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Cain Brothers House Calls



Looking Back, Looking Forward: A Golden Age of Healthcare Innovation?

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Since the middle of 2020, during the early days of the pandemic, several long-developing trends within the U.S. healthcare economy accelerated toward critical mass, attracted dramatic amounts of capital at record high valuations, and made a genuine impact on the perpetual goal of better care at lower cost. These trends include: the proliferation of value-based care delivery and payment models, greater consumerism, the shift to decentralized care delivery (away from hospitals to alternative care settings), and growth in digital healthcare solutions in both the B2C and B2B realms.



The sector's public and private market investment levels, M&A activity, and partnering across sectors and companies hit new heights. The implication of these trends is clear. Healthcare is undergoing a paradigm shift in business models and practices. Holistic consumer and value-centric delivery are replacing fragmented, transactional and reimbursement-focused services.

Without question, the COVID pandemic accelerated the healthcare industry's ongoing transformation. Healthcare organizations of all stripes continue to adopt digital technologies at an urgent pace to address the massive healthcare needs of our country and to navigate COVID-related work disruptions. Medicare Advantage enrollment levels continued to rise, giving more traction to risk-based contracting models that incorporate prevention, care management and health promotion, even as the number of plans available to consumers increases¹ and competition intensifies². Care delivery decentralized through virtual channels, primary care and urgent care clinics and utilization of an array of home-based care capabilities.

These developments reflect decades of investment and work by forward-thinking healthcare organizations and entrepreneurial ventures, fueled by long-term investments from venture capital and private equity firms and large corporations from across the U.S. economy (i.e., not only healthcare organizations but also technology and consumer companies). The progress they have made in addressing many of healthcare's deep-rooted challenges, in the face of a global pandemic and at the likely tail end of history's longest bull market, is something to behold.

It is notable that in 2021 and 2020, the healthcare industry showed remarkable resilience and adaptability in managing the challenges presented by the pandemic: including shocking and tragic hospitalization levels, burnout among frontline healthcare professionals, labor shortages in virtually every industry, disrupted supply chains, work routines and purchasing patterns, and ongoing political tension and division. Opioid deaths, addiction, depression, anxiety and the need for mental health services are growing at unprecedented rates. The healthcare industry, and those who finance it, have stood tall in the face of these problems, and worked tirelessly for solutions.

We obviously don't know what the months ahead will bring, but we feel confident that these trends and the underlying focus on innovation will continue to influence the healthcare landscape in 2022.

¹ <https://www.kff.org/medicare/issue-brief/medicare-advantage-in-2021-enrollment-update-and-key-trends/>

² <https://www.healthcarediver.com/news/humana-slashes-medicare-advantage-outlook/616828/>

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1) *The Adoption of Value-based Care Models*

In 2021, providers and payers made substantial progress in their long-anticipated transition to value-based care and population health models. While adoption of true risk-sharing models between providers and payers has been an industry vision for over a decade, progress has been slow and the benefits anemic for providers, payers, self-insured employers and consumers.

Today, growth in Medicare Advantage enrollment and other risk-based payment models are changing entrenched payer and provider behaviors. Increasingly, innovative companies focused on the treatment of debilitating and expensive chronic healthcare conditions are gaining traction and capital investment, driving more change in care delivery. COVID's disproportionate impact on vulnerable populations also pushed health equity and social determinants of health to the forefront of America's health policy agenda.

Cain Brothers described the impetus for this transition to value in 2020 in our “*Future of Hospitals*” series, which speculated that value-based models would become increasingly attractive for health systems in competitive markets going forward.

Within a year, speculation gave rise to implementation. In 2021, we produced a four-part series entitled “*All Roads Lead to Value*” which looks closely at the strategies health systems, alternate site providers, insurers and technology companies are employing to enable risk-based contracting:

- The series' first commentary focused on the strategies that financially secure health systems in competitive markets are taking to build their risk-taking capacities, particularly through joint ventures, consolidation, new platform offerings, specialization and brand-enhancement. (August 17, 2021)
- The second commentary examined how physician groups are enabling or enhancing their risk-taking capabilities by partnering with “risk-management organizations” that provide the technological and administrative support necessary. (October 7, 2021)
- The third commentary explored strategies for establishing risk-based contracting in rural America. (December 2, 2021)
- The fourth commentary detailed the communications technologies that providers are using to engage patient populations in managing their own care. (January 20, 2022)

The mechanics of value-based care are increasingly integral to all sectors within the healthcare ecosystem. This includes life sciences which is decentralizing clinical trials and med tech which is incorporating outcome measures into total-cost contracting arrangements. The movement toward consumerism, digital adoption, decentralized care delivery, population health, personalized medicine, data analytics, and social determinants of health are the key components of this macro trend.

2) *Record-Level Investment Activity*

2021 was a watershed year for capital raising, investment, and mergers and acquisitions in U.S. healthcare. The following forces contributed to the increased investor interest, and valuations, throughout healthcare:

- Adoption of digital health tools for delivering clinical care
- More emphasis on consumer engagement, fitness and wellbeing
- Use of decentralized trials and real-world evidence to speed treatment innovation
- Increased need for digital and IT solutions to manage providers' and payers' accelerated migrations to risk-based payment models
- New care delivery models for chronic disease management

Cain Brothers House Calls

Digital tech investment was particularly noteworthy. Digital health technology companies attracted a record \$29.1 billion in funding last year, nearly double the previous record of \$15 billion in 2020. Biopharma and med tech digital technologies led the pack, including such companies as Reify Health³, Elligo Health⁴, Medable⁵ and Pear Therapeutics⁶, while the mental health sector dwarfed investments in other clinical disease areas at \$5.1 billion. The next highest category was diabetes care at \$1.8 billion.⁷

Investment levels in 2021 were likely boosted by “tourist” investors without specialized healthcare teams or significant prior investment activity in the sector. Given the early 2022 stock market correction and the ongoing impact of inflation, it’s worth considering whether this level of investment and deal-making is sustainable. However, the macro trends, the ongoing implementation of technology solutions and market acceptance of new care paradigms and payment tools indicate such activity should continue.

Years of investment in data, digital tech, alternative care settings / channels and consumerism are beginning to shape healthcare's workflows, productivity and care delivery. At Cain Brothers' October 2021 Healthcare conference, speakers on both our private equity and venture capital investment panels, and in virtually every individual company presentation, shared a view that the long-term investment horizon for healthcare remains positive because the need for industry transformation remains so massive.

The Year Ahead

The first quarter of 2022 has continued much like 2021. The annual JP Morgan conference went virtual for a second straight year. The pace of notable transactions hasn't slowed: Vera acquired Castlight⁸; Stryker acquired Vocera⁹; Babylon acquired HIGI¹⁰; R1 acquired CloudMed¹¹; Aledade acquired Iris¹²; Medtronic acquired Affera¹³; and IBM is selling Watson Health¹⁴ to Francisco Partners. And so it goes.

At the same time, the public equity markets have entered correction territory. Many of healthcare's high-flyer IPO classes of 2020 and 2021 have seen dramatic declines of their valuations. While these declines are sobering for both investors and companies in the queue for future public offerings, valuation levels for healthcare enterprises, measured by both aggregate enterprise values and traditional multiples metrics, remain at levels that are nearly unprecedented.

Healthcare investors will continue to support innovation in areas of healthcare that have great need and significant growth potential, including mental health, diabetes, cardiovascular care, oncology, health and fitness, primary care, health equity and social determinants of health. This will be true for companies across healthcare, from life sciences and medical devices, to insurers, providers, and digital ventures.

2022 will also likely see expanded growth in services and offerings tailored to consumers as consumerism takes hold. We may look back on 2022 and call it the Year of the Consumer.

³ <https://blog.reifyhealth.com/reify-health-raises-millions-eliminate-waiting-clinical-trials>

⁴ <https://www.elligohealthresearch.com/news/morgan-stanley-expansion-capital-and-ally-bridge-group-lead-135-million-investment-in-elligo/>

⁵ <https://www.medable.com/resource-center/series-d-funding>

⁶ <https://peartherapeutics.com/pear-therapeutics-and-thimble-point-announce-closing-of-business-combination-to-create-publicly-traded-prescription-digital-therapeutics-company/>

⁷ <https://rockhealth.com/insights/2021-year-end-digital-health-funding-seismic-shifts-beneath-the-surface/>

⁸ <https://www.prnewswire.com/news-releases/castlight-health-and-vera-whole-health-to-combine-to-pioneer-and-scale-value-based-care-in-commercial-market-301454477.html>

⁹ <https://www.globenewswire.com/news-release/2022/01/06/2362418/0/en/Stryker-announces-definitive-agreement-to-acquire-Vocera-Communications.html>

¹⁰ <https://www.prnewswire.com/news-releases/babylon-a-world-leading-digital-first-value-based-care-company-announces-plans-to-become-a-public-company-via-4-2-billion-merger-with-alkuri-global-acquisition-corp-301305279.html>

¹¹ <https://www.globenewswire.com/news-release/2022/01/10/2363709/0/en/R1-RCM-to-Acquire-Cloudmed-Creating-the-Strategic-Revenue-Partner-for-Healthcare-Providers.html>

¹² <https://www.globenewswire.com/news-release/2022/01/11/2364603/0/en/Aledade-Acquires-Advance-Care-Planning-Company-Iris-Healthcare-as-Part-of-New-Health-Services-Arm.html>

¹³ <https://www.crunchbase.com/acquisition/medtronic-acquires-affera-inc-cfc2df07>

¹⁴ <https://www.healthcareitnews.com/news/ibm-sell-watson-health-assets-francisco-partners>

Cain Brothers House Calls

Regulatory and payment reforms will speed adoption of value-based care delivery models. Breakthroughs in digital tech, medical science and genetics will accelerate the pace of transformation. Consolidation, business model innovation, capital investment and consumerism will reconfigure the healthcare marketplace, spurring new and improved services, enhanced efficiencies, more competition and growth. The alignment of these forces has the potential to catalyze innovation at an unprecedented pace and scale.

Below, readers will find the list of House Calls that Cain Brothers' bankers produced in 2021. As a final note, we list the "Bold Predictions" that Cain Brothers bankers made on the various House Calls podcasts in 2021. Feel free to let us know how well you think those predictions are shaking out.

We look forward to producing more thoughtful commentary and analysis in the year ahead.

Cain Brothers House Calls

Bold Predictions¹⁵

“Medicare Advantage is going to continue to see significant growth in the value based care space. I don't think we're going to have Medicare for all in the foreseeable future, but I do think we're going to have Medicare Advantage available to many more.”

- **David Morlock**, Managing Director, Co-Head of Health Systems M&A

“We're going to see a significant acceleration in the consumerization of health care over the next couple of years. Health care companies that target the consumer and put them front and center will be the winners.”

- **Stacy Guffanti**, Director

“In the addiction sector, we're on the cusp of more cooperation between payers, providers and other stakeholders across the care continuum, with a real opportunity to help get people back to their normal everyday lives.”

- **Erika Haanpaa**, Director

“With continued outsourcing, hospitals will become almost like large department stores today where you can walk in and find many different businesses operating inside.”

- **Christian Pesci**, Managing Director

“The top 25 health systems will control more than 75 percent of the revenue that's generated in a hospital setting within the next 10 years.”

- **David Levine**, Director

“We're going to see a tremendous proliferation of risk models in the physician practice space. These organizations will really start to challenge the status quo, whether that's the hospital system or the payer, and they're going to become very formidable allies or enemies, depending on how each market responds.”

- **Mike Elizondo**, Director

“Over the next 12 months, we'll see a significant acceleration of funding and announcements for rural start ups.”

- **Colby Kittrell**, Director

“There's going to be more convergence between service providers and tech vendors, as service providers invest in technology companies or buy them outright, and technology software providers partner with service providers or build-out their own service capabilities.”

- **Bryan Cloncs**, Managing Director

¹⁵ <https://www.key.com/businesses-institutions/industry-expertise/healthcare/house-calls-podcast.jsp>

Cain Brothers House Calls

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<https://www.key.com/businesses-institutions/industry-expertise/healthcare/insights-ideas.jsp>

The Many Flavors of Healthcare's Not-For-Profit/For-Profit Partnerships

Stacy Guffanti

<https://www.key.com/businesses-institutions/business-expertise/articles/flavor-of-healthcare.jsp>

Health Systems Embrace Platforming and Innovative Financing Strategies

David Morlock

<https://www.key.com/businesses-institutions/business-expertise/articles/health-systems-embrace.jsp>

Stigma vs. Science: Overcoming Opioid Addiction with Evidence-based Treatments and Services

Erika Haanpaa

Medicaid, Motherhood and America's Future: Giving Birth to Better Maternity Outcomes

Christian Pesci

<https://www.key.com/businesses-institutions/business-expertise/articles/medicaid-motherhood-americas-future.jsp>

All Roads Lead to Value Part I: What is a Health System Supposed to Be?

David Levine

All Roads Lead to Value Part II: Positioning Physicians to Manage Care Risk

Mike Elizondo

Growth and Innovation Driving Deal Activity: Cain Brothers' 2021 Healthcare Conference

All Roads to Value Part III: Making Inroads in Rural America

Colby Kittrell

All Roads to Value Part IV: Building The Last Mile to the Patient

Bryan Cloncs

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