift in demand towards the private sector, particularly by corporate and multiple practice owners. This is to balance the risk of forthcoming phased contract reforms, to mitigate the net reduction in NHS funding and to drive revenue yield at practice level.

Banks continue to support the sector in favour of other asset classes

Compared to many other business sectors, dentistry offers a safe haven for banks and other investors. Whilst private dentistry can be considered discretionary, the restriction of treatments on the NHS means that even in a challenging economy, demand for private dental treatment remains robust.

Continued private equity interest and investment in the sector

There continues to be huge interest in the dental sector from a range of private equity investors. At the top of the market, Livingbridge exited its highly successful investment in Portman to be replaced by Core Equity Holdings, signalling its ambition to support the next phase of growth.

This completed the 'marquee' transactions at the top of the market following investments made by Rodericks and Colosseum in the previous year. Small and mid cap private equity is therefore turning to smaller platform opportunities to gain a foothold into the market, as evidenced by Apposite Capital's investment in Riverdale and subsequent acquisition of Alpha Vitality and G Square Capital's investment in Dental Care Group.

Compared to many other business sectors, dentistry offers a safe haven for banks and other investors.

Alternative 'partnership' structures

A number of companies are now offering sellers of dental practices a financial stake after completion. This can align the interests of both buyer and seller and can be an effective way of creating additional value in a rising market.

Despite contract reforms due in 2020, there is no reduction in demand from first time buyers for smaller single site NHS practices

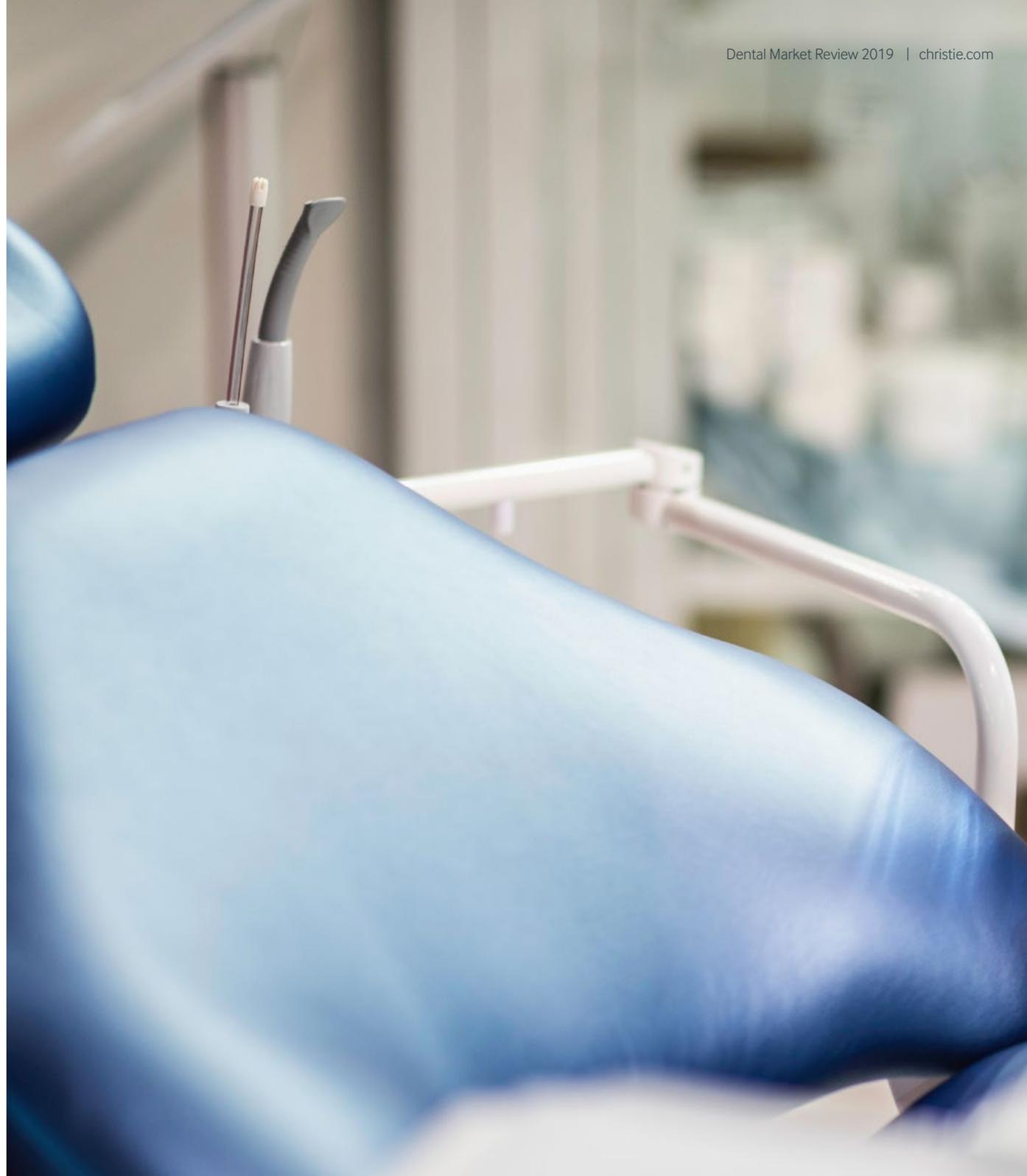
After a number of years of pilots and prototypes, the 'new' dental contract is currently planned to be phased in during 2020. It is yet to be confirmed how many practices will be affected, but it seems that the first phase of conversions may be on a voluntary basis to establish proof of concept.

Crucially, there is no suggestion that GDS contracts will be time limited nor will UDA values be reduced. We expect continued high demand for mixed practices, particularly from independents who are essentially 'buying a job' as owners and principals.

Hiatus in the orthodontic sector until the outcome of the current procurement process is known

A significant change in NHS orthodontic provision has taken place in the South of England over the last few months. This is as a result of the implementation of the NHS orthodontic commissioning guide which led to mandatory tendering for NHS orthodontic contracts. The size and scale of the re-procurement has made it a highly competitive process.

A large number of existing NHS practices in the South, which have lost or not continued with their orthodontic contracts, are currently in the process of winding down and transferring their waiting lists of patients to new providers. We are already witnessing the first 'new' orthodontic practices being marketed with enhanced contracts of 10 (7+3) years. These offer greater security than previously, albeit at lower UOA values and are proving extremely sought after.



Christie & Co Key Recent Activity



SOLD HOUSTON DENTAL GROUP

KEY HIGHLIGHTS

Confidentially marketed, the business attracted significant interest from dental and financial buyers.

A number of substantial offers were received resulting in the sale of the business and property portfolio.

We had regular occasion to call upon the invaluable assistance, sound advice and wise counsel of Christie & Co. We always found them to be professional, knowledgeable with insight into the market. There was always a willingness to support our position and the reassuring desire to achieve the best outcome on our behalf. The quality and breadth of the service we received would ensure our strong and unreserved recommendation of Christie & Co to any colleague contemplating selling a dental practice.

David Houston

One of the UK's leading independent dental groups sold to Alliance Dental Care

Established in 1990 as a single site practice, Houston Dental Group has evolved to be one of the leading independent dental groups in the UK, with 44 surgeries across North Somerset and the wider South West region.

Ceri and David Houston, owners of the group, approached Christie & Co for preliminary advice. As the Houston Group's valuers, we had an excellent knowledge of the business, resulting in us being appointed to market the business in 2018.

The purchaser, Alliance Dental Care, owns and operates a small, high quality group of practices situated in Hertfordshire. The group is owned by Dr Punita Taneja and Dr Anshul Pangotra, two highly experienced and qualified dentists. The Houston Group is a perfect fit geographically and propels Alliance to the next stage of its development as a force in UK dentistry.



I have known the Dental team at Christie & Co for several years. When they approached me with the opportunity to acquire the Houston Group, I immediately felt that it would be a perfect acquisition for Alliance Dental. Whilst the sale process was undoubtedly competitive, they respected my needs as a purchaser, enabling us to agree a deal that worked well for everyone. Alliance is proud to be the new owner of the Houston Group.

Anshul Pangotra

High quality dental group sold to BUPA Dental Care

Total Dental Care comprises four practices owned and operated by Anthony and Michael Zybutz, located across London and the South East of England.

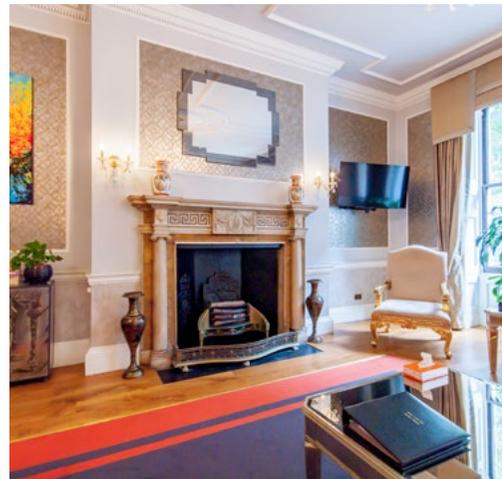
Originating in Camden in 1992, the business has since expanded with practices now in Folkestone, Dover, Peterborough and Harley Street. Three of the practices feature TDC implant centres, offering award winning, same day implant services.

Christie & Co met Anthony and Michael in 2016. It was advised that the sale of the entire group was likely to achieve optimum returns and in early 2018, we were instructed to approach a select group of potential purchasers.



We were comfortable that Christie & Co had the network and capability to manage our business sale. The sale process was fairly complicated, though we felt fully supported throughout. We are delighted with the outcome and would recommend the Christie & Co Dental team to anybody considering selling a group of practices.

Michael Zybutz



SOLD TOTAL DENTAL CARE

KEY HIGHLIGHTS

A detailed Information Memorandum was produced which presented this quality business to potential buyers.

An online data room enabled prospective purchasers to undertake due diligence.

Several offers were received and BUPA Dental Care selected as the preferred bidder.

It's not often that a dental business of this quality becomes available for sale. Demand for small groups is extremely strong from dental groups and private equity investors.

VALUATION/ ADVISORY ACTIVITY

A summary of the high profile valuation and advisory activity carried out by Christie & Co



LLOYDS BANK

164 commercial Red Book Compliant valuations with a combined value of £205m.

PORTMAN
dental care

Continued professional rental advice provided in support of the ongoing growth of the group.



111 commercial Red Book Compliant valuations with a combined value of £128m.

WESLEYAN BANK

we are all about you

Continued professional advice provided in support of lending within the dental sector.



Ongoing valuation advice provided in support of group expansion.



Christie & Co's Consultancy team has provided buy side due diligence advice in connection with several of the most notable recent corporate transactions.

KEY DEALS

Over
£320m
 of dental businesses advised on, valued or sold in the last 12 months



Metamorphosis Orthodontics, London

- Specialist private orthodontic practice
- Multiple offers received
- Landmark orthodontic sale

Caledonian Dental Care, Perth

- 19 surgery practice
- Largest dental transaction in Scotland
- Sold to Portman Dental Care



Withers & Ripley Dental Surgery, Bolton, Greater Manchester

- High turnover NHS practice
- Generated multiple offers (many above guide price)
- Sold to an expanding regional group



Brian G Easton Dental Practice, Linlithgow

- Four surgery, mixed income practice
- Potential to add further surgeries
- Sold off market to existing associate



Garvey & Hicks / Fulwell Dental Practice, Sunderland

- Three surgery, mixed income practice
- Multiple offers received
- Sold to an experienced operator

Breeze Family Dental Care, Fife

- Portfolio of three dental practices
- Multiple offers received
- Sold to an independent operator



Project Prime, Merseyside

- Two high turnover NHS practices
- Multiple offers received
- Sold to Dental Partners



A summary of some of the high profile deals brokered by Christie & Co

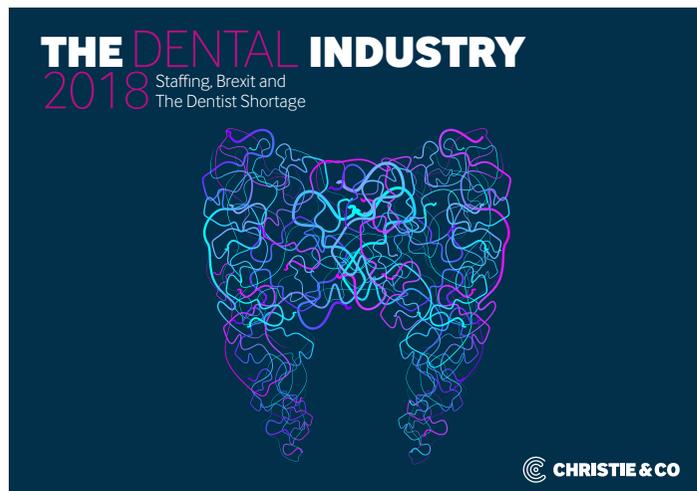
UK Dental Industry



CHANGES IN THE DENTAL WORKFORCE

In late 2018 our Consultancy team produced a leading research document which considered how changes in the workforce and external forces, including Brexit, are impacting the dental sector.

On this page we summarise some of the key findings, a copy of the full report is available for download from our website. Other bespoke reports that can be produced for clients include **market studies, benchmarking reports and a range of commercial due diligence services.**



Key themes discussed in the report



Number and role of other dental care professionals



Pay, UDA rates



Qualification trends



Brexit



Regional trends/where dentists want to live



Number of dentists

PRICE TRENDS

As highlighted in our most recent Business Outlook report we saw an average price increase of:

5.2%

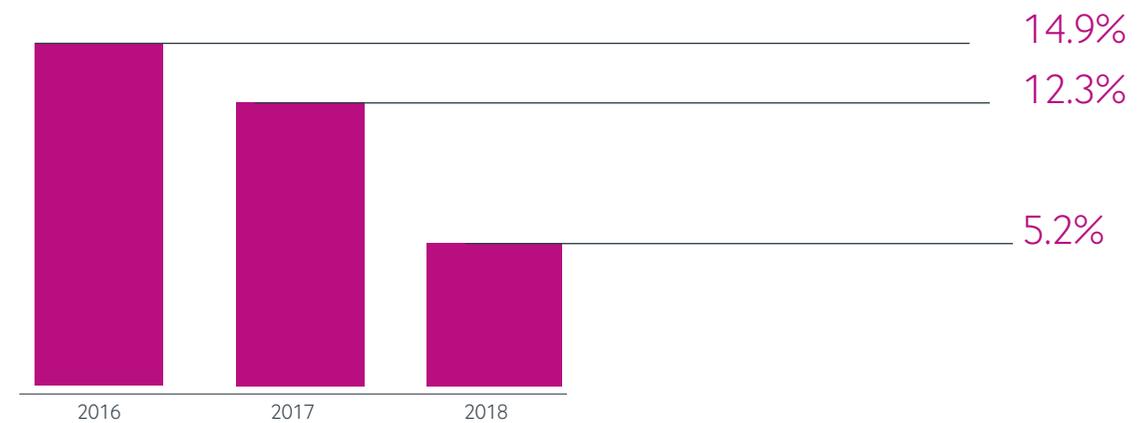
However, when segmented by geography and practice type/size, it is apparent that price increases were not universal.

Prices for larger private practices have increased at the fastest rate, albeit from a low base.

Mixed practices are still extremely sought after, but location is now more important.

An increase in average prices, but not across all market segments

MOVEMENT IN AVERAGE PRICES, YEAR ON YEAR



OPERATIONAL BENCHMARKING

Pricing flexibility in the private sector enables cost increases to be absorbed.

Challenges in the recruitment market cause continued associate cost inflation.

A lack of therapists restricts better utilisation of skills mix at practice level.

UDA pay rates vary significantly across the sector and materially impact profitability.

There are challenges to cost management in both private and NHS segments.

Analysis from our valuation and brokerage instructions confirms cost increases in all market segments

NHS (+80% INCOME)

	Low	Mean	High
UDA output (per associate)	2,500	6,750	11,000
Net UDA rate (per associate)	9.25	10.85	14
Labs + materials (% revenue)	5.7	12	15
Employed staff (% revenue)	15	18	25
EBITDA (%)	15	21	28

(Assumes 'associate led' model)

PRIVATE (+80% INCOME)

	Low	Mean	High
Gross income per associate	150,000	230,000	775,000
Associate pay scale (%)	30*	43	55*
Labs + materials (% revenue)	11.5	14	21*
Employed staff (% revenue)	13	17	24
EBITDA (%)	10	18	23

(Assumes 'associate led' model)

* Low + high reflects specialist work undertaken

CURRENT EBITDA MULTIPLES BY REGION

The heat maps and charts set out our analysis of dental practice sales over the last 12 months and new deals agreed in the same period to give the most up to date reading on the market. Practices have been grouped with reference to geography, type and size. We have also separated smaller practices with a turnover of less than £600,000 (which are likely to be owner/principal run) from larger, associate led practices to reflect the difference in operating margins and multiples paid. Smaller practices, particularly those with an NHS contract still tend to be priced by purchasers on a multiple of turnover, whereas buyers of larger practices are generally more sophisticated and adopt a multiple of EBITDA.

The EBITDA used to calculate the multiple paid reflects the actual performance of the business. We make no adjustments to staff costs or associate rates unless the vendor has specifically committed to adjusting the cost base to this level prior to completion. This follows the market which is particularly sensitive to any such adjustments.

The multiples expressed are averages and representative (generally) of the market, however, can be influenced by factors like:

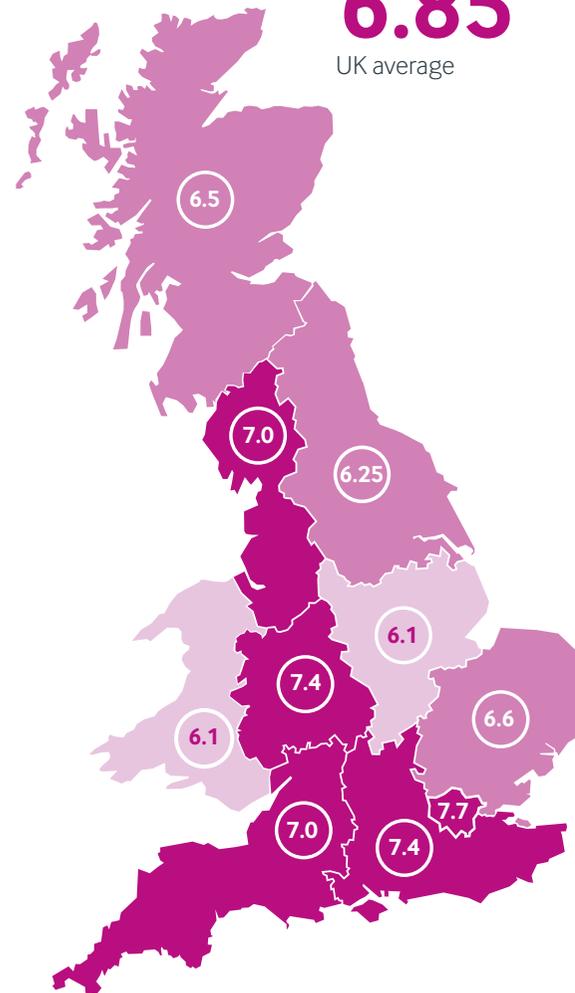
- The sample size in a particular region or practice type
- An EBITDA which is significantly higher/lower than normal
- A purchaser with a special interest in acquiring a particular practice and who is willing to pay a premium
- The timeline of a sale being constrained due to impairment or other reasons

Multiples of EBITDA increase with a clear premium paid for dental groups

Average **associate led** practice EBITDA multiples

6.85

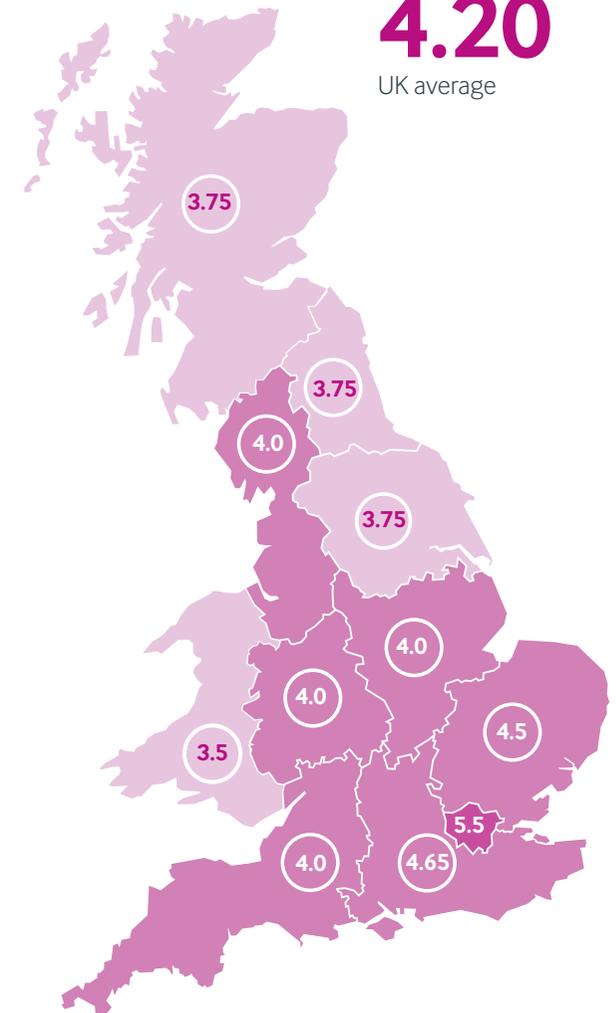
UK average



Average **owner operated** practice EBITDA multiples

4.20

UK average



CURRENT EBITDA MULTIPLES BY PRACTICE SIZE AND TYPE

Multiples have generally increased across the board, sometimes simply due to prices remaining static and profits falling.

Multiples paid for larger, associate led practices have increased at a faster rate. This reflects a lack of supply and an increase in the buyer pool for this type of practice.

Generally, multiples increase according to practice size with a clear premium being paid for group opportunities.

Multiples paid for larger private practices now mirror those achieved for their NHS counterparts

The average multiples of EBITDA shown for various locations and practice types relate to single practice sales.

The significant interest in the sector from consolidators and private equity investors, has led to a surge in demand for dental groups of all sizes, which now sell for a significant premium to single practices.

This reflects scarcity value and the arbitrage opportunity that currently exists.

Average EBITDA Multiple by Practice Type

Mixed

Associate led 7.2

Owner operated 5.2

Private

Associate led 7.1

Owner operated 4.0

Average EBITDA Multiple by Number of Chairs

1 to 2

Owner operated 4.0

6 or more

Associate led 7.8

3 to 5

Associate led 7.3

Owner operated 5.6

CHRISTIE FINANCE

An update on the current lending market for dental practices

The dental market continues to receive a positive reception from lenders

However, many have witnessed a rapidly changing landscape in recent years and have adapted accordingly.

They have observed the rise of the private dental market and the willingness of patients to pay for their own enhanced treatments, rather than relying on the NHS.

Most private practices and dentists see a steady, increasing level of fee income without the reliance of plan income. Previously, lenders have provided preferential lending to NHS-based practices, but now treat non-plan private practices in the same manner.

Their only stipulation is to ensure that the outgoing, income-billing principal has an agreed tie-in for a suitable period of time, dependent on the patient list.

Lenders no longer provide funding to dentists without carrying out extensive due diligence

Whether a target practice is NHS, mixed or private, lenders are carefully investigating the business, whilst looking closely at the buyer.

Lenders want to understand how a buyer is looking to operate the business; the level of management experience they have; how many days they plan to work there and development plans for the business. It is the aim of any lender to ensure their investment is secure, in turn providing the buyer with comfort around their substantial investment.

For existing practice owners, particularly group operators, certain lenders, due to their own internal restrictions, have become ever more cautious. Banks are enforcing the right

to revalue a portfolio and are scrutinising original lending covenants.

Should these covenants be breached, certain lenders may apply pressure on their customers to reorganise their portfolio. Examples of this would be to introduce more cash, sell to reduce the level of borrowing or strongly encourage them to refinance.

For first time buyer associates or group operators

Christie Finance has a team of specialist dental brokers across the UK, who understand both the dental sector itself and exactly what lenders are looking for. You often only get one opportunity with a lender, so your approach needs to be right first time.



David Ward
Senior Director
- Head of Medical Finance

Christie Finance instructed to
secure in excess of

£40,000,000

of finance for the medical sector in 2018

CONTACTS

CORPORATE SERVICES

Our specialist Dental team offers a full range of services aimed at larger independent dental practice owners, multiples and corporate operators. These include:

- Acquisition & Disposals Advice
- RICS Accredited Valuations for Loan Security
- Expert Witness / Dispute Resolution
- Landlord & Tenant Services
- Benchmarking Reports
- Strategic Business Advice / Market Mapping
- Commercial Due Diligence
- Market Research

Our Dental Team



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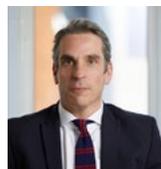
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Valuation Team

We have a team of **Chartered Surveyors and RICS Registered Valuers** dedicated to the dental sector. Working closely with our transactional colleagues we are able to draw on current market sentiment and comparable evidence.

With access to comprehensive market data, we are in a unique position to benchmark both the business performance and practice value, ensuring reports and professional advice is always well researched and well informed.

We are recognised as leading valuers by all the high street banks, as well as most of the other specialist lending institutions. Much of the work we undertake is for loan security, accounts and balance sheet, acquisition, disposal, dispute resolution, statutory compensation and taxation purposes.



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Christie & Co's dental consultancy proposition is unique, with the team advising on some of the largest transactions in the sector whilst providing bespoke research to a number of operators, investors and private equity companies.

Key strengths include our market leading level of proprietary data, sophisticated analytic tools and our granular understanding of the dental sector. The latter is reinforced by a close working relationship between consultancy and colleagues within our dental brokerage and valuation teams, enabling clients to benefit from high quality advice combining data with in depth market insight.

Our team consists of a high-calibre group of professionals with an extensive and diverse range of analytical, financial, operational and property-based skills. The team was responsible for the production of Christie & Co's ground breaking research report on Staffing, Brexit and the Dentist Shortage, published in autumn 2018 and widely reported across national and trade media.

We specialise in tailoring bespoke outputs to meet client needs. Typical types of assignment include commercial, research and property due diligence, market analysis, market studies and business planning.

Christie Finance is a specialist commercial finance broker, helping dental practice operators to develop and grow their business for over 40 years. As an independent broker, we are not tied to any particular lender, knowing which ones to approach to source you the commercial mortgage you require.

As a member of the Christie & Co Network, we are known and respected throughout the dental sector, meaning our clients are taken seriously by lenders. Whether you are a first time buyer, an existing operator, or looking to release capital for a new venture, we can guide you through the process to secure competitive funding.

Our network of five regional hubs across the UK enables us to combine a local knowledge with national insight. A Christie Finance dental specialist local to you will deal personally with every aspect of your commercial mortgage application.

Our Christie Finance Unsecured division can work with you to secure fast and flexible finance, offering a straightforward solution to covering costs of key dental practice investment.

All funding is subject to status.

RCC Business Mortgages plc, trading as Christie Finance, is authorised and regulated by the Financial Conduct Authority. Our Firm Reference number is 709982. Not all types of business we undertake is authorised and regulated by the Financial Conduct Authority. Christie Finance operate as an intermediary and are not a principal lender.

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