SYNSTRAT NEWS

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VETERINARY NEWSLETTER

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Searching for Practices to Buy

Most buyers are seeking to buy practices in the metropolitan areas of major cities. This is unsurprising as they have an attractive catchment and are the preferred place for a vet to live.

Demand for such practices far exceeds supply and it is not just vet practitioners seeking these practices; they are high on the shopping list with corporate acquirers as well.

Those vets wishing to buy small animal practices in capital cities or major regional centres will be lucky to find one advertised for sale. Rather, you have to find it.

Vets working in such a practice who have an ambition to buy in long-term need to impress the practice owners with their diligence and willingness to tackle new procedures. Undoubtedly vets who have developed substantial surgical skill are more likely to be offered partnerships in larger practices.

Practices that are advertised for sale are mainly relatively small to medium mixed animal practices, mostly a significant distance from capital cities. These practices are less popular with buyers and a seller can anticipate a lengthy marketing campaign for a sale. There are of course major rural practices with multiple revolving partners which are lucrative and in which partnerships are prized.

The Market for Veterinary Practices

There are many facets necessary for a market to be efficient but one of the main requirements is a mechanism for communicating price information. This is an issue for the market for vet practices as most transactions are private and no price information is publicly available. At Synstrat we see a number of transactions each year but by no means do we see enough transactions to call the market.

Of course that cloak of secrecy does not apply to listed corporate companies such as Greencross and National Vet Care, who are obliged to make information available under their ASX disclosure obligations. However, these transactions are a small portion of the overall number of vet practice transactions and, because of the paucity of other data, there is a risk that the multiples used in these transactions are extrapolated to the whole market. This is a mistake. Corporate owned vets represent around 8%-10% of the total vet practice market in Australia and, although they have come from nowhere 10 years ago and are continuing to grow their share of the practice market, they still represent a significant minority of the vet practice transactions in any one year.

Another factor impacting the information available in the market is the emergence of the aggregator/broker who bundles up a number of practices and implements a bulk sale to a corporate (either listed or private equity) buyer, clipping the ticket on the way. The prices quoted to sellers to get their attention and to garner interest are necessarily high. Of course the problem for the seller is that they do not know who will buy them, when, at what price and under what conditions but none of that negative information filters through to the market, only the high price offered.

Greencross and National Vet Care are trading at around 12 to 13 times EBIT (with debt added back) and this gives them a powerful currency for practice purchases. Put simply, if they can purchase a practice at less than 12 times EBIT then it should increase the value of their companies. Publicly available documents from Greencross indicate their policy is to pay around 4.5 times EBIT for practices. This has held true up until the last 12 months or so after which their disclosures have made it harder to fathom what they are paying. NVC's prospectus indicates they paid up to 6 times EBIT for their initial portfolio of practises. It is perhaps the case that they paid over the odds up for the initial portfolio as it was important to reach a critical mass quickly so as to get the IPO away. It will be interesting to see if their pricing tempers in the coming months.

How applicable are these prices to the general vet practice market? Well, there is a problem in comparing these prices to a classic walk-in-walk-out sale to another veterinarian. Firstly, corporates are very picky on the practices they want and even if you fit the profile they are looking to reduce their risk post settlement by locking the vendors in for as long as possible. For example, a 2-5 year employment contract is typically part and parcel of the sales agreement, with a comparatively low salary compared to the owner's previous remuneration with performance bonuses to top this up. In addition, it is not unusual to see deferred settlement of the purchase price and for payment to be partly in shares, all of which aim to link the performance of the practice post acquisition to the remuneration of the vendor.

This is fundamentally different to a typical walk-in-walk-out sale to another veterinarian where the vendor receives cash and can leave or retire quickly if they want.

This information asymmetry is starting to push prices up across the board and in some cases for practices that do not warrant a premium. At the same time as this is happening the Australian banking sector is being placed under government pressure to limit credit expansion, which is serving to temper their appetite for goodwill lending. Not to the extent that they do not want to get involved but for the first time we are starting to see banks' credit teams get nervous on some of the multiples being paid for practices.

The impact of all of this is that if you are thinking of purchasing a practice it is imperative that you get a valuation done as early in the process as possible. Never has it been more important to get a true understanding of what it is you are buying and what its true value is. If you do not have this in hand before you commence negotiations and they begin around an unrealistic price point based on corporate transactions, then experience tells us that it can be almost impossible to shift the vendor to a more realistic point. Often it becomes impossible to conclude a transaction and get it financed without a significant capital injection from your own funds.

For an impartial vet practice valuation telephone David Collins or Graham Middleton on 03 9843 7777.

Synstrat Publications

For those vets up to the challenge of sustaining a veterinary career, Synstrat's two publications, ***50 Rules for Financial Success as a Veterinary Surgeon*** and ***Buying and Selling Veterinary Practices*** are available free of charge. Email your postal address to annie@synstrat.com.au and additionally, if you wish to receive Synstrat's Veterinary Newsletter via email, please indicate.

Independent Financial Planning and Life Insurance for Vets

Synstrat is experienced at providing financial plans for vets. These take into account veterinary practice profitability and benchmarks, as well as ownership of premises and other family assets and other financial issues. Telephone Graham Middleton, Cameron Darnley or Roger Armitage, each of whom are experienced financial planners, on 03 9843 7777. Cameron can also assist with life insurance. Synstrat Management Pty Ltd holds its own financial services licence. It is not obliged to recommend the products of a particular bank or insurance company.

More Information by Email

We periodically send out more information to vets than we can fit into the Veterinary Newsletter, but for you to receive that information you need to advise your email address to annie@synstrat.com.au and advise the postal address we currently send your newsletter to.

Running a Successful Veterinary Practice Business

Overhead expenses in veterinary practices are quite high compared to medical or dental practices. Successful veterinary practices have the following characteristics:

- Support staff costs as a percentage of fees are at or below benchmark.
- Good stock control.
- Clean waiting rooms with no pharmaceutical advertisements.
- Purchases and laboratory costs are at or below benchmark standard.
- Practices are run by owners who know their clients. They have efficient, personable receptionists.
- Fees are not discounted.
- Maximum surgery is done within the practice.
- The premises are functional but not over-capitalised. There is negligible evidence that ASAVA accreditation adds to profit, but it may require expensive building modification. If rebuilding, keep to simple, functional layouts.

Australia has far too many vets and more vet schools than are needed. In this environment, practices will work hard at internalising as many procedures as possible and refer out the barest minimum. Good practices need to be recognised among their clientele as 'full service' practices.

Visit www.synstrat.com.au for more information on these topics.

THE SYNSTRAT GROUP ARE AUSTRALIA'S MOST EXPERIENCED VETERINARY PRACTICE BUSINESS ADVISERS, ACCOUNTANTS, PRACTICE VALUERS AND LICENCED FINANCIAL ADVISERS

For further information on these subjects, please call:

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