

Evolving Perspectives: The Impact of COVID-19 on the Dermatology Market and Consolidation Activity



Experts weigh in on the effect of COVID-19 on Mergers & Acquisitions trends in dermatology.

BY CLINT BUNDY

>> As the business and health care environments continue to adjust, evaluate, learn, and experiment with a changing landscape because of COVID-19, it is evident that the dermatology market is no exception to this analysis. Furthermore, the consolidation race that had previously been accelerating in the dermatology market may have finally hit its first caution flag. The question for many practice owners contemplating a sale or bringing on a capital partner is when the green flag will be waved and the Mergers & Acquisitions trend will resume.

Practices across the country have had to close their offices, convert to telehealth, drastically cut back on in-patient visits, cease Mohs surgery and excisions, or a combination of all. This has resulted in temporary lower financial performance for many dermatology practices, which could risk the overall value of those businesses. Furthermore, both seasoned buyers and practice owners are currently assessing the

health of the dermatology market in this new normal and deciding what is the best path forward in terms of investing in this healthcare specialty.

The consolidation race that had previously been accelerating in the dermatology market may have finally hit its first caution flag with the coronavirus pandemic and its impact on the space. Many dermatology practices are reporting temporary lower financial performance, which could risk the overall value of those businesses. While the dermatology sector continues to be an attractive market and generates a great deal of interest in terms of investment activity, 2020 will test the resiliency of the sector.

thebottomline

DERMATOLOGY MARKET

As we are immersed in another recession, many consider the dermatology market to be a relatively resilient sector. From 2007–2009, the dermatology market grew at approximately a 2.1 percent compounded annual growth rate, while the US GDP decreased 4.3 percent from Q4 2007 to Q2 2009 (i.e., the Great Recession).^{1,2} However, the COVID-19 pandemic and its effects on dermatology practices are more

direct than the Great Recession. While there is little doubt of the longer term positive prospects for the dermatology sector, the short- to medium-term implications of the pandemic economy are currently unknown. Here I share a collective roundtable analysis from leaders active in the dermatology and physician practice management sectors regarding the future of the dermatology market.



“Still Good Value to Be Found”

We are seeing dermatology in two different market segments: the medical dermatology practice is ramping back up in a “V” shaped model solely dependent on the practice’s ability to move patients in and out efficiently and within COVID-19 guidelines. There is a backlog in demand and a shortage of open appointments. The second is the “retail” practice that includes cosmetic procedures, products, and services. The rebound for this model is solely dependent on practice location, brand, and market demographic. Not all segments of the economy are doing poorly, as some sectors are winning. If a cosmetic dermatology practice has a clientele that is primarily in a geography that is affluent and a patient base that is “winning” financially, the practice is holding up well. Dermatology practices that dabbled in cosmetic services as an add-on or fringe product line are the most negatively affected during this downturn.

Our conclusion is that there is still good value to be found, however, it will require a lot more work to sort through the information to determine winning investment opportunities.

—Tom Ferkovic

Chief Executive Officer, Medic Management Group, LLC
Medic Management provides a one-stop solution for all things health care management, which includes revenue cycle optimization, practice management, and consulting.

“Surprisingly Resilient”

We are seeing demand for elective medical care like dermatology remain surprisingly resilient throughout the late spring and early summer. The initial surge of patient procedures post-reopening was originally thought to be the result of clearing out of pent-up demand, but higher-than-anticipated volumes continue to buoy practices—this is very positive news for dermatology practices across the country.

August will be a crucial barometer of the health of the dermatology space for 2020 and 2021. If we continue to see strong patient volumes despite the potential curtailing of federal unemployment benefits, it will be likely that dermatology practices will escape 2020 relatively unscathed.

New patient acquisition for elective care continues to be strong, especially when leveraging digital approaches and for those practices providing a virtual option for an initial consultation. In our health care marketing practice at iVelocity Marketing, we are seeing patient engagement numbers equal to, or in many cases, higher than pre-COVID rates. To illustrate the

point, June searches on Google for “dermatologist near me” are up nearly 300 percent from a low point in April and are 45 percent higher than June 2019. This is clear indication of healthy demand for dermatological services. Practices that make moves to increase their presence online may actually see YoY growth for their services through the remainder of the year.

—Scott Alexander

Chief Executive Officer, iVelocity Marketing
iVelocity Marketing is one of the nation’s premier health-care-focused digital marketing firms, known for helping practices grow their elective patient procedures through a combination of real-world health care experience, a deep focus on data, and some of the top marketing minds in the country.

“Continue to Flourish and Grow”

As a global CRO, Catawba Research is not immune to the global and domestic economic climate. A CRO is a service provider reliant on a loyal client base and walk up business. We are no different from other service providers, like restaurants, motor mechanics, and donut shops. In our case, our customers are dermatology pharmaceutical drug development companies who are challenged and anxious over these uncertain times. Our customers, like others, are conservative in their approach to spending money, and opting to conserve their resources during these uncertain times. Moreover, the CRO industry has also been impacted by trends in patient engagement. With regional programs encouraging “shelter in place,” it has been challenging for CROs to fulfill their obligation to ensure a full panel of patients to participate in clinical trials.

The CRO industry has been “double-whammied” by the pharma industry’s ‘let’s wait and see approach’ and by dearth of available patients willing to leave their home and participate in clinical trials. As a result, our industry has seen massive layoffs, furloughing their staff and closing clinics. COVID has killed not only people, but businesses, too.

How has Catawba Research fared through these troublesome times? Spectacularly well. We have been the recipient of increased business due to the failure of our competitors. Catawba Research has had the good fortune to hire the cream of the crop of clinical research professionals. With remote working culture and technology, geography has been mitigated. Catawba Research with its own network of research sites, 3A Research, has flexibility and autonomy to be creative when it comes to patient recruitment. 3A Research COVID enrollment numbers have not suffered.

“Out of crises comes opportunity.” In the case of Catawba Research, we have taken full advantage of our opportunity and continue to flourish and grow.

—Zaidoon Al-Zubaidy

President and Chief Executive Officer, Catawba Research, LLC

Catawba Research, LLC (CR) is a full-service contract research organization (CRO) providing clinical management services to pharmaceutical, device, formulation development, and biotechnology companies. Catawba Research has a primary focus on the dermatology sector.

MERGERS & ACQUISITIONS FOR THE DERMATOLOGY MARKET

Within the health care Mergers & Acquisitions market, dermatology has proven to be one of the most attractive health care segments over the past seven years. As an example, from just January to July 2018, there were 36 transactions in the dermatology sector. With many practices operating at below their normal capacity as a result of COVID-19, many experienced buyers have taken a “wait and

see” approach in regard to further acquisitions. The M&A activity will inevitably restart for the dermatology sector, but many questions remain regarding the impact of COVID-19 on consolidation and valuations for dermatology practices. Outlined below are observations from a number of experienced buyers and private equity investors active in the dermatology sector.

“Poised for Continued Consolidation”

No medical practice was fully prepared for the disruption of COVID-19. At Advanced Dermatology & Cosmetic Surgery we were forced to make many difficult decisions prioritizing the safety of patients, providers, staff, and our communities. We have taken many learnings away from the scope of the COVID-19 disruption but there are some clear positives as well. During the peak of the outbreak, our practices across the country took advantage of regulatory and payor landscape changes and rapidly implemented and embraced telehealth, which we continue to offer as an option for patients today. Dermatology is a diverse and resilient specialty. Skin health, skin cancer awareness, and demand for high quality aesthetics services continue to drive demand for dermatologic services. As the initial outbreak of COVID settled, patient demand quickly returned to normal, and we have experienced increased interest from independent practices considering joining a larger platform. We believe the industry is poised for continued consolidation with a goal of offering consistent and high-quality patient care across the country.

—Justin Simoncini

Vice President & Chief Development Officer, Advanced Dermatology & Cosmetic Surgery
Advanced Dermatology and Cosmetic Surgery is the nation's premier dermatology practice with a presence in 14 states. Justin Simoncini, a seasoned health care transaction professional, leads ADCS' practice acquisition efforts.

“Focus on a Much Longer Horizon”

The COVID-related shutdowns were a surprise and negatively impacted our dermatology platforms in the near term.

Despite the near-term headwinds caused by the pandemic, our view is that the dermatology sector has secular tailwinds that have staying power. Unlike the mandated selling horizons of traditional private equity investors that seek to exit their investments in five years or less, as family office investors we don't have predefined timelines requiring us to sell our investments. We focus on a much longer horizon, abiding by Warren Buffet's famous saying, “If you aren't thinking about owning an investment for 10 years, don't even think about owning it for 10 minutes.” Simply put, we like the long-term prospects for the dermatology sector and welcome the opportunity to speak with providers that would benefit from partnering with an investor that is experienced in and committed to the sector long term.

—Erick Clifford

Managing Partner, Lead Capital

A multi-family office investor focused on partnering with founders and management teams in the health care and dermatology sectors, provided his insights on the dermatology M&A market.

“Confident in the Future”

We are seeing an environment where practices that have historically been accustomed to high patient demand, stable revenues, and predictable margins are suddenly challenged with managing a business with surging unit supply costs, dramatically reduced revenues, and unrelenting fixed expenses. Compounding the financial strains, physician owners are forced to stay up-to-date with their local community and state's regulations, implementing critical new compliance processes, and tackling uncharted human resource

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obstacles, all while committing the majority of their time to patient care. We have been contacted by dermatologists exploring their options of aligning with a larger entity that could potentially relieve them of some of these pressures, while also mitigating their personal risks. Riverchase Dermatology is actively pursuing these opportunities to partner with the right practices and physician owners that share our philosophies and vision. We continue to feel confident in the future of dermatology and that the larger size and sophistication equips us to provide infrastructure and best practices to navigate these unprecedented times, while pivoting to new services and technologies such as telemedicine when appropriate. We anticipate more activity in M&A as we move forward, as a less fragmented industry will be better equipped to manage the environment of the foreseeable future.

—Sara Ritacca

Chief Development Officer, Riverchase Dermatology
A leading dermatology practice management business providing general, surgical, and cosmetic dermatology services along with related pathology lab services.

TEST OF RESILIENCY

As the impact of the pandemic economic continues to play out in the dermatology sector, there are many different types of organizations (i.e., dermatology practice owners; strategic and private equity buyers; clinical research organizations) diligently evaluating the situation. While the dermatology sector continues to be an attractive market and generates a great deal of interest in terms of investment activity, 2020 will test the resiliency of the sector. The second half of 2020 is expected to see an uptick in dermatology M&A activity, reflecting renewed buyer confidence in this highly attractive health care market. ■

Clint Bundy is a Managing Director with Bundy Group, a boutique investment bank that specializes in representing business and practice owners in business sales, capital raises and acquisitions. Clint and the Bundy Group team have an extensive track record in the dermatology and health care markets advising practice owners, physician groups, and other businesses related to these markets. www.bundygroup.com

1. Oliver, Kelsey. IBISWorld Industry Report OD4168: Dermatologists in the U.S. IBISWorld: December 2016.

2. Rich, Robert. The Great Recession: December 2007 – June 2009. Federal Reserve History. Published online November 22, 2013.